CHARTER COMMUNICATIONS INC /MO/
Form 424B3
November 10, 2005

As filed pursuant to Rule 424(b)(3)
Registration Statement File No. 333-121561

PROSPECTUS SUPPLEMENT NO. 6
DATED NOVEMBER 10, 2005

Charter Communications, Inc.

This document supplements the Prospectus, dated July 19, 2005, Prospectus Supplement No. 1, dated August 9, 2005, Prospectus Supplement No. 2, dated August 30, 2005, Prospectus Supplement No. 3, dated September 15, 2005, Prospectus Supplement No. 4, dated September 23, 2005 and Prospectus Supplement No. 5, dated October 18, 2005 (collectively, the "Prospectus"), relating to the resale by certain holders of up to $862,500,000 aggregate principal amount of Charter Communications, Inc.'s 5.875% convertible senior notes due 2009 (the "Notes") and shares of common stock issuable upon conversion thereof.

This Prospectus Supplement relates to the resale by the holders of the Notes.

The Prospectus is hereby amended as follows:

(1) The information contained in the attached Current Report on Form 8-K filed on November 4, 2005.
(2) The information contained in the attached sections of the Quarterly Report on Form 10-Q filed on November 2, 2005 (Part I. Item 1-4 and Part II. Item 1 and Item 3-5).
(3) The information appearing in the Selling Securityholder table included in this Prospectus Supplement, as of the date hereof, supersedes the information in the table appearing under the heading "Selling Securityholders" in the Prospectus.

If the information in this Prospectus Supplement is inconsistent with any information contained in the Prospectus or in the reports, proxy statements or other documents previously filed with the Securities and Exchange Commission (collectively, the "SEC Reports") incorporated by reference in the Prospectus or delivered in connection therewith, the Prospectus and/or any SEC Report, as applicable, shall be deemed superseded by this Supplement.

In all other ways, the Prospectus shall remain unchanged.

This Prospectus Supplement should be read in conjunction with, and may not be delivered or utilized without, the Prospectus.

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2005

or

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

For the transition period from ________to _________

Commission file number: 000-27927

Charter Communications, Inc.
(Exact name of registrant as specified in its charter)

Delaware	**43-1857213**
(State or other jurisdiction of incorporation or organization)	*(I.R.S. Employer Identification Number)*

12405 Powerscourt Drive
St. Louis, Missouri 63131
(Address of principal executive offices including zip code)

(314) 965-0555
(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 an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). YES [X] NO [ ]

Number of shares of Class A common stock outstanding as of September 30, 2005: 348,576,466
Number of shares of Class B common stock outstanding as of September 30, 2005: 50,000

Charter Communications, Inc.
Quarterly Report on Form 10-Q for the Period ended September 30, 2005

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This quarterly report on Form 10-Q is for the three and nine months ended September 30, 2005. The Securities and Exchange Commission ("SEC") allows us to "incorporate by reference" information that we file with the SEC, which means that we can disclose important information to you by referring you directly to those documents. Information incorporated by reference is considered to be part of this quarterly report. In addition, information that we file with the SEC in the future will automatically update and supersede information contained in this quarterly report. In this quarterly report, "we," "us" and "our" refer to Charter Communications, Inc., Charter Communications Holding Company, LLC and their subsidiaries.

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS:

This quarterly report includes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act"), and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), regarding, among other things, our plans, strategies and prospects, both business and financial including, without limitation, the forward-looking statements set forth in the "Results of Operations" and "Liquidity and Capital Resources" sections under Part I, Item 2. "Management's Discussion and Analysis of Financial Condition and Results of Operations" in this quarterly report. Although we believe that our plans, intentions and expectations reflected in or suggested by these forward-looking statements are reasonable, we cannot assure you that we will achieve or realize these plans, intentions or expectations. Forward-looking statements are inherently subject to risks, uncertainties and assumptions including, without limitation, the factors described under "Certain Trends and Uncertainties" under Part I, Item 2. "Management's Discussion and Analysis of Financial Condition and Results of Operations" in this quarterly report. Many of the forward-looking statements contained in this quarterly report may be identified by the use of forward-looking words such as "believe," "expect," "anticipate," "should," "planned," "will," "may," "intend," "estimated" and "potential" among others. Important factors that could cause actual results to differ materially from the forward-looking statements we make in this quarterly report are set forth in this quarterly report and in other reports or documents that we file from time to time with the SEC, and include, but are not limited to:

- the availability, in general, of funds to meet interest payment obligations under our debt and to fund our operations and necessary capital expenditures, either through cash flows from operating activities, further borrowings or other sources and, in particular, our ability to be able to provide under applicable debt instruments such funds (by dividend, investment or otherwise) to the applicable obligor of such debt;
- our ability to sustain and grow revenues and cash flows from operating activities by offering video, high-speed Internet, telephone and other services and to maintain and grow a stable customer base, particularly in the face of increasingly aggressive competition from other service providers;
- our ability to comply with all covenants in our indentures, the Bridge Loan and credit facilities, any violation of which would result in a violation of the applicable facility or indenture and could trigger a default of other obligations under cross-default provisions;
- our ability to pay or refinance debt prior to or when it becomes due and/or to take advantage of market opportunities and market windows to refinance that debt in the capital markets through new issuances, exchange offers or otherwise, including restructuring our balance sheet and leverage position;
- our ability to obtain programming at reasonable prices or to pass programming cost increases on to our customers;
- general business conditions, economic uncertainty or slowdown; and
- the effects of governmental regulation, including but not limited to local franchise authorities, on our business.

All forward-looking statements attributable to us or any person acting on our behalf are expressly qualified in their entirety by this cautionary statement. We are under no duty or obligation to update any of the forward-looking statements after the date of this quarterly report.

PART 1. FINANCIAL INFORMATION.

Item 1. Financial Statments.

CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(DOLLARS IN MILLIONS, EXCEPT SHARE DATA)

	September 30, 2005 (Unaudited)	December 31, 2004
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 22	$ 650
Accounts receivable, less allowance for doubtful accounts of $15 and $15, respectively	188	190
Prepaid expenses and other current assets	80	82
Total current assets	290	922
INVESTMENT IN CABLE PROPERTIES:		
Property, plant and equipment, net of accumulated depreciation of $6,393 and $5,311, respectively	5,936	6,289
Franchises, net	9,830	9,878
Total investment in cable properties, net	15,766	16,167
OTHER NONCURRENT ASSETS	468	584
Total assets	$ 16,524	$ 17,673
LIABILITIES AND SHAREHOLDERS' DEFICIT		
CURRENT LIABILITIES:		
Accounts payable and accrued expenses	$ 1,172	$ 1,217
Total current liabilities	1,172	1,217
LONG-TERM DEBT	19,120	19,464
DEFERRED MANAGEMENT FEES - RELATED PARTY	14	14
OTHER LONG-TERM LIABILITIES	504	681
MINORITY INTEREST	665	648
PREFERRED STOCK - REDEEMABLE; $.001 par value; 1 million shares authorized; 545,259 shares issued and outstanding	55	55
SHAREHOLDERS' DEFICIT:		
Class A Common stock; $.001 par value; 1.75 billion shares authorized; 348,576,466 and 305,203,770 shares issued and outstanding, respectively	--	--
Class B Common stock; $.001 par value; 750 million shares authorized; 50,000 shares issued and outstanding	--	--
Preferred stock; $.001 par value; 250 million shares authorized; no non-redeemable shares issued and outstanding	--	--
Additional paid-in capital	4,821	4,794
Accumulated deficit	(9,830)	(9,196)

Accumulated other comprehensive income (loss)		3		(4)
Total shareholders' deficit		(5,006)		(4,406)
Total liabilities and shareholders' deficit	$	16,524	$	17,673

The accompanying notes are an integral part of these condensed consolidated financial statements.

CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(DOLLARS IN MILLIONS, EXCEPT SHARE AND PER SHARE DATA)
Unaudited

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2005	2004	2005	2004
REVENUES	$ 1,318	$ 1,248	$ 3,912	$ 3,701
COSTS AND EXPENSES:				
Operating (excluding depreciation and amortization)	586	525	1,714	1,552
Selling, general and administrative	269	252	762	735
Depreciation and amortization	375	371	1,134	1,105
Impairment of franchises	--	2,433	--	2,433
Asset impairment charges	--	--	39	--
(Gain) loss on sale of assets, net	1	--	5	(104)
Option compensation expense, net	3	8	11	34
Hurricane asset retirement loss	19	--	19	--
Special charges, net	2	3	4	100
	1,255	3,592	3,688	5,855
Income (loss) from operations	63	(2,344)	224	(2,154)
OTHER INCOME AND EXPENSES:				
Interest expense, net	(462)	(424)	(1,333)	(1,227)
Gain (loss) on derivative instruments and hedging activities, net	17	(8)	43	48
Loss on debt to equity conversions	--	--	--	(23)
Gain (loss) on extinguishment of debt	490	--	498	(21)
Gain on investments	--	--	21	--
	45	(432)	(771)	(1,223)
Income (loss) before minority interest, income taxes and cumulative effect of accounting change	108	(2,776)	(547)	(3,377)
MINORITY INTEREST	(3)	34	(9)	24
Income (loss) before income taxes and cumulative effect of accounting change	105	(2,742)	(556)	(3,353)

INCOME TAX BENEFIT (EXPENSE)	(29)	213	(75)	116
Income (loss) before cumulative effect of accounting change	76	(2,529)	(631)	(3,237)
CUMULATIVE EFFECT OF ACCOUNTING CHANGE, NET OF TAX	--	(765)	--	(765)
Net income (loss)	76	(3,294)	(631)	(4,002)
Dividends on preferred stock - redeemable	(1)	(1)	(3)	(3)
Net income (loss) applicable to common stock	$ 75	$ (3,295)	$ (634)	$ (4,005)
EARNINGS (LOSS) PER COMMON SHARE:				
Basic	$ 0.24	$ (10.89)	$ (2.06)	$ (13.38)
Diluted	$ 0.09	$ (10.89)	$ (2.06)	$ (13.38)
Weighted average common shares outstanding, basic	316,214,740	302,604,978	307,761,930	299,411,053
Weighted average common shares outstanding, diluted	1,012,591,842	302,604,978	307,761,930	299,411,053

The accompanying notes are an integral part of these condensed consolidated financial statements.

CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(DOLLARS IN MILLIONS)
Unaudited

	Nine Months Ended September 30, 2005	2004
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$ (631)	$ (4,002)
Adjustments to reconcile net loss to net cash flows from operating activities:		
Minority interest	9	(24)
Depreciation and amortization	1,134	1,105
Asset impairment charges	39	--
Impairment of franchises	--	2,433
Option compensation expense, net	11	30
Hurricane asset retirement loss	19	--
Special charges, net	--	85
Noncash interest expense	188	237
Gain on derivative instruments and hedging activities, net	(43)	(48)
(Gain) loss on sale of assets, net	5	(104)
Loss on debt to equity conversions	--	23
(Gain) loss on extinguishment of debt	(504)	18
Gain on investments	(21)	--
Deferred income taxes	71	(119)
Cumulative effect of accounting change, net of tax	--	765
Other, net	--	(1)
Changes in operating assets and liabilities, net of effects from dispositions:		
Accounts receivable	(3)	1
Prepaid expenses and other assets	85	2
Accounts payable, accrued expenses and other	(241)	(18)
Net cash flows from operating activities	118	383
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property, plant and equipment	(815)	(639)
Change in accrued expenses related to capital expenditures	36	(23)
Proceeds from sale of assets	38	729
Purchases of investments	(3)	(15)
Proceeds from investments	17	--
Other, net	(2)	(2)
Net cash flows from investing activities	(729)	50
CASH FLOWS FROM FINANCING ACTIVITIES:		
Borrowings of long-term debt	897	2,873
Repayments of long-term debt	(1,141)	(4,707)
Proceeds from issuance of debt	294	1,500

Payments for debt issuance costs		(67)		(97)
Net cash flows from financing activities		(17)		(431)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS		(628)		2
CASH AND CASH EQUIVALENTS, beginning of period		650		127
CASH AND CASH EQUIVALENTS, end of period	$	22	$	129
CASH PAID FOR INTEREST	$	1,170	$	824
NONCASH TRANSACTIONS:				
Issuance of debt by CCH I Holdings, LLC	$	2,423	$	--
Issuance of debt by CCH I, LLC	$	3,686	$	--
Issuance of debt by Charter Communications Operating, LLC	$	333	$	--
Retirement of Charter Communications Holdings, LLC debt	$	(7,000)	$	--
Debt exchanged for Charter Class A common stock	$	--	$	30

The accompanying notes are an integral part of these condensed consolidated financial statements.

CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)
(dollars in millions, except share and per share amounts and where indicated)

1. Organization and Basis of Presentation

Charter Communications, Inc. ("Charter") is a holding company whose principal assets at September 30, 2005 are the 48% controlling common equity interest in Charter Communications Holding Company, LLC ("Charter Holdco") and "mirror" notes which are payable by Charter Holdco to Charter and have the same principal amount and terms as those of Charter's convertible senior notes. Charter Holdco is the sole owner of CCHC, LLC, which is the sole owner of Charter Communications Holdings, LLC ("Charter Holdings"). The condensed consolidated financial statements include the accounts of Charter, Charter Holdco, Charter Holdings and all of their subsidiaries where the underlying operations reside, which are collectively referred to herein as the "Company." Charter consolidates Charter Holdco on the basis of voting control. Charter Holdco's limited liability company agreement provides that so long as Charter's Class B common stock retains its special voting rights, Charter will maintain a 100% voting interest in Charter Holdco. Voting control gives Charter full authority and control over the operations of Charter Holdco. All significant intercompany accounts and transactions among consolidated entities have been eliminated. The Company is a broadband communications company operating in the United States. The Company offers its customers traditional cable video programming (analog and digital video) as well as high-speed Internet services and, in some areas, advanced broadband services such as high definition television, video on demand and telephone. The Company sells its cable video programming, high-speed Internet and advanced broadband services on a subscription basis. The Company also sells local advertising on satellite-delivered networks.

The accompanying condensed consolidated financial statements of the Company have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and the rules and regulations of the Securities and Exchange Commission (the "SEC"). Accordingly, certain information and footnote disclosures typically included in Charter's Annual Report on Form 10-K have been condensed or omitted for this quarterly report. The accompanying condensed consolidated financial statements are unaudited and are subject to review by regulatory authorities. However, in the opinion of management, such financial statements include all adjustments, which consist of only normal recurring adjustments, necessary for a fair presentation of the results for the periods presented. Interim results are not necessarily indicative of results for a full year. The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Areas involving significant judgments and estimates include capitalization of labor and overhead costs; depreciation and amortization costs; impairments of property, plant and equipment, franchises and goodwill; income taxes; and contingencies. Actual results could differ from those estimates.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Areas involving significant judgments and estimates include capitalization of labor and overhead costs; depreciation and amortization costs; impairments of property, plant and equipment, franchises and goodwill; income taxes; and contingencies. Actual results could differ from those estimates.

Reclassifications

Certain 2004 amounts have been reclassified to conform with the 2005 presentation.

2. Liquidity and Capital Resources

The Company had net income applicable to common stock of $75 million for the three months ended September 30, 2005. The Company incurred net loss applicable to common stock of $634 million for the nine months ended September 30, 2005 and $3.3 billion and $4.0 billion for the three and nine months ended September 30, 2004, respectively. The Company's net cash flows from operating activities were $118 million and $383 million for the nine months ended September 30, 2005 and 2004, respectively.

The Company has a significant level of debt. The Company's long-term financing as of September 30, 2005 consists of $5.5 billion of credit facility debt, $12.7 billion accreted value of high-yield notes and $866 million accreted value of convertible senior notes. For the remainder of 2005, $7 million of the Company's debt matures, and in 2006, an additional $55 million of the Company's debt matures. In 2007 and beyond, significant additional amounts will become due under the Company's remaining long-term debt obligations.

CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)
(dollars in millions, except share and per share amounts and where indicated)

In September 2005, Charter Holdings and its wholly owned subsidiaries, CCH I, LLC ("CCH I") and CCH I Holdings, LLC ("CIH"), completed the exchange of approximately $6.8 billion total principal amount of outstanding debt securities of Charter Holdings in a private placement for new debt securities. Holders of Charter Holdings notes due in 2009 and 2010 exchanged $3.4 billion principal amount of notes for $2.9 billion principal amount of new 11% CCH I senior secured notes due 2015. Holders of Charter Holdings notes due 2011 and 2012 exchanged $845 million principal amount of notes for $662 million principal amount of 11% CCH I senior secured notes due 2015. In addition, holders of Charter Holdings notes due 2011 and 2012 exchanged $2.5 billion principal amount of notes for $2.5 billion principal amount of various series of new CIH notes. Each series of new CIH notes has the same stated interest rate and provisions for payment of cash interest as the series of old Charter Holdings notes for which such CIH notes were exchanged. In addition, the maturities for each series were extended three years. See Note 6 for discussion of transaction and related financial statement impact.

The Company has historically required significant cash to fund debt service costs, capital expenditures and ongoing operations. Historically, the Company has funded these requirements through cash flows from operating activities, borrowings under its credit facilities, sales of assets, issuances of debt and equity securities and from cash on hand. However, the mix of funding sources changes from period to period. For the nine months ended September 30, 2005, the Company generated $118 million of net cash flows from operating activities, after paying cash interest of $1.2 billion. In addition, the Company used approximately $815 million for purchases of property, plant and equipment. Finally, the Company had net cash flows used in financing activities of $17 million.

In October 2005, CCO Holdings, LLC ("CCO Holdings") and CCO Holdings Capital Corp., as guarantor thereunder, entered into a senior bridge loan agreement (the "Bridge Loan") with JPMorgan Chase Bank, N.A., Credit Suisse, Cayman Islands Branch and Deutsche Bank AG Cayman Islands Branch (the "Lenders") whereby the Lenders have committed to make loans to CCO Holdings in an aggregate amount of $600 million. CCO Holdings may draw upon the facility between January 2, 2006 and September 29, 2006 and the loans will mature on the sixth anniversary of the first borrowing under the Bridge Loan.

The Company expects that cash on hand, cash flows from operating activities and the amounts available under its credit facilities and Bridge Loan will be adequate to meet its cash needs for the remainder of 2005 and 2006. Cash flows from operating activities and amounts available under the Company’s credit facilities and Bridge Loan may not be sufficient to fund the Company’s operations and satisfy its interest payment obligations in 2007. It is likely that the Company will require additional funding to satisfy its debt repayment obligations in 2007. The Company believes that cash flows from operating activities and amounts available under its credit facilities and Bridge Loan will not be sufficient to fund its operations and satisfy its interest and principal repayment obligations thereafter.

The Company is working with its financial advisors to address its funding requirements. However, there can be no assurance that such funding will be available to the Company. Although Paul G. Allen, Charter’s Chairman and controlling shareholder, and his affiliates have purchased equity from the Company in the past, Mr. Allen and his affiliates are not obligated to purchase equity from, contribute to or loan funds to the Company in the future.

Credit Facilities and Covenants

The Company’s ability to operate depends upon, among other things, its continued access to capital, including credit under the Charter Communications Operating, LLC ("Charter Operating") credit facilities. These credit facilities, along with the Company’s indentures and Bridge Loan, contain certain restrictive covenants, some of which require the

Company to maintain specified financial ratios and meet financial tests and to provide audited financial statements with an unqualified opinion from the Company's independent auditors. As of September 30, 2005, the Company is in compliance with the covenants under its indentures and credit facilities and the Company expects to remain in compliance with those covenants and the Bridge Loan covenants for the next twelve months. The Company's total potential borrowing availability under the current credit facilities totaled $786 million as of September 30, 2005, although the actual availability at that time was only $648 million because of limits imposed by covenant restrictions. In addition, effective January 2, 2006, the Company will have additional borrowing availability of $600 million as a result of the Bridge Loan. Continued access to the Company's credit facilities and Bridge Loan is subject to the

CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)
(dollars in millions, except share and per share amounts and where indicated)

Company remaining in compliance with the covenants of these credit facilities and Bridge Loan, including covenants tied to the Company's operating performance. If the Company's operating performance results in non-compliance with these covenants, or if any of certain other events of non-compliance under these credit facilities, Bridge Loan or indentures governing the Company's debt occur, funding under the credit facilities and Bridge Loan may not be available and defaults on some or potentially all of the Company's debt obligations could occur. An event of default under the covenants governing any of the Company's debt instruments could result in the acceleration of its payment obligations under that debt and, under certain circumstances, in cross-defaults under its other debt obligations, which could have a material adverse effect on the Company's consolidated financial condition or results of operations.

Specific Limitations

Charter's ability to make interest payments on its convertible senior notes, and, in 2006 and 2009, to repay the outstanding principal of its convertible senior notes of $25 million and $863 million, respectively, will depend on its ability to raise additional capital and/or on receipt of payments or distributions from Charter Holdco or its subsidiaries, including Charter Holdings, CIH, CCH I, CCH II, LLC ("CCH II"), CCO Holdings and Charter Operating. During the nine months ended September 30, 2005, Charter Holdings distributed $60 million to Charter Holdco. As of September 30, 2005, Charter Holdco was owed $57 million in intercompany loans from its subsidiaries, which amount was available to pay interest and principal on Charter's convertible senior notes. In addition, Charter has $123 million of governmental securities pledged as security for the next five semi-annual interest payments on Charter's 5.875% convertible senior notes.

Distributions by Charter's subsidiaries to a parent company (including Charter and Charter Holdco) for payment of principal on parent company notes are restricted by the Bridge Loan and indentures governing the CIH notes, CCH I notes, CCH II notes, CCO Holdings notes, and Charter Operating notes, unless under their respective indentures there is no default and a specified leverage ratio test is met at the time of such event. For the quarter ended September 30, 2005, there was no default under any of the aforementioned indentures. However, CCO Holdings did not meet its leverage ratio test of 4.5 to 1.0. As a result, distributions from CCO Holdings to CCH II, CCH I, CIH, Charter Holdings, Charter Holdco or Charter for payment of principal of the respective parent company's debt are currently restricted and will continue to be restricted until that test is met. However distributions for payment of the respective parent company's interest are permitted.

The indentures governing the Charter Holdings notes permit Charter Holdings to make distributions to Charter Holdco for payment of interest or principal on the convertible senior notes, only if, after giving effect to the distribution, Charter Holdings can incur additional debt under the leverage ratio of 8.75 to 1.0, there is no default under Charter Holdings' indentures and other specified tests are met. For the quarter ended September 30, 2005, there was no default under Charter Holdings' indentures and other specified tests were met. However, Charter Holdings did not meet the leverage ratio of 8.75 to 1.0 based on September 30, 2005 financial results. As a result, distributions from Charter Holdings to Charter or Charter Holdco for payment of interest or principal on the convertible senior notes are currently restricted and will continue to be restricted until that test is met. During this restriction period, the indentures governing the Charter Holdings notes permit Charter Holdings and its subsidiaries to make specified investments in Charter Holdco or Charter, up to an amount determined by a formula, as long as there is no default under the indentures.

3. Sale of Assets

In July 2005, the Company closed the sale of certain cable systems in Texas and West Virginia and closed the sale of an additional cable system in Nebraska in October 2005, representing a total of approximately 33,000 customers. During the nine months ended September 30, 2005, those cable systems met the criteria for assets held for sale under Statement of Financial Accounting Standards ("SFAS") No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*. As such, the assets were written down to fair value less estimated costs to sell resulting in asset impairment charges during the nine months ended September 30, 2005 of approximately $39 million. At September 30, 2005 assets held for sale, included in investment in cable properties, are approximately $7 million.

CHARTER COMMUNICATIONS, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)
(dollars in millions, except share and per share amounts and where indicated)

In March 2004, the Company closed the sale of certain cable systems in Florida, Pennsylvania, Maryland, Delaware and West Virginia to Atlantic Broadband Finance, LLC. The Company closed the sale of an additional cable system in New York to Atlantic Broadband Finance, LLC in April 2004. These transactions resulted in a $106 million pretax gain recorded as a gain on sale of assets in the Company's consolidated statements of operations. The total net proceeds from the sale of all of these systems were approximately $735 million. The proceeds were used to repay a portion of amounts outstanding under the Company's revolving credit facility.

Gain on investments for the nine months ended September 30, 2005 primarily represents a gain realized on an exchange of the Company's interest in an equity investee for an investment in a larger enterprise.

4. Franchises and Goodwill

Franchise rights represent the value attributed to agreements with local authorities that allow access to homes in cable service areas acquired through the purchase of cable systems. Management estimates the fair value of franchise rights at the date of acquisition and determines if the franchise has a finite life or an indefinite-life as defined by SFAS No. 142, *Goodwill and Other Intangible Assets*. Franchises that qualify for indefinite-life treatment under SFAS No. 142 are tested for impairment annually each October 1 based on valuations, or more frequently as warranted by events or changes in circumstances. Such test resulted in a total franchise impairment of approximately $3.3 billion during the third quarter of 2004. The October 1, 2005 annual impairment test will be finalized in the fourth quarter of 2005 and any impairment resulting from such test will be recorded in the fourth quarter. Franchises are aggregated into essentially inseparable asset groups to conduct the valuations. The asset groups generally represent geographic clustering of the Company's cable systems into groups by which such systems are managed. Management believes such grouping represents the highest and best use of those assets.

The Company's valuations, which are based on the present value of projected after tax cash flows, result in a value of property, plant and equipment, franchises, customer relationships and its total entity value. The value of goodwill is the difference between the total entity value and amounts assigned to the other assets.

Franchises, for valuation purposes, are defined as the future economic benefits of the right to solicit and service potential customers (customer marketing rights), and the right to deploy and market new services such as interactivity and telephone to the potential customers (service marketing rights). Fair value is determined based on estimated discounted future cash flows using assumptions consistent with internal forecasts. The franchise after-tax cash flow is calculated as the after-tax cash flow generated by the potential customers obtained and the new services added to those customers in future periods. The sum of the present value of the franchises' after-tax cash flow in years 1 through 10 and the continuing value of the after-tax cash flow beyond year 10 yields the fair value of the franchise.

The Company follows the guidance of Emerging Issues Task Force ("EITF") Issue 02-17, *Recognition of Customer Relationship Intangible Assets Acquired in a Business Combination,* in valuing customer relationships. Customer relationships, for valuation purposes, represent the value of the business relationship with existing customers and are calculated by projecting future after-tax cash flows from these customers including the right to deploy and market additional services such as interactivity and telephone to these customers. The present value of these after-tax cash flows yields the fair value of the customer relationships. Substantially all acquisitions occurred prior to January 1, 2002. The Company did not record any value associated with the customer relationship intangibles related to those acquisitions. For acquisitions subsequent to January 1, 2002 the Company did assign a value to the customer relationship intangible, which is amortized over its estimated useful life.

In September 2004, the SEC staff issued EITF Topic D-108 which requires the direct method of separately valuing all intangible assets and does not permit goodwill to be included in franchise assets. The Company adopted Topic D-108 in its impairment assessment as of September 30, 2004 that resulted in a total franchise impairment of approximately $3.3 billion. The Company recorded a cumulative effect of accounting change of $765 million (approximately $875 million before tax effects of $91 million and minority interest effects of $19 million) for the nine months ended September 30, 2004 representing the portion of the Company's total franchise impairment attributable to no longer including goodwill with franchise assets. The effect of the adoption was to increase net loss and loss per share by

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$765 million and $2.55, respectively, for the nine months ended September 30, 2004. The remaining $2.4 billion of the total franchise impairment was attributable to the use of lower projected growth rates and the resulting revised estimates of future cash flows in the Company's valuation, and was recorded as impairment of franchises in the Company's accompanying consolidated statements of operations for the nine months ended September 30, 2004. Sustained analog video customer losses by the Company in the third quarter of 2004 primarily as a result of increased competition from direct broadcast satellite providers and decreased growth rates in the Company's high-speed Internet customers in the third quarter of 2004, in part, as a result of increased competition from digital subscriber line service providers led to the lower projected growth rates and the revised estimates of future cash flows from those used at October 1, 2003.

As of September 30, 2005 and December 31, 2004, indefinite-lived and finite-lived intangible assets are presented in the following table:

	September 30, 2005			December 31, 2004		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Indefinite-lived intangible assets:						
Franchises with indefinite lives	$ 9,797	$ --	$ 9,797	$ 9,845	$ --	$ 9,845
Goodwill	52	--	52	52	--	52
	$ 9,849	$ --	$ 9,849	$ 9,897	$ --	$ 9,897
Finite-lived intangible assets:						
Franchises with finite lives	$ 40	$ 7	$ 33	$ 37	$ 4	$ 33

Franchises with indefinite lives decreased $39 million as a result of the asset impairment charges recorded related to three cable asset sales and $9 million as a result of the closing of two of the cable asset sales in July 2005 (see Note 3). Franchise amortization expense for the three and nine months ended September 30, 2005 and 2004 was $1 million and $3 million, respectively, which represents the amortization relating to franchises that did not qualify for indefinite-life treatment under SFAS No. 142, including costs associated with franchise renewals. The Company expects that amortization expense on franchise assets will be approximately $3 million annually for each of the next five years. Actual amortization expense in future periods could differ from these estimates as a result of new intangible asset acquisitions or divestitures, changes in useful lives and other relevant factors.

5. Accounts Payable and Accrued Expenses

Accounts payable and accrued expenses consist of the following as of September 30, 2005 and December 31, 2004:

	September 30, 2005	December 31, 2004
Accounts payable - trade	$ 84	$ 148

Accrued capital expenditures		101		65
Accrued expenses:				
Interest		298		324
Programming costs		287		278
Franchise-related fees		56		67
Compensation		85		66
Other		261		269
	$	1,172	$	1,217

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6. Long-Term Debt

Long-term debt consists of the following as of September 30, 2005 and December 31, 2004:

	September 30, 2005		December 31, 2004	
	Principal Amount	Accreted Value	Principal Amount	Accreted Value
Long-Term Debt				
Charter Communications, Inc.:				
4.75% convertible senior notes due 2006	$ 25	$ 25	$ 156	$ 156
5.875% convertible senior notes due 2009	863	841	863	834
Charter Communications Holdings, LLC:				
8.250% senior notes due 2007	105	105	451	451
8.625% senior notes due 2009	292	292	1,244	1,243
9.920% senior discount notes due 2011	198	198	1,108	1,108
10.000% senior notes due 2009	154	154	640	640
10.250% senior notes due 2010	49	49	318	318
11.750% senior discount notes due 2010	43	43	450	448
10.750% senior notes due 2009	131	131	874	874
11.125% senior notes due 2011	217	217	500	500
13.500% senior discount notes due 2011	94	91	675	589
9.625% senior notes due 2009	107	107	640	638
10.000% senior notes due 2011	137	136	710	708
11.750% senior discount notes due 2011	125	116	939	803
12.125% senior discount notes due 2012	113	97	330	259
CCH I Holdings, LLC:				
11.125% senior notes due 2014	151	151	--	--
9.920% senior discount notes due 2014	471	471	--	--
10.000% senior notes due 2014	299	299	--	--
11.750% senior discount notes due 2014	815	759	--	--
13.500% senior discount notes due 2014	581	559	--	--
12.125% senior discount notes due 2015	217	187	--	--
CCH I, LLC:				
11.00% senior notes due 2015	3,525	3,686	--	--
CCH II, LLC:				

10.250% senior notes due 2010		1,601		1,601		1,601	1,601
CCO Holdings, LLC:							
8¾% senior notes due 2013		800		794		500	500
Senior floating rate notes due 2010		550		550		550	550
Charter Communications Operating, LLC:							
8% senior second lien notes due 2012		1,100		1,100		1,100	1,100
8 3/8% senior second lien notes due 2014		733		733		400	400
Renaissance Media Group LLC:							
10.000% senior discount notes due 2008		114		115		114	116
CC V Holdings, LLC:							
11.875% senior discount notes due 2008		--		--		113	113
Credit Facilities							
Charter Operating		5,513		5,513		5,515	5,515
	$	19,123	$	19,120	$	19,791	$ 19,464

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The accreted values presented above represent the principal amount of the notes less the original issue discount at the time of sale plus the accretion to the balance sheet date. The accreted value of CIH notes and CCH I notes issued in exchange for Charter Holdings notes are recorded in accordance with generally accepted accounting principles ("GAAP"). GAAP requires that the CIH notes issued in exchange for Charter Holdings notes and the CCH I notes issued in exchange for the 8.625% Charter Holdings notes due 2009 be recorded at the historical book values of the Charter Holdings notes as opposed to the current accreted value for legal purposes and notes indenture purposes (the amount that is currently payable if the debt becomes immediately due). As of September 30, 2005, the accreted value of the Company's debt for legal purposes and notes indenture purposes is $18.6 billion.

In October 2005, CCO Holdings and CCO Holdings Capital Corp., as guarantor thereunder, entered into the Bridge Loan with the Lenders whereby the Lenders have committed to make loans to CCO Holdings in an aggregate amount of $600 million. CCO Holdings may draw upon the facility between January 2, 2006 and September 29, 2006 and the loans will mature on the sixth anniversary of the first borrowing under the Bridge Loan. Each loan will accrue interest at a rate equal to an adjusted LIBOR rate plus a spread. The spread will initially be 450 basis points and will increase (a) by an additional 25 basis points at the end of the six-month period following the date of the first borrowing, (b) by an additional 25 basis points at the end of each of the next two subsequent three month periods and (c) by 62.5 basis points at the end of each of the next two subsequent three-month periods. CCO Holdings will be required to prepay loans from the net proceeds from (i) the issuance of equity or incurrence of debt by Charter and its subsidiaries, with certain exceptions, and (ii) certain asset sales (to the extent not used for other purposes permitted under the Bridge Loan).

In August 2005, CCO Holdings issued $300 million in debt securities, the proceeds of which were used for general corporate purposes, including the payment of distributions to its parent companies, including Charter Holdings, to pay interest expense.

Gain (loss) on extinguishment of debt

In September 2005, Charter Holdings and its wholly owned subsidiaries, CCH I and CIH, completed the exchange of approximately $6.8 billion total principal amount of outstanding debt securities of Charter Holdings in a private placement for new debt securities. Holders of Charter Holdings notes due in 2009 and 2010 exchanged $3.4 billion principal amount of notes for $2.9 billion principal amount of new 11% CCH I senior secured notes due 2015. Holders of Charter Holdings notes due 2011 and 2012 exchanged $845 million principal amount of notes for $662 million principal amount of 11% CCH I senior secured notes due 2015. In addition, holders of Charter Holdings notes due 2011 and 2012 exchanged $2.5 billion principal amount of notes for $2.5 billion principal amount of various series of new CIH notes. Each series of new CIH notes has the same stated interest rate and provisions for payment of cash interest as the series of old Charter Holdings notes for which such CIH notes were exchanged. In addition, the maturities for each series were extended three years. The exchanges resulted in a net gain on extinguishment of debt of approximately $490 million for the three and nine months ended September 30, 2005.

In March and June 2005, Charter Operating consummated exchange transactions with a small number of institutional holders of Charter Holdings 8.25% senior notes due 2007 pursuant to which Charter Operating issued, in private placements, approximately $333 million principal amount of new notes with terms identical to Charter Operating's 8.375% senior second lien notes due 2014 in exchange for approximately $346 million of the Charter Holdings 8.25% senior notes due 2007. The exchanges resulted in gain on extinguishment of debt of approximately $10 million for the nine months ended September 30, 2005. The Charter Holdings notes received in the exchange were thereafter

distributed to Charter Holdings and cancelled.

During the nine months ended September 30, 2005, the Company repurchased, in private transactions, from a small number of institutional holders, a total of $131 million principal amount of its 4.75% convertible senior notes due 2006. These transactions resulted in a net gain on extinguishment of debt of approximately $4 million for the nine months ended September 30, 2005.

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In March 2005, Charter's subsidiary, CC V Holdings, LLC, redeemed all of its 11.875% notes due 2008, at 103.958% of principal amount, plus accrued and unpaid interest to the date of redemption. The total cost of redemption was approximately $122 million and was funded through borrowings under the Charter Operating credit facilities. The redemption resulted in a loss on extinguishment of debt for the nine months ended September 30, 2005 of approximately $5 million. Following such redemption, CC V Holdings, LLC and its subsidiaries (other than non-guarantor subsidiaries) guaranteed the Charter Operating credit facilities and granted a lien on all of their assets as to which a lien can be perfected under the Uniform Commercial Code by the filing of a financing statement.

7. Minority Interest and Equity Interest of Charter Holdco

Charter is a holding company whose primary assets are a controlling equity interest in Charter Holdco, the indirect owner of the Company's cable systems, and $866 million and $990 million at September 30, 2005 and December 31, 2004, respectively, of mirror notes that are payable by Charter Holdco to Charter and have the same principal amount and terms as those of Charter's convertible senior notes. Minority interest on the Company's consolidated balance sheets as of September 30, 2005 and December 31, 2004 primarily represents preferred membership interests in CC VIII, LLC ("CC VIII"), an indirect subsidiary of Charter Holdco, of $665 million and $656 million, respectively. As more fully described in Note 20, this preferred interest arises from the approximately $630 million of preferred membership units issued by CC VIII in connection with an acquisition in February 2000 and was the subject of a dispute between Charter and Mr. Allen, Charter's Chairman and controlling shareholder that was settled October 31, 2005. The Company is currently determining the impact of the settlement to be recorded in the fourth quarter of 2005. Due to the uncertainties that existed prior to October 31, 2005, related to the ultimate resolution, effective January 1, 2005, the Company ceased recognizing minority interest in earnings or losses of CC VIII for financial reporting purposes until such time as the resolution of the matter was determinable or other events occurred. For the three and nine months ended September 30, 2005, the Company's results include income of $8 million and $25 million, respectively, attributable to CC VIII. Subsequent to recording the impact of the settlement in the fourth quarter of 2005, approximately 6% of CC VIII's income will be allocated to minority interest.

Minority interest historically included the portion of Charter Holdco's member's equity not owned by Charter. However, members' deficit of Charter Holdco was $5.0 billion and $4.4 billion as of September 30, 2005 and December 31, 2004, respectively, thus minority interest in Charter Holdco has been eliminated. Minority interest was approximately 52% as of September 30, 2005 and 53% as of December 31, 2004. Minority interest includes the proportionate share of changes in fair value of interest rate derivative agreements. Such amounts are temporary as they are contractually scheduled to reverse over the life of the underlying instrument. Additionally, reported losses allocated to minority interest on the consolidated statement of operations are limited to the extent of any remaining minority interest on the balance sheet related to Charter Holdco. As such, Charter absorbs all losses before income taxes that otherwise would be allocated to minority interest. Subject to any changes in Charter Holdco's capital structure, future losses will continue to be absorbed by Charter.

Changes to minority interest consist of the following:

		Minority Interest
Balance, December 31, 2004	$	648
CC VIII 2% Priority Return (see Note 20)		9

Changes in fair value of interest rate agreements		8
Balance, September 30, 2005	$	665

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8. Share Lending Agreement

On July 29, 2005, Charter issued 27.2 million shares of Class A common stock in a public offering, which was effected pursuant to an effective registration statement that initially covered the issuance and sale of up to 150 million shares of Class A common stock. The shares were issued pursuant to the share lending agreement, pursuant to which Charter had previously agreed to loan up to 150 million shares to Citigroup Global Markets Limited ("CGML"). Because less than the full 150 million shares covered by the share lending agreement were sold in the offering, Charter remains obligated to issue, at CGML's request, up to an additional 122.8 million loaned shares in subsequent registered public offerings pursuant to the share lending agreement.

This offering of Charter's Class A common stock was conducted to facilitate transactions by which investors in Charter's 5.875% convertible senior notes due 2009, issued on November 22, 2004, hedged their investments in the convertible senior notes. Charter did not receive any of the proceeds from the sale of this Class A common stock. However, under the share lending agreement, Charter received a loan fee of $.001 for each share that it lends to CGML.

The issuance of up to a total of 150 million shares of common stock (of which 27.2 million were issued in July 2005) pursuant to a share lending agreement executed by Charter in connection with the issuance of the 5.875% convertible senior notes in November 2004 is essentially analogous to a sale of shares coupled with a forward contract for the reacquisition of the shares at a future date. An instrument that requires physical settlement by repurchase of a fixed number of shares in exchange for cash is considered a forward purchase instrument. While the share lending agreement does not require a cash payment upon return of the shares, physical settlement is required (i.e., the shares borrowed must be returned at the end of the arrangement.) The fair value of the 27.2 million shares lent in July 2005 is approximately $41 million as of September 30, 2005. However, the net effect on shareholders' deficit of the shares lent in July pursuant to the share lending agreement, which includes Charter's requirement to lend the shares and the counterparties' requirement to return the shares, is de minimis and represents the cash received upon lending of the shares and is equal to the par value of the common stock to be issued.

9. Comprehensive Income (Loss)

Certain marketable equity securities are classified as available-for-sale and reported at market value with unrealized gains and losses recorded as accumulated other comprehensive income (loss) on the accompanying condensed consolidated balance sheets. Additionally, the Company reports changes in the fair value of interest rate agreements designated as hedging the variability of cash flows associated with floating-rate debt obligations, that meet the effectiveness criteria of SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, in accumulated other comprehensive income (loss), after giving effect to the minority interest share of such gains and losses. Comprehensive income for the three months ended September 30, 2005 was $77 million and comprehensive loss for the three months ended September 30, 2004 was $3.3 billion and was $627 million and $4.0 billion for the nine months ended September 30, 2005 and 2004, respectively.

10. Accounting for Derivative Instruments and Hedging Activities

The Company uses interest rate risk management derivative instruments, such as interest rate swap agreements and interest rate collar agreements (collectively referred to herein as interest rate agreements) to manage its interest costs.

The Company's policy is to manage interest costs using a mix of fixed and variable rate debt. Using interest rate swap agreements, the Company has agreed to exchange, at specified intervals through 2007, the difference between fixed and variable interest amounts calculated by reference to an agreed-upon notional principal amount. Interest rate collar agreements are used to limit the Company's exposure to and benefits from interest rate fluctuations on variable rate debt to within a certain range of rates.

The Company does not hold or issue derivative instruments for trading purposes. The Company does, however, have certain interest rate derivative instruments that have been designated as cash flow hedging instruments. Such

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instruments effectively convert variable interest payments on certain debt instruments into fixed payments. For qualifying hedges, SFAS No. 133 allows derivative gains and losses to offset related results on hedged items in the consolidated statement of operations. The Company has formally documented, designated and assessed the effectiveness of transactions that receive hedge accounting. For the three months ended September 30, 2005 and 2004, net gain (loss) on derivative instruments and hedging activities includes gains of $1 million and $1 million, respectively, and for the nine months ended September 30, 2005 and 2004, net gain (loss) on derivative instruments and hedging activities includes gains of $2 million and $3 million, respectively, which represent cash flow hedge ineffectiveness on interest rate hedge agreements arising from differences between the critical terms of the agreements and the related hedged obligations. Changes in the fair value of interest rate agreements designated as hedging instruments of the variability of cash flows associated with floating-rate debt obligations that meet the effectiveness criteria of SFAS No. 133 are reported in accumulated other comprehensive loss. For the three months ended September 30, 2005 and 2004, a gain of $5 million and $2 million, respectively, and for the nine months ended September 30, 2005 and 2004, a gain of $14 million and $31 million, respectively, related to derivative instruments designated as cash flow hedges, was recorded in accumulated other comprehensive income (loss) and minority interest. The amounts are subsequently reclassified into interest expense as a yield adjustment in the same period in which the related interest on the floating-rate debt obligations affects earnings (losses).

Certain interest rate derivative instruments are not designated as hedges as they do not meet the effectiveness criteria specified by SFAS No. 133. However, management believes such instruments are closely correlated with the respective debt, thus managing associated risk. Interest rate derivative instruments not designated as hedges are marked to fair value, with the impact recorded as gain (loss) on derivative instruments and hedging activities in the Company's condensed consolidated statements of operations. For the three months ended September 30, 2005 and 2004, net gain (loss) on derivative instruments and hedging activities includes gains of $16 million and losses of $9 million, respectively, and for the nine months ended September 30, 2005 and 2004, net gain (loss) on derivative instruments and hedging activities includes gains of $41 million and $45 million, respectively, for interest rate derivative instruments not designated as hedges.

As of September 30, 2005 and December 31, 2004, the Company had outstanding $2.1 billion and $2.7 billion and $20 million and $20 million, respectively, in notional amounts of interest rate swaps and collars, respectively. The notional amounts of interest rate instruments do not represent amounts exchanged by the parties and, thus, are not a measure of exposure to credit loss. The amounts exchanged are determined by reference to the notional amount and the other terms of the contracts.

Certain provisions of the Company's 5.875% convertible senior notes issued in November 2004 were considered embedded derivatives for accounting purposes and were required to be accounted for separately from the convertible senior notes. In accordance with SFAS No. 133, these derivatives are marked to market with gains or losses recorded in interest expense on the Company's condensed consolidated statement of operations. For the three and nine months ended September 30, 2005, the Company recognized losses of $1 million and gains of $26 million, respectively. The loss resulted in an increase in interest expense whereas the gain resulted in a reduction in interest expense related to these derivatives. At September 30, 2005 and December 31, 2004, $2 million and $10 million, respectively, is recorded in accounts payable and accrued expenses relating to the short-term portion of these derivatives and $3 million and $21 million, respectively, is recorded in other long-term liabilities related to the long-term portion.

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11. Revenues

Revenues consist of the following for the three and nine months ended September 30, 2005 and 2004:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2005	2004	2005	2004
Video	$ 848	$ 839	$ 2,551	$ 2,534
High-speed Internet	230	189	671	538
Advertising sales	74	73	214	205
Commercial	71	61	205	175
Other	95	86	271	249
	$ 1,318	$ 1,248	$ 3,912	$ 3,701

12. Operating Expenses

Operating expenses consist of the following for the three and nine months ended September 30, 2005 and 2004:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2005	2004	2005	2004
Programming	$ 357	$ 328	$ 1,066	$ 991
Service	203	173	572	489
Advertising sales	26	24	76	72
	$ 586	$ 525	$ 1,714	$ 1,552

13. Selling, General and Administrative Expenses

Selling, general and administrative expenses consist of the following for the three and nine months ended September 30, 2005 and 2004:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2005	2004	2005	2004
General and administrative	$ 231	$ 220	$ 658	$ 636
Marketing	38	32	104	99
	$ 269	$ 252	$ 762	$ 735

Components of selling expense are included in general and administrative and marketing expense.

14. Hurricane Asset Retirement Loss

Certain of the Company's cable systems in Louisiana suffered significant plant damage as a result of hurricanes Katrina and Rita. Based on preliminary evaluations, the Company wrote off $19 million of its plants' net book value. Insignificant amounts of other expenses were recorded related to hurricanes Katrina and Rita.

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The Company has insurance coverage for both property and business interruption. The Company has not recorded any potential insurance recoveries as it is still assessing the damage of its plant and the extent of insurance coverage.

15. Special Charges

The Company has recorded special charges as a result of reducing its workforce, consolidating administrative offices and management realignment in 2004 and 2005. The activity associated with this initiative is summarized in the table below.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2005	2004	2005	2004
Beginning Balance	$ 4	$ 6	$ 6	$ 14
Special Charges	1	6	5	9
Payments	(1)	(3)	(7)	(14)
Balance at September 30,	$ 4	$ 9	$ 4	$ 9

For the three and nine months ended September 30, 2005, special charges also included $1 million related to legal settlements. For the nine months ended September 30, 2005, special charges were offset by approximately $2 million related to an agreed upon discount in respect of the portion of the settlement consideration payable under the Stipulations of Settlement of the consolidated Federal Class Action and the Federal Derivative Action allocable to plaintiff's attorney fees and Charter's insurance carrier as a result of the election to pay such fees in cash (see Note 17).

For the nine months ended September 30, 2004, special charges also includes approximately $85 million, as part of the terms set forth in memoranda of understanding regarding settlement of the consolidated Federal Class Action and Federal Derivative Action and approximately $9 million of litigation costs related to the tentative settlement of the South Carolina national class action suit, which were approved by the respective courts. For the three and nine months ended September 30, 2004, the severance costs were offset by $3 million received from a third party in settlement of a dispute.

16. Income Taxes

All operations are held through Charter Holdco and its direct and indirect subsidiaries. Charter Holdco and the majority of its subsidiaries are not subject to income tax. However, certain of these subsidiaries are corporations and are subject to income tax. All of the taxable income, gains, losses, deductions and credits of Charter Holdco are passed through to its members: Charter, Charter Investment, Inc. ("Charter Investment") and Vulcan Cable III Inc. ("Vulcan Cable"). Charter is responsible for its share of taxable income or loss of Charter Holdco allocated to Charter in accordance with the Charter Holdco limited liability company agreement (the "LLC Agreement") and partnership tax rules and regulations.

As of September 30, 2005 and December 31, 2004, the Company had net deferred income tax liabilities of approximately $287 million and $216 million, respectively. Approximately $214 million and $208 million of the

deferred tax liabilities recorded in the condensed consolidated financial statements at September 30, 2005 and December 31, 2004, respectively relate to certain indirect subsidiaries of Charter Holdco, which file separate income tax returns.

During the three and nine months ended September 30, 2005, the Company recorded $29 million and $75 million of income tax expense, respectively, and during the three and nine months ended September 30, 2004, the Company recorded $304 million and $207 million of income tax benefit, respectively. The Company recorded the portion of the income tax benefit associated with the adoption of Topic D-108 as a $91 million reduction of the cumulative effect of accounting change on the accompanying statement of operations for the three and nine months ended September 30,

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2004. The sale of systems to Atlantic Broadband, LLC in March and April 2004 resulted in income tax expense of $15 million for the nine months ended September 30, 2004.

Income tax expense is recognized through increases in the deferred tax liabilities related to Charter’s investment in Charter Holdco, as well as current federal and state income tax expense and increases to the deferred tax liabilities of certain of Charter’s indirect corporate subsidiaries. The Company recorded an additional deferred tax asset of approximately $222 million during the nine months ended September 30, 2005 relating to net operating loss carryforwards, but recorded a valuation allowance with respect to this amount because of the uncertainty of the ability to realize a benefit from the Company’s carryforwards in the future.

The Company has deferred tax assets of approximately $3.7 billion and $3.5 billion as of September 30, 2005 and December 31, 2004, respectively, which primarily relate to financial and tax losses allocated to Charter from Charter Holdco. The deferred tax assets include approximately $2.3 billion and $2.1 billion of tax net operating loss carryforwards as of September 30, 2005 and December 31, 2004, respectively (generally expiring in years 2005 through 2025), of Charter and its indirect corporate subsidiaries. Valuation allowances of $3.4 billion and $3.2 billion as of September 30, 2005 and December 31, 2004, respectively, exist with respect to these deferred tax assets.

Realization of any benefit from the Company’s tax net operating losses is dependent on: (1) Charter and its indirect corporate subsidiaries’ ability to generate future taxable income and (2) the absence of certain future "ownership changes" of Charter’s common stock. An "ownership change," as defined in the applicable federal income tax rules, would place significant limitations, on an annual basis, on the use of such net operating losses to offset any future taxable income the Company may generate. Such limitations, in conjunction with the net operating loss expiration provisions, could effectively eliminate the Company’s ability to use a substantial portion of its net operating losses to offset any future taxable income. Future transactions and the timing of such transactions could cause an ownership change. Such transactions include additional issuances of common stock by the Company (including but not limited to the issuance of up to a total of 150 million shares of common stock (of which 27.2 million were issued in July 2005) under the share lending agreement, the issuance of shares of common stock upon future conversion of Charter’s convertible senior notes and the issuance of common stock in the class action settlement discussed in Note 17, reacquisition of the borrowed shares by Charter, or acquisitions or sales of shares by certain holders of Charter’s shares, including persons who have held, currently hold, or accumulate in the future five percent or more of Charter’s outstanding stock (including upon an exchange by Mr. Allen or his affiliates, directly or indirectly, of membership units of Charter Holdco into CCI common stock)). Many of the foregoing transactions are beyond management’s control.

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will be realized. Because of the uncertainties in projecting future taxable income of Charter Holdco, valuation allowances have been established except for deferred benefits available to offset certain deferred tax liabilities.

Charter Holdco is currently under examination by the Internal Revenue Service for the tax years ending December 31, 2002 and 2003. The results of the Company (excluding Charter and the indirect corporate subsidiaries) for these years are subject to this examination. Management does not expect the results of this examination to have a material adverse effect on the Company’s financial condition or results of operations.

17. Contingencies

Securities Class Actions and Derivative Suits

Fourteen putative federal class action lawsuits (the "Federal Class Actions") were filed in 2002 against Charter and certain of its former and present officers and directors in various jurisdictions allegedly on behalf of all purchasers of Charter's securities during the period from either November 8 or November 9, 1999 through July 17 or July 18, 2002. Unspecified damages were sought by the plaintiffs. In general, the lawsuits alleged that Charter utilized misleading accounting practices and failed to disclose these accounting practices and/or issued false and misleading financial

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statements and press releases concerning Charter's operations and prospects. The Federal Class Actions were specifically and individually identified in public filings made by Charter prior to the date of this quarterly report. On March 12, 2003, the Panel transferred the six Federal Class Actions not filed in the Eastern District of Missouri to that district for coordinated or consolidated pretrial proceedings with the eight Federal Class Actions already pending there. The Court subsequently consolidated the Federal Class Actions into a single action (the "Consolidated Federal Class Action") for pretrial purposes. On August 5, 2004, the plaintiffs' representatives, Charter and the individual defendants who were the subject of the suit entered into a Memorandum of Understanding setting forth agreements in principle to settle the Consolidated Federal Class Action. These parties subsequently entered into Stipulations of Settlement dated as of January 24, 2005 (described more fully below) that incorporate the terms of the August 5, 2004 Memorandum of Understanding.

On September 12, 2002, a shareholders derivative suit (the "State Derivative Action") was filed in the Circuit Court of the City of St. Louis, State of Missouri (the "Missouri State Court"), against Charter and its then current directors, as well as its former auditors. The plaintiffs alleged that the individual defendants breached their fiduciary duties by failing to establish and maintain adequate internal controls and procedures. On March 12, 2004, an action substantively identical to the State Derivative Action was filed in Missouri State Court against Charter and certain of its current and former directors, as well as its former auditors. On July 14, 2004, the Court consolidated this case with the State Derivative Action.

Separately, on February 12, 2003, a shareholders derivative suit (the "Federal Derivative Action") was filed against Charter and its then current directors in the United States District Court for the Eastern District of Missouri. The plaintiff in that suit alleged that the individual defendants breached their fiduciary duties and grossly mismanaged Charter by failing to establish and maintain adequate internal controls and procedures.

As noted above, Charter and the individual defendants entered into a Memorandum of Understanding on August 5, 2004 setting forth agreements in principle regarding settlement of the Consolidated Federal Class Action, the State Derivative Action(s) and the Federal Derivative Action (the "Actions"). Charter and various other defendants in those actions subsequently entered into Stipulations of Settlement dated as of January 24, 2005, setting forth a settlement of the Actions in a manner consistent with the terms of the Memorandum of Understanding. The Stipulations of Settlement, along with various supporting documentation, were filed with the Court on February 2, 2005. On May 23, 2005 the United States District Court for the Eastern District of Missouri conducted the final fairness hearing for the Actions, and on June 30, 2005, the Court issued its final approval of the settlements. Members of the class had 30 days from the issuance of the June 30 order approving the settlement to file an appeal challenging the approval. Two notices of appeal were filed relating to the settlement. Those appeals were directed to the amount of fees that the attorneys for the class were to receive and to the fairness of the settlement. At the end of September 2005, Stipulations of Dismissal were filed with the Eighth Circuit Court of Appeals resulting in the dismissal of both appeals with prejudice. Procedurally therefore, the settlements are final.

As amended, the Stipulations of Settlement provide that, in exchange for a release of all claims by plaintiffs against Charter and its former and present officers and directors named in the Actions, Charter would pay to the plaintiffs a combination of cash and equity collectively valued at $144 million, which will include the fees and expenses of plaintiffs' counsel. Of this amount, $64 million would be paid in cash (by Charter's insurance carriers) and the $80 million balance was to be paid (subject to Charter's right to substitute cash therefor as described below) in shares of Charter Class A common stock having an aggregate value of $40 million and ten-year warrants to purchase shares of Charter Class A common stock having an aggregate warrant value of $40 million, with such values in each case

being determined pursuant to formulas set forth in the Stipulations of Settlement. However, Charter had the right, in its sole discretion, to substitute cash for some or all of the aforementioned securities on a dollar for dollar basis. Pursuant to that right, Charter elected to fund the $80 million obligation with 13.4 million shares of Charter Class A common stock (having an aggregate value of approximately $15 million pursuant to the formula set forth in the Stipulations of Settlement) with the remaining balance (less an agreed upon $2 million discount in respect of that portion allocable to plaintiffs' attorneys' fees) to be paid in cash. In addition, Charter had agreed to issue additional shares of its Class A common stock to its insurance carrier having an aggregate value of $5 million; however, by agreement with its carrier, Charter paid $4.5 million in cash in lieu of issuing such shares. Charter delivered the

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settlement consideration to the claims administrator on July 8, 2005, and it was held in escrow pending resolution of the appeals. Those appeals are now resolved. On July 14, 2005, the Circuit Court for the City of St. Louis dismissed with prejudice the State Derivative Actions. The claims administrator is responsible for disbursing the settlement consideration.

As part of the settlements, Charter committed to a variety of corporate governance changes, internal practices and public disclosures, all of which have already been undertaken and none of which are inconsistent with measures Charter is taking in connection with the recent conclusion of the SEC investigation.

Government Investigations

In August 2002, Charter became aware of a grand jury investigation being conducted by the U.S. Attorney's Office for the Eastern District of Missouri into certain of its accounting and reporting practices, focusing on how Charter reported customer numbers, and its reporting of amounts received from digital set-top terminal suppliers for advertising. The U.S. Attorney's Office publicly stated that Charter was not a target of the investigation. Charter was also advised by the U.S. Attorney's Office that no current officer or member of its board of directors was a target of the investigation. On July 24, 2003, a federal grand jury charged four former officers of Charter with conspiracy and mail and wire fraud, alleging improper accounting and reporting practices focusing on revenue from digital set-top terminal suppliers and inflated customer account numbers. Each of the indicted former officers pled guilty to single conspiracy counts related to the original mail and wire fraud charges and were sentenced April 22, 2005. Charter fully cooperated with the investigation, and following the sentencings, the U.S. Attorney's Office for the Eastern District of Missouri announced that its investigation was concluded and that no further indictments would issue.

Indemnification

Charter was generally required to indemnify, under certain conditions, each of the named individual defendants in connection with the matters described above pursuant to the terms of its bylaws and (where applicable) such individual defendants' employment agreements. In accordance with these documents, in connection with the grand jury investigation, a now-settled SEC investigation and the above-described lawsuits, some of Charter's current and former directors and current and former officers were advanced certain costs and expenses incurred in connection with their defense. On February 22, 2005, Charter filed suit against four of its former officers who were indicted in the course of the grand jury investigation. These suits seek to recover the legal fees and other related expenses advanced to these individuals. One of these former officers has counterclaimed against Charter alleging, among other things, that Charter owes him additional indemnification for legal fees that Charter did not pay, and another of these former officers has counterclaimed against Charter for accrued sick leave.

Other Litigation

Charter is also party to other lawsuits and claims that arose in the ordinary course of conducting its business. In the opinion of management, after taking into account recorded liabilities, the outcome of these other lawsuits and claims are not expected to have a material adverse effect on the Company's consolidated financial condition, results of operations or its liquidity.

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18. Earnings (Loss) Per Share

Basic earnings (loss) per share is based on the average number of shares of common stock outstanding during the period. Diluted earnings per share is based on the average number of shares used for the basic earnings per share calculation, adjusted for the dilutive effect of stock options, restricted stock, convertible debt, convertible redeemable preferred stock and exchangeable membership units. Basic loss per share equals diluted loss per share for the three months ended September 30, 2004 and the nine months ended September 30, 2004 and 2005.

	Three Months Ended September 30, 2005				
	Earnings		Shares	Earnings Per Share	
Basic earnings per share	$	75	316,214,740	$	0.24
Effect of restricted stock		--	840,112		--
Effect of Charter Investment Class B Common Stock		--	222,818,858		(0.10)
Effect of Vulcan Cable III Inc. Class B Common Stock		--	116,313,173		(0.02)
Effect of 5.875% convertible senior notes due 2009		13	356,404,959		(0.03)
Diluted earnings per share	$	88	1,012,591,842	$	0.09

The effect of restricted stock represents the shares resulting from the vesting of nonvested restricted stock, calculated using the treasury stock method. Charter Investment Class B common stock and Vulcan Cable III Inc. Class B common stock represent membership units in Charter Holdco, held by entities controlled by Mr. Allen, that are exchangeable at any time on a one-for-one basis for shares of Charter Class B common stock, which are in turn convertible on a one-for-one basis into shares of Charter Class A common stock. The 5.875% convertible senior notes due 2009 represent the shares resulting from the assumed conversion of the notes into shares of Charter's Class A common stock.

All options to purchase common stock, which were outstanding during the three months ended September 30, 2005, were not included in the computation of diluted earnings per share because the options' exercise price was greater than the average market price of the common shares or they were otherwise antidilutive. Charter's 4.75% convertible senior notes, Charter's series A convertible redeemable preferred stock and all of the outstanding exchangeable membership units in Charter's indirect subsidiary, CC VIII, LLC, also were not included in the computation of diluted earnings per share because the effect of the conversions would have been antidilutive.

The 27.2 million shares issued in July pursuant to the share lending agreement are required to be returned, in accordance with the contractual arrangement, and are treated in basic and diluted earnings per share as if they were already returned and retired. Consequently, there is no impact of the shares of common stock lent under the share lending agreement in the earnings per share calculation.

19. Stock Compensation Plans

Prior to January 1, 2003, the Company accounted for stock-based compensation in accordance with Accounting Principles Board ("APB") Opinion No. 25, *Accounting for Stock Issued to Employees*, and related interpretations, as permitted by SFAS No. 123, *Accounting for Stock-Based Compensation*. On January 1, 2003, the Company adopted the fair value measurement provisions of SFAS No. 123 using the prospective method, under which the Company recognizes compensation expense of a stock-based award to an employee over the vesting period based on the fair value of the award on the grant date consistent with the method described in Financial Accounting Standards Board Interpretation No. 28, *Accounting for Stock Appreciation Rights and Other Variable Stock Option or Award Plans*. Adoption of these provisions resulted in utilizing a preferable accounting method as the condensed consolidated financial statements will present the estimated fair value of stock-based compensation in expense consistently with other forms of compensation and other expense associated with goods and services received for equity instruments. In accordance with SFAS No. 148, *Accounting for Stock-Based Compensation - Transition and Disclosure,* the fair value

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method is being applied only to awards granted or modified after January 1, 2003, whereas awards granted prior to such date will continue to be accounted for under APB No. 25, unless they are modified or settled in cash. The ongoing effect on consolidated results of operations or financial condition will depend on future stock-based compensation awards granted by the Company.

SFAS No. 123 requires pro forma disclosure of the impact on earnings as if the compensation expense for these plans had been determined using the fair value method. The following table presents the Company's net income (loss) and income (loss) per share as reported and the pro forma amounts that would have been reported using the fair value method under SFAS No. 123 for the periods presented:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2005	2004	2005	2004
Net income (loss) applicable to common stock	$ 75	$ (3,295)	$ (634)	$ (4,005)
Add back stock-based compensation expense related to stock options included in reported net income (loss)	3	8	11	34
Less employee stock-based compensation expense determined under fair value based method for all employee stock option awards	(3)	(6)	(11)	(37)
Effects of unvested options in stock option exchange	--	--	--	48
Pro forma	$ 75	$ (3,293)	$ (634)	$ (3,960)
Basic income (loss) per common share	$ 0.24	$ (10.89)	$ (2.06)	$ (13.38)
Add back stock-based compensation expense related to stock options included in reported net income (loss)	0.01	0.03	0.04	0.11
Less employee stock-based compensation expense determined under fair value based method for all employee stock option awards	(0.01)	(0.02)	(0.04)	(0.12)
Effects of unvested options in stock option exchange	--	--	--	0.16
Pro forma	$ 0.24	$ (10.88)	$ (2.06)	$ (13.23)
Diluted income (loss) per common share	$ 0.09	$ (10.89)	$ (2.06)	$ (13.38)

Add back stock-based compensation expense related to stock options included in reported net income (loss)		--		0.03		0.04		0.11
Less employee stock-based compensation expense determined under fair value based method for all employee stock option awards		--		(0.02)		(0.04)		(0.12)
Effects of unvested options in stock option exchange		--		--		--		0.16
Pro forma	$	0.09	$	(10.88)	$	(2.06)	$	(13.23)

In January 2004, Charter began an option exchange program in which the Company offered its employees the right to exchange all stock options (vested and unvested) under the 1999 Charter Communications Option Plan and 2001 Stock Incentive Plan that had an exercise price over $10 per share for shares of restricted Charter Class A common stock or, in some instances, cash. Based on a sliding exchange ratio, which varied depending on the exercise price of an employee's outstanding options, if an employee would have received more than 400 shares of restricted stock in exchange for tendered options, Charter issued to that employee shares of restricted stock in the exchange. If, based on the exchange ratios, an employee would have received 400 or fewer shares of restricted stock in exchange for tendered options, Charter instead paid the employee cash in an amount equal to the number of shares the employee would have received multiplied by $5.00. The offer applied to options (vested and unvested) to purchase a total of 22,929,573 shares of Charter Class A common stock, or approximately 48% of the Company's 47,882,365 total options (vested and unvested) issued and outstanding as of December 31, 2003. Participation by employees was voluntary. Those members of Charter's board of directors who were not also employees of the Company were not eligible to participate in the exchange offer.

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In the closing of the exchange offer on February 20, 2004, the Company accepted for cancellation eligible options to purchase approximately 18,137,664 shares of Charter Class A common stock. In exchange, the Company granted 1,966,686 shares of restricted stock, including 460,777 performance shares to eligible employees of the rank of senior vice president and above, and paid a total cash amount of approximately $4 million (which amount includes applicable withholding taxes) to those employees who received cash rather than shares of restricted stock. The restricted stock was granted on February 25, 2004. Employees tendered approximately 79% of the options exchangeable under the program.

The cost to the Company of the stock option exchange program was approximately $10 million, with a 2004 cash compensation expense of approximately $4 million and a non-cash compensation expense of approximately $6 million to be expensed ratably over the three-year vesting period of the restricted stock issued in the exchange.

In January 2004, the Compensation Committee of the board of directors of Charter approved Charter's Long-Term Incentive Program ("LTIP"), which is a program administered under the 2001 Stock Incentive Plan. Under the LTIP, employees of Charter and its subsidiaries whose pay classifications exceed a certain level are eligible to receive stock options and more senior level employees are eligible to receive stock options and performance shares. The stock options vest 25% on each of the first four anniversaries of the date of grant. The performance units vest on the third anniversary of the grant date and shares of Charter Class A common stock are issued, conditional upon Charter's performance against financial performance targets established by Charter's management and approved by its board of directors. Charter granted 6.9 million performance shares in January 2004 under this program and recognized expense of $2 million and $8 million during the three and nine months ended September 30, 2004, respectively. However, in the fourth quarter of 2004, the Company reversed the $8 million of expense recorded in the first three quarters of 2004 based on the Company's assessment of the probability of achieving the financial performance measures established by Charter and required to be met for the performance shares to vest. In March and April 2005, Charter granted 2.8 million performance shares under the LTIP and recognized approximately $1 million during the three and nine months ended September 30, 2005.

20. Related Party Transactions

The following sets forth certain transactions in which the Company and the directors, executive officers and affiliates of the Company are involved. Unless otherwise disclosed, management believes that each of the transactions described below was on terms no less favorable to the Company than could have been obtained from independent third parties.

CC VIII

As part of the acquisition of the cable systems owned by Bresnan Communications Company Limited Partnership in February 2000, CC VIII, Charter's indirect limited liability company subsidiary, issued, after adjustments, 24,273,943 Class A preferred membership units (collectively the "CC VIII interest") with a value and an initial capital account of approximately $630 million to certain sellers affiliated with AT&T Broadband, subsequently owned by Comcast Corporation (the "Comcast sellers"). While held by the Comcast sellers, the CC VIII interest was entitled to a 2% priority return on its initial capital account and such priority return was entitled to preferential distributions from available cash and upon liquidation of CC VIII. While held by the Comcast sellers, the CC VIII interest generally did not share in the profits and losses of CC VIII. Mr. Allen granted the Comcast sellers the right to sell to him the CC VIII interest for approximately $630 million plus 4.5% interest annually from February 2000 (the "Comcast put

right"). In April 2002, the Comcast sellers exercised the Comcast put right in full, and this transaction was consummated on June 6, 2003. Accordingly, Mr. Allen, indirectly through a company controlled by him, Charter Investment, Inc. ("CII"), became the holder of the CC VIII interest. Consequently, subject to the matters referenced in the next paragraph, Mr. Allen generally thereafter has been allocated his pro rata share (based on number of membership interests outstanding) of profits or losses of CC VIII. In the event of a liquidation of CC VIII, Mr. Allen would be entitled to a priority distribution with respect to the 2% priority return (which will continue to accrete). Any remaining distributions in liquidation would be distributed to CC V Holdings, LLC, an indirect subsidiary of Charter ("CC V"), and Mr. Allen in proportion to CC V's capital account and Mr. Allen's capital account (which will equal the

initial capital account of the Comcast sellers of approximately $630 million, increased or decreased by Mr. Allen's pro rata share of CC VIII's profits or losses (as computed for capital account purposes) after June 6, 2003). The limited liability company agreement of CC VIII does not provide for a mandatory redemption of the CC VIII interest.

An issue arose as to whether the documentation for the Bresnan transaction was correct and complete with regard to the ultimate ownership of the CC VIII interest following consummation of the Comcast put right. Specifically, under the terms of the Bresnan transaction documents that were entered into in June 1999, the Comcast sellers originally would have received, after adjustments, 24,273,943 Charter Holdco membership units, but due to an FCC regulatory issue raised by the Comcast sellers shortly before closing, the Bresnan transaction was modified to provide that the Comcast sellers instead would receive the preferred equity interests in CC VIII represented by the CC VIII interest. As part of the last-minute changes to the Bresnan transaction documents, a draft amended version of the Charter Holdco limited liability company agreement was prepared, and contract provisions were drafted for that agreement that would have required an automatic exchange of the CC VIII interest for 24,273,943 Charter Holdco membership units if the Comcast sellers exercised the Comcast put right and sold the CC VIII interest to Mr. Allen or his affiliates. However, the provisions that would have required this automatic exchange did not appear in the final version of the Charter Holdco limited liability company agreement that was delivered and executed at the closing of the Bresnan transaction. The law firm that prepared the documents for the Bresnan transaction brought this matter to the attention of Charter and representatives of Mr. Allen in 2002.

Thereafter, the board of directors of Charter formed a Special Committee (currently comprised of Messrs. Merritt, Tory and Wangberg) to investigate the matter and take any other appropriate action on behalf of Charter with respect to this matter. After conducting an investigation of the relevant facts and circumstances, the Special Committee determined that a "scrivener's error" had occurred in February 2000 in connection with the preparation of the last-minute revisions to the Bresnan transaction documents and that, as a result, Charter should seek reformation of the Charter Holdco limited liability company agreement, or alternative relief, in order to restore and ensure the obligation that the CC VIII interest be automatically exchanged for Charter Holdco units. The Special Committee further determined that, as part of such contract reformation or alternative relief, Mr. Allen should be required to contribute the CC VIII interest to Charter Holdco in exchange for 24,273,943 Charter Holdco membership units. The Special Committee also recommended to the board of directors of Charter that, to the extent contract reformation were achieved, the board of directors should consider whether the CC VIII interest should ultimately be held by Charter Holdco or Charter Holdings or another entity owned directly or indirectly by them.

Mr. Allen disagreed with the Special Committee's determinations described above and so notified the Special Committee. Mr. Allen contended that the transaction was accurately reflected in the transaction documentation and contemporaneous and subsequent company public disclosures.

The parties engaged in a process of non-binding mediation to seek to resolve this matter, without success. The Special Committee evaluated what further actions or processes to undertake to resolve this dispute. To accommodate further deliberation, each party agreed to refrain from initiating legal proceedings over this matter until it had given at least ten days' prior notice to the other. In addition, the Special Committee and Mr. Allen determined to utilize the Delaware Court of Chancery's program for mediation of complex business disputes in an effort to resolve the CC VIII interest dispute.

As of October 31, 2005, Mr. Allen, the Special Committee, Charter, Charter Holdco and certain of their affiliates, having investigated the facts and circumstances relating to the dispute involving the CC VIII interest, after

consultation with counsel and other advisors, and as a result of the Delaware Chancery Court's non-binding mediation program, agreed to settle the dispute, and execute certain permanent and irrevocable releases pursuant to the Settlement Agreement and Mutual Release agreement dated October 31, 2005 (the "Settlement").

Pursuant to the Settlement, CII has retained 30% of its CC VIII interest (the "Remaining Interests"). The Remaining Interests are subject to certain drag along, tag along and transfer restrictions as detailed in the revised CC VIII Limited Liability Company Agreement. CII transferred the other 70% of the CC VIII interest directly and indirectly, through Charter Holdco, to a newly formed entity, CCHC, LLC (a direct subsidiary of Charter Holdco and the direct parent of

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Charter Holdings, "CCHC"). Of that other 70% of the CC VIII preferred interests, 7.4% has been transferred by CII for a subordinated exchangeable note of CCHC with an initial accreted value of $48.2 million, accreting at 14%, compounded quarterly, with a 15-year maturity (the "Note"). The remaining 62.6% has been transferred for no consideration.

As part of the Settlement, CC VIII issued approximately 49 million additional Class B units to CC V in consideration for prior capital contributions to CC VIII by CC V, with respect to transactions that were unrelated to the dispute in connection with CII's membership units in CC VIII. As a result, Mr. Allen's pro rata share of the profits and losses of CC VIII attributable to the Remaining Interests is approximately 5.6%.

The Note is exchangeable, at CII's option, at any time, for Charter Holdco Class A Common units at a rate equal to then accreted value, divided by $2.00 (the "Exchange Rate"). Customary anti-dilution protections have been provided that could cause future changes to the Exchange Rate. Additionally, the Charter Holdco Class A Common units received will be exchangeable by the holder into Charter common stock in accordance with existing agreements between CII, Charter and certain other parties signatory thereto. Beginning three years and four months after the closing of the Settlement, if the closing price of Charter common stock is at or above the Exchange Rate for a certain period of time as specified in the Exchange Agreement, Charter Holdco may require the exchange of the Note for Charter Holdco Class A Common units at the Exchange Rate.

CCHC has the right to redeem the Note under certain circumstances, for cash in an amount equal to the then accreted value. CCHC must redeem the Note at its maturity for cash in an amount equal to the initial stated value plus the accreted return through maturity.

The Board of Directors has determined that the transferred CC VIII interests remain at CCHC.

TechTV, Inc.

TechTV, Inc. ("TechTV") operated a cable television network that offered programming mostly related to technology. Pursuant to an affiliation agreement that originated in 1998 and that terminates in 2008, TechTV has provided the Company with programming for distribution via Charter's cable systems. The affiliation agreement provides, among other things, that TechTV must offer Charter certain terms and conditions that are no less favorable in the affiliation agreement than are given to any other distributor that serves the same number of or fewer TechTV viewing customers. Additionally, pursuant to the affiliation agreement, the Company was entitled to incentive payments for channel launches through December 31, 2003.

In March 2004, Charter Holdco entered into agreements with Vulcan Programming and TechTV, which provide for (i) Charter Holdco and TechTV to amend the affiliation agreement which, among other things, revises the description of the TechTV network content, provides for Charter Holdco to waive certain claims against TechTV relating to alleged breaches of the affiliation agreement and provides for TechTV to make payment of outstanding launch receivables due to Charter Holdco under the affiliation agreement, (ii) Vulcan Programming to pay approximately $10 million and purchase over a 24-month period at fair market rates, $2 million of advertising time across various cable networks on Charter cable systems in consideration of the agreements, obligations, releases and waivers under the agreements and in settlement of the aforementioned claims and (iii) TechTV to be a provider of content relating to technology and video gaming for Charter's interactive television platforms through December 31, 2006 (exclusive for the first year). For each of the three and nine months ended September 30, 2005 and 2004, the Company recognized approximately

$0.3 million and $1 million, respectively, of the Vulcan Programming payment as an offset to programming expense. For the three and nine months ended September 30, 2005, the Company paid approximately $1 million and $2 million, respectively, and for the three and nine months ended September 30, 2004, the Company paid approximately $0.5 million and $1 million, respectively, under the affiliation agreement.

The Company believes that Vulcan Programming, which is 100% owned by Mr. Allen, owned an approximate 98% equity interest in TechTV at the time Vulcan Programming sold TechTV to an unrelated third party in May 2004. Until September 2003, Mr. Savoy, a former Charter director, was the president and director of Vulcan Programming and was a director of TechTV. Mr. Wangberg, one of Charter's directors, was the chairman, chief executive officer

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and a director of TechTV. Mr. Wangberg resigned as the chief executive officer of TechTV in July 2002. He remained a director of TechTV along with Mr. Allen until Vulcan Programming sold TechTV.

Digeo, Inc.

In March 2001, a subsidiary of Charter, Charter Communications Ventures, LLC ("Charter Ventures"), and Vulcan Ventures Incorporated formed DBroadband Holdings, LLC for the sole purpose of purchasing equity interests in Digeo, Inc. ("Digeo"), an entity controlled by Mr. Allen. In connection with the execution of the broadband carriage agreement, DBroadband Holdings, LLC purchased an equity interest in Digeo funded by contributions from Vulcan Ventures Incorporated. The equity interest is subject to a priority return of capital to Vulcan Ventures up to the amount contributed by Vulcan Ventures on Charter Ventures' behalf. After Vulcan Ventures recovers its amount contributed and any cumulative loss allocations, Charter Ventures has a 100% profit interest in DBroadband Holdings, LLC. Charter Ventures is not required to make any capital contributions, including capital calls, to Digeo. DBroadband Holdings, LLC is therefore not included in the Company's consolidated financial statements. Pursuant to an amended version of this arrangement, in 2003 Vulcan Ventures contributed a total of $29 million to Digeo, $7 million of which was contributed on Charter Ventures' behalf, subject to Vulcan Ventures' aforementioned priority return. Since the formation of DBroadband Holdings, LLC, Vulcan Ventures has contributed approximately $56 million on Charter Ventures' behalf.

On March 2, 2001, Charter Ventures entered into a broadband carriage agreement with Digeo Interactive, LLC ("Digeo Interactive"), a wholly owned subsidiary of Digeo. The carriage agreement provided that Digeo Interactive would provide to Charter a "portal" product, which would function as the television-based Internet portal (the initial point of entry to the Internet) for Charter's customers who received Internet access from Charter. The agreement term was for 25 years and Charter agreed to use the Digeo portal exclusively for six years. Before the portal product was delivered to Charter, Digeo terminated development of the portal product.

On September 27, 2001, Charter and Digeo Interactive amended the broadband carriage agreement. According to the amendment, Digeo Interactive would provide to Charter the content for enhanced "Wink" interactive television services, known as Charter Interactive Channels ("i-channels"). In order to provide the i-channels, Digeo Interactive sublicensed certain Wink technologies to Charter. Charter is entitled to share in the revenues generated by the i-channels. Currently, the Company's digital video customers who receive i-channels receive the service at no additional charge.

On September 28, 2002, Charter entered into a second amendment to its broadband carriage agreement with Digeo Interactive. This amendment superseded the amendment of September 27, 2001. It provided for the development by Digeo Interactive of future features to be included in the Basic i-TV service to be provided by Digeo and for Digeo's development of an interactive "toolkit" to enable Charter to develop interactive local content. Furthermore, Charter could request that Digeo Interactive manage local content for a fee. The amendment provided for Charter to pay for development of the Basic i-TV service as well as license fees for customers who would receive the service, and for Charter and Digeo to split certain revenues earned from the service. The Company paid Digeo Interactive approximately $1 million and $2 million for the three and nine months ended September 30, 2005, respectively, and $1 million and $2 million for the three and nine months ended September 30, 2004, respectively, for customized development of the i-channels and the local content tool kit. This amendment expired pursuant to its terms on December 31, 2003. Digeo Interactive is continuing to provide the Basic i-TV service on a month-to-month basis.

On June 30, 2003, Charter Holdco entered into an agreement with Motorola, Inc. for the purchase of 100,000 digital video recorder ("DVR") units. The software for these DVR units is being supplied by Digeo Interactive, LLC under a license agreement entered into in April 2004. Under the license agreement Digeo Interactive granted to Charter Holdco the right to use Digeo's proprietary software for the number of DVR units that Charter deployed from a maximum of 10 headends through year-end 2004. This maximum number of headends was increased from 10 to 15 pursuant to a letter agreement executed on June 11, 2004 and the date for entering into license agreements for units deployed was extended to June 30, 2005. The number of headends was increased from 15 to 20 pursuant to a letter

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agreement dated August 4, 2004, from 20 to 30 pursuant to a letter agreement dated September 28, 2004 and from 30 to 50 headends by a letter agreement in February 2005. The license granted for each unit deployed under the agreement is valid for five years. In addition, Charter will pay certain other fees including a per-headend license fee and maintenance fees. Maximum license and maintenance fees during the term of the agreement are expected to be approximately $7 million. The agreement provides that Charter is entitled to receive contract terms, considered on the whole, and license fees, considered apart from other contract terms, no less favorable than those accorded to any other Digeo customer. Charter paid approximately $1 million in license and maintenance fees for each of the three and nine months ended September 30, 2005.

In April 2004, the Company launched DVR service using units containing the Digeo software in Charter's Rochester, Minnesota market using a broadband media center that is an integrated set-top terminal with a cable converter, DVR hard drive and connectivity to other consumer electronics devices (such as stereos, MP3 players, and digital cameras).

In May 2004, Charter Holdco entered into a binding term sheet with Digeo Interactive for the development, testing and purchase of 70,000 Digeo PowerKey DVR units. The term sheet provided that the parties would proceed in good faith to negotiate, prior to year-end 2004, definitive agreements for the development, testing and purchase of the DVR units and that the parties would enter into a license agreement for Digeo's proprietary software on terms substantially similar to the terms of the license agreement described above. In November 2004, Charter Holdco and Digeo Interactive executed the license agreement and in December 2004, the parties executed the purchase agreement, each on terms substantially similar to the binding term sheet. Product development and testing has been completed. Total purchase price and license and maintenance fees during the term of the definitive agreements are expected to be approximately $41 million. The definitive agreements are terminable at no penalty to Charter in certain circumstances. Charter paid approximately $7 million and $9 million for the three and nine months ended September 30, 2005, respectively, and $0.2 million for each of the three and nine months ended September 30, 2004 in capital purchases under this agreement.

In late 2003, Microsoft sued Digeo for $9 million in a breach of contract action, involving an agreement that Digeo and Microsoft had entered into in 2001. Digeo informed us that it believed it had an indemnification claim against us for half that amount. Digeo settled with Microsoft agreeing to make a cash payment and to purchase certain amounts of Microsoft software products and consulting services through 2008. In consideration of Digeo agreeing to release us from its potential claim against us, after consultation with outside counsel we agreed, in June 2005, to purchase a total of $2.3 million in Microsoft consulting services through 2008, a portion of which amounts Digeo has informed us will count against Digeo's purchase obligations with Microsoft.

In October 2005, Charter Holdco and Digeo Interactive entered into a binding Term Sheet for the test market deployment of the Moxi Entertainment Applications Pack ("MEAP"). The MEAP is an addition to the Moxi Client Software and will contain ten games (such as Video Poker and Blackjack), a photo application and jukebox application. The term sheet is limited to a test market application of approximately 14,000 subscribers and the aggregate value is not expected to exceed $0.1 million. In the event the test market proves successful, the companies will replace the Term Sheet with a long form agreement including a planned roll-out across additional markets. The Term Sheet expires on May 1, 2006.

The Company believes that Vulcan Ventures, an entity controlled by Mr. Allen, owns an approximate 60% equity interest in Digeo, Inc., on a fully-converted non-diluted basis. Mr. Allen, Lance Conn and Jo Allen Patton, directors of Charter, are directors of Digeo, and Mr. Vogel was a director of Digeo in 2004. During 2004 and 2005, Mr. Vogel

held options to purchase 10,000 shares of Digeo common stock.

Oxygen Media LLC

Oxygen Media LLC ("Oxygen") provides programming content aimed at the female audience for distribution over cable systems and satellite. On July 22, 2002, Charter Holdco entered into a carriage agreement with Oxygen whereby the Company agreed to carry programming content from Oxygen. Under the carriage agreement, the Company currently makes Oxygen programming available to approximately 5 million of its video customers. The term of the

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carriage agreement was retroactive to February 1, 2000, the date of launch of Oxygen programming by the Company, and runs for a period of five years from that date. For the three and nine months ended September 30, 2005, the Company paid Oxygen approximately $2 million and $7 million, respectively, and for the three and nine months ended September 30, 2004, the Company paid Oxygen approximately $3 million and $11 million, respectively, for programming content. In addition, Oxygen pays the Company marketing support fees for customers launched after the first year of the term of the carriage agreement up to a total of $4 million. The Company recorded approximately $0.1 million related to these launch incentives as a reduction of programming expense for the nine months ended September 30, 2005 and $0.4 million and $1 million for the three and nine months ended September 30, 2004, respectively.

Concurrently with the execution of the carriage agreement, Charter Holdco entered into an equity issuance agreement pursuant to which Oxygen’s parent company, Oxygen Media Corporation ("Oxygen Media"), granted a subsidiary of Charter Holdco a warrant to purchase 2.4 million shares of Oxygen Media common stock for an exercise price of $22.00 per share. In February 2005, this warrant expired unexercised. Charter Holdco was also to receive unregistered shares of Oxygen Media common stock with a guaranteed fair market value on the date of issuance of $34 million, on or prior to February 2, 2005, with the exact date to be determined by Oxygen Media, but this commitment was later revised as discussed below.

The Company recognized the guaranteed value of the investment over the life of the carriage agreement as a reduction of programming expense. For the nine months ended September 30, 2005, the Company recorded approximately $2 million as a reduction of programming expense and for the three and nine months ended September 30, 2004, the Company recorded approximately $3 million and $11 million as a reduction of programming expense, respectively. The carrying value of the Company’s investment in Oxygen was approximately $33 million and $32 million as of September 30, 2005 and December 31, 2004, respectively.

In August 2004, Charter Holdco and Oxygen entered into agreements that amended and renewed the carriage agreement. The amendment to the carriage agreement (a) revises the number of the Company’s customers to which Oxygen programming must be carried and for which the Company must pay, (b) releases Charter Holdco from any claims related to the failure to achieve distribution benchmarks under the carriage agreement, (c) requires Oxygen to make payment on outstanding receivables for marketing support fees due to the Company under the carriage agreement and (d) requires that Oxygen provide its programming content to the Company on economic terms no less favorable than Oxygen provides to any other cable or satellite operator having fewer subscribers than the Company. The renewal of the carriage agreement (a) extends the period that the Company will carry Oxygen programming to the Company’s customers through January 31, 2008 and (b) requires license fees to be paid based on customers receiving Oxygen programming, rather than for specific customer benchmarks.

In August 2004, Charter Holdco and Oxygen also amended the equity issuance agreement to provide for the issuance of 1 million shares of Oxygen Preferred Stock with a liquidation preference of $33.10 per share plus accrued dividends to Charter Holdco on February 1, 2005 in place of the $34 million of unregistered shares of Oxygen Media common stock. Oxygen Media delivered these shares in March 2005. The preferred stock is convertible into common stock after December 31, 2007 at a conversion ratio per share of preferred stock, the numerator of which is the liquidation preference and the denominator of which is the fair market value per share of Oxygen Media common stock on the conversion date.

As of September 30, 2005, through Vulcan Programming, Mr. Allen owned an approximate 31% interest in Oxygen assuming no exercises of outstanding warrants or conversion or exchange of convertible or exchangeable securities. Ms. Jo Allen Patton is a director and the President of Vulcan Programming. Mr. Lance Conn is a Vice President of Vulcan Programming. Mr. Nathanson has an indirect beneficial interest of less than 1% in Oxygen.

Helicon

In 1999, the Company purchased the Helicon cable systems. As part of that purchase, Mr. Allen entered into a put agreement with a certain seller of the Helicon cable systems that received a portion of the purchase price in the form of a preferred membership interest in Charter Helicon, LLC with a redemption price of $25 million plus accrued interest.

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Under the Helicon put agreement, such holder had the right to sell any or all of the interest to Mr. Allen prior to its mandatory redemption in cash on July 30, 2009. On August 31, 2005, 40% of the preferred membership interest was put to Mr. Allen. The remaining 60% of the preferred interest in Charter Helicon, LLC remained subject to the put to Mr. Allen. Such preferred interest was recorded in other long-term liabilities as of September 30, 2005 and December 31, 2004. On October 6, 2005, Charter Helicon, LLC redeemed all of the preferred membership interest for the redemption price of $25 million plus accrued interest.

21. Subsequent Events

In October 2005, Charter repurchased 484,908 shares of its Series A Convertible Redeemable Preferred Stock (the "Preferred Stock") for an aggregate purchase price of approximately $29 million (or $60 per share). The shares had liquidation preference of approximately $48 million and had accrued but unpaid dividends of approximately $3 million. Following the repurchase, 60,351 shares of Preferred Stock remained outstanding.

In connection with the repurchase, the holders of Preferred Stock consented to an amendment to the Certificate of Designation governing the Preferred Stock that will eliminate the quarterly dividends on all of the outstanding Preferred Stock and will provide that the liquidation preference for the remaining shares outstanding will be $105.4063 per share, which amount shall accrete from September 30, 2005 at an annual rate of 7.75%, compounded quarterly. Certain holders of Preferred Stock also released Charter from various threatened claims relating to their acquisition and ownership of the Preferred Stock, including threatened claims for breach of contract.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

General

Charter Communications, Inc. ("Charter") is a holding company whose principal assets as of September 30, 2005 are a 48% controlling common equity interest in Charter Communications Holding Company, LLC ("Charter Holdco") and "mirror" notes that are payable by Charter Holdco to Charter and have the same principal amount and terms as Charter's convertible senior notes. "We," "us" and "our" refer to Charter and its subsidiaries.

The chart below sets forth our organizational structure and that of our principal direct and indirect subsidiaries pro forma for the creation of CCHC, LLC and settlement of the CC VIII, LLC dispute. See Note 20 to the condensed consolidated financial statements. Equity ownership and voting percentages are actual percentages as of September 30, 2005 and do not give effect to any exercise, conversion or exchange of options, preferred stock, convertible notes or other convertible or exchangeable securities.

(1) Charter acts as the sole manager of Charter Holdco and its direct and indirect limited liability company subsidiaries. Charter's certificate of incorporation requires that its principal assets be securities of Charter Holdco, the terms of which mirror the terms of securities issued by Charter.

(2) These membership units are held by Charter Investment, Inc. and Vulcan Cable III Inc., each of which is 100% owned by Paul G. Allen, our chairman and controlling shareholder. They are exchangeable at any time on a one-for-one basis for shares of Charter Class A common stock.

(3) The percentages shown in this table reflect the issuance of the 27.2 million shares of Class A common stock issued on July 29, 2005 and the corresponding issuance of an equal number of mirror membership units by Charter Holdco to Charter. However, for accounting purposes, Charter's common equity interest in Charter Holdco is 48%, and Paul G. Allen's ownership of Charter Holdco is 52%. These percentages exclude the 27.2 million mirror membership units issued to Charter due to the required return of the issued mirror units upon return of the shares offered pursuant to the share lending agreement. See Note 8 to the condensed consolidated financial statements.

(4) Represents the impact of the settlement of the CC VIII, LLC dispute. See Note 20 to the condensed consolidated financial statements.

We are a broadband communications company operating in the United States. We offer our customers traditional cable video programming (analog and digital video) as well as high-speed Internet services and, in some areas, advanced broadband services such as high definition television, video on demand, telephone and interactive television. We sell our cable video programming, high-speed Internet and advanced broadband services on a subscription basis.

The following table summarizes our customer statistics for analog and digital video, residential high-speed Internet and residential telephone as of September 30, 2005 and 2004:

	Approximate as of	
	September 30, 2005 (a)	**September 30, 2004 (a)**
Cable Video Services:		
Analog Video:		
Residential (non-bulk) analog video customers (b)	5,636,100	5,825,000
Multi-dwelling (bulk) and commercial unit customers (c)	270,200	249,600
Total analog video customers (b)(c)	5,906,300	6,074,600
Digital Video:		
Digital video customers (d)	2,749,400	2,688,900
Non-Video Cable Services:		
Residential high-speed Internet customers (e)	2,120,000	1,819,900
Residential telephone customers (f)	89,900	40,200

The September 30, 2005 statistics presented above reflect the minimal loss of customers related to hurricanes Katrina and Rita. Based on preliminary estimates, customer losses related to hurricanes Katrina and Rita are expected to be approximately 10,000 to 15,000.

After giving effect to the sale of certain non-strategic cable systems in July 2005, September 30, 2004 analog video customers, digital video customers and high-speed Internet customers would have been 6,046,900, 2,677,600 and 1,819,300, respectively.

(a) "Customers" include all persons our corporate billing records show as receiving service (regardless of their payment status), except for complimentary accounts (such as our employees). At September 30, 2005 and 2004, "customers" include approximately 44,400 and 46,000 persons whose accounts were over 60 days past due in payment, approximately 9,800 and 5,500 persons whose accounts were over 90 days past due in

payment, and approximately 6,000 and 2,000 of which were over 120 days past due in payment, respectively.

(b) "Residential (non-bulk) analog video customers" include all customers who receive video services, except for complimentary accounts (such as our employees).

(c) Included within "video customers" are those in commercial and multi-dwelling structures, which are calculated on an equivalent bulk unit ("EBU") basis. EBU is calculated for a system by dividing the bulk price charged to accounts in an area by the most prevalent price charged to non-bulk residential customers in that market for the comparable tier of service. The EBU method of estimating analog video customers is consistent with the methodology used in determining costs paid to programmers and has been consistently applied year over year. As we increase our effective analog prices to residential customers without a corresponding increase in the prices charged to commercial service or multi-dwelling customers, our EBU count will decline even if there is no real loss in commercial service or multi-dwelling customers.

(d) "Digital video customers" include all households that have one or more digital set-top terminals. Included in "digital video customers" on September 30, 2005 and 2004 are approximately 8,900 and 10,700 customers, respectively, that receive digital video service directly through satellite transmission.

(e) "Residential high-speed Internet customers" represent those customers who subscribe to our high-speed Internet service. At September 30, 2005 and 2004, approximately 1,896,000 and 1,614,400 of these high-speed Internet customers, respectively, receive video services from us and are included within our video statistics above.

(f) "Residential telephone customers" include all households who subscribe to our telephone service.

Overview of Operations

We have a history of net losses. Despite having net earnings for the three months ended September 30, 2005, we expect to continue to report net losses for the foreseeable future. Our net losses are principally attributable to insufficient revenue to cover the combination of operating costs and interest costs we incur because of our high level of debt, depreciation expenses that we incur resulting from the capital investments we have made and continue to make in our business, and impairment of our franchise intangibles. We expect that these expenses (other than impairment of franchises) will remain significant, and we therefore expect to continue to report net losses for the foreseeable future. Additionally, reported losses allocated to minority interest on the statement of operations are limited to the extent of any remaining minority interest balance on the balance sheet related to Charter Holdco. Because minority interest in Charter Holdco has been eliminated, Charter absorbs all losses before income taxes that otherwise would be allocated to minority interest. Subject to any changes in Charter Holdco’s capital structure, future losses will continue to be absorbed by Charter. Effective January 1, 2005, we ceased recognizing minority interest in earnings or losses of CC VIII, LLC for financial reporting purposes until the resolution of the dispute between Charter and Paul G. Allen, Charter’s Chairman and controlling shareholder, regarding the preferred membership units in CC VIII, LLC was determinable or other events occurred. This dispute was settled October 31, 2005. We are currently determining the impact of the settlement. Subsequent to recording the impact of the settlement in the fourth quarter of 2005, approximately 6% of CC VIII’s income will be allocated to minority interest.

For the three and nine months ended September 30, 2005, our income from operations, which includes depreciation and amortization expense and asset impairment charges but excludes interest expense, was $63 million and $224 million, respectively. For the three and nine months ended September 30, 2004, our loss from operations was $2.3 billion and $2.2 billion, respectively. We had operating margins of 5% and 6% for the three and nine months ended September 30, 2005, respectively, and negative operating margins of 188% and 58% for the three and nine months ended September 30, 2004, respectively. The increase in income from operations and operating margins for the three and nine months ended September 30, 2005 compared to 2004 was principally due to impairment of franchises of $2.4

billion recorded in 2004 which did not recur in 2005.

Historically, our ability to fund operations and investing activities has depended on our continued access to credit under our credit facilities. We expect we will continue to borrow under our credit facilities from time to time to fund cash needs. The occurrence of an event of default under our credit facilities could result in borrowings from

these credit facilities being unavailable to us and could, in the event of a payment default or acceleration, also trigger events of default under the indentures governing our outstanding notes and would have a material adverse effect on us. Approximately $7 million of our debt matures during the remainder of 2005, which we expect to fund through borrowings under our revolving credit facility. See "— Liquidity and Capital Resources."

Critical Accounting Policies and Estimates

For a discussion of our critical accounting policies and the means by which we develop estimates therefore, see "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations" in our 2004 Annual Report on Form 10-K.

RESULTS OF OPERATIONS

Three Months Ended September 30, 2005 Compared to Three Months Ended September 30, 2004

The following table sets forth the percentages of revenues that items in the accompanying condensed consolidated statements of operations constituted for the periods presented (dollars in millions, except per share and share data):

	Three Months Ended September 30,			
	2005		2004	
Revenues	$ 1,318	100%	$ 1,248	100%
Costs and expenses:				
Operating (excluding depreciation and amortization)	586	45%	525	42%
Selling, general and administrative	269	20%	252	20%
Depreciation and amortization	375	29%	371	30%
Impairment of franchises	--	--	2,433	195%
Loss on sale of assets, net	1	--	--	--
Option compensation expense, net	3	--	8	1%
Hurricane asset retirement loss	19	1%	--	--
Special charges, net	2	--	3	--
	1,255	95%	3,592	288%
Income (loss) from operations	63	5%	(2,344)	(188)%
Interest expense, net	(462)		(424)	
Gain (loss) on derivative instruments and hedging activities, net	17		(8)	
Gain on extinguishment of debt	490		--	
	45		(432)	
Income (loss) before minority interest, income taxes and cumulative effect of accounting change	108		(2,776)	
Minority interest	(3)		34	
Income (loss) before income taxes and cumulative effect of accounting change	105		(2,742)	
Income tax benefit (expense)	(29)		213	
Income (loss) before cumulative effect of accounting change	76		(2,529)	

Cumulative effect of accounting change, net of tax		--		(765)
Net income (loss)		76		(3,294)
Dividends on preferred stock - redeemable		(1)		(1)
Net income (loss) applicable to common stock	$	75	$	(3,295)
Earnings (loss) per common share:				
Basic	$	0.24	$	(10.89)
Diluted	$	0.09	$	(10.89)
Weighted average common shares outstanding, basic		316,214,740		302,604,978
Weighted average common shares outstanding, diluted		1,012,591,842		302,604,978

Revenues. Revenues increased by $70 million, or 6%, from $1.2 billion for the three months ended September 30, 2004 to $1.3 billion for the three months ended September 30, 2005. This increase is principally the result of an increase of 300,100 high-speed Internet and 60,500 digital video customers, as well as price increases for video and high-speed Internet services, and is offset partially by a decrease of 168,300 analog video customers and $6 million of credits issued to hurricane Katrina impacted customers related to service outages. Through September and October, we have been restoring service to our impacted customers and, as of the date of this report, substantially all of our customers' service has been restored. Included in the reduction in analog video customers and reducing the increase in digital video and high-speed Internet customers are 26,800 analog video customers, 12,000 digital video customers and 600 high-speed Internet customers sold in the cable system sales in Texas and West Virginia, which closed in July 2005 (referred to in this section as the "System Sales"). The System Sales reduced the increase in revenues by approximately $4 million. Our goal is to increase revenues by improving customer service, which we believe will stabilize our analog video customer base, implementing price increases on certain services and packages and increasing the number of customers who purchase high-speed Internet services, digital video and advanced products and services such as telephone, video on demand ("VOD"), high definition television and digital video recorder service.

Average monthly revenue per analog video customer increased to $74.15 for the three months ended September 30, 2005 from $68.15 for the three months ended September 30, 2004 primarily as a result of incremental revenues from advanced services and price increases. Average monthly revenue per analog video customer represents total quarterly revenue, divided by three, divided by the average number of analog video customers during the respective period.

Revenues by service offering were as follows (dollars in millions):

	Three Months Ended September 30,					
	2005		2004		2005 over 2004	
	Revenues	% of Revenues	Revenues	% of Revenues	Change	% Change
Video	$ 848	64%	$ 839	67%	$ 9	1%
High-speed Internet	230	18%	189	15%	41	22%
Advertising sales	74	6%	73	6%	1	1%
Commercial	71	5%	61	5%	10	16%
Other	95	7%	86	7%	9	10%
	$ 1,318	100%	$ 1,248	100%	$ 70	6%

Video revenues consist primarily of revenues from analog and digital video services provided to our non-commercial customers. Video revenues increased by $9 million, or 1%, from $839 million for the three months ended September 30, 2004 to $848 million for the three months ended September 30, 2005. Approximately $34 million of the increase was the result of price increases and incremental video revenues from existing customers and approximately $3 million was the result of an increase in digital video customers. The increases were offset by decreases of approximately $20 million related to a decrease in analog video customers, approximately $3 million resulting from the System Sales and approximately $5 million of credits issued to hurricanes Katrina and Rita impacted customers related to service outages.

Revenues from high-speed Internet services provided to our non-commercial customers increased $41 million, or 22%, from $189 million for the three months ended September 30, 2004 to $230 million for the three months ended September 30, 2005. Approximately $34 million of the increase related to the increase in the average number of customers receiving high-speed Internet services, whereas approximately $8 million related to the increase in average price of the service. The increase was offset by approximately $1 million of credits issued to hurricanes Katrina and

Rita impacted customers related to service outages.

Advertising sales revenues consist primarily of revenues from commercial advertising customers, programmers and other vendors. Advertising sales increased $1 million, or 1%, from $73 million for the three months ended September 30, 2004 to $74 million for the three months ended September 30, 2005, primarily as a result of $2 million ad buys by programmers offset by a decline in national advertising sales. For each of the three months

ended September 30, 2005 and 2004, we received $5 million and $3 million, respectively, in advertising sales revenues from vendors.

Commercial revenues consist primarily of revenues from cable video and high-speed Internet services to our commercial customers. Commercial revenues increased $10 million, or 16%, from $61 million for the three months ended September 30, 2004 to $71 million for the three months ended September 30, 2005, primarily as a result of an increase in commercial high-speed Internet revenues.

Other revenues consist of revenues from franchise fees, telephone revenue, equipment rental, customer installations, home shopping, dial-up Internet service, late payment fees, wire maintenance fees and other miscellaneous revenues. Other revenues increased $9 million, or 10%, from $86 million for the three months ended September 30, 2004 to $95 million for the three months ended September 30, 2005. The increase was primarily the result of an increase in franchise fees of $6 million, telephone revenue of $5 million and installation revenue of $2 million.

Operating Expenses. Operating expenses increased $61 million, or 12%, from $525 million for the three months ended September 30, 2004 to $586 million for the three months ended September 30, 2005. The increase in operating expenses was reduced by $2 million as a result of the System Sales. Programming costs included in the accompanying condensed consolidated statements of operations were $357 million and $328 million, representing 28% and 9% of total costs and expenses for the three months ended September 30, 2005 and 2004, respectively. Key expense components as a percentage of revenues were as follows (dollars in millions):

	Three Months Ended September 30,					
	2005		2004		2005 over 2004	
	Expenses	% of Revenues	Expenses	% of Revenues	Change	% Change
Programming	$ 357	27%	$ 328	26%	$ 29	9%
Service	203	16%	173	14%	30	17%
Advertising sales	26	2%	24	2%	2	8%
	$ 586	45%	$ 525	42%	$ 61	12%

Programming costs consist primarily of costs paid to programmers for analog, premium, digital channels, VOD and pay-per-view programming. The increase in programming costs of $29 million, or 9%, for the three months ended September 30, 2005 over the three months ended September 30, 2004, was a result of price increases, particularly in sports programming, partially offset by a decrease in analog video customers. Additionally, the increase in programming costs was reduced by $1 million as a result of the System Sales. Programming costs were offset by the amortization of payments received from programmers in support of launches of new channels of $9 million and $15 million for the three months ended September 30, 2005 and 2004, respectively.

Our cable programming costs have increased in every year we have operated in excess of U.S. inflation and cost-of-living increases, and we expect them to continue to increase because of a variety of factors, including inflationary or negotiated annual increases, additional programming being provided to customers and increased costs to purchase or produce programming. In 2005, programming costs have increased and we expect will continue to increase at a higher rate than in 2004. These costs will be determined in part on the outcome of programming negotiations in 2005 and will likely be subject to offsetting events or otherwise affected by factors similar to the ones mentioned in the preceding paragraph. Our increasing programming costs will result in declining operating margins for our video services to the extent we are unable to pass on cost increases to our customers. We expect to partially offset any resulting margin compression from our traditional video services with revenue from advanced video services, increased high-speed Internet revenues, advertising revenues and commercial service revenues.

Service costs consist primarily of service personnel salaries and benefits, franchise fees, system utilities, costs of providing high-speed Internet service, maintenance and pole rent expense. The increase in service costs of $30 million, or 17%, resulted primarily from increased labor and maintenance costs to support improved service levels and our advanced products, higher fuel prices and pole rent expense. Advertising sales expenses consist of costs related to traditional advertising services provided to advertising customers, including salaries, benefits and commissions. Advertising sales expenses increased $2 million, or 8%, for the three months ended September 30,

2005 compared to the three months ended September 30, 2004 primarily as a result of increased salaries and benefits and an increase in marketing.

Selling, General and Administrative Expenses. Selling, general and administrative expenses increased by $17 million, or 7%, from $252 million for the three months ended September 30, 2004 to $269 million for the three months ended September 30, 2005. The increase in selling, general and administrative expenses was reduced by $1 million as a result of the System Sales. Key components of expense as a percentage of revenues were as follows (dollars in millions):

	Three Months Ended September 30,					
	2005		2004		2005 over 2004	
	Expenses	**% of Revenues**	**Expenses**	**% of Revenues**	**Change**	**% Change**
General and administrative	$ 231	17%	$ 220	18%	$ 11	5%
Marketing	38	3%	32	2%	6	19%
	$ 269	20%	$ 252	20%	$ 17	7%

General and administrative expenses consist primarily of salaries and benefits, rent expense, billing costs, call center costs, internal network costs, bad debt expense and property taxes. The increase in general and administrative expenses of $11 million, or 5%, resulted primarily from increases in professional fees associated with consulting services of $11 million and a rise in salaries and benefits of $10 million related to increased emphasis on improved service levels and operational efficiencies offset by decreases in property taxes of $4 million, property and casualty insurance of $4 million, bad debt expense of $3 million and the System Sales of $1 million.

Marketing expenses increased $6 million, or 19%, as a result of an increased investment in targeted marketing campaigns.

Depreciation and Amortization. Depreciation and amortization expense increased by $4 million, or 1%, from $371 million for the three months ended September 30, 2004 to $375 million for the three months ended September 30, 2005. The increase in depreciation was related to an increase in capital expenditures.

Impairment of Franchises. We performed an impairment assessment during the third quarter of 2004 using an independent third-party appraiser. The use of lower projected growth rates and the resulting revised estimates of future cash flows in our valuation, primarily as a result of increased competition, led to the recognition of a $2.4 billion impairment charge for the three months ended September 30, 2004.

Loss on Sale of Assets, Net. The loss on sale of assets of $1 million for the three months ended September 30, 2005 primarily represents the loss recognized on the disposition of plant and equipment.

Option Compensation Expense, Net. Option compensation expense for the three months ended September 30, 2005 and 2004 primarily represents options expensed in accordance with SFAS No. 123, *Accounting for Stock-Based Compensation.* The decrease of $5 million, or 63%, from $8 million for the three months ended September 30, 2004 to $3 million for the three months ended September 30, 2005 is primarily a result of a decrease in the fair value of such options related to a decrease in the price of our Class A common stock combined with a decrease in the number of options issued.

Hurricane Asset Retirement Loss. Hurricane asset retirement loss represents the loss associated with the write-off of the net book value of assets destroyed by hurricanes Katrina and Rita in the third quarter of 2005.

Special Charges, Net. Special charges of $2 million for the three months ended September 30, 2005 primarily represents $1 million of severance and related costs of our management realignment and $1 million related to legal settlements. Special charges of $3 million for the three months ended September 30, 2004 represents $6 million of severance and related costs of our workforce reduction offset by $3 million received from a third party in settlement of a dispute.

Interest Expense, Net. Net interest expense increased by $38 million, or 9%, from $424 million for the three months ended September 30, 2004 to $462 million for the three months ended September 30, 2005. The increase in net interest expense was a result of an increase in our average borrowing rate from 8.84% in the third quarter of 2004 to 9.07% in the third quarter of 2005 and an increase of $770 million in average debt outstanding from $18.4 billion for the third quarter of 2004 compared to $19.2 billion for the third quarter of 2005 and $1 million in losses related to embedded derivatives in Charter's 5.875% convertible senior notes issued in November 2004. See Note 10 to the condensed consolidated financial statements.

Gain (Loss) on Derivative Instruments and Hedging Activities, Net. Net gain on derivative instruments and hedging activities increased $25 million from a loss of $8 million for the three months ended September 30, 2004 to a gain of $17 million for the three months ended September 30, 2005. The increase is primarily the result of an increase in gains on interest rate agreements that do not qualify for hedge accounting under SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities,* which increased from a loss of $9 million for the three months ended September 30, 2004 to a gain of $16 million for the three months ended September 30, 2005.

Gain on Extinguishment of Debt. Gain on extinguishment of debt of $490 million for the three months ended September 30, 2005 represents the net gain realized on the exchange of approximately $6.8 billion total principal amount of outstanding debt securities of Charter Holdings for new CCH I, LLC ("CCH I") and CCH I Holdings, LLC ("CIH") debt securities. See Note 6 to the condensed consolidated financial statements.

Minority Interest. Minority interest represents the 2% accretion of the preferred membership interests in our indirect subsidiary, CC VIII, LLC, and in the second quarter of 2004, the pro rata share of the profits and losses of CC VIII, LLC. Effective January 1, 2005, we ceased recognizing minority interest in earnings or losses of CC VIII for financial reporting purposes until the dispute between Charter and Mr. Allen regarding the preferred membership interests in CC VIII was resolved. This dispute was settled October 31, 2005. See Note 7 to the condensed consolidated financial statements. Additionally, reported losses allocated to minority interest on the statement of operations are limited to the extent of any remaining minority interest on the balance sheet related to Charter Holdco. Because minority interest in Charter Holdco is eliminated, Charter absorbs all losses before income taxes that otherwise would be allocated to minority interest. Subject to any changes in Charter Holdco's capital structure, future losses will continue to be substantially absorbed by Charter.

Income Tax Benefit (Expense). Income tax expense of $29 million and income tax benefit of $213 million was recognized for the three months ended September 30, 2005 and 2004, respectively. The income tax expense is recognized through increases in deferred tax liabilities related to our investment in Charter Holdco, as well as through current federal and state income tax expense and increases in the deferred tax liabilities of certain of our indirect corporate subsidiaries. The income tax benefit was realized as a result of decreases in certain deferred tax liabilities related to our investment in Charter Holdco as well as decreases in the deferred tax liabilities of certain of our indirect corporate subsidiaries.

The income tax benefit recognized in the three months ended September 30, 2004 was directly related to the impairment of franchises as discussed above. We do not expect to recognize a similar benefit associated with the impairment of franchises in future periods. However, the actual tax provision calculations in future periods will be the result of current and future temporary differences, as well as future operating results.

Cumulative Effect of Accounting Change, Net of Tax. Cumulative effect of accounting change of $765 million (net of minority interest effects of $19 million and tax effects of $91 million) in 2004 represents the impairment charge recorded as a result of our adoption of EITF Topic D-108.

Net Income (Loss). Net loss decreased by $3.4 billion from net loss of $3.3 billion for the three months ended September 30, 2004 to net income of $76 million for the three months ended September 30, 2005 as a result of the

factors described above.

Preferred Stock Dividends. On August 31, 2001, Charter issued 505,664 shares (and on February 28, 2003 issued an additional 39,595 shares) of Series A Convertible Redeemable Preferred Stock in connection with the Cable USA acquisition, on which Charter pays or accrues a quarterly cumulative cash dividend at an annual rate of 5.75% if paid or 7.75% if accrued on a liquidation preference of $100 per share. Beginning January 1, 2005, Charter is accruing the dividend on its Series A Convertible Redeemable Preferred Stock.

Income (Loss) Per Common Share. Basic loss per common share decreased by $11.13 from a loss of $10.89 per common share for the three months ended September 30, 2004 to income of $0.24 per common share for the three months ended September 30, 2005 as a result of the factors described above.

Nine Months Ended September 30, 2005 Compared to Nine Months Ended September 30, 2004

The following table sets forth the percentages of revenues that items in the accompanying consolidated statements of operations constituted for the periods presented (dollars in millions, except per share and share data):

	Nine Months Ended September 30,					
	2005			2004		
Revenues	$	3,912	100%	$	3,701	100%
Costs and expenses:						
Operating (excluding depreciation and amortization)		1,714	44%		1,552	42%
Selling, general and administrative		762	19%		735	20%
Depreciation and amortization		1,134	29%		1,105	30%
Impairment of franchises		--	--		2,433	66%
Asset impairment charges		39	1%		--	--
(Gain) loss on sale of assets, net		5	--		(104)	(3)%
Option compensation expense, net		11	--		34	1%
Hurricane asset retirement loss		19	1%		--	--
Special charges, net		4	--		100	2%
		3,688	94%		5,855	158%
Income (loss) from operations		224	6%		(2,154)	(58)%
Interest expense, net		(1,333)			(1,227)	
Gain on derivative instruments and hedging activities, net		43			48	
Loss on debt to equity conversions		--			(23)	
Gain (loss) on extinguishment of debt		498			(21)	
Gain on investments		21			--	
		(771)			(1,223)	
Loss before minority interest, income taxes and cumulative effect of accounting change		(547)			(3,377)	
Minority interest		(9)			24	
Loss before income taxes and cumulative effect of accounting change		(556)			(3,353)	

Income tax benefit (expense)		(75)		116
Loss before cumulative effect of accounting change		(631)		(3,237)
Cumulative effect of accounting change, net of tax		--		(765)
Net loss		(631)		(4,002)
Dividends on preferred stock - redeemable		(3)		(3)
Net loss applicable to common stock	$	(634)	$	(4,005)
Loss per common share, basic and diluted	$	(2.06)	$	(13.38)
Weighted average common shares outstanding, basic and diluted		307,761,930		299,411,053

Revenues. Revenues increased by $211 million, or 6%, from $3.7 billion for the nine months ended September 30, 2004 to $3.9 billion for the nine months ended September 30, 2005. This increase is principally the result of an increase of 300,100 and 60,500 high-speed Internet and digital video customers, respectively, as well as price increases for video and high-speed Internet services, and is offset partially by a decrease of 168,300 analog video customers and $6 million of credits issued to hurricane Katrina impacted customers related to service outages. Through September and October, we have been restoring service to our impacted customers and, as of the date of this report, substantially all of our customers' service has been restored. Included in the reduction in analog video customers and reducing the increase in digital video and high-speed Internet customers are 26,800 analog video customers, 12,000 digital video customers and 600 high-speed Internet customers sold in the cable system sales in Texas and West Virginia, which closed in July 2005. The cable system sales to Atlantic Broadband Finance, LLC, which closed in March and April 2004 and the cable system sales in Texas and West Virginia, which closed in July 2005 (referred to in this section as the "System Sales") reduced the increase in revenues by approximately $33 million. Our goal is to increase revenues by improving customer service, which we believe will stabilize our analog video customer base, implementing price increases on certain services and packages and increasing the number of customers who purchase high-speed Internet services, digital video and advanced products and services such as telephone, VOD, high definition television and digital video recorder service.

Average monthly revenue per analog video customer increased to $72.97 for the nine months ended September 30, 2005 from $66.24 for the nine months ended September 30, 2004 primarily as a result of incremental revenues from advanced services and price increases. Average monthly revenue per analog video customer represents total revenue for the nine months ended during the respective period, divided by nine, divided by the average number of analog video customers during the respective period.

Revenues by service offering were as follows (dollars in millions):

	Nine Months Ended September 30,					
	2005		2004			2005 over 2004
	Revenues	% of Revenues	Revenues	% of Revenues	(58,602)	
Balance at December 31, 2011	$ (1,306)	$ 580	$ (132,695)		$ (21,054)	$ (154,475)

The activity in other comprehensive income (loss) and related income tax effects were as follows (in thousands):

	September 30,	September 30,	September 30,
		Year Ended December 31,	
	2011	2010	2009
Derivatives:			
Unrealized loss on foreign currency hedges, net of tax benefit of $3,549 and $6,368 in 2011 and 2010, respectively	$ (5,272)	$ (9,422)	$ (94)
Less: reclassification adjustment for loss (gain) included in net income, net of tax provision of $7,216 in 2011 and tax benefit of $2,441 in 2010	10,719	(3,613)	(11,806)
Unrealized gain (loss) on derivatives, net	5,447	(13,035)	(11,900)
Unrealized gain (loss) on investments:			
Unrealized gain (loss) on available-for-sale securities, net of tax benefit of $360 in 2011 and tax provision of $230 in 2010	(535)	340	658
Postretirement benefits:			
	(51,172)	(16,637)	(179)

Net actuarial losses and prior service credits, net of tax benefit of $34,424 and $11,254 in 2011 and 2010, respectively			
Amortization of actuarial gains and prior service credits, net of tax provision of $352 in 2011 and tax benefit of $415 in 2010	524	(614)	412
Postretirement benefits	(50,648)	(17,251)	233
Proportionate share of Telesat other comprehensive loss:			
Proportionate share of Telesat other comprehensive loss, net of tax benefit of $8,651 and $2,052 in 2011 and 2010, respectively	(12,866)	(3,049)	(5,139)
Other comprehensive loss	$ (58,602)	$ (32,995)	$ (16,148)

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LORAL SPACE & COMMUNICATIONS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

4. Contracts-in-Process and Long-Term Receivables

Contracts-in-Process

Contracts-in-Process consists of (in thousands):

	September 30, December 31, 2011	September 30, 2010
U.S. government contracts:		
Amounts billed	$ 34	$ 265
Unbilled receivables	1,311	1,634
	1,345	1,899
Commercial contracts:		
Amounts billed	107,886	125,328
Unbilled receivables	50,030	59,669
	157,916	184,997
	$ 159,261	$ 186,896

As of December 31, 2011 and 2010, billed receivables were reduced by an allowance for doubtful accounts of $0.2 million.

Unbilled amounts include recoverable costs and accrued profit on progress completed, which have not been billed. Such amounts are billed in accordance with the contract terms, typically upon shipment of the product, achievement of contractual milestones, or completion of the contract and, at such time, are reclassified to billed receivables. Fresh-start fair value adjustments relating to contracts-in-process are amortized on a percentage of completion basis as performance under the related contract is completed.

Long-Term Receivables

Billed receivables relating to long-term contracts are expected to be collected within one year. We classify deferred billings and the orbital receivable component of unbilled receivables expected to be collected beyond one year as long-term. Fresh-start fair value adjustments relating to long-term receivables are amortized using the effective interest method over the life of the related orbital stream.

Receivable balances related to satellite orbital incentive payments, deferred billings and the Telesat consulting services fee (see Note 17) as of December 31, 2011 are scheduled to be received as follows (in thousands):

	September 30, Long-Term Receivables
2012	$ 14,837

2013		16,145
2014		17,487
2015		19,046
2016		20,600
Thereafter		289,410
		377,525
Less, current portion included in contracts-in-process		(14,837)
Long-term receivables	$	362,688

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LORAL SPACE & COMMUNICATIONS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Financing Receivables

The following summarizes the age of financing receivables that have a contractual maturity of over one year as of December 31, 2011 (in thousands):

	September 30, Total	September 30, Unlaunched	September 30, Launched	September 30, Financing Receivables Subject To Aging	September 30, Current	September 30, 90 Days or Less	September 30, More Than 90 Days
Satellite Manufacturing:							
Orbital Receivables							
Long term orbitals	$ 340,015	$ 141,518	$ 198,497	$ 198,497	$ 198,497	$	$
Short term unbilled	11,370		11,370	11,370	11,370		
Short term billed	3,467		3,467	3,467	1,084		2,383
	354,852	141,518	213,334	213,334	210,951		2,383
Deferred Receivables	1,973			1,973	1,973		
Consulting Services:							
Telesat receivables	20,700			20,700	20,700		
	377,525	141,518	213,334	236,007	233,624		2,383
Contracts-in-Process:							
Unbilled receivables	39,971	39,971					
Total	$ 417,496	$ 181,489	$ 213,334	$ 236,007	$ 233,624	$	$ 2,383

The following summarizes the age of financing receivables that have a contractual maturity of over one year as of December 31, 2010 (in thousands):

	September 30, Total	September 30, Unlaunched	September 30, Launched	September 30, Financing Receivables Subject To Aging	September 30, Current	September 30, 90 Days or Less	September 30, More Than 90 Days
Satellite Manufacturing:							
Orbital Receivables							
Long term orbitals	$ 298,977	$ 133,688	$ 165,289	$ 165,289	$ 165,289	$	$
Short term unbilled	11,009		11,009	11,009	11,009		
Short term billed	2,426		2,426	2,426	659		1,767
	312,412	133,688	178,724	178,724	176,957		1,767

Deferred Receivables	2,893			2,893	2,893		
Consulting Services:							
Telesat receivables	17,556			17,556	17,556		
	332,861	133,688	178,724	199,173	197,406		1,767
Contracts-in-Process:							
Unbilled receivables	50,294	50,294					
Total	$ 383,155	$ 183,982	$ 178,724	$ 199,173	$ 197,406	$	$ 1,767

Billed receivables of $104.5 million and $123.2 million as of December 31, 2011 and 2010, respectively (not including billed orbital receivables of $3.5 million and $2.4 million as of December 31, 2011 and 2010, respectively), have been excluded from the table above as they have contractual maturities of less than one year.

Long term unbilled receivables include satellite orbital incentives related to satellites under construction of $141.5 million and $133.7 million as of December 31, 2011 and 2010, respectively. These receivables are not included in financing receivables subject to aging in the table above since the timing of their collection is not determinable until the applicable satellite is launched. Contracts-in-process include $40.0 million and $50.3 million as of December 31, 2011 and 2010, respectively, of unbilled receivables that represent accumulated incurred costs and earned profits net of losses on contracts in process that have been recorded as sales but have not yet been billed to customers. These receivables are not included in financing receivables subject to aging in the table above since the timing of their collection is not determinable until the contractual obligation to bill the customer is fulfilled.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

We assign internal credit ratings for all our customers with financing receivables. The credit worthiness of each customer is based upon public information and/or information obtained directly from our customers. We utilize credit ratings where available from the major credit rating agencies in our analysis. We have therefore assigned our rating categories to be comparable to those used by the major credit rating agencies. Credit risk profile by internally assigned ratings, consisted of the following:

Rating Categories	September 30, December 31, 2011	September 30, December 31, 2010
A/BBB	$ 41,607	$ 37,303
BB/B	246,373	225,533
B/CCC	94,156	80,222
Customers in bankruptcy	39,307	39,376
Other	(3,947)	721
Total financing receivables	$ 417,496	$ 383,155

5. Inventories

Inventories are comprised of the following (in thousands):

	September 30, December 31, 2011	September 30, December 31, 2010
Inventories-gross	$ 110,087	$ 104,029
Impaired inventory	(31,360)	(31,370)
	78,727	72,659
Inventories included in other assets	(1,426)	(1,426)
	$ 77,301	$ 71,233

The Company recorded inventory impairment charges of nil, $4.3 million and $1.0 million for the years ended December 31, 2011, 2010 and 2009, respectively. The charge recorded in 2010 related primarily to long-term inventories.

6. Property, Plant and Equipment

Property, plant and equipment consists of (in thousands):

	September 30, December 31, 2011	September 30, 2010
Land and land improvements	$ 27,036	$ 27,036

Buildings	69,182	68,899
Leasehold improvements	16,696	14,007
Equipment	182,987	159,432
Furniture and fixtures	31,412	26,368
Satellite capacity under construction (see Note 17)		40,495
Other construction in progress	25,828	20,187
	353,141	356,425
Accumulated depreciation and amortization	(149,419)	(120,520)
	$ 203,722	$ 235,905

Depreciation and amortization expense for property, plant and equipment was $29.5 million, $25.8 million and $25.2 million for the years ended December 31, 2011, 2010 and 2009, respectively.

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LORAL SPACE & COMMUNICATIONS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

7. Investments in Affiliates

Investments in affiliates consist of (in thousands):

	December 31,			
	September 30, 2011		September 30, 2010	
Telesat Holdings Inc.	$	377,244	$	295,797
XTAR, LLC		68,991		65,293
Other				1,466
	$	446,235	$	362,556

Equity in net income of affiliates consists of (in thousands):

	Year Ended December 31,					
	September 30, 2011		September 30, 2010		September 30, 2009	
Telesat Holdings Inc.	$	114,476	$	92,798	$	213,241
XTAR, LLC		(6,681)		(6,991)		(2,743)
Other		(1,466)		(182)		(200)
	$	106,329	$	85,625	$	210,298

Equity in net income of affiliates for the year ended December 31, 2011 includes a charge of $1.5 million to reduce the carrying value of our investment in an affiliate to zero based on our determination that the investment has been impaired and the impairment is other than temporary.

The consolidated statements of operations reflect the effects of the following amounts related to transactions with or investments in affiliates (in thousands):

	Year Ended December 31,					
	September 30, 2011		September 30, 2010		September 30, 2009	
Revenues	$	139,960	$	137,244	$	92,144
Elimination of Loral s proportionate share of profits relating to affiliate transactions		(18,498)		(14,734)		(10,071)
Profits relating to affiliate transactions not eliminated		10,411		8,294		5,671

The above amounts related to transactions with affiliates exclude the effect of Loral s sale to Telesat in April 2011 of its portion of the payload on the ViaSat-1 satellite and related net assets. As a result of this sale to Telesat, Loral received a $13 million sale premium and reversed $5 million of cumulative intercompany profit eliminations that were recorded when the satellite was being built for Loral. This combined benefit was reduced by the $11 million elimination of the portion of the benefit applicable to Loral s 64% interest in Telesat, which has been reflected as a reduction of our investment in Telesat, and the remaining $7 million has been reflected as a gain on our consolidated statement of operations for the year ended December 31, 2011.

We use the equity method of accounting for our majority economic interest in Telesat because we own 33 $^{1}/3$% of the voting stock and do not exercise control by other means to satisfy the U.S. GAAP requirement for treatment as a consolidated subsidiary. Loral s equity in net income or loss of Telesat is based on our proportionate share of Telesat s results in accordance with U.S. GAAP and in U.S. dollars. Our proportionate share of Telesat s net income or loss is based on our 64% economic interest as our holdings consist of common stock and non-voting participating preferred shares that have all the rights of common stock with respect to dividends, return of capital and surplus distributions, but have no voting rights. The ability of Telesat to pay dividends and consulting fees in cash to Loral is governed by applicable covenants relating to Telesat s debt and shareholder agreements. Telesat is permitted to pay cash dividends of $75 million plus 50% of cumulative consolidated net income to its shareholders and consulting fees to Loral only when Telesat s ratio of consolidated total debt to consolidated EBITDA is less than 5.0 to 1.0. For the year ended December 31, 2011, Loral has received cash payments from Telesat for consulting fees and interest thereon of $3.2 million. Loral did not receive any cash payments from Telesat for consulting fees and interest for the years ended December 31, 2010 and 2009. Through December 31, 2011, Loral has received no dividend payments from Telesat.

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LORAL SPACE & COMMUNICATIONS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The contribution of Loral Skynet, a wholly owned subsidiary of Loral prior to its contribution, to Telesat in 2007 was recorded by Loral at the historical book value of our retained interest combined with the gain recognized on the contribution. However, the contribution was recorded by Telesat at fair value. Accordingly, the amortization of Telesat fair value adjustments applicable to the Loral Skynet assets and liabilities is proportionately eliminated in determining our share of the income or losses of Telesat. Our equity in the net income of Telesat also reflects the elimination of our profit, to the extent of our economic interest, on satellites we are constructing for Telesat.

Telesat

We hold equity interests in Telesat Holdco representing 64% of the economic interests and $33\frac{1}{3}$% of the voting interests. Our Canadian partner, Public Sector Pension Investment Board (PSP), holds 36% of the economic interests and $66\frac{2}{3}$% of the voting interests in Telesat Holdco (except with respect to the election of directors as to which it holds a 30% voting interest).

The following table presents summary financial data for Telesat in accordance with U.S. GAAP, as of December 31, 2011 and 2010 and for the years ended December 31, 2011, 2010 and 2009 (in thousands):

	September 30,	September 30,	September 30,
		Year Ended December 31,	
	2011	2010	2009
Statement of Operations Data:			
Revenues	$ 817,269	$ 797,283	$ 691,566
Operating expenses	(188,119)	(190,632)	(203,417)
Depreciation, amortization and stock-based compensation	(248,012)	(249,318)	(230,176)
Gain on insurance proceeds	136,507		
Impairment of intangible assets	(1,112)		
(Loss) gain on disposition of long-lived assets	(1,499)	3,714	29,311
Operating income	515,034	361,047	287,284
Interest expense	(220,598)	(234,556)	(227,986)
Foreign exchange (losses) gains	(80,991)	159,191	439,160
Gains (losses) on financial instruments	50,731	(76,937)	(148,954)
Other income (expense)	1,964	619	(764)
Income tax expense	(65,271)	(41,177)	(2,185)
Net income	200,869	168,187	346,555

	September 30,	September 30,
	Year Ended December 31,	
	2011	2010
Balance Sheet Data:		
Current assets	$ 351,802	$ 291,367
Total assets	5,347,174	5,309,441
Current liabilities	289,351	294,485
Long-term debt, including current portion	2,817,857	2,928,916
Total liabilities	4,045,619	4,145,336
Redeemable preferred stock	138,485	141,718
Shareholders equity	1,163,070	1,022,387

Following the launch in May 2011 of Telstar 14R/Estrela do Sul 2, an SS/L-built satellite, the satellite s north solar array failed to fully deploy. The north solar array anomaly has diminished the amount of power available for the satellite s transponders and has reduced the life expectancy of the satellite. As a result, during the third quarter of 2011, Telesat carried out an impairment test for the satellite. Based on Telesat management s best estimates and assumptions, there was no impairment in Telstar 14R/Estrela do Sul 2 and as a result no adjustment to the

carrying value of the asset was required. In December 2011, Telesat received insurance proceeds of $132.7 million from its insurers with respect to the claim Telesat filed for the failed solar array deployment.

Gain on disposition of long-lived assets in 2009 results from the transfer of Telesat s leasehold interests in the Telstar 10 satellite and related contracts to APT Satellite for a total consideration of approximately $69 million.

LORAL SPACE & COMMUNICATIONS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

XTAR

We own 56% of XTAR, a joint venture between us and Hisdesat Servicios Estrategicos, S.A. (Hisdesat) of Spain. We account for our ownership interest in XTAR under the equity method of accounting because we do not control certain of its significant operating decisions.

XTAR owns and operates an X-band satellite, XTAR-EUR, located at 29° E.L., which is designed to provide X-band communications services exclusively to United States, Spanish and allied government users throughout the satellite s coverage area, including Europe, the Middle East and Asia. XTAR also leases 7.2 72MHz X-band transponders on the Spainsat satellite located 30° W.L., owned by Hisdesat. These transponders, designated as XTAR-LANT, provide capacity to XTAR for additional X-band services and greater coverage and flexibility.

We regularly evaluate our investment in XTAR to determine whether there has been a decline in fair value that is other than temporary. During November 2011 and January 2012, XTAR reduced its revenue forecast for 2012 and subsequent years. We have performed an impairment test for our investment in XTAR as of December 31, 2011, using the January 2012 forecast, and concluded that our investment in XTAR was not impaired. Any further declines in XTAR s projected revenues may result in a future impairment charge.

In January 2005, Hisdesat provided XTAR with a convertible loan in the principal amount of $10.8 million due February 2011, for which Hisdesat received enhanced governance rights in XTAR. The loan was subsequently extended to December 31, 2011. In November 2011, Loral and Hisdesat made capital contributions to XTAR in proportion to their respective ownership interests, and the proceeds were used to repay the loan balance of $18.5 million, which included the principal amount and accrued interest. Loral s capital contribution was $10.4 million.

XTAR s lease obligation to Hisdesat for the XTAR-LANT transponders was $24 million in 2011, with increases thereafter to a maximum of $28 million per year through the end of the useful life of the satellite which is estimated to be in 2022. Under this lease agreement, Hisdesat may also be entitled under certain circumstances to a share of the revenues generated on the XTAR-LANT transponders. Interest on XTAR s outstanding lease obligations to Hisdesat is paid through the issuance of a class of non-voting membership interests in XTAR, which enjoy priority rights with respect to dividends and distributions over the ordinary membership interests currently held by us and Hisdesat. In March 2009, XTAR entered into an agreement with Hisdesat pursuant to which the past due balance on XTAR-LANT transponders of $32.3 million as of December 31, 2008, together with a deferral of $6.7 million in payments due in 2009, will be payable to Hisdesat over 12 years through annual payments of $5 million (the Catch Up Payments). XTAR has a right to prepay, at any time, all unpaid Catch Up Payments discounted at 9%. Cumulative amounts paid to Hisdesat for Catch-Up Payments through December 31, 2011 were $14.2 million. XTAR has also agreed that XTAR s excess cash balance (as defined) will be applied towards making limited payments on future lease obligations, as well as payments of other amounts owed to Hisdesat, Telesat and Loral for services provided by them to XTAR (see Note 17). The ability of XTAR to pay dividends and management fees in cash to Loral is governed by XTAR s shareholder agreements.

XTAR-EUR was launched on Arianespace, S.A. s (Arianespace) Ariane ECA launch vehicle in 2005. The price for this launch had two components the first, consisting of a $15.8 million 10% interest paid-in-kind loan provided by Arianespace, was repaid in full by XTAR on July 6, 2007. The second component of the launch price consisted of a revenue-based fee to be paid to Arianespace over XTAR-EUR s 15 year in-orbit operations. This fee, also referred to as an incentive fee, equaled 3.5% of XTAR s annual operating revenues, subject to a maximum threshold. On February 29, 2008, XTAR paid Arianespace $1.5 million representing the incentive fee through December 31, 2007. On January 27, 2009, Arianespace agreed to eliminate the remaining incentive fee in exchange for $8.0 million payable in three installments. As of December 31, 2009, XTAR had paid all three installments and has no further obligations under the launch services agreement with Arianespace. As a result, XTAR s net loss for the year ended December 31, 2009 included a gain of $11.7 million related to the extinguishment of this liability.

To enable XTAR to make these settlement payments to Arianespace, XTAR issued a capital call to its LLC members. The capital call required Loral to increase its investment in XTAR by approximately $4.5 million in the first quarter of 2009, representing Loral s 56% share of the $8 million capital call.

LORAL SPACE & COMMUNICATIONS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following table presents summary financial data for XTAR as of December 31, 2011 and 2010 and for each of the three years in the period ended December 31, 2011 (in thousands):

Statement of Operations Data:

	September 30,	September 30,	September 30,
	Year Ended December 31,		
	2011	2010	2009
Revenues	$ 37,055	$ 37,907	$ 32,038
Operating expenses	(34,734)	(35,724)	(34,594)
Depreciation and amortization	(9,617)	(9,618)	(9,618)
Operating loss	(7,296)	(7,435)	(12,174)
Gain on settlement of Arianespace incentive cap			11,668
Net loss	(11,882)	(12,435)	(4,849)

	September 30,	September 30,
	December 31,	
	2011	2010
Balance Sheet Data:		
Current assets	$ 10,558	$ 9,290
Total assets	88,033	96,383
Current liabilities	45,704	61,839
Total liabilities	54,614	69,616
Members equity	33,419	26,767

Other

As of December 31, 2011 and 2010, the Company held various indirect ownership interests in two foreign companies that currently serve as exclusive service providers for Globalstar service in Mexico and Russia. The Company accounts for these ownership interests using the equity method of accounting. Loral has written-off its investments in these companies, and, because we have no future funding requirements relating to these investments, there is no requirement for us to provide for our allocated share of these companies net losses.

8. Intangible Assets

Intangible Assets were established in connection with our adoption of fresh-start accounting and consist of (in thousands):

	September 30, Weighted Average Remaining Amortization Period (Years)	September 30,	September 30,	September 30,	September 30,
		December 31, 2011		December 31, 2010	
		Gross Amount	Accumulated Amortization	Gross Amount	Accumulated Amortization
Internally developed software and technology	1	$ 59,027	$ (57,173)	$ 59,027	$ (54,702)

Trade names	14	9,200	(2,875)	9,200	(2,415)
Total		$ 68,227	$ (60,048)	$ 68,227	$ (57,117)

Total amortization expense for intangible assets was $2.9 million, $9.2 million and $11.3 million for the years ended December 31, 2011, 2010 and 2009, respectively. Annual amortization expense for intangible assets for the five years ended December 31, 2016 is estimated to be as follows (in thousands):

	September 30,
2012	$ 2,314
2013	460
2014	460
2015	460
2016	460

LORAL SPACE & COMMUNICATIONS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following summarizes fair value adjustments made in connection with our adoption of fresh start accounting related to contracts-in-process, long-term receivables, customer advances and billings in excess of costs and profits and long-term liabilities (in thousands):

	December 31, 2011	December 31, 2010
Gross fair value adjustments	$ (36,896)	$ (36,896)
Accumulated amortization	20,255	19,299
	$ (16,641)	$ (17,597)

Net amortization of these fair value adjustments was a credit to expense of $1.0 million in 2011, a credit to expense of $2.9 million in 2010 and a charge to expense of $2.6 million in 2009.

9. Debt Obligations

SS/L Credit Agreement

On December 20, 2010, SS/L entered into an amended and restated credit agreement (the Credit Agreement) with several banks and other financial institutions. The Credit Agreement provides for a $150 million senior secured revolving credit facility (the Revolving Facility). On December 8, 2011, the Credit Agreement was amended to increase the letter of credit sublimit from $50 million to $100 million. The Revolving Facility includes a $10 million swingline commitment. The Credit Agreement matures on January 24, 2014 (the Maturity Date). The prior $100 million credit agreement was entered into on October 16, 2008 and had a maturity date of October 16, 2011.

The following summarizes information related to the Credit Agreement and prior credit agreement (in thousands):

	December 31, 2011	December 31, 2010
Letters of credit outstanding	$ 4,785	$ 4,911
Borrowings		

	Year Ended December 31, 2011	2010	2009
Interest expense (including commitment and letter of credit fees)	$ 1,302	$ 818	$ 1,168
Amortization of issuance costs	725	1,570	878

The Credit Agreement contains customary conditions precedent to each borrowing, including absence of defaults and accuracy of representations and warranties. The Revolving Facility is available to finance the working capital needs and general corporate purposes of SS/L.

The obligations under the Credit Agreement are secured by (i) a first mortgage on substantially all real property owned by SS/L and (ii) a first priority security interest in substantially all tangible and intangible assets of SS/L and certain of its subsidiaries. There is no Loral guarantee of the facility.

SS/L may elect to borrow under the Revolving Facility on either a daily basis or for periods ending in one, two, three or six months. Daily borrowings bear interest at an annual rate equal to 2.75% plus the greater of (1) the Prime Rate then in effect, (2) the Federal Funds Rate then in effect plus 0.5% and (3) the one month Eurodollar Rate then in effect plus 1.0%. Borrowings for periods ending in one, two, three or six months will bear interest at an annual rate equal to 3.75% plus the appropriate Eurodollar Rate. Interest on a daily loan is paid quarterly, and interest on a Eurodollar loan is paid either on the last day of the interest period or quarterly, whichever is shorter. In addition, the Credit Agreement requires the Company to pay certain customary fees, costs and expenses of the lenders.

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LORAL SPACE & COMMUNICATIONS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The Credit Agreement contains certain covenants which, among other things, limit the incurrence of additional indebtedness, capital expenditures, investments, restricted payments including dividends, asset sales, mergers and consolidations, liens, changes to the line of business and other matters customarily restricted in such agreements. The material financial covenants, ratios or tests contained in the Credit Agreement are:

SS/L must not permit its consolidated leverage ratio as of (i) the last day of any period of four consecutive fiscal quarters or (ii) the date of incurrence of certain indebtedness to exceed 3.00 to 1.00.

SS/L must maintain a minimum consolidated interest coverage ratio of at least 3.50 to 1.00 (or 3.00 to 1.00 if SS/L elects to provide a dividend to its shareholders of preferred stock which entitles holders thereof to receive cash distributions based on orbital incentives received by SS/L) as of the last day of any fiscal quarter for the period of four consecutive fiscal quarters ending on such day.

The Credit Agreement restricts the payments SS/L may make to Loral. SS/L is permitted to make payments to Loral to fund tax liabilities and to make annual payments to Loral of up to $1.5 million as a management fee and up to $15 million for corporate overhead, subject to restrictions. Additionally, SS/L is permitted to make dividend payments related to its cumulative consolidated net income beginning October 1, 2010, subject to restrictions. Notwithstanding the dividend related to the cumulative consolidated net income amount, though offsetting the amount available for such dividends, SS/L is permitted to pay dividends of up to $20 million in the aggregate in any fiscal year and $60 million during the term of the Credit Agreement. The Credit Agreement also provides that SS/L may make a one-time payment to Loral on or before January 14, 2011 of up to $66 million. In January 2011, SS/L made a one-time dividend payment of $50 million to Loral.

SS/L may prepay outstanding principal in whole or in part, together with accrued interest, without premium or penalty. The Credit Agreement requires SS/L to prepay outstanding principal and accrued interest upon certain events, including certain asset sales. If an event of default shall occur and be continuing, the commitments of all lenders under the Credit Agreement may be terminated and the principal amount outstanding, together with all accrued and unpaid interest, may be declared immediately due and payable. Under the Credit Agreement, events of default include, among other things, non-payment of amounts due under the Credit Agreement, default in payment of certain other indebtedness, breach of certain covenants, bankruptcy, violations under ERISA, violations under certain United States export control laws and regulations, a change of control of SS/L and if certain liens on the collateral securing the obligations under the Credit Agreement fail to be perfected. All outstanding principal is payable in full upon the Maturity Date.

Debt issuance costs for the Credit Agreement of approximately $2.2 million are being amortized on a straight line basis over the life of the Revolving Facility.

10. Income Taxes

The (provision) benefit for income taxes on the income before income taxes and equity in net income of affiliates consists of the following (in thousands):

	September 30,	September 30,	September 30,
	Year Ended December 31,		
	2011	**2010**	**2009**
Current:			
U.S. Federal	$ (12,243)	$ (4,575)	$ (2,597)
State and local	(7,679)	(12,026)	(3,166)

Total current	(19,922)	(16,601)	(5,763)
Deferred:			
U.S. Federal	(61,248)	277,916	669
State and local	(7,975)	47,307	(477)
Total deferred	(69,223)	325,223	192
Total income tax (provision) benefit	$ (89,145)	$ 308,622	$ (5,571)

LORAL SPACE & COMMUNICATIONS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Our current tax (provision) benefit includes an increase to our liability for UTPs for (in thousands):

	September 30,	September 30,	September 30,
		Year Ended December 31,	
	2011	2010	2009
(Increase) decrease to unrecognized tax benefits	$ (10,593)	$ (5,517)	$ 2,817
Interest expense	(4,809)	(5,391)	(4,426)
Penalties	(1,659)	(633)	(701)
Total	$ (17,061)	$ (11,541)	$ (2,310)

For 2011, the deferred income tax provision of $69.2 million related primarily to our equity in net income of Telesat for the current year after having reversed our valuation allowance in the fourth quarter of 2010.

For 2010, the deferred income tax benefit of $325.2 million related primarily to (i) a benefit of $335.3 million from the reversal of a significant portion of our valuation allowance during the fourth quarter after having determined that based on all available evidence, it was more likely than not that we would realize the benefit from a significant portion of our deferred tax assets in the future offset by (ii) a provision of $10.1 million for the decrease to our deferred tax asset for federal AMT credits.

For 2009, the deferred income benefit of $0.2 million is detailed above.

In addition to the (provision) benefit for income taxes presented above, we recorded: (i) a deferred tax benefit of $39.4 million and $22.3 million for 2011 and 2010, respectively, related to tax adjustments in other comprehensive loss (see Note 3) and (ii) a current state tax benefit of $1.2 million and $0.4 million for 2011 and 2010, respectively, related to the excess tax benefits from stock option exercises recorded to paid-in-capital. The Company uses the with-and-without approach of determining when excess tax benefits from equity compensation have been realized. There were no additional items for 2009.

The (provision) benefit for income taxes differs from the amount computed by applying the statutory U.S. Federal income tax rate on income before income taxes and equity in net income of affiliates because of the effect of the following items (in thousands):

	September 30,	September 30,	September 30,
		Year Ended December 31,	
	2011	2010	2009
Tax provision at U.S. Statutory Rate of 35%	$ (38,497)	$ (32,583)	$ (9,441)
Permanent adjustments which change statutory amounts:			
State and local income taxes, net of federal income tax	(9,703)	(31,898)	(16,703)
Equity in net income of affiliates	(37,216)	(29,969)	(73,604)
Losses in litigation	1,542	(583)	(526)
Provision for unrecognized tax benefits	1,457	2,542	(1,356)
Nondeductible expenses	(2,500)	(987)	(2,076)
Change in valuation allowance	375	402,809	96,617
Other, net	(4,603)	(709)	1,518
Total income tax (provision) benefit	$ (89,145)	$ 308,622	$ (5,571)

The following table summarizes the activity related to our unrecognized tax benefits (in thousands):

	September 30,	September 30,	September 30,
		Year Ended December 31,	
	2011	2010	2009
Balance at January 1	$ 132,211	$ 120,124	$ 108,592
Increases related to prior year tax positions	1,220	339	8,855
Decreases related to prior year tax positions	(24,745)	(1,933)	(1,969)
Decrease as a result of statute expirations	(1,629)	(1,886)	(3,178)
Decrease as a result of tax settlements	(7,606)	(5,207)	(4,887)
Increases related to current year tax positions	15,842	20,774	12,711
Balance at December 31	$ 115,293	$ 132,211	$ 120,124

LORAL SPACE & COMMUNICATIONS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

With few exceptions, the Company is no longer subject to U.S. federal, state or local income tax examinations by tax authorities for years prior to 2007. Earlier years related to certain foreign jurisdictions remain subject to examination. Various state and foreign income tax returns are currently under examination. However, to the extent allowed by law, the tax authorities may have the right to examine prior periods where net operating losses were generated and carried forward, and make adjustments up to the amount of the net operating loss carryforward. While we intend to contest any future tax assessments for uncertain tax positions, no assurance can be provided that we would ultimately prevail. During the next twelve months, the statute of limitations for assessment of additional tax will expire with regard to UTPs related to Old Loral, as well as several of our federal and state income tax returns filed for 2007 and 2008, potentially resulting in a $61.0 million reduction to our unrecognized tax benefits.

Our liability for UTPs increased from $122.8 million at December 31, 2010 to $139.9 million at December 31, 2011 and is included in long-term liabilities in the consolidated balance sheets. At December 31, 2011, we have accrued $29.0 million and $24.5 million for the potential payment of tax-related interest and penalties, respectively. If our positions are sustained by the taxing authorities, approximately $108.1 million of the tax benefits will reduce the Company s income tax provision. Other than as described above, there were no significant changes to our unrecognized tax benefits during the twelve months ended December 31, 2011, and we do not anticipate any other significant increases or decreases to our unrecognized tax benefits during the next twelve months.

In connection with the Telesat transaction, Loral retained the benefit of tax recoveries related to the transferred assets and indemnified Telesat for Loral Skynet tax liabilities relating to periods preceding 2007. The unrecognized tax benefits related to the Loral Skynet subsidiaries were transferred to Telesat subject to the contractual tax indemnification provided by Loral. Loral s net receivable at December 31, 2011 for the probable outcome of these matters is not material. (see Note 17)

At December 31, 2011, we had federal NOL carryforwards of $380.4 million, state NOL carryforwards, primarily California, of $244.0 million, and federal research credits of $5.8 million which expire from 2012 to 2031, as well as federal and state AMT credit carryforwards of approximately $14.4 million that may be carried forward indefinitely.

The reorganization of the Company on the Effective Date constituted an ownership change under section 382 of the Internal Revenue Code. Accordingly, use of our tax attributes, such as NOLs and tax credits generated prior to the ownership change, are subject to an annual limitation of approximately $32.6 million, subject to increase or decrease based on certain factors. Our annual limitation was increased significantly each year through 2010, the last year allowed for the recognition of additional benefits from our net unrealized built-in gains (i.e., the excess of fair market value over tax basis for our assets) as of the Effective Date.

We assess the recoverability of our NOLs and other deferred tax assets and based upon this analysis, record a valuation allowance to the extent recoverability does not satisfy the more likely than not recognition criteria. We continue to maintain our valuation allowance until sufficient positive evidence exists to support full or partial reversal. As of December 31, 2011, we had a valuation allowance totaling $10.9 million against our deferred tax assets for certain tax credit and loss carryovers due to the limited carryforward periods and character of such attributes. During 2011, the valuation allowance decreased by $0.3 million, primarily recorded as a benefit in our statement of operations.

During the fourth quarter of 2010, we determined, based on all available evidence, that it was more likely than not that we would realize the benefit from a significant portion of the deferred tax assets in the future and no longer required a full valuation allowance. We based this conclusion on cumulative profits generated in recent periods, as well as our current expectation that future operations would generate sufficient taxable income to realize the tax benefit from certain deferred tax assets. Accordingly, during 2010, our valuation allowance decreased from $414.0 million to $11.2 million. Of the $402.8 million change, which was recorded as a benefit in our statement of operations, $335.5 million was reversed as a deferred income tax benefit during the fourth quarter of 2010.

During 2009, our valuation allowance decreased by $73.7 million. The net change consisted primarily of (i) a decrease of $96.6 million recorded as a benefit in our statement of operations, (ii) an increase of $7.0 million charged to accumulated other comprehensive loss and (iii) an increase of $15.9 million offset by a corresponding increase to the deferred tax asset.

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LORAL SPACE & COMMUNICATIONS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The significant components of the net deferred income tax assets are (in thousands):

	September 30, December 31, 2011	September 30, 2010
Deferred tax assets:		
Postretirement benefits other than pensions	$ 26,685	$ 25,504
Inventoried costs	20,165	24,666
Net operating loss and tax credit carryforwards	139,070	151,497
Compensation and benefits	24,984	26,996
Deferred research & development costs	3,269	6,575
Income recognition on long-term contracts	22,402	24,686
Investments in and advances to affiliates	6,175	34,227
Other, net	5,850	5,468
Federal benefit of uncertain tax positions	29,576	29,249
Pension costs	93,948	70,268
Total deferred tax assets before valuation allowance	372,124	399,136
Less valuation allowance	(10,887)	(11,228)
Net deferred tax assets	361,237	387,908
Deferred tax liabilities:		
Property, plant and equipment	(27,515)	(23,189)
Intangible assets	(3,289)	(4,480)
Total deferred tax liabilities	(30,804)	(27,669)
Net deferred tax assets	$ 330,433	$ 360,239
Classification on consolidated balance sheets:		
Current deferred tax assets	$ 67,070	$ 66,220
Long-term deferred tax assets	263,363	294,019
Total deferred tax assets	$ 330,433	$ 360,239

11. Stock-Based Compensation

Stock Plans

The Loral amended and restated 2005 stock incentive plan (the Stock Incentive Plan) allows for the grant of several forms of stock-based compensation awards including stock options, stock appreciation rights, restricted stock, restricted stock units, stock bonuses and other stock-based awards (collectively, the Awards). The total number of shares of voting common stock reserved and available for issuance under the Stock Incentive Plan is 1,742,879 shares of which 1,158,879 were available for future grant at December 31, 2011. This number of shares of voting common stock available for issuance would be reduced if restricted stock units or SS/L phantom stock appreciation rights are settled in voting common stock. In addition, shares of common stock that are issuable under awards that expire, are forfeited or canceled, or withheld in

payment of the exercise price or taxes relating to an Award, will again be available for Awards under the Stock Incentive Plan. Options issued under the Stock Incentive Plan generally have an exercise price equal to the fair market value of our stock, as defined, vest over a four year period and have a five to seven year life. The Awards provide for accelerated vesting if there is a change in control, as defined in the Stock Incentive Plan.

In June 2009, Michael B. Targoff, Chief Executive Officer of Loral, was awarded an option to purchase 125,000 shares of voting common stock with an exercise price of $35 per share (the June 2009 CEO Grant). The option was vested with respect to 25% of the underlying shares upon grant, with the remainder of the option subject to vesting as to 25% of the underlying shares on each of the first three anniversaries of the grant date. The option expires on June 30, 2014.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The fair value of the June 2009 CEO Grant was estimated using the Hull-White I barrier lattice model based on the assumptions below. There were no stock options granted in 2011 or 2010.

		September 30, Year Ended December 31, 2009
Risk free interest rate		2.72%
Expected life (years)		4.67
Estimated volatility		64.77%
Expected dividends		None
Weighted average grant date fair value	$	11.39

A summary of the Company s stock option activity for the year ended December 31, 2011 is presented below:

	September 30, Shares		September 30, Weighted Average Exercise Price	September 30, Weighted Average Remaining Contractual Term		September 30, Aggregate Intrinsic Value (In thousands)
Outstanding at January 1, 2011	1,134,915	$	28.46	1.3 years	$	54,524
Granted		$				
Exercised	(795,915)	$	27.43			
Forfeited		$				
Outstanding at December 31, 2011	339,000	$	30.86	1.5 years	$	11,533
Vested and expected to vest at December 31, 2011	339,000	$	30.86	1.5 years	$	11,533
Exercisable at December 31, 2011	307,750	$	30.44	1.4 years	$	10,599

A summary of the Company s non-vested restricted stock activity for the year ended December 31, 2011 is presented below:

	September 30, Shares		September 30, Weighted Average Grant- Date Fair Value
Non-vested restricted stock at January 1, 2011	6,000	$	33.58
Granted		$	
Vested	(2,000)	$	33.58

Forfeited		$	
Non-vested restricted stock at December 31, 2011	4,000	$	33.58

On March 5, 2009, the Compensation Committee approved awards of restricted stock units (the RSUs) for certain executives of the Company. Each RSU has a value equal to one share of voting common stock and generally provides the recipient with the right to receive one share of voting common stock or cash equal to the value of one share of voting common stock, at the option of the Company, on the settlement date.

Mr. Targoff was awarded 85,000 RSUs (the Initial Grant) on March 5, 2009 (the Grant Date). In addition, the Company agreed to issue Mr. Targoff 50,000 RSUs on the first anniversary of the Grant Date and 40,000 RSUs on the second anniversary of the Grant Date (the Subsequent Grants). Vesting of the Initial Grant requires the satisfaction of two conditions: a time-based vesting condition and a stock price vesting condition. Vesting of the Subsequent Grants is subject only to the stock-price vesting condition. The time-based vesting condition for the Initial Grant was satisfied upon Mr. Targoff s continued employment through March 5, 2010, the first anniversary of the Grant Date. The stock price vesting condition, which applies to both the Initial Grant and the Subsequent Grants, has been satisfied. Both the Initial Grant and the Subsequent Grants will be settled on March 31, 2013 or earlier under certain circumstances.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The fair value of the RSUs awarded in 2009 that vest upon achievement of a market condition and a time-based vesting condition was estimated using Monte Carlo simulation. Ex-dividend prices were simulated and those prices were used to determine when the price hurdle target will be achieved, if ever. The following assumptions were used to derive the fair value of such RSUs and the period over which the price hurdle target would be achieved:

	September 30, Year Ended December 31, 2009
Risk free interest rate	1.581%
Estimated volatility	59.83%
Expected dividends	None
Weighted average grant date fair value	$ 8.51

C. Patrick DeWitt, formerly Senior Vice President of Loral and Chief Executive Officer of SS/L and currently Chairman of the Board of SS/L, was awarded 25,000 RSUs on March 5, 2009, of which 66.67% vested on March 5, 2010, with the remainder vesting ratably on a quarterly basis over the subsequent two years. All of Mr. DeWitt s RSUs will be settled on March 12, 2012 or earlier under certain circumstances. The fair value of these RSUs is based upon the market price of Loral voting common stock as of the grant date. The weighted average grant date fair value of the award was $12.41.

A summary of the Company s non-vested RSU activity for the year ended December 31, 2011 is presented below:

	September 30, Shares	September 30, Weighted Average Grant- Date Fair Value
Non-vested RSUs at January 1, 2011	70,811	$ 18.25
Granted	15,000	$ 64.11
Vested	(61,211)	$ 15.88
Forfeited		$
Non-vested RSUs at December 31, 2011	24,600	$ 52.11

In April 2009, other SS/L employees were granted 66,259 shares of Loral voting common stock, which were fully vested as of the grant date. The grant date fair value of the award is based on Loral s average stock price of $24.01 at the date of grant.

In June 2009, the Company introduced a performance based long-term incentive compensation program consisting of SS/L phantom stock appreciation rights (SS/L Phantom SARs). Because SS/L common stock is not freely tradable on the open market and thus does not have a readily ascertainable market value, SS/L equity value under the program is derived from an Adjusted EBITDA-based formula. Each SS/L Phantom SAR provides the recipient with the right to receive an amount equal to the increase in SS/L s notional stock price over the base price multiplied by the number of SS/L Phantom SARs vested on the applicable vesting date, subject to adjustment. SS/L Phantom SARs are settled and the SAR value (if any) is paid out on each vesting date. SS/L Phantom SARs may be settled in Loral voting common stock (based on the fair value of Loral voting common stock on the date of settlement) or cash at the option of the Company. SS/L Phantom SARs expire on June 30, 2016.

LORAL SPACE & COMMUNICATIONS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

A summary of SS/L Phantom SARs granted along with their vesting schedule is presented below. The fair value of the SS/L Phantom SARs in included as a liability in our consolidated balance sheet.

	September 30,	September 30,	September 30,	September 30,	September 30,	September 30,
				Vesting Date March 18,		
Grant Date	**SARs granted**	**2010**	**2011**	**2012**	**2013**	**2014**
June-2009	225,000	50%	25%	25%		
Oct-2009	217,500	50%	25%	25%		
Oct-2009	65,000	25%	25%	25%	25%	
Dec-2009	32,500	50%	25%	25%		
May-2010	175,000		25%	25%	25%	25%

A summary of the Company s non-vested SS/L Phantom SAR activity for the year ended December 31, 2011 is presented below:

	September 30,	September 30,
	Shares	**Weighted Average Grant- Date Fair Value**
Non-vested SS/L Phantom SARs at January 1, 2011	461,250	$ 5.17
Granted		
Vested	(178,750)	5.60
Forfeited	(7,500)	9.08
Non-vested SS/L Phantom SARs at December 31, 2011	275,000	$ 4.78

During fiscal years 2011, 2010 and 2009, the following activity occurred under the Stock Incentive Plan (in thousands):

	September 30,	September 30,	September 30,
		Year Ended December 31,	
	2011	**2010**	**2009**
Total intrinsic value of options exercised	$ 39,018	$ 16,889	$ 1,578
Total fair value of restricted stock vested	$ 155	$ 1,493	$ 1,395
Total fair value of stock awards vested	$	$	$ 1,591
Total fair value of restricted stock units vested	$ 3,969	$ 12,687	$

We recorded total stock compensation expense of $4.0 million (of which $2.8 million was or is expected to be paid in cash), $10.0 million (of which $7.5 million was paid in cash) and $9.6 million (of which $2.1 million was paid in cash) for the years ended December 31, 2011, 2010 and 2009, respectively. As of December 31, 2011, total unrecognized compensation costs related to non-vested awards were $2.2 million and are expected to be recognized over a weighted average remaining period of 1.2 years.

12. Earnings Per Share

Telesat has awarded employee stock options, which, if exercised, would result in dilution of Loral s ownership interest in Telesat. The following table presents the dilutive impact of Telesat stock options on Loral s reported net income for the purpose of computing diluted earnings per share

(in thousands):

	September 30, Year Ended December 31, 2011	September 30, Year Ended December 31, 2010
Net income attributable to Loral common shareholders basic	$ 126,677	$ 486,846
Less: Adjustment for dilutive effect of Telesat stock options	(4,352)	(4,177)
Net income attributable to Loral common shareholders diluted	$ 122,325	$ 482,669

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Telesat stock options were excluded from the calculations of 2009 diluted earnings per share because they did not have a significant dilutive effect in 2009.

Basic earnings per share is computed based upon the weighted average number of shares of voting and non-voting common stock outstanding. The following is the computation of common shares outstanding for diluted earnings per share:

	September 30,	September 30, Year Ended December 31,	September 30,
	2011	2010 (In thousands)	2009
Common shares outstanding for diluted earnings per share:			
Weighted average common shares outstanding	30,680	30,085	29,761
Stock options	257	495	48
Unvested restricted stock units	226	206	115
Unvested restricted stock	3	8	4
Unvested SS/L Phantom SARS		93	53
Common shares outstanding for diluted earnings per share	31,166	30,887	29,981

For the year ended December 31, 2009, the effect of certain stock options outstanding, which would be calculated using the treasury stock method and certain non-vested restricted stock and non-vested RSUs were excluded from the calculation of diluted earnings per share, as the effect would have been antidilutive. The following summarizes stock options outstanding, non-vested restricted stock and non-vested restricted stock units excluded from the calculation of diluted earnings per share:

	September 30, Year Ended December 31, 2009 (In thousands)
Stock options outstanding	125
Unvested restricted stock units	8
Unvested restricted stock	30

13. Pensions and Other Employee Benefits

Pensions

We maintain qualified pension and supplemental retirement plans. These plans are defined benefit pension plans, and members may contribute to the pension plan in order to receive enhanced benefits. Employees hired after June 30, 2006 do not participate in the defined benefit pension plans, but participate in our defined contribution savings plan with an additional Company contribution. Benefits are based primarily on members compensation and/or years of service. Our funding policy is to fund the pension plan in accordance with the Internal Revenue Code and regulations thereon and to fund the supplemental retirement plans on a discretionary basis. Plan assets are generally invested in equity investments and fixed income investments. Pension plan assets are managed primarily by Russell Investment Corp. (Russell), which allocates

the assets into funds as we direct.

Other Benefits

In addition to providing pension benefits, we provide certain health care and life insurance benefits for retired employees and dependents. Participants are eligible for these benefits generally when they retire from active service and meet the eligibility requirements for our pension plans. These benefits are funded primarily on a pay-as-you-go basis, with the retiree generally paying a portion of the cost through contributions, deductibles and coinsurance provisions.

LORAL SPACE & COMMUNICATIONS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Funded Status

The following tables provide a reconciliation of the changes in the plans benefit obligations and fair value of assets for 2011 and 2010, and a statement of the funded status as of December 31, 2011 and 2010, respectively. We use a December 31 measurement date for the pension plans and other post retirement benefit plans.

	September 30,	September 30,	September 30,	September 30,
	Pension Benefits		Other Benefits	
	Year Ended December 31,		Year Ended December 31,	
	2011	2010	2011	2010
	(In thousands)		(In thousands)	
Reconciliation of benefit obligation				
Obligation at beginning of period	$ 476,031	$ 420,076	$ 62,840	$ 67,392
Service cost	12,265	10,677	522	672
Interest cost	25,504	24,673	3,198	3,411
Participant contributions	1,469	1,507	2,014	1,968
Plan amendment				(1,386)
Actuarial loss (gain)	57,824	41,826	1,755	(5,085)
Benefit payments	(24,080)	(22,728)	(4,280)	(4,132)
Obligation at December 31,	549,013	476,031	66,049	62,840
Reconciliation of fair value of plan assets				
Fair value of plan assets at beginning of period	289,036	256,166	269	507
Actual return on plan assets	(2,453)	28,133	(2)	2
Employer contributions	34,110	24,932	2,026	1,924
Participant contributions	1,469	1,507	2,014	1,968
Benefit payments	(22,870)	(21,702)	(4,280)	(4,132)
Fair value of plan assets at December 31,	299,292	289,036	27	269
Funded status at end of period	$ (249,721)	$ (186,995)	$ (66,022)	$ (62,571)

The benefit obligations for pensions and other employee benefits exceeded the fair value of plan assets by $315.7 million at December 31, 2011 (the unfunded benefit obligations). The unfunded benefit obligations were measured using a discount rate of 4.75% and 5.5% at December 31, 2011 and 2010, respectively. Lowering the discount rate by 0.5% would have increased the unfunded benefit obligations by approximately $36.5 million and $31.6 million as of December 31, 2011 and 2010, respectively. Market conditions and interest rates will significantly affect future assets and liabilities of Loral s pension and other employee benefits plans.

The pre-tax amounts recognized in accumulated other comprehensive loss as of December 31, 2011 and 2010 consist of (in thousands):

	September 30,	September 30,	September 30,	September 30,
	Pension Benefits		Other Benefits	
	December 31,		December 31,	

	2011	2010	2011	2010
Actuarial (loss) gain	$ (187,275)	$ (108,826)	$ 9,578	$ 12,402
Amendments-prior service credit	19,954	22,673	2,416	3,144
	$ (167,321)	$ (86,153)	$ 11,994	$ 15,546

The amounts recognized in other comprehensive loss during the year ended December 31, 2011 consist of (in thousands):

	September 30, Pension Benefits	September 30, Other Benefits
Actuarial loss during the period	$ (83,828)	$ (1,768)
Amortization of actuarial loss (gain)	5,379	(1,056)
Amortization of prior service credit	(2,719)	(728)
Total recognized in other comprehensive loss	$ (81,168)	$ (3,552)

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LORAL SPACE & COMMUNICATIONS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Amounts recognized in the balance sheet consist of (in thousands):

	Pension Benefits December 31, 2011	Pension Benefits December 31, 2010	Other Benefits December 31, 2011	Other Benefits December 31, 2010
Current Liabilities	$ 971	$ 1,223	$ 3,499	$ 3,526
Long-Term Liabilities	248,750	185,772	62,523	59,045
	$ 249,721	$ 186,995	$ 66,022	$ 62,571

The estimated actuarial loss and prior service credit for the pension benefits that will be amortized from accumulated other comprehensive income into net periodic cost over the next fiscal year is $11.9 million and $2.7 million, respectively. The estimated actuarial gain and prior service credit for other benefits that will be amortized from accumulated other comprehensive income into net periodic cost over the next fiscal year is $0.4 million and $0.7 million, respectively.

The accumulated pension benefit obligation was $530.0 million and $464.2 million at December 31, 2011 and 2010, respectively.

During 2011, we contributed $34.1 million to the qualified pension plan and $2.0 million for other employee post-retirement benefit plans. In addition, we made benefit payments relating to the supplemental retirement plan of $1.2 million. During 2012, based on current estimates, we expect to contribute approximately $41 million to the qualified pension plan and expect to fund approximately $3 million for other employee post-retirement benefit plans.

The following table provides the components of net periodic cost for the plans for the years ended December 31, 2011, 2010 and 2009 (in thousands):

	Pension Benefits For the Year Ended December 31, 2011	Pension Benefits 2010	Pension Benefits 2009	Other Benefits For the Year Ended December 31, 2011	Other Benefits 2010	Other Benefits 2009
Service cost	$ 12,265	$ 10,677	$ 9,436	$ 522	$ 672	$ 863
Interest cost	25,504	24,673	24,447	3,198	3,411	3,965
Expected return on plan assets	(23,552)	(20,641)	(17,176)	(12)	(31)	(50)
Amortization of prior service credit	(2,719)	(2,719)	(2,719)	(728)	(728)	(481)
Amortization of net actuarial loss (gain)	5,379	3,536	4,083	(1,056)	(1,118)	(471)
Net periodic cost	$ 16,877	$ 15,526	$ 18,071	$ 1,924	$ 2,206	$ 3,826

Assumptions

Assumptions used to determine net periodic cost:

	September 30,	September 30,	September 30,
	For the Year Ended December 31,		
	2011	2010	2009
Discount rate	5.50%	6.00%	6.50%
Expected return on plan assets	8.00%	8.00%	8.00%
Rate of compensation increase	4.25%	4.25%	4.25%

Assumptions used to determine the benefit obligation:

	September 30,	September 30,	September 30,
		December 31,	
	2011	2010	2009
Discount rate	4.75%	5.50%	6.00%
Rate of compensation increase	4.25%	4.25%	4.25%

The expected long-term rate of return on pension plan assets is selected by taking into account the expected duration of the projected benefit obligation for the plans, the asset mix of the plans and the fact that the plan assets are actively managed to mitigate risk. The expected long-term rate of return on plan assets determined on this basis was 8.0% for the years ended December 31, 2011, 2010 and 2009. Our expected long-term rate of return on plan assets for 2012 is 8.0%.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Actuarial assumptions to determine the benefit obligation for other benefits as of December 31, 2011 used a health care cost trend rate of 9.0% decreasing gradually to 5% by 2019. Actuarial assumptions to determine the benefit obligation for other benefits as of December 31, 2010, used a health care cost trend rate of 9.0% decreasing gradually to 5% by 2018. Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plans. A 1% change in assumed health care cost trend rates for 2011 would have the following effects (in thousands):

	September 30, 1% Increase	September 30, 1% Decrease
Effect on total of service and interest cost components of net periodic postretirement health care benefit cost	$ 276	$ (224)
Effect on the health care component of the accumulated postretirement benefit obligation	$ 5,310	$ (4,490)

Plan Assets

The Company has established the pension plan as a retirement vehicle for participants and as a funding vehicle to secure promised benefits. The investment goal is to provide a total return that over time will earn a rate of return to satisfy the benefit obligations given investment risk levels, contribution amounts and expenses. The pension plan invests in compliance with the Employee Retirement Income Security Act 1974, as amended (ERISA), and any subsequent applicable regulations and laws.

The Company has adopted an investment policy for the management and oversight of the pension plan. It sets forth the objectives for the pension plans, the strategies to achieve these objectives, procedures for monitoring and control and the delegation of responsibilities for the oversight and management of pension plan assets.

The Company s Board of Directors has delegated primary fiduciary responsibility for pension assets to an investment committee. In carrying out its responsibilities, the investment committee establishes investment policy, makes asset allocation decisions, determines asset class strategies and retains investment managers to implement asset allocation and asset class strategy decisions. It is responsible for the investment policy and may amend such policy from time to time.

Pension plan assets are invested in various asset classes in what we believe is a prudent manner for the exclusive purpose of providing benefits to participants. U.S. equities are held for their long-term expected return premium over fixed income investments and inflation. Non-U.S. equities are held for their expected return premium (along with U.S. equities), as well as diversification relative to U.S. equities and other asset classes. Fixed income investments are held for diversification relative to equities. Alternative investments are held for both diversification and higher returns than those typically available in traditional asset classes. Asset allocation policy is reviewed regularly.

Asset allocation policy is the principal method for achieving the pension plans investment objectives stated above. Asset allocation policy is reviewed regularly by the investment committee. The pension plans actual and targeted asset allocations are as follows:

	September 30,	September 30,	September 30,	September 30,
	December 31, Actual Allocation		Target Allocation	
	2011	2010	Target	Target Range
Equities	58%	61%	60%	50-65%
Fixed Income	42%	39%	40%	35-50%
	100%	100%	100%	100%

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The target and target range levels can be further defined as follows:

	September 30,	September 30,
	Target Allocation	
	Target	Target Range
U.S. Large Cap Equities	25%	15-40%
U.S. Small Cap Equities	5%	0-10%
Global Equities	10%	5-20%
Non-U.S. Equities	10%	5-20%
Alternative Equity Investments	10%	0-20%
Total Equities	60%	50-70%
Fixed Income	30%	20-40%
Alternative Fixed Income Investments	10%	0-20%
Total Fixed Income	40%	30-50%
Total Target Allocation	100%	100%

The pension plan s assets are actively managed using a multi-asset, multi-style, multi-manager investment approach. Portfolio risk is controlled through this diversification process and monitoring of money managers. Consideration of such factors as differing rates of return, volatility and correlation are utilized in the asset and manager selection process. Diversification reduces the impact of losses in single investments. Performance results and fund accounting are provided to the Company by Russell on a monthly basis. Periodic reviews of the portfolio are performed by the investment committee with Russell. These reviews typically consist of a market and economic review, a performance review, an allocation review and a strategy review. Performance is judged by investment type against market indexes. Allocation adjustments or fund changes may occur after these reviews. Performance is reported to the Company s Board of Directors at quarterly board meetings.

Fair Value Measurements

The values of the fund trusts are calculated using systems and procedures widely used across the investment industry. Generally, investments are valued based on information in financial publications of general circulation, statistical and valuation services, discounted cash flow methodology, records of security exchanges, appraisal by qualified persons, transactions and bona fide offers.

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LORAL SPACE & COMMUNICATIONS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The tables below provides the fair values of the Company s pension plan assets at December 31, 2011 and 2010, by asset category. The table also identifies the level of inputs used to determine the fair value of assets in each category. The Company s pension plan assets are mainly held in commingled employee benefit fund trusts.

	September 30,	September 30,	September 30, Fair Value Measurements	September 30,	September 30,
Asset Category	Total	Percentage	Quoted Prices In Active Markets For Identical Assets Level 1 (In thousands)	Significant Observable Inputs Level 2	Significant Unobservable Inputs Level 3
At December 31, 2011:					
Equity securities:					
U.S. large-cap[1]	$ 60,813	20%		$ 60,813	
U.S. small-cap[2]	18,010	6%	$ 3,901	14,109	
Global [3]	20,273	7%		20,273	
Non-U.S.[4]	33,781	11%	1,037	32,744	
Alternative investments:					
Equity long/short fund[5]	16,509	6%		5,952	$ 10,557
Real Estate Securities fund[6]	17,689	6%		5,854	11,835
Private equity fund[7]	6,870	2%			6,870
	173,945	58%	4,938	139,745	29,262
Fixed income securities:					
Commingled funds[8]	100,178	33%		100,178	
Alternative investments:					
Distressed opportunity limited partnership[9]	5,217	2%			5,217
Multi-strategy limited partnerships[10]	19,916	7%			19,916
Diversified alternatives fund[11]					
Other limited partnerships[12]	36				36
	125,347	42%		100,178	25,169
	$ 299,292	100%	$ 4,938	$ 239,923	$ 54,431
At December 31, 2010:					
Equity securities:					
U.S. large-cap[1]	$ 86,866	30%		$ 86,866	
U.S. small-cap[2]	16,002	6%	$ 3,783	12,219	
Non-U.S.[4]	53,101	18%	1,249	51,852	
Alternative investments:					

Equity long/short fund[5]	11,993	4%		6,111	$ 5,882
Private equity fund[7]	6,934	2%			6,934
	174,896	61%	5,032	157,048	12,816
Fixed income securities:					
Commingled funds[8]	110,152	38%		110,152	
Alternative investments:					
Distressed opportunity limited partnership[9]	3,598	1%			3,598
Diversified alternatives fund[11]	353	0%			353
Other limited partnerships[12]	37	0%			37
	114,140	39%		110,152	3,988
	$ 289,036	100%	$ 5,032	$ 267,200	$ 16,804

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(1) Investments in common stocks that rank among the largest 1,000 companies in the U.S. stock market.

(2) Investments in common stocks that rank among the small capitalization stocks in the U.S. stock market.

(3) Investments in common stocks across the world without being limited by national borders or to specific regions.

(4) Investments in common stocks of companies from developed and emerging countries outside the United States.

(5) Investments primarily in long and short positions in equity securities of U.S. and non-U.S. companies. We are invested in two funds; one fund has semi-annual tender offer redemption periods on June 30 and December 31 and is reported on a one month lag. The other fund has no limitations on redemptions and is reported on a current basis.

(6) Investments in real estate through both the private and public sector. The pension plan is invested in two funds of funds. One fund invests in global public real estate securities (REITs) while the second fund invests in private real estate investments. The private real estate fund is valued on a quarterly lag.

(7) Fund invests in portfolios of secondary interest in established venture capital, buyout, mezzanine and special situation funds on a global basis. The pension plan committed to invest up to $10 million in this fund. The remaining outstanding commitment at December 31, 2011 is $1.55 million. The amount invested in the fund, net of distributions, is $6.45 million and $7.30 million at December 31, 2011 and 2010, respectively. Fund is valued on a quarterly lag with adjustment for subsequent cash activity.

(8) Investments in bonds representing many sectors of the broad bond market with both short-term and intermediate-term maturities.

(9) Investments mainly in discounted debt securities, bank loans, trade claims and other debt and equity securities of financially troubled companies. This partnership has a one year lock-up period with semi-annual withdrawal rights on June 30 and December 31 thereafter. As of December 31, 2011, $2 million was subject to the lock-up period which will expire in June 2012. This fund is reported on a one month lag.

(10) Investments mainly in partnerships that have multi-strategy investment programs and do not rely on a single investment model. In 2011, the pension plan invested in two limited partnerships that have multi-strategy investment programs. One partnership has quarterly liquidation rights with notice of 65 days while the second partnership has monthly liquidation rights with notice of 33 days. Both funds are reported on a one month lag.

(11) Fund is a fund of hedge funds. Fund was closed and unwound its holdings. At December 31, 2010, the remaining assets were sold with the cash proceeds received in 2011.

(12) The pension plan invested in other partnerships that have reached their end of life and have closed and are unwinding their holdings. Mainly partnerships that provided mezzanine financing.

LORAL SPACE & COMMUNICATIONS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The significant amount of Level 2 investments in the table results from including in this category investments in commingled funds that contain investments with values based on quoted market prices, but for which the funds are not valued on a quoted market basis. These commingled funds are valued at their net asset values (NAVs) that are calculated by the investment manager or sponsor. Equity investments in both U.S and non-U.S. stocks as well as public real estate investment trusts are primarily valued using a market approach based on the quoted market prices of identical securities. Fixed income investments are primarily valued using a market approach with inputs that include broker quotes, benchmark yields, base spreads and reported trades.

Additional information pertaining to the changes in the fair value of the pension plan assets classified as Level 3 for the years ended December 31, 2011 and 2010 is presented below:

	Fair Value Measurements Using Significant Unobservable Inputs (Level 3)							
	Private Equity Fund	Equity Long/Short Fund	Distressed Opportunity Ltd. Partnership	Diversified Alternatives Fund	Other Limited Partnership	Multi Strategy Funds	Real Estate Fund	Total
	(In thousands)							
Balance at January 1, 2010	$ 6,245	$ 5,468	$ 3,204	$ 3,135	$ 218	$	$	$ 18,270
Unrealized gain/(loss)	339	414	394	(884)	(66)			197
Realized gain/(loss)				(697)	233			(464)
Purchases	1,300				35			1,335
Sales	(950)			(1,201)	(383)			(2,534)
Balance at December 31, 2010	$ 6,934	$ 5,882	$ 3,598	$ 353	$ 37	$	$	$ 16,804
Unrealized gain/(loss)	786	(325)	(381)	2,521	(1)	(84)	335	2,851
Realized gain/(loss)				(2,527)				(2,527)
Purchases	200	5,000	2,000			20,000	11,500	38,700
Sales	(1,050)			(347)				(1,397)
Balance at December 31, 2011	$ 6,870	$ 10,557	$ 5,217	$	$ 36	$ 19,916	$ 11,835	$ 54,431

Both the Equity Long/Short Fund and the Distressed Opportunity Limited Partnership are valued at each month-end based upon quoted market prices by the investment managers. They are included in Level 3 due to their restrictions on redemption to semi-annual periods on June 30 and December 31.

The Multi-Strategy Funds invest in various underlying securities. Each fund s net asset value is calculated by the fund manager and is not publicly available. The fund managers accumulate all the underlying security values and use them in determining the funds net asset values.

During 2011, the pension plan received the cash proceeds from its the investment balance in the Diversified Alternatives Fund that was closed and liquidating its remaining assets at December 31, 2010.

The private equity fund and limited partnership valuations are primarily based on cost/price of recent investments, earnings/performance multiples, net assets, discounted cash flows, comparable transactions and industry benchmarks.

The real estate fund is a fund of funds. The fund records its investments at acquisition cost and the value is adjusted quarterly to reflect the fund s share of income, appreciation or depreciation and additional contributions to or withdrawals from the underlying funds. The underlying funds real estate investments are independently appraised at least once per year and debt is marked to market on a quarterly basis.

The annual audited financial statements of all funds are reviewed by the Company.

Assets designated to fund the obligations of our supplemental retirement plan are held in a trust. Such assets amounting to $0.8 million and $2.1 million as of December 31, 2011 and 2010, respectively, are available to general creditors in the event of bankruptcy and, therefore, do not qualify as plan assets. Accordingly, other current assets included $0.8 million of these assets as of December 31, 2011 and 2010, respectively, and other assets included nil and $1.3 million of these assets as of December 31, 2011 and 2010, respectively.

Benefit Payments

The following benefit payments, which reflect future services, as appropriate, are expected to be paid (in thousands):

	September 30,	September 30,	September 30,
		Other Benefits	
	Pension Benefits	Gross Benefit Payments	Medicare Subsidy Receipts
2012	27,281	3,873	265
2013	27,952	4,131	278
2014	28,959	4,383	293
2015	29,671	4,551	310
2016	30,426	4,682	321
2017 to 2021	170,801	24,487	1,773

Employee Savings (401k) Plan

We have an employee savings (401k) plan, to which the Company provides contributions which match up to 6% of a participant s base salary at a rate of $66^{2}/_{3}$%, and retirement contributions. Retirement contributions represent contributions made by the Company to provide added retirement benefits to employees hired on or after July 1, 2006, as they are not eligible to participate in our defined benefit pension plan. Retirement contributions are provided regardless of an employee s contribution to the savings (401k) plan. Matching contributions and retirement contributions are collectively known as Company contributions. Company contributions are made in cash and placed in each participant s age appropriate life cycle fund. For the years ended December 2011, 2010 and 2009, Company contributions were $11.5 million, $10.0 million and $8.7 million, respectively. Participants of the savings (401k) plan are able to redirect Company contributions to any available fund within the plan. Participants are also able to direct their contributions to any available fund.

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14. Financial Instruments, Derivative Instruments and Hedging

Financial Instruments

The carrying amount of cash equivalents and restricted cash approximates fair value because of the short maturity of those instruments. The fair value of short-term investments, investments in available-for-sale securities and supplemental retirement plan assets is based on market quotations. The fair value of derivatives is based on the income approach, using observable Level II market expectations at the measurement date and standard valuation techniques to discount future amounts to a single present value.

Foreign Currency

In the normal course of business, we are subject to the risks associated with fluctuations in foreign currency exchange rates. To limit this foreign exchange rate exposure, the Company seeks to denominate its contracts in U.S. dollars. If we are unable to enter into a contract in U.S. dollars, we review our foreign exchange exposure and, where appropriate, derivatives are used to minimize the risk of foreign exchange rate fluctuations to operating results and cash flows. We do not use derivative instruments for trading or speculative purposes.

As of December 31, 2011, SS/L had the following amounts denominated in Japanese yen and euros (which have been translated into U.S. dollars based on the December 31, 2011 exchange rates) that were unhedged:

	September 30, Foreign Currency		September 30, U.S.$	
	(In thousands)			
Future revenues Japanese yen	¥	50,062	$	650
Future expenditures Japanese yen	¥	2,275,318	$	29,567
Future revenues euros		17,635	$	22,867
Future expenditures euros		5,317	$	6,894

Derivatives and Hedging Transactions

All derivative instruments are recorded at fair value as either assets or liabilities in our consolidated balance sheets. Each derivative instrument is generally designated and accounted for as either a hedge of a recognized asset or a liability (fair value hedge) or a hedge of a forecasted transaction (cash flow hedge). Certain of these derivatives are not designated as hedging instruments and are used as economic hedges to manage certain risks in our business.

As a result of the use of derivative instruments, the Company is exposed to the risk that counterparties to derivative contracts will fail to meet their contractual obligations. The Company does not hold collateral or other security from its counterparties supporting its derivative instruments. In addition, there are no netting arrangements in place with the counterparties. To mitigate the counterparty credit risk, the Company has a policy of entering into contracts only with carefully selected major financial institutions based upon their credit ratings and other factors.

There were no derivative instruments in an asset position as of December 31, 2011. Therefore, there was no exposure to loss at such date as a result of the potential failure of the counterparties to perform as contracted.

Cash Flow Hedges

The Company enters into long-term construction contracts with customers and vendors, some of which are denominated in foreign currencies. Hedges of expected foreign currency denominated contract revenues and related purchases are designated as cash flow hedges and evaluated for effectiveness at least quarterly. Effectiveness is tested using regression analysis. The effective portion of the gain or loss on a cash flow hedge is

recorded as a component of other comprehensive income (OCI) and reclassified to income in the same period or periods in which the hedged transaction affects income. The ineffective portion of a cash flow hedge gain or loss is included in income.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

In June 2010 and July 2008, SS/L was awarded satellite contracts denominated in euros and entered into a series of foreign exchange forward contracts with maturities through 2013 and 2011, respectively, to hedge associated foreign currency exchange risk because our costs are denominated principally in U.S. dollars. These foreign exchange forward contracts have been designated as cash flow hedges of future euro denominated receivables.

The maturity of foreign currency exchange contracts held as of December 31, 2011 is consistent with the contractual or expected timing of the transactions being hedged, principally receipt of customer payments under long-term contracts. These foreign exchange contracts mature as follows:

	September 30,	September 30, To Sell	September 30,
		At	At
Maturity	Euro Amount	Contract Rate	Market Rate
		(In thousands)	
2012	27,244	$ 32,894	$ 35,275
2013	27,000	32,967	35,208
	54,244	$ 65,861	$ 70,483

Balance Sheet Classification

The following summarizes the fair values and location in our consolidated balance sheet of all derivatives held by the Company as of December 31, 2011 (in thousands):

	September 30, Asset Derivatives	September 30,	September 30, Liability Derivatives	September 30,
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Derivatives designated as hedging instruments				
Foreign exchange contracts			Other current liabilities	$ 2,381
			Other liabilities	2,185
				4,566
Derivatives not designated as hedging instruments				
Foreign exchange contracts	Other current assets	$ 1		
			Other liabilities	56
Total derivatives		$ 1		$ 4,622

The following summarizes the fair values and location in our consolidated balance sheet of all derivatives held by the Company as of December 31, 2010 (in thousands):

	Asset Derivatives September 30,	Asset Derivatives September 30,	Liability Derivatives September 30,	Liability Derivatives September 30,
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Derivatives designated as hedging instruments				
Foreign exchange contracts	Other current assets	$ 4,152	Other current liabilities	$ 9,451
			Other liabilities	5,360
		$ 4,152		14,811
Derivatives not designated as hedging instruments				
Foreign exchange contracts	Other current assets	$ 396	Other current liabilities	133
			Other liabilities	63
Total derivatives		$ 4,548		$ 15,007

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Cash Flow Hedge Gains (Losses) Recognition

The following summarizes the gains (losses) recognized in the consolidated statements of operations and in accumulated other comprehensive loss for all derivatives for the years ended December 31, 2011 and 2010 (in thousands):

Derivatives in Cash Flow Hedging Relationships	September 30, Loss Recognized in OCI on Derivatives (Effective Portion)	September 30, Gain (Loss) Reclassified from Accumulated OCI into Income (Effective Portion) Location	September 30, Amount	September 30, Gain (Loss) on Derivative Ineffectiveness and Amounts Excluded from Effectiveness Testing Location	September 30, Amount
Year ended December 31, 2011					
Foreign exchange contracts	$ (8,821)	Revenue	$ (17,935)	Revenue	$ (411)
				Interest income	$ (1)
Year ended December 31, 2010					
Foreign exchange contracts	$ (15,790)	Revenue	$ 6,054	Revenue	$ 636
				Interest income	$ (13)

Cash Flow Derivatives Not Designated as Hedging Instruments	September 30, Gain (Loss) Recognized in Income on Derivatives Location	September 30, Amount
Year ended December 31, 2011		
Foreign exchange contracts	Revenue	$ (254)
Year ended December 31, 2010		
Foreign exchange contracts	Revenue	$ 33

We estimate that $6.5 million of net losses from derivative instruments included in accumulated other comprehensive loss will be reclassified into earnings within the next 12 months.

15. Commitments and Contingencies

Financial Matters

Due to the long lead times required to produce purchased parts, we have entered into various purchase commitments with suppliers. These commitments aggregated approximately $442 million as of December 31, 2011 and primarily relate to Satellite Manufacturing backlog.

SS/L has deferred revenue and accrued liabilities for warranty payback obligations relating to performance incentives for satellites sold to customers, which could be affected by future performance of the satellites. These reserves for expected costs for warranty reimbursement and support are based on historical failure rates. However, in the event of a catastrophic failure of a satellite, which cannot be predicted, these reserves likely will not be sufficient. SS/L periodically reviews and adjusts the deferred revenue and accrued liabilities for warranty reserves based on the actual performance of each satellite and remaining warranty period. A reconciliation of such deferred amounts for the year ended December 31, 2011 is as follows (in thousands):

	September 30, 2011
Balance of deferred amounts at January 1	$ 35,730
Warranty costs incurred including payments	(2,131)
Accruals relating to pre-existing contracts (including changes in estimates)	3,514
Balance of deferred amounts at December 31	$ 37,113

LORAL SPACE & COMMUNICATIONS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Many of SS/L s satellite contracts permit SS/L s customers to pay a portion of the purchase price for the satellite over time subject to the continued performance of the satellite (orbital incentives), and certain of SS/L s satellite contracts require SS/L to provide vendor financing to its customers, or a combination of these contractual terms. Some of these arrangements are provided to customers that are start-up companies, companies in the early stages of building their businesses or highly leveraged companies, including some with near-term debt maturities. There can be no assurance that these companies or their businesses will be successful and, accordingly, that these customers will be able to fulfill their payment obligations under their contracts with SS/L. We believe that these provisions will not have a material adverse effect on our consolidated financial position or our results of operations, although no assurance can be provided. Moreover, SS/L s receipt of orbital incentive payments is subject to the continued performance of its satellites generally over the contractually stipulated life of the satellites. Because these orbital receivables could be affected by future satellite performance, there can be no assurance that SS/L will be able to collect all or a portion of these receivables. Orbital receivables included in our consolidated balance sheet as of December 31, 2011 were $355 million, net of fair value adjustments of $16 million. Approximately $230 million of the gross orbital receivables are related to satellites launched as of December 31, 2011, and $141 million are related to satellites under construction as of December 31, 2011.

On October 19, 2010, TerreStar Networks Inc. (TerreStar), an SS/L customer, filed for bankruptcy under chapter 11 of the Bankruptcy Code. As of December 31, 2011, SS/L had $19 million of past due receivables from TerreStar related to an in-orbit SS/L built satellite and other related ground system deliverables and $16 million of past due receivables from TerreStar related to a second satellite under construction. SS/L had previously exercised its contractual right to stop work on the satellite under construction as a result of TerreStar s payment default. The in-orbit satellite long-term orbital receivable balance, net of fair value adjustment, reflected on the balance sheet at December 31, 2011 is $16 million. The long-term orbital receivable balance reflected on the balance sheet for the satellite under construction is $13 million.

In July 2011, the TerreStar Bankruptcy Court approved an agreement between TerreStar and a subsidiary of DISH Network Corporation (DISH Subsidiary) pursuant to which DISH Subsidiary agreed to purchase substantially all of TerreStar s assets. In connection with the sale, pursuant to a Stipulation and Order entered into between TerreStar and SS/L and approved by the TerreStar Bankruptcy Court in July 2011, the parties agreed to amend the satellite construction contract for the in-orbit satellite, the contract for related ground system deliverables and the contract for the satellite under construction, and TerreStar agreed to assume and assign to DISH Subsidiary, and DISH Subsidiary will take assignment of, such contracts as amended. The contract amendments provide for restructuring of certain past due payments and payments to become due as a result of which SS/L will maintain the collective profit position of the contracts and will not realize any impairment to its receivables. In addition, SS/L will be entitled to an allowed unsecured claim against TerreStar in the amount of approximately $5 million. The assumption will be effective as of the earlier of the closing of the asset sale to DISH Subsidiary or the effective date of confirmation of a plan of reorganization for TerreStar. The assignment will be effective as of the closing of the asset sale to DISH Subsidiary. On February 15, 2012, the TerreStar Bankruptcy Court entered an order confirming TerreStar s plan of reorganization. The effective date of the plan of reorganization and the closing of the asset sale are each subject to a number of conditions, including, among others, FCC and other regulatory approvals. Pending assumption and assignment of the contracts, TerreStar is required to make payments that fall due in the ordinary course of business under the contracts as amended. Assuming closing of the asset sale to DISH Subsidiary and assumption and assignment of the contracts as amended, SS/L believes that it will not incur a loss with respect to the receivables due from TerreStar.

As of December 31, 2011, SS/L had receivables included in contracts in process from DBSD Satellite Services G.P. (formerly known as ICO Satellite Services G.P. and referred to herein as ICO), a customer with an SS/L-built satellite in orbit, in the aggregate amount of approximately $1 million. In addition, under its contract, ICO has future payment obligations to SS/L that total approximately $23 million, of which approximately $11 million (including $9 million of orbital incentives) is included in long-term receivables. ICO, which sought to reorganize under chapter 11 of the Bankruptcy Code in May 2009, has agreed to, and the ICO Bankruptcy Court has approved, ICO s assumption of its contract with SS/L, with certain modifications. The contract modifications do not have a material adverse effect on SS/L, and, although the timing of payments to be received from ICO has changed (for example, certain significant payments become due only on or after the effective date of ICO s plan of reorganization), SS/L will receive substantially the same net present value from ICO as SS/L was entitled to receive under the original contract. In March 2011, the ICO Bankruptcy Court approved an investment agreement pursuant to which DISH Network Corporation (DISH) agreed to acquire ICO. In connection with this investment agreement, in April 2011, DISH purchased certain claims against ICO for cash, including SS/L claims aggregating approximately $7.0 million plus approximately $1.4 million of accrued interest. SS/L believes that, based upon completion of the tender offer and other payments by ICO to SS/L under the modified contract, it is not probable that SS/L will incur a material loss with respect to the receivables from ICO. Although, in July 2011, the ICO Bankruptcy Court confirmed a plan of reorganization for ICO, closing of DISH s acquisition of ICO and ICO s emergence from chapter 11 is still subject to certain other conditions, including, FCC regulatory approval.

LORAL SPACE & COMMUNICATIONS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

See Note 17 Related Party Transactions *Transactions with Affiliates Telesat* for commitments and contingencies relating to our agreement to indemnify Telesat for certain liabilities and our arrangements with ViaSat, Inc. and Telesat.

Satellite Matters

Satellites are built with redundant components or additional components to provide excess performance margins to permit their continued operation in case of component failure, an event that is not uncommon in complex satellites. Thirty-seven of the satellites built by SS/L, launched since 1997 and still on-orbit have experienced some loss of power from their solar arrays. There can be no assurance that one or more of the affected satellites will not experience additional power loss. In the event of additional power loss, the extent of the performance degradation, if any, will depend on numerous factors, including the amount of the additional power loss, the level of redundancy built into the affected satellite s design, when in the life of the affected satellite the loss occurred, how many transponders are then in service and how they are being used. It is also possible that one or more transponders on a satellite may need to be removed from service to accommodate the power loss and to preserve full performance capabilities on the remaining transponders. A complete or partial loss of a satellite s capacity could result in a loss of performance incentives by SS/L. SS/L has implemented remediation measures that SS/L believes will reduce this type of anomaly for satellites launched after June 2001. Based upon information currently available relating to the power losses, we believe that this matter will not have a material adverse effect on our consolidated financial position or our results of operations, although no assurance can be provided.

Non-performance can increase costs and subject SS/L to damage claims from customers and termination of the contract for SS/L s default. SS/L s contracts contain detailed and complex technical specifications to which the satellite must be built. It is very common that satellites built by SS/L do not conform in every single respect to, and contain a small number of minor deviations from, the technical specifications. Customers typically accept the satellite with such minor deviations. In the case of more significant deviations, however, SS/L may incur increased costs to bring the satellite within or close to the contractual specifications or a customer may exercise its contractual right to terminate the contract for default. In some cases, such as when the actual weight of the satellite exceeds the specified weight, SS/L may incur a predetermined penalty with respect to the deviation. A failure by SS/L to deliver a satellite to its customer by the specified delivery date, which may result from factors beyond SS/L s control, such as delayed performance or non-performance by its subcontractors or failure to obtain necessary governmental licenses for delivery, would also be harmful to SS/L unless mitigated by applicable contract terms, such as excusable delay. As a general matter, SS/L s failure to deliver beyond any contractually provided grace period would result in the incurrence of liquidated damages by SS/L, which may be substantial, and if SS/L is still unable to deliver the satellite upon the end of the liquidated damages period, the customer will generally have the right to terminate the contract for default. If a contract is terminated for default, SS/L would be liable for a refund of customer payments made to date, and could also have additional liability for excess re-procurement costs and other damages incurred by its customer, although SS/L would own the satellite under construction and attempt to recoup any losses through resale to another customer. A contract termination for default could have a material adverse effect on SS/L and us.

SS/L currently has a contract-in-process with an estimated delivery date later than the contractually specified date after which the customer may terminate the contract for default. The customer is an established operator which will utilize the satellite in the operation of its existing business. SS/L and the customer are continuing to perform their obligations under the contract, and the customer continues to make milestone payments to SS/L. Although there can be no assurance, the Company believes that the customer will take delivery of this satellite and will not seek to terminate the contract for default. If the customer should successfully terminate the contract for default, the customer would be entitled to a full refund of its payments, liquidated damages and interest, which through December 31, 2011 totaled approximately $204 million, plus re-procurement costs. In the event of termination for default, SS/L would own the satellite and would attempt to recoup any losses through resale to another customer.

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LORAL SPACE & COMMUNICATIONS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

SS/L is building a satellite known as CMBStar under a contract with EchoStar Corporation (EchoStar). Satellite construction is substantially complete. EchoStar and SS/L have agreed to suspend final construction of the satellite pending, among other things, further analysis relating to efforts to meet the satellite performance criteria and/or confirmation that alternative performance criteria would be acceptable. In May 2010, SS/L provided EchoStar, at its request, with a proposal to complete construction and prepare the satellite for launch under the current specifications. In August 2010, SS/L provided EchoStar, at its request, additional proposal information. There can be no assurance that a dispute will not arise as to whether the satellite meets its technical performance specifications or if such a dispute did arise that SS/L would prevail. SS/L believes that if a loss is incurred with respect to this program, such loss would not be material.

SS/L relies, in part, on patents, trade secrets and know-how to develop and maintain its competitive position. There can be no assurance that infringement of existing third party patents has not occurred or will not occur. In the event of infringement, we could be required to pay royalties to obtain a license from the patent holder, refund money to customers for components that are not useable or redesign our products to avoid infringement, all of which would increase our costs. We could also be subject to injunctions prohibiting us from using components or methods. We may also be required under the terms of our customer contracts to indemnify our customers for damages relating to infringement. For example, ViaSat, Inc. and ViaSat Communications, Inc. (formerly known as WildBlue Communications, Inc.) have commenced a lawsuit in the United States District Court for the Southern District of California against SS/L and Loral alleging, among other things, that SS/L and Loral infringed certain ViaSat patents and that SS/L breached non-disclosure obligations in certain contracts with ViaSat in connection with the manufacture of satellites by SS/L for customers other than ViaSat. The lawsuit also seeks to hold Loral liable for SS/L s alleged infringement and breach of contract. See *Legal Proceedings* below for details of this lawsuit.

See Note 17 Related Party Transactions *Transactions with Affiliates Telesat* for commitments and contingencies relating to SS/L s obligation to make payments to Telesat for transponders on Telstar 18.

Regulatory Matters

SS/L is required to obtain licenses and enter into technical assistance agreements, presently under the jurisdiction of the State Department, in connection with the export of satellites and related equipment, and with the disclosure of technical data or provision of defense services to foreign persons. Due to the relationship between launch technology and missile technology, the U.S. government has limited, and is likely in the future to limit, launches from China and other foreign countries. Delays in obtaining the necessary licenses and technical assistance agreements have in the past resulted in, and may in the future result in, the delay of SS/L s performance on its contracts, which could result in the cancellation of contracts by its customers, the incurrence of penalties or the loss of incentive payments under these contracts.

Lease Arrangements

We lease certain facilities and equipment under agreements expiring at various dates. Certain leases covering facilities contain renewal and/or purchase options which may be exercised by us. We have no sublease income in any of the periods presented. Rent expense, is as follows (in thousands):

	September 30, Rent Expense
Year ended December 31, 2011	$ 16,234
Year ended December 31, 2010	$ 18,911
Year ended December 31, 2009	$ 16,337

Property, plant and equipment relating to capital leases was $3.4 million at December 31, 2011 and nil at December 31, 2010 with accumulated amortization of $0.7 million and nil, respectively. Depreciation and amortization of assets recorded under capital leases was $0.7 million in 2011 and nil in 2010 and 2009.

LORAL SPACE & COMMUNICATIONS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following is a schedule of future minimum payments, by year and in the aggregate, under leases with initial or remaining terms of one year or more as of December 31, 2011 (in thousands):

	September 30, Capital Leases	September 30, Operating Leases
2012	$ 1,201	$ 10,155
2013	1,201	7,783
2014		6,876
2015		5,747
2016		3,670
Thereafter		4,894
Total minimum lease payments	2,402	$ 39,125
Less amount representing interest	(159)	
Present value of future minimum lease payments	$ 2,243	

Legal Proceedings

In February 2012, ViaSat, Inc. and ViaSat Communications, Inc. (formerly known as WildBlue Communications, Inc.) (collectively, ViaSat) commenced a lawsuit in the United States District Court for the Southern District of California against SS/L and Loral, Case No. 3:12-cv-00260-H-WVG. The complaint alleges, among other things, that SS/L and Loral infringed certain ViaSat patents and that SS/L breached non-disclosure obligations in certain contracts with ViaSat in connection with the manufacture of satellites by SS/L for customers other than ViaSat. The complaint also seeks to hold Loral liable for SS/L s alleged infringement and breach of contract. The complaint seeks, among other things, damages (including treble damages with respect to the patent infringement claims) in amounts to be determined at trial and to enjoin SS/L and Loral from further infringement of the ViaSat patents and breach of contract. Although SS/L and Loral intend to engage in discussions with ViaSat to resolve the matter, there can be no assurance that the parties will resolve the matter. If the parties are not able to resolve the matter through discussions and the matter proceeds to trial, SS/L and Loral believe that they each have, and intend vigorously to pursue, meritorious defenses and counterclaims to ViaSat s claims. There can be no assurance, however, that SS/L s and Loral s defenses and counterclaims will be successful with respect to all or some of ViaSat s claims. We believe that SS/L s and Loral s conduct was consistent with, and in due regard for, any applicable and valid intellectual property rights of ViaSat. Although no assurance can be provided, we do not believe that this matter will have a material adverse effect on SS/L s or Loral s financial position or results of operations.

Other and Routine Litigation

We are subject to various other legal proceedings and claims, either asserted or unasserted, that arise in the ordinary course of business. Although the outcome of these legal proceedings and claims cannot be predicted with certainty, we do not believe that any of these other existing legal matters will have a material adverse effect on our consolidated financial position or our results of operations.

16. Segments

Loral has two segments: satellite manufacturing and satellite services. Our segment reporting data includes unconsolidated affiliates that meet the reportable segment criteria. The satellite services segment includes 100% of the results reported by Telesat for the years ended December 31, 2011, 2010 and 2009. Although we analyze Telesat s revenue and expenses under the satellite services segment, we eliminate its results in our consolidated financial statements, where we report our 64% share of Telesat s results as equity in net income of affiliates. Our investment in

XTAR, for which we use the equity method of accounting, is included in Corporate.

The common definition of EBITDA is Earnings Before Interest, Taxes, Depreciation and Amortization . In evaluating financial performance, we use revenues and operating income before depreciation, amortization and stock-based compensation (excluding stock-based compensation from SS/L Phantom SARs expected to be settled in cash), gain on disposition of net assets and directors indemnification expense (Adjusted EBITDA) as the measure of a segment s profit or loss. Adjusted EBITDA is equivalent to the common definition of EBITDA before: gains on disposition of net assets, directors indemnification expense, gains or losses on litigation not related to our operations; other expense; and equity in net income of affiliates.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Adjusted EBITDA allows us and investors to compare our operating results with that of competitors exclusive of depreciation and amortization, interest and investment income, interest expense, gains on disposition of net assets, directors indemnification expense, gains or losses on litigation not related to our operations, other expense and equity in net income of affiliates. Financial results of competitors in our industry have significant variations that can result from timing of capital expenditures, the amount of intangible assets recorded, the differences in assets lives, the timing and amount of investments, the effects of other expense, which are typically for non-recurring transactions not related to the on-going business, and effects of investments not directly managed. The use of Adjusted EBITDA allows us and investors to compare operating results exclusive of these items. Competitors in our industry have significantly different capital structures. The use of Adjusted EBITDA maintains comparability of performance by excluding interest expense.

We believe the use of Adjusted EBITDA along with U.S. GAAP financial measures enhances the understanding of our operating results and is useful to us and investors in comparing performance with competitors, estimating enterprise value and making investment decisions. Adjusted EBITDA as used here may not be comparable to similarly titled measures reported by competitors. We also use Adjusted EBITDA to evaluate operating performance of our segments, to allocate resources and capital to such segments, to measure performance for incentive compensation programs and to evaluate future growth opportunities. Adjusted EBITDA should be used in conjunction with U.S. GAAP financial measures and is not presented as an alternative to cash flow from operations as a measure of our liquidity or as an alternative to net income as an indicator of our operating performance.

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LORAL SPACE & COMMUNICATIONS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Intersegment revenues primarily consists of satellites under construction by satellite manufacturing for satellite services and the leasing of transponder capacity by satellite manufacturing from satellite services. Summarized financial information concerning the reportable segments is as follows:

Segment Information

(In thousands)

	September 30,	September 30, Year Ended December 31,	September 30,
	2011	2010 (In thousands)	2009
Revenues			
Satellite manufacturing:			
External revenues	$ 967,432	$ 1,021,768	$ 901,283
Intersegment revenues[1]	140,763	143,318	107,401
Satellite manufacturing revenues	1,108,195	1,165,086	1,008,684
Satellite services revenues[2]	817,269	797,283	691,566
Operating segment revenues before eliminations	1,925,464	1,962,369	1,700,250
Intercompany eliminations[3]	(830)	(6,101)	(15,284)
Affiliate eliminations[2]	(817,269)	(797,283)	(691,566)
Total revenues as reported	$ 1,107,365	$ 1,158,985	$ 993,400
Segment Adjusted EBITDA[4]			
Satellite manufacturing	$ 137,659	$ 143,076	$ 90,565
Satellite services[2]	629,150	606,651	488,149
Corporate[5]	(17,170)	(17,866)	(21,371)
Adjusted EBITDA before eliminations	749,639	731,861	557,343
Intercompany eliminations[3]	(279)	(1,465)	(1,673)
Affiliate eliminations[2]	(629,150)	(606,651)	(488,149)
Adjusted EBITDA	120,210	123,745	67,521
Reconciliation to Operating Income			
Depreciation, Amortization and Stock-Based Compensation[4]			
Satellite manufacturing	(32,514)	(34,675)	(44,203)
Satellite services[2]	(248,010)	(249,318)	(230,176)
Corporate	(1,175)	(1,605)	(3,107)
Segment depreciation before affiliate eliminations	(281,699)	(285,598)	(277,486)
Affiliate eliminations[2]	248,010	249,318	230,176
Depreciation, amortization and stock-based compensation as reported	(33,689)	(36,280)	(47,310)

Gain on disposition of net assets[6]	6,913		
Directors indemnification expense[7]		(6,857)	
Operating income as reported	$ 93,434	$ 80,608	$ 20,211
Capital Expenditures			
Satellite manufacturing	$ 36,615	$ 35,378	$ 26,426
Satellite services[2]	390,641	254,020	231,654
Corporate	350	18,679	17,131
Segment capital expenditures before affiliate eliminations[8]	427,606	308,077	275,211
Affiliate eliminations[2]	(390,641)	(254,020)	(231,654)
Capital expenditures as reported	$ 36,965	$ 54,057	$ 43,557

	September 30, As of December 31, 2011	September 30, 2010
	(In thousands)	
Total Assets[8]		
Satellite manufacturing	$ 929,408	$ 920,647
Satellite services[9]	5,724,418	5,605,239
Corporate	529,501	538,464
Total assets before affiliate eliminations	7,183,327	7,064,350
Affiliate eliminations[2]	(5,347,174)	(5,309,441)
Total assets as reported	$ 1,836,153	$ 1,754,909

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LORAL SPACE & COMMUNICATIONS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(1) Intersegment revenues include $140 million, $137 million and $92 million for the years ended December 31, 2011, 2010 and 2009, respectively, of revenue from affiliates.

(2) Satellite services represents Telesat. Affiliate eliminations represent the elimination of amounts attributable to Telesat whose results are reported under the equity method of accounting in our consolidated statements of operations (see Note 7).

(3) Represents the elimination of intercompany sales and intercompany Adjusted EBITDA for a satellite under construction by SS/L for Loral.

(4) Compensation expense related to SS/L Phantom SARs and restricted stock units paid in cash or expected to be paid in cash is included in Adjusted EBITDA. Compensation expense related to SS/L Phantom SARs and restricted stock units paid in Loral common stock or expected to be paid in Loral common stock is included in depreciation, amortization and stock-based compensation.

(5) Includes corporate expenses incurred in support of our operations and includes our equity investments in XTAR and Globalstar service providers.

(6) Represents the gain on the sale of Loral s portion of the payload on the ViaSat-1 satellite and related net assets to Telesat adjusted for elimination of Loral s 64% ownership interest in Telesat (see Note 17).

(7) Represents indemnification expense, net of insurance recovery, in connection with defense costs incurred by MHR affiliated directors in the Delaware shareholder derivative case (see Note 15).

(8) Amounts are presented after the elimination of intercompany profit.

(9) Includes $2.4 billion of satellite services goodwill related to Telesat as of December 31, 2011 and 2010, respectively.

Revenue by Customer Location

The following table presents our revenues by country based on customer location for the years ended December 31, 2011, 2010 and 2009 (in thousands):

	September 30,	September 30,	September 30,
	For the Year Ended December 31,		
	2011	2010	2009
United States	$ 397,389	$ 645,769	$ 534,294
Canada	137,610	137,195	92,094
Spain	113,546	85,161	85,499
Bermuda	83,600		
Mexico	82,657	49,157	22
France	80,923	24,657	344

People s Republic of China (including Hong Kong)	47,967	44,135	54,677
United Kingdom	40,741	57,976	101,499
Australia	40,067		
Luxembourg	31,107	70,678	61,673
Norway	29,809		
The Netherlands	18,501	26,721	59,509
Other	3,448	17,536	3,789
	$ 1,107,365	$ 1,158,985	$ 993,400

During 2011, three of our customers accounted for approximately 13%, 12% and 10% of our consolidated revenues. During 2010, five of our customers accounted for approximately 19%, 13%, 12%, 12% and 11% of our consolidated revenues. During 2009, three of our customers accounted for approximately 22%, 16% and 10% of our consolidated revenues.

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LORAL SPACE & COMMUNICATIONS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

17. Related Party Transactions

Transactions with Affiliates

Telesat

As described in Note 7, we own 64% of Telesat and account for our ownership interest under the equity method of accounting.

In connection with the acquisition of our ownership interest in Telesat (which we refer to as the Telesat transaction), Loral and certain of its subsidiaries, our Canadian partner, PSP and one of its subsidiaries, Telesat Holdco and certain of its subsidiaries, including Telesat, and MHR entered into a Shareholders Agreement (the Shareholders Agreement). The Shareholders Agreement provides for, among other things, the manner in which the affairs of Telesat Holdco and its subsidiaries will be conducted and the relationships among the parties thereto and future shareholders of Telesat Holdco. The Shareholders Agreement also contains an agreement by Loral not to engage in a competing satellite communications business and agreements by the parties to the Shareholders Agreement not to solicit employees of Telesat Holdco or any of its subsidiaries. Additionally, the Shareholders Agreement details the matters requiring the approval of the shareholders of Telesat Holdco (including veto rights for Loral over certain extraordinary actions), provides for preemptive rights for certain shareholders upon the issuance of certain capital shares of Telesat Holdco and provides for either PSP or Loral to cause Telesat Holdco to conduct an initial public offering of its equity shares if an initial public offering has not been completed by October 31, 2011, the fourth anniversary of the Telesat transaction. The Shareholders Agreement also restricts the ability of holders of certain shares of Telesat Holdco to transfer such shares unless certain conditions are met or approval of the transfer is granted by the directors of Telesat Holdco, provides for a right of first offer to certain Telesat Holdco shareholders if a holder of equity shares of Telesat Holdco wishes to sell any such shares to a third party and provides for, in certain circumstances, tag-along rights in favor of shareholders that are not affiliated with Loral if Loral sells equity shares and drag-along rights in favor of Loral in case Loral or its affiliate enters into an agreement to sell all of its Telesat Holdco equity securities.

Under the Shareholders Agreement, in the event that, either (i) ownership or control, directly or indirectly, by Dr. Rachesky, President of MHR, of Loral s voting stock falls below certain levels or (ii) there is a change in the composition of a majority of the members of the Loral Board of Directors over a consecutive two-year period, Loral will lose its veto rights relating to certain extraordinary actions by Telesat Holdco and its subsidiaries. In addition, after either of these events, PSP will have certain rights to enable it to exit from its investment in Telesat Holdco, including a right to cause Telesat Holdco to conduct an initial public offering in which PSP s shares would be the first shares offered or, if no such offering has occurred within one year due to a lack of cooperation from Loral or Telesat Holdco, to cause the sale of Telesat Holdco and to drag along the other shareholders in such sale, subject to Loral s right to call PSP s shares at fair market value.

The Shareholders Agreement provides for a board of directors of each of Telesat Holdco and certain of its subsidiaries, including Telesat, consisting of 10 directors, three nominated by Loral, three nominated by PSP and four independent directors to be selected by a nominating committee comprised of one PSP nominee, one nominee of Loral and one of the independent directors then in office. Each party to the Shareholders Agreement is obligated to vote all of its Telesat Holdco shares for the election of the directors nominated by the nominating committee. Pursuant to action by the board of directors taken on October 31, 2007, Dr. Rachesky, who is non-executive Chairman of the Board of Directors of Loral, was appointed non-executive Chairman of the Board of Directors of Telesat Holdco and certain of its subsidiaries, including Telesat. In addition, Michael B. Targoff, Loral s Vice Chairman, Chief Executive Officer and President, serves on the board of directors of Telesat Holdco and certain of its subsidiaries, including Telesat.

As of December 31, 2011, SS/L had contracts with Telesat for the construction of the Nimiq 6 and Anik G1 satellites. Information related to satellite construction contracts with Telesat is as follows:

	September 30,	September 30,	September 30,
	For Year Ended December 31,		
	2011	2010	2009
	(In thousands)		

Revenues from Telesat satellite construction contracts	$ 139,911	$ 137,195	$ 92,095
Milestone payments received from Telesat	126,579	168,130	89,419

Amounts receivable by SS/L from Telesat related to satellite construction contracts as of December 31, 2011 and 2010 were $4.6 million and nil, respectively.

LORAL SPACE & COMMUNICATIONS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

On October 31, 2007, Loral and Telesat entered into a consulting services agreement (the Consulting Agreement). Pursuant to the terms of the Consulting Agreement, Loral provides to Telesat certain non-exclusive consulting services in relation to the business of Loral Skynet which was transferred to Telesat as part of the Telesat transaction as well as with respect to certain aspects of the satellite communications business of Telesat. The Consulting Agreement has a term of seven years with an automatic renewal for an additional seven-year term if certain conditions are met. In exchange for Loral s services under the Consulting Agreement, Telesat will pay Loral an annual fee of US $5.0 million payable quarterly in arrears on the last day of March, June, September and December of each year during the term of the Consulting Agreement. If the terms of Telesat s bank or bridge facilities or certain other debt obligations prevent Telesat from paying such fees in cash, Telesat may issue junior subordinated promissory notes to Loral in the amount of such payment, with interest on such promissory notes payable at the rate of 7% per annum, compounded quarterly, from the date of issue of such promissory note to the date of payment thereof. Our selling, general and administrative expenses for each of the years ended December 31, 2011, 2010 and 2009, included income of $5.0 million related to the Consulting Agreement. We also had a long-term receivable related to the Consulting Agreement from Telesat of $20.7 million and $17.6 million as of December 31, 2011 and 2010, respectively. We received payments from Telesat of $3.2 million under this agreement for the year ended December 31, 2011. No payments were received from Telesat for the years ended December 31, 2010 and 2009.

In connection with the Telesat transaction, Loral has retained the benefit of tax recoveries related to the transferred assets and has indemnified Telesat for certain liabilities including Loral Skynet s tax liabilities arising prior to January 1, 2007. As of December 31, 2011 and 2010, we had recognized a net receivable from Telesat of $0.5 million, representing our estimate of the probable outcome of these tax matters, which is included as other assets of $2.6 million and long-term liabilities of $2.1 million in the consolidated balance sheet as of December 31, 2011. There can be no assurance, however, that these tax matters will be ultimately settled for the net amount recorded.

In June 2011, Loral, along with Telesat Holdco, Telesat, PSP and 4440480 Canada Inc., an indirect wholly-owned subsidiary of Loral (the Special Purchaser), entered into Grant Agreements (the Grant Agreements) with Daniel Goldberg, Michael C. Schwartz and Michel G. Cayouette (each, a Participant and collectively, the Participants). Each of the Participants is an executive of Telesat, which is owned by the Company together with its Canadian partner, PSP, through their ownership of Telesat Holdco. The Grant Agreements document grants previously approved and made in September 2008. Mr. Goldberg s agreement is effective as of May 20, 2011, and the agreements for each of Messrs. Schwartz and Cayouette are effective as of May 31, 2011.

The Grant Agreements confirm grants of Telesat Holdco stock options (including tandem SAR rights) to the Participants and provide for certain rights, obligations and restrictions related to such stock options, which include, among other things: (w) the right of each Participant to require the Special Purchaser to purchase a portion of the shares in Telesat Holdco owned by him in the event of exercise after termination of employment to cover taxes that are greater than the minimum withholding amount; (x) the possible obligation of the Special Purchaser to purchase the shares in the place of Telesat Holdco should Telesat Holdco be prohibited by applicable law or under the terms of any credit agreement applicable to Telesat Holdco from purchasing such shares, or otherwise default on such purchase obligation, pursuant to the terms of the Grant Agreements; (y) the obligation of the Special Purchaser to purchase shares upon exercise by Telesat Holdco of its call right under Telesat Holdco s Management Stock Incentive Plan in the event of a Participant s termination of employment; and (z) the right of each Participant to require Telesat Holdco to cause the Special Purchaser or Loral to purchase a portion of the shares in Telesat Holdco owned by him, or that are issuable to him under Telesat Holdco s Management Stock Incentive Plan at the relevant time, in the event that more than 90% of Loral s common stock is acquired by an unaffiliated third party that does not also purchase all of PSP s and its affiliates interest in Telesat Holdco.

The Grant Agreements further provide that, in the event the Special Purchaser is required to purchase shares, such shares, together with the obligation to pay for such shares, shall be transferred to a subsidiary of the Special Purchaser, which subsidiary shall be wound up into Telesat Holdco, with Telesat Holdco agreeing to the acquisition of such subsidiary by Telesat Holdco from the Special Purchaser for nominal consideration and with the purchase price for the shares being paid by Telesat Holdco within ten (10) business days after completion of the winding-up of such subsidiary into Telesat Holdco.

ViaSat/Telesat

In connection with an agreement entered into between SS/L and ViaSat, Inc. (ViaSat) for the construction by SS/L for ViaSat of a high capacity broadband satellite called ViaSat-1, on January 11, 2008, we entered into certain agreements, described below, pursuant to which, we invested in the Canadian coverage portion of the ViaSat-1 satellite. Michael B. Targoff and another Loral director serve as members of the ViaSat Board of Directors.

LORAL SPACE & COMMUNICATIONS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

A Beam Sharing Agreement between us and ViaSat provided for, among other things, (i) the purchase by us of a portion of the ViaSat-1 satellite payload providing coverage into Canada (the Loral Payload) and (ii) payment by us of 15% of the actual costs of launch and associated services, launch insurance and telemetry, tracking and control services for the ViaSat-1 satellite. SS/L commenced construction of the Viasat-1 satellite in January 2008. We recorded sales to ViaSat under this contract of $17.7 million, $34.6 million and $86.6 million for the years ended December 31, 2011, 2010 and 2009, respectively.

On April 11, 2011, Loral assigned to Telesat and Telesat assumed from Loral all of Loral s rights and obligations with respect to the Loral Payload and all related agreements. In consideration for the assignment, Loral received $13 million from Telesat and was reimbursed by Telesat, for approximately $48.2 million of net costs incurred through closing of the sale, including costs for the satellite, launch and insurance, and costs of the gateways and related equipment. Also, in connection with the assignment if Telesat agreed that if it obtains certain supplemental capacity on the payload, Loral will be entitled to receive one-half of any net revenue actually earned by Telesat in connection with the leasing of such supplemental capacity to its customers during the first four years after the commencement of service using the supplemental capacity. In connection with the sale, Loral also assigned to Telesat and Telesat assumed Loral s 15-year contract with Xplornet Communications, Inc. (Xplornet) (formerly known as Barrett Xplore Inc.) for delivery of high throughput satellite Ka-band capacity and gateway services for broadband services in Canada. Our consolidated statements of operations for the year ended December 31, 2011 included a $6.9 million gain on this transaction representing the $13 million of proceeds in excess of costs adjusted for cumulative intercompany profit eliminations and our retained ownership interest in Telesat. During 2010, a subsidiary of Loral entered into contracts with ViaSat for procurement of equipment and services and with Telesat for consulting, management, engineering and integration services related to the gateways that enable commercial services using the Loral Payload. Prior to April 11, 2011, we had made cumulative payments of $3.9 million to ViaSat and $1.4 million to Telesat under these agreements.

Costs of satellite manufacturing for sales to related parties were $124.5 million, $140.5 million and $153.5 million for the years ended December 31, 2011, 2010 and 2009, respectively.

In connection with an agreement reached in 1999 and an overall settlement reached in February 2005 with ChinaSat relating to the delayed delivery of ChinaSat 8, SS/L has provided ChinaSat with usage rights to two Ku-band transponders on Telesat s Telstar 10 for the life of such transponders (subject to certain restoration rights) and to one Ku-band transponder on Telesat s Telstar 18 for the life of the Telstar 10 satellite plus two years, or the life of such transponder (subject to certain restoration rights), whichever is shorter. Pursuant to an amendment to the agreement executed in June 2009, in lieu of rights to one of the Ku-band transponders on Telstar 10, ChinaSat has rights to an equivalent amount of Ku-band capacity on Telstar 18 (the Alternative Capacity). The Alternative Capacity may be utilized by ChinaSat until April 30, 2019 subject to certain conditions. Under the agreement, SS/L makes monthly payments to Telesat for the transponders allocated to ChinaSat. Effective with the termination of Telesat s leasehold interest in Telstar 10 in July 2009, SS/L makes monthly payments with respect to capacity used by ChinaSat on Telstar 10 directly to APT, the owner of the satellite. As of December 31, 2011 and 2010, our consolidated balance sheets included a liability of $3.7 million and $6.0 million, respectively, for the future use of these transponders. Interest expense on this liability was $0.5 million, $0.7 million and $0.9 million for the years ended December 31, 2011, 2010 and 2009, respectively. For the year ended December 31, 2011, we made payments of $2.7 million to Telesat pursuant to the agreement.

LORAL SPACE & COMMUNICATIONS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

XTAR

As described in Note 7, we own 56% of XTAR, a joint venture between Loral and Hisdesat and account for our investment in XTAR under the equity method of accounting. SS/L constructed XTAR s satellite, which was successfully launched in February 2005. XTAR and Loral have entered into a management agreement whereby Loral provides general and specific services of a technical, financial, and administrative nature to XTAR. For the services provided by Loral, XTAR is charged a quarterly management fee equal to 3.7% of XTAR s quarterly gross revenues. Amounts due to Loral primarily due to the management agreement as of December 31, 2011 and 2010 were $4.2 million and $3.0 million, respectively. Beginning in 2008, Loral and XTAR agreed to defer amounts owed to Loral under this agreement, and XTAR has agreed that its excess cash balance (as defined), will be applied at least quarterly towards repayment of receivables owed to Loral, as well as to Hisdesat and Telesat. No cash was received under this agreement for the years ended December 31, 2011 and 2010. Our selling, general and administrative expenses included offsetting income to the extent of cash received under this agreement of $1.2 million for the year ended December 31, 2009.

MHR Fund Management LLC

Two of the managing principals of MHR, Mark H. Rachesky and Hal Goldstein are members of Loral s board of directors. A former managing principal of MHR, Sai S. Devabhaktuni, was a member of the Loral Board until his resignation in January 2012.

In June 2009, Loral filed a shelf registration statement covering shares of voting common stock and non-voting common stock held by the MHR Funds and Dr. Rachesky, which registration statement was declared effective in July 2009. Various funds affiliated with MHR and Dr. Rachesky held, as of December 31, 2011 and 2010, approximately 38.6% and 38.9%, respectively, of the outstanding voting common stock and as of December 31, 2011 and 2010 had a combined ownership of outstanding voting and non-voting common stock of Loral of 57.7% and 58.0%, respectively.

Funds affiliated with MHR were participants in a $200 million credit facility of Protostar Ltd. (Protostar), dated March 19, 2008, with an aggregate participation of $6.0 million. The MHR funds also owned certain equity interests in Protostar. During July 2009, Protostar filed for bankruptcy protection under chapter 11 of the Bankruptcy Code. The United States Bankruptcy Court for the District of Delaware entered an order confirming the plan of reorganization for Protostar and its affiliated debtors on October 6, 2010. The plan provided for the establishment of liquidating trusts for the Protostar debtors remaining assets, and Protostar commenced distributions on October 21, 2010 to the agent under the above-referenced facility for the benefit of its lenders. The plan of reorganization provided for no recovery by holders of equity interests in Protostar, and all equity interests were deemed cancelled as of the effective date of the plan.

Pursuant to a contract with Protostar valued at $26 million, SS/L has modified a satellite that Protostar acquired from China Telecommunications Broadcast Satellite Corporation, China National Postal and Telecommunication Broadcast Satellite Corporation and China National Postal and Telecommunications Appliances Corporation under an agreement reached in 2006. This satellite, renamed Protostar I, was launched on July 8, 2008. Pursuant to a bankruptcy auction, Protostar I was sold in November 2009. For the year ended December 31, 2009, as a result of Protostar s bankruptcy process and the sale of the satellite, SS/L recorded a charge of approximately $3 million to increase its allowance for billed receivables from Protostar.

As of December 31, 2010, funds affiliated with MHR held $83.7 million in principal amount of Telesat 11% Senior Notes and $29.75 million in principal amount of Telesat 12.5% Senior Subordinated Notes. As of December 31, 2011, MHR did not own any Telesat Senior Notes or Senior Subordinated Notes.

LORAL SPACE & COMMUNICATIONS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

18. Selected Quarterly Financial Information (unaudited, in thousands, except per share amounts)

	September 30,	September 30,	September 30,	September 30,
	Quarter Ended			
Year ended December 31, 2011	**March 31,**	**June 30,**	**September 30,**	**December 31,**
Revenues	$ 279,899	$ 252,422	$ 268,845	$ 306,199
Operating income	27,452	23,484	14,371	28,127
Income before income taxes and equity in net income (losses) of affiliates	36,912	26,105	17,189	29,784
Equity in net income (losses) of affiliates	46,246	23,940	(77,262)	113,405
Net income (loss)	67,795	29,626	(77,298)	107,051
Net income (loss) attributable to Loral common shareholders	67,819	29,333	(77,368)	106,893
Basic and diluted income (loss) per share[1]:				
Basic income (loss) per share	2.21	0.96	(2.52)	3.48
Diluted income (loss) per share	2.10	0.91	(2.52)	3.28

	September 30,	September 30,	September 30,	September 30,
	Quarter Ended			
Year ended December 31, 2010	**March 31,**	**June 30,**	**September 30,**	**December 31,**
Revenues	$ 228,914	$ 279,962	$ 323,438	$ 326,671
Operating income (loss)	(16,267)	23,098	39,621	34,156
Income (loss) before income taxes and equity in net income (losses) of affiliates	(13,704)	26,355	41,462	38,981
Equity in net income (losses) of affiliates	44,592	(44,374)	40,011	45,396
Net income (loss)	29,373	(19,665)	72,392	405,241
Net income (loss) attributable to Loral common shareholders	29,373	(19,665)	72,392	404,746
Basic and diluted income (loss) per share[1]:				
Basic income (loss) per share	0.98	(0.66)	2.40	13.36
Diluted income (loss) per share	0.97	(0.66)	2.29	12.87

[1] The quarterly earnings per share information is computed separately for each period. Therefore, the sum of such quarterly per share amounts may differ from the total for the year.

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SCHEDULE II

LORAL SPACE & COMMUNICATIONS INC.

VALUATION AND QUALIFYING ACCOUNTS

For the Year Ended December 31, 2011, 2010 and 2009

(In thousands)

Description	September 30, Balance at Beginning of Period	September 30, Charged to Costs and Expenses	September 30, Additions Charged to Other Accounts[1]	September 30, Deductions From Reserves[2]	September 30, Balance at End of Period
Year ended 2009					
Allowance for billed receivables	$ 923	$ 2,759	$	$	$ 3,682
Inventory allowance	$ 27,200	$ 1,042	$ 55	$	$ 28,297
Deferred tax valuation allowance	$ 487,762	$ (96,617)	$ 22,893	$	$ 414,038
Year ended 2010					
Allowance for billed receivables	$ 3,682	$	$	$ (3,459)	$ 223
Inventory allowance	$ 28,297	$ 4,297	$	$ (1,224)	$ 31,370
Deferred tax valuation allowance	$ 414,038	$ (402,809)[3]	$	$	$ 11,229
Year ended 2011					
Allowance for billed receivables	$ 223	$	$	$	$ 223
Inventory allowance	$ 31,370	$ (10)	$	$	$ 31,360
Deferred tax valuation allowance	$ 11,229	$ (375)	$ 33	$	$ 10,887

(1) The allowance for long-term receivables is recorded as a reduction to revenues. Changes in the deferred tax valuation allowance which have been charged to other accounts have been recorded in accumulated other comprehensive loss and other deferred tax assets.

(2) Deductions from reserves reflect write-offs of uncollectible billed receivables and disposals of inventory.

(3) During the fourth quarter of 2010, we determined, based on all available evidence, that a full valuation allowance was no longer required on our deferred tax assets and, therefore, $335.3 million of the valuation allowance was reversed as an income tax benefit. In addition, the valuation allowance was reduced by $67.5 million recorded as benefit to continuing operations.

Report of Independent Registered Chartered Accountants

To the Board of Directors and Shareholders of Telesat Holdings Inc.

We have audited the accompanying consolidated financial statements of Telesat Holdings Inc. and subsidiaries (the Company), which comprise the consolidated balance sheets as at December 31, 2011, December 31, 2010 and January 1, 2010 and the consolidated statements of income, statements of comprehensive income, statements of changes in shareholders equity and statements of cash flows for the years ended December 31, 2011 and December 31, 2010, and a summary of significant accounting policies and other explanatory information.

Management s Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor s Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards and the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Telesat Holdings Inc. and subsidiaries as at December 31, 2011, December 31, 2010 and January 1, 2010 and their financial performance and cash flows for the years ended December 31, 2011 and December 31, 2010 in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board.

/s/ Deloitte & Touche LLP

Independent Registered Chartered Accountants

Licensed Public Accountants

February 21, 2012

Toronto, Canada

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Telesat Holdings Inc.

Consolidated Statements of Income

For the year ended December 31

(in thousands of Canadian dollars)	September 30, Notes	September 30, 2011	September 30, 2010 (Note 5)
Revenue	6	808,361	821,361
Operating expenses	7	(187,765)	(206,464)
		620,596	614,897
Depreciation	14	(198,626)	(202,183)
Amortization		(41,021)	(45,468)
Other operating gains, net	8	114,068	83,018
Operating income		495,017	450,264
Interest expense	9	(227,051)	(256,582)
Interest and other income		1,554	5,752
Gain (loss) on changes in fair value of financial instruments		98,585	(11,168)
(Loss) gain on foreign exchange		(78,844)	163,966
Income before tax		289,261	352,232
Tax expense	10	(51,986)	(66,131)
Net income		237,275	286,101

See accompanying notes to the consolidated financial statements

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Telesat Holdings Inc.

Consolidated Statements of Comprehensive Income

For the year ended December 31

(in thousands of Canadian dollars)	September 30, Notes	September 30, 2011	September 30, 2010 (Note 5)
Net income		237,275	286,101
Other comprehensive loss:			
Foreign currency translation adjustments, net of tax		(3,541)	(1,692)
Actuarial losses on defined benefit plans, net of tax	25	(31,077)	(9,450)
Other comprehensive loss		(34,618)	(11,142)
Total comprehensive income		202,657	274,959

See accompanying notes to the consolidated financial statements

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Telesat Holdings Inc.

Consolidated Statements of Changes in Shareholders Equity

Year ended December 31

(in thousands of Canadian dollars)	Notes	Common shares	Preferred shares	Total share capital	Accumulated earnings (deficit)	Equity-settled employee benefits reserve	Foreign currency translation reserve	Total reserves	Total shareholders equity
Balance at January 1, 2010	**5**	**756,414**	**541,764**	**1,298,178**	**(112,817)**	**19,906**		**19,906**	**1,205,267**
Net income for the year					286,101				286,101
Dividends declared on preferred shares					(30)				(30)
Other comprehensive loss, net of tax of $3,357					(9,450)		(1,692)	(1,692)	(11,142)
Share based payments	24					4,667		4,667	4,667
Balance at December 31, 2010	**5**	**756,414**	**541,764**	**1,298,178**	**163,804**	**24,573**	**(1,692)**	**22,881**	**1,484,863**
Balance at January 1, 2011	**5**	**756,414**	**541,764**	**1,298,178**	**163,804**	**24,573**	**(1,692)**	**22,881**	**1,484,863**
Net income for the year					237,275				237,275
Dividends declared on preferred shares					(10)				(10)
Other comprehensive loss, net of tax of $10,486					(31,077)		(3,541)	(3,541)	(34,618)
Share based payments	24					2,654		2,654	2,654
Balance at December 31, 2011		**756,414**	**541,764**	**1,298,178**	**369,992**	**27,227**	**(5,233)**	**21,994**	**1,690,164**

See accompanying notes to the consolidated financial statements

Telesat Holdings Inc.

Consolidated Balance Sheets

(in thousands of Canadian dollars)	September 30, Notes	September 30, December 31, 2011	September 30, December 31, 2010 (Note 5)	September 30, January 1, 2010 (Note 5)
Assets				
Cash and cash equivalents	26	277,962	220,295	154,189
Trade and other receivables	11	46,789	44,083	70,200
Other current financial assets	23	7,010	6,944	7,317
Prepaid expenses and other current assets	12	22,126	20,937	23,001
Total current assets		353,887	292,259	254,707
Satellites, property and other equipment	6, 14	2,151,915	1,978,789	1,898,898
Other long-term financial assets	23	142,408	78,631	21,733
Other long-term assets	13	5,536	12,027	19,031
Intangible assets	6, 15	896,078	945,547	925,921
Goodwill	16	2,446,603	2,446,603	2,446,603
Total assets		5,996,427	5,753,856	5,566,893
Liabilities				
Trade and other payables		45,156	49,974	43,413
Other current financial liabilities		82,988	104,082	102,124
Other current liabilities	17	67,877	62,645	72,121
Current indebtedness	19	86,495	96,848	23,602
Total current liabilities		282,516	313,549	241,260
Long-term indebtedness	19	2,748,131	2,771,802	3,021,820
Deferred tax liabilities	10	451,896	414,717	353,637
Other long-term financial liabilities		259,783	265,629	239,825
Other long-term liabilities	18	422,502	361,861	363,649
Senior preferred shares	20	141,435	141,435	141,435
Total liabilities		4,306,263	4,268,993	4,361,626
Shareholders Equity				
Share capital	21	1,298,178	1,298,178	1,298,178
Accumulated earnings (deficit)		369,992	163,804	(112,817)
Reserves		21,994	22,881	19,906
Total shareholders equity		1,690,164	1,484,863	1,205,267
Total liabilities and shareholders equity		5,996,427	5,753,856	5,566,893

See accompanying notes to the consolidated financial statements

Telesat Holdings Inc.

Consolidated Statements of Cash Flows

For the year ended December 31

(in thousands of Canadian dollars)	September 30, Notes	September 30, 2011	September 30, 2010 (Note 5)
Cash flows from operating activities			
Net income		237,275	286,101
Adjustments to reconcile net income to cash flows from operating activities:			
Amortization and depreciation		239,647	247,651
Deferred tax expense	10	51,854	63,852
Unrealized foreign exchange loss (gain)		67,706	(170,016)
Unrealized loss (gain) on derivatives	23	(87,914)	13,955
Dividends on senior preferred shares	20	1,650	2,075
Share-based compensation	24	2,654	4,667
Loss (gain) on disposal of assets	8	1,483	(3,826)
Impairment loss on intangible assets	8	19,468	
Reversal of impairment loss on satellites, property and other equipment	8		(7,923)
Reversal of impairment loss on intangible assets	8		(71,269)
Insurance proceeds	8	(135,019)	
Other		(30,801)	(24,930)
Customer prepayments on future satellite services		57,768	30,982
Insurance proceeds		11,228	
Operating assets and liabilities	26	(13,113)	(29,815)
Net cash from operating activities		423,886	341,504
Cash flows used in investing activities			
Satellite programs		(356,199)	(257,725)
Purchase of other property and equipment		(17,566)	(3,966)
Purchase of intangible assets	29	(12,618)	
Insurance proceeds	8	135,019	
Proceeds from sale of assets		148	26,926
Net cash used in investing activities		(251,216)	(234,765)
Cash flows used in financing activities			
Repayment of indebtedness	19	(108,741)	(34,946)
Dividends paid on preferred shares		(10)	(30)
Satellite performance incentive payments		(5,928)	(5,099)
Net cash used in financing activities		(114,679)	(40,075)
Effect of changes in exchange rates on cash and cash equivalents		(324)	(558)
Increase in cash and cash equivalents		57,667	66,106
Cash and cash equivalents, beginning of year		220,295	154,189
Cash and cash equivalents, end of year	26	277,962	220,295

Supplemental disclosure of cash flow information		
Interest received	2,121	2,404
Interest paid	242,905	279,053
Income taxes paid	2,329	3,391

See accompanying notes to the consolidated financial statements

Telesat Holdings Inc.

Notes to the 2011 Consolidated Financial Statements

(all amounts in thousands of Canadian dollars, except for per share amounts and where otherwise noted)

1. BACKGROUND OF THE COMPANY

Telesat Holdings Inc. (the Company or Telesat) is a Canadian corporation. Telesat is a global fixed satellite services operator providing secure satellite-delivered communications solutions worldwide to broadcast, telecom, corporate and government customers. The Company has a fleet of 12 satellites plus the Canadian Ka-band payload on ViaSat-1 with two more satellites under construction. Telesat also manages the operations of additional satellites for third parties. Telesat is headquartered at 1601 Telesat Court, Ottawa, Ontario, Canada, KIB 5P4 with offices and facilities around the world.

On October 31, 2007, Canada s Public Sector Pension Investment Board (PSP Investments) and Loral Space & Communications Inc. (Loral), through a newly formed entity called Telesat Holdings Inc. completed the acquisition of Telesat Canada from BCE Inc. Loral and PSP Investments indirectly hold an economic interest in Telesat of 64% and 36%, respectively. Loral indirectly holds a voting interest of 33 1/3% on all matters including the election of directors. PSP Investments indirectly holds a voting interest of 66 2/3% on all matters except for the election of directors, and a 30% voting interest for the election of directors. The remaining voting interest of 36 2/3% for the election of directors is held by shareholders of the Company s director voting preferred shares.

2. BASIS OF PRESENTATION

Statement of Compliance

The consolidated financial statements were prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB). The Company, as a first-time adopter of IFRS, has followed the requirements of *IFRS 1* , *First-time Adoption of International Financial Reporting Standards* (IFRS 1). The first date on which IFRS was applied was January 1, 2010. The accounting policies described in note 3 were consistently applied to all the periods presented.

Approval of Financial Statements

These financial statements were approved by the Company s Board of Directors and authorized for issue on February 21, 2012.

Transition to International Financial Reporting Standards (IFRS)

The Company s consolidated financial statements were previously prepared in accordance with Canadian generally accepted accounting principles (Canadian GAAP). Canadian GAAP differs in some areas from IFRS. In preparing these consolidated financial statements, the Company has amended certain accounting and measurement methods previously applied in the Canadian GAAP financial statements to comply with IFRS. Note 5 of these consolidated financial statements contains reconciliations and descriptions of the impact of the transition from Canadian GAAP to IFRS on equity, income and comprehensive income as at December 31, 2010. Note 5 also has the January 1, 2010 reconciliation of shareholders equity. In addition the note discloses the reconciliation for the consolidated statement of income and consolidated statement of comprehensive income for the year ended December 31, 2010 and a line by line reconciliation of the consolidated balance sheets as at January 1, 2010 and December 31, 2010.

Basis of Consolidation

These consolidated financial statements include the results of the Company and subsidiaries controlled by the Company. Control is achieved when the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. The most significant wholly owned subsidiaries are listed in note 28.

3. SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements have been prepared on the historical cost basis except for financial instruments which are measured at fair values, as explained in the accounting policies below. Historical cost is based on the fair value of the consideration given in exchange for assets.

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Telesat Holdings Inc.

Notes to the 2011 Consolidated Financial Statements

(all amounts in thousands of Canadian dollars, except for per share amounts and where otherwise noted)

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Segment Reporting

The Company s operating segments are organized around the group s service lines, which represent the group s business activities. The operating segments are reported in a manner consistent with the internal reporting provided to the Company s Chief Operating Decision Maker (the CODM), who is the Company s Chief Executive Officer. To be reported, a segment is usually based on quantitative thresholds but can also encompass qualitative factors management deems significant. The Company operates in a single industry segment, in which it provides satellite-based services to its broadcast, enterprise and consulting customers around the world.

Foreign Currency Translation

Unless otherwise specified, all figures reported in the consolidated financial statements and associated note disclosures are presented in Canadian dollars, which is the functional and presentation currency of the Company. Each of the subsidiaries of the Company determines its own functional currency and uses that currency to measure items on its separate financial statements.

Upon consolidation of the Company s foreign operations having a functional currency other than the Canadian dollar, assets and liabilities are translated at the period-end exchange rate, and revenue and expenses are translated at average exchange rates for the period. Gains or losses on translation of foreign subsidiaries are recognized in other comprehensive income (OCI).

On the financial statements of the Company and its subsidiaries, foreign currency non-monetary assets and liabilities are translated at their historical exchange rates, foreign currency monetary assets and liabilities are translated at the period-end exchange rates, and foreign denominated revenue and expenses are translated at average exchange rates for the period. Gains or losses on translation of these items are recognized as a component of net income.

Cash and Cash Equivalents

All highly liquid investments with an original maturity of three months or less are classified as cash and cash equivalents. Cash and cash equivalents are comprised of cash on hand, demand deposits and short term investments. Restricted cash expected to be used within the next twelve months has been classified as cash and cash equivalents.

Revenue Recognition

Telesat recognizes revenue when earned, as services are rendered or as products are delivered to customers. Revenue is measured at the fair value of the consideration received or receivable. There must be clear evidence that an arrangement exists, the amount of revenue must be known or determinable and collectability must be reasonably assured. Revenue from a contract to sell services is recognized as follows:

Consulting revenue for cost plus contracts are recognized after the work has been completed and accepted by the customer.

The percentage of completion method is used for fixed price consulting revenue contracts. Percentage of completion is measured by comparing actual cost incurred to total cost expected.

Equipment sales revenue is recognized when the equipment is delivered to and accepted by the customer. Only equipment sales are subject to warranty or return and there is no general right of return.

Historically Telesat has not incurred significant expense for warranties and consequently no provision for warranty is recorded. When a transaction involves more than one product or service, revenue is allocated to each deliverable based on its relative fair value; otherwise, revenue is recognized as products are delivered or as services are provided over the term of the customer contract. When it is questionable whether or not Telesat is the principal in a transaction, the transaction is evaluated to determine whether it should be recorded on a gross or net basis.

Telesat Holdings Inc.

Notes to the 2011 Consolidated Financial Statements

(all amounts in thousands of Canadian dollars, except for per share amounts and where otherwise noted)

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Deferred Revenue

Deferred revenue represents the Company s liability for the provision of future services and is classified on the balance sheet in other current liabilities and other long-term liabilities. Deferred revenue consists of remuneration received in advance of the provision of service and is recognized in income on a straight-line basis over the term of the related customer contract.

Borrowing Costs

Borrowing costs are incurred on the Company s debt financing. Borrowing costs directly attributable to the acquisition, production or construction of a qualifying asset are added to the cost of that asset. The Company has defined a qualifying asset as an asset that takes longer than twelve months to get ready for its intended use or sale. Capitalization of borrowing costs continues until such time as the asset is substantially ready for its intended use or ready for sale. Borrowing costs are determined based on specific financing related to the asset or in the absence of specific financing, the borrowing costs are calculated on the basis of a capitalization rate which is equal to the Company s average cost of debt. All other borrowing costs are expensed in the period in which they are incurred.

Satellites, Property and Other Equipment

Satellites, property and other equipment, which are carried at cost, less accumulated depreciation and any accumulated impairment losses, include the contractual cost of equipment, capitalized engineering costs, and with respect to satellites, the cost of launch services, launch insurance and capitalized borrowing costs during construction.

Depreciation is calculated using the straight-line method over the respective estimated useful lives of the assets. The estimates of useful lives are reviewed at least annually and adjusted prospectively if necessary. Below are the estimated useful lives in years of satellites, property and other equipment as of December 31, 2011.

	September 30, Years	
Satellites	12	15
Property and other equipment	3	30

Construction in progress is not depreciated as depreciation only starts when the asset is ready for its intended use. For satellites, depreciation commences on the day the satellite becomes available for service and continues until the accumulated depreciation equals the amount of the cost.

Liabilities related to decommissioning and restoration of retiring property and equipment are measured at fair value with a corresponding increase to the carrying amount of the related asset. The liability is accreted over the period of expected cash flows with a corresponding charge to interest expense. The liabilities recorded to date have not been significant and are reassessed at the end of each reporting period. There are no decommissioning or restoration obligations for satellites.

In the event of an unsuccessful launch or total in-orbit satellite failure, all unamortized costs that are not recoverable under launch or in-orbit insurance are recorded as an operating expense.

Telesat Holdings Inc.

Notes to the 2011 Consolidated Financial Statements

(all amounts in thousands of Canadian dollars, except for per share amounts and where otherwise noted)

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

The investment in each satellite will be removed from the property accounts when the satellite has been fully depreciated and is no longer in service. When other property is retired from operations at the end of its useful life, the amount of the asset and accumulated depreciation are removed from the accounts. Earnings are credited with the amount of any net salvage and charged with any net cost of removal. When an item is sold prior to the end of its useful life, the gain or loss is recognized in income immediately.

Impairment of Long-Lived Assets

Tangible fixed assets and finite life intangible assets are assessed for impairment on a quarterly basis or more frequently when events or changes in circumstances indicate that the carrying value of assets exceeds the recoverable amount.

An impairment test consists of assessing the recoverable amount of an asset, which is the higher of its fair value less cost to sell and its value in use. If it is not practicable to estimate the recoverable amount for a particular asset, the Company determines the recoverable amount of the cash generating unit (CGU) with which it is associated. A cash generating unit is the smallest identifiable group of assets that generates cash inflows which are largely independent of the cash inflows from other assets or groups of assets.

The Company estimates value in use on the basis of the estimated future cash flows to be generated by an asset or CGU. These future cash flows are based on the Company s latest business plan information approved by senior management and are discounted using rates that best reflect the time value of money and the specific risks associated with the underlying asset or assets in the CGU.

The fair value less cost to sell is the amount obtainable from the sale of the asset or CGU in the course of an arm s length transaction between interested, knowledgeable and willing parties, less selling costs.

An impairment loss is the amount by which the carrying amount of an asset or CGU exceeds its recoverable amount. Impairment losses and reversals of impairment losses are recognized in Other operating gains (losses).

When an impairment loss subsequently reverses, the carrying amount of the asset (or CGU) is increased to the revised estimate of its recoverable amount, so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset (or CGU) in prior years. A reversal of an impairment loss is recognized immediately in Other operating gains (losses).

Deferred Satellite Performance Incentive Payments

Deferred satellite performance incentive payments are obligations payable to satellite manufacturers over the lives of certain satellites. The present value of the payments are capitalized as part of the cost of the satellite and recognized in income as part of the depreciation of the satellite.

Goodwill and Intangible Assets

The Company accounts for business combinations using the acquisition method of accounting, which establishes specific criteria for the recognition of intangible assets separately from goodwill. Goodwill represents the excess between the total of the consideration transferred over the fair value of net assets acquired. After initial recognition at cost, goodwill is measured at cost less any cumulative impairment charge. The Company distinguishes intangible assets between assets with finite and indefinite useful lives. Intangible assets with indefinite useful lives are comprised of the Company s trade name and orbital slots.

Telesat Holdings Inc.

Notes to the 2011 Consolidated Financial Statements

(all amounts in thousands of Canadian dollars, except for per share amounts and where otherwise noted)

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Finite life intangible assets, which are carried at cost less accumulated amortization, consist of revenue backlog, customer relationships, customer contract, concession rights, transponder rights and patents. Intangible assets with finite lives are amortized over their estimated useful lives using the straight-line method of amortization, except for revenue backlog which is based on the expected period of recognition of the related revenue.

	September 30, Years
Revenue backlog	4 to 17
Customer relationships	11 to 21
Customer contract	15
Concession rights	15
Transponder rights	6 to 14
Patents	18

The estimates of useful lives are reviewed every year and adjusted prospectively if necessary.

Impairment of Goodwill and Indefinite Life Intangible Assets

An assessment for impairment of goodwill and indefinite life intangible assets is performed annually, or more frequently whenever events or changes in circumstances indicate that the carrying amount of these assets are likely to exceed their recoverable amount, which is the higher of fair value less cost to sell and value in use. Goodwill is tested for impairment at the entity level as this represents the lowest level within the entity at which the goodwill is monitored for internal management purposes, and is not larger than an operating segment. Indefinite life intangibles have not been allocated to any CGU and are tested for impairment at the asset level.

An impairment test consists of assessing the recoverable amount of an asset, which is the higher of its fair value less cost to sell and its value in use.

Goodwill

In performing the goodwill impairment analysis, the Company uses the income approach as well as the market approach in the determination of the fair value of goodwill at the entity level. Under the income approach, the sum of the projected discounted cash flows for the next five years in addition to a terminal value are used to determine the fair value at the entity level. In this model, significant assumptions used include: revenue, expenses, capital expenditures, working capital, terminal growth rate and discount rate.

Under the market based approach, the fair value of the reporting unit is determined based on market multiples derived from comparable public companies. As part of that analysis, assumptions are made regarding comparability of selected companies including revenue, earnings before interest, taxes, depreciation and amortization multiples for valuation purposes, growth rates, size and overall profitability.

Under both approaches, all assumptions used in the model, with the exception of the discount rate, are based on management s best estimates. The discount rates are consistent with external sources of information.

Trade name

For the purposes of impairment testing, the fair value of the trade name was determined using an income approach, specifically the relief from royalties method. The relief from royalty method is comprised of two major steps: i) a determination of the hypothetical royalty rate, and ii) the subsequent application of the royalty rate to projected revenue. In determining the hypothetical royalty rate in the relief from royalty approach, the Company considered comparable license agreements, operating earnings benchmark rule of thumb, an excess earnings analysis to determine aggregate intangible asset earnings, and other qualitative factors. The key assumptions used included the tax rate and discount rate.

Telesat Holdings Inc.

Notes to the 2011 Consolidated Financial Statements

(all amounts in thousands of Canadian dollars, except for per share amounts and where otherwise noted)

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Orbital slots

In performing the orbital slots impairment analysis, the Company estimated fair value using the build up method to determine the cash flows for the income approach, with the resulting projected cash flows discounted at an appropriate weighted average cost of capital. In instances where the build up method did not generate positive value for an orbital slot, but the orbital slot was expected to generate revenue, a value was assigned based upon independent source data for recent transactions of similar orbital slots.

Under the build up approach, the amount an investor would be willing to pay for an orbital slot to operate a satellite business is calculated by first estimating the cash flows that typical market participants would assume could be available from the operation of satellites using the subject slot in a similar market. It was assumed that rather than acquiring such a business as a going concern, the buyer would hypothetically obtain a slot and build a new operation with similar attributes from scratch. Thus the buyer or builder is considered to incur the start-up costs and losses typically associated with the going concern value and pay for all other tangible and intangible assets.

The key assumptions used in estimating the recoverable amounts of the orbital slots included i) market penetration leading to revenue growth, ii) profit margin, iii) duration and profile of the build up period, iv) estimated start-up costs and losses incurred during the build up period and v) the weighted average cost of capital.

Financial Instruments

Telesat uses derivative financial instruments to manage its exposure to foreign exchange rate risk associated with anticipated purchases and with debt denominated in foreign currencies, as well as to reduce its exposure to interest rate risk associated with debt. Currently, Telesat does not designate any of its derivative financial instruments as hedging instruments for accounting purposes. All realized and unrealized gains and losses on these derivative financial instruments are recorded in the statement of income and included as part of gain (loss) on changes in fair value of financial instruments.

Financial assets and financial liabilities that are classified as held-for-trading (HFT) are measured at fair value. The unrealized gains and losses relating to the HFT assets and liabilities are recorded in the consolidated statement of income included in gain (loss) on changes in fair value of financial instruments. Loans and receivables and other liabilities are recorded at amortized cost in accordance with the effective interest rate method.

Derivatives, including embedded derivatives that must be separately accounted for, are recorded at fair value on the consolidated balance sheet at inception and marked to market at each reporting period thereafter. Derivatives embedded in other financial instruments are treated as separate derivatives when their risk and characteristics are not closely related to those of the host contract and the host contract is measured separately according to its characteristics.

The Company accounts for embedded foreign currency derivatives in a host contract as a single instrument where the contract requires payments denominated in the currency that is commonly used in contracts to procure non-financial items in the economic environment in which Telesat transacts.

Transaction costs for financial instruments classified as HFT are expensed as incurred. Transaction costs that are directly attributable to the acquisition of the financial assets and financial liabilities (other than HFT) are added or deducted from the fair value of the financial asset and financial liability on initial recognition.

Financing Costs

The debt issuance costs related to the revolving Canadian dollar denominated credit facility and the Canadian term loan facility are accounted for as short-term and long-term deferred charges and included in Prepaid expenses and other current assets and Other long-term assets. The deferred charges are amortized to interest expense on a straight-line basis. All other debt issuance costs are amortized to interest expense using the effective interest method.

Telesat Holdings Inc.

Notes to the 2011 Consolidated Financial Statements

(all amounts in thousands of Canadian dollars, except for per share amounts and where otherwise noted)

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Employee Benefit Plans

Telesat maintains one contributory and three non-contributory defined benefit pension plans which provide benefits based on length of service and rate of pay. Telesat is responsible for adequately funding these defined benefit pension plans. Contributions are made based on actuarial cost methods that are permitted by pension regulatory bodies and reflect assumptions about future investment returns, salary projections and future service benefits. Telesat also provides other post-employment and retirement benefits, including health care and life insurance benefits on retirement and various disability plans, workers compensation and medical benefits to former or inactive employees, their beneficiaries and covered dependents, after employment but before retirement, under certain circumstances. The Company accrues the present value of its obligations under employee benefit plans and the related costs, adjusted for any unrecognized past service cost and reduced by the fair value of plan assets. Any asset resulting from this calculation is limited to any unrecognized past service cost plus the present value of available refunds and reductions in future contributions to the plan. Pension costs and other retirement benefits are determined using the projected benefit method prorated on service and management s best estimate of expected investment performance, salary escalation, retirement ages of employees and expected health care costs.

Pension plan assets are valued at fair value which is also the basis used for calculating the expected rate of return on plan assets. The discount rate is based on the market interest rate of high quality bonds as determined in accordance with guidance described by the Canadian Institute of Actuaries in an Educational Note dated September 2011. Past service costs arising from plan amendments are recognized immediately to the extent that the benefits are already vested, and otherwise are amortized on a straight-line basis over the average remaining vesting period. All actuarial gains and losses are recognized immediately in other comprehensive income in the period in which they occur and recognized in accumulated earnings (deficit). A valuation is performed at least every three years to determine the present value of the accrued pension and other retirement benefits. The 2010 pension expense calculations are extrapolated from a valuation performed as of January 1, 2007 while the 2011 pension expense calculations are extrapolated from the calculation performed as of January 1, 2010. The accrued benefit obligation is extrapolated from an actuarial valuation as of January 1, 2010. The most recent valuation of the pension plans for funding purposes was as of January 1, 2011, and the next required valuation is as of January 1, 2012.

In addition, Telesat provides certain health care and life insurance benefits for retired employees. These benefits are funded primarily on a pay-as-go basis, with the retiree generally paying a portion of the cost through contributions, deductibles and co-insurance provisions. Payments to defined contribution retirement benefit plans are recognized as an expense when employees have rendered service entitling them to the contributions.

Share-Based Compensation Plan

The Company offers an equity-settled share-based incentive plan for certain key employees under which it receives services from employees in exchange for equity instruments of the Company. The expense is based on fair value of the awards granted using the Black-Scholes option pricing model. The expense is recognized over the vesting period, which is the period over which all of the specified vesting conditions are satisfied, with a corresponding increase in equity. For awards with graded vesting, the fair value of each tranche is recognized over the respective vesting period.

Telesat Holdings Inc.

Notes to the 2011 Consolidated Financial Statements

(all amounts in thousands of Canadian dollars, except for per share amounts and where otherwise noted)

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

Inventory

Inventories are valued at lower of cost and net realizable value and consist of finished goods and work in process. Cost for substantially all network equipment inventories is determined on a weighted average cost basis. Cost for work in process and certain one-of-a-kind finished goods is determined using the specific identification method.

Income Taxes

Current income tax is measured at the amount expected to be paid to the taxation authorities, net of recoveries, based on the tax rates and laws enacted or substantively enacted at the balance sheet date.

Income tax expense, comprised of current and deferred income tax, is recognized in income except to the extent it relates to items recognized in other comprehensive income or equity, in which case the income tax expense is recognized in other comprehensive income or equity, respectively.

Deferred taxes are the result of temporary differences arising between the tax bases of assets and liabilities and their carrying amount. Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period where the asset is realized or the liability is settled, based on tax rates and laws that have been enacted or substantively enacted at the balance sheet date.

Deferred tax assets are recognized for all deductible temporary differences to the extent that it is probable that taxable profit will be available against which the deductible temporary difference can be utilized.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that the deferred tax assets will be realized. Unrecognized deferred tax assets are reassessed at each balance sheet date and recognized to the extent that it has become probable that future taxable profit will allow the deferred tax assets to be recovered.

Deferred tax liabilities are recognized for all taxable temporary differences except when the deferred tax liability arises from the initial recognition of goodwill or the initial recognition of an asset or liability in a transaction which is not a business combination. For taxable temporary differences associated with investments in subsidiaries, a deferred tax liability is recognized unless the parent can control the timing of the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

Future Changes in Accounting Policies

The IASB recently issued a number of new accounting standards. The new standards determined to be applicable to the Company are disclosed below. The remaining standards have been excluded as they are not applicable.

Financial instruments

IFRS 9, *Financial Instruments* (IFRS 9) was issued by the International Accounting Standards Board (IASB) on October 28, 2010, and will replace IAS 39, *Financial Instruments: Recognition and Measurement* (IAS 39). IFRS 9 uses a single approach to determine whether a financial asset is measured at amortized cost or fair value, replacing multiple rules in IAS 39. The approach in IFRS 9 is based on how an entity manages its financial instruments in the context of its business model and the contractual cash flow characteristics of the financial assets. Two measurement categories continue to exist to account for financial liabilities in IFRS 9, fair value through profit or loss (FVTPL) and amortized

cost. Financial liabilities held for trading are measured at FVTPL, and all other financial liabilities are measured at amortized cost unless the fair value option is applied. The treatment of embedded derivatives under the new standard is consistent with IAS 39 and is applied to financial liabilities and non-derivative hosts not within the scope of this standard.

Telesat Holdings Inc.

Notes to the 2011 Consolidated Financial Statements

(all amounts in thousands of Canadian dollars, except for per share amounts and where otherwise noted)

3. SIGNIFICANT ACCOUNTING POLICIES (continued)

IFRS 9 is effective for annual periods beginning on or after January 1, 2015. The Company is currently evaluating the impact of IFRS 9 on its consolidated financial statements.

Accounting for post employment benefits

On June 16, 2011, the IASB issued the amended version of IAS 19, *Employee Benefits* (IAS 19). The amendments make changes in eliminating the accounting option to defer the recognition of actuarial gains and losses, streamlining the presentation of changes in assets and liabilities arising from defined benefit plans as well as amendments to disclosure requirements. Changes in the defined benefit obligation and plan assets are disaggregated into three components: service costs, net interest on the net defined benefit obligation (asset) and remeasurements of the net defined benefit obligation (asset). The revised standard is effective for annual periods beginning on or after January 1, 2013 with earlier application permitted. The Company is currently evaluating the impact of revised IAS 19 on its consolidated financial statements.

Fair value measurement and disclosure requirements

IASB issued IFRS 13, *Fair value measurement* (IFRS 13) on May 12, 2011. IFRS 13 provides guidance on how fair value measurement should be applied whenever its use is already required or permitted by other standards within IFRS. IFRS 13 is effective for annual periods beginning on or after January 1, 2013 with earlier application permitted. The Company is currently evaluating the impact of revised IFRS 13 on its consolidated financial statements.

4. CRITICAL ACCOUNTING JUDGMENTS AND ESTIMATES

Critical judgments in applying accounting policies

The following are the critical judgments made in applying the Company s accounting policies which have the most significant effect on the amounts reported in the financial statements:

Revenue recognition

The Company s accounting policy relating to revenue recognition is described in note 3. The percentage of completion method is used for fixed price consulting revenue contracts and requires judgment by management to determine the appropriateness of using the method for revenue recognition as this method requires the ability to accurately estimate costs incurred and accurately estimate costs required to complete contracts.

Uncertain income tax positions

The Company operates in numerous jurisdictions and is subject to country-specific tax laws. Management uses significant judgment when determining the worldwide provision for tax and estimates provisions for uncertain tax positions as the amounts expected to be paid based on a qualitative assessment of all relevant factors. In the assessment, management considers risk with respect to tax matters under active discussion, audit, dispute or appeal with tax authorities, or which are otherwise considered to involve uncertainty. Management reviews the provisions at each balance sheet date.

IFRIC 4 Determining whether an arrangement contains a lease

The Company assesses for each new arrangement whether it contains a lease based on IFRIC 4. The determination of whether an arrangement is, or contains a lease, is based on the substance of the arrangement at inception date or whether the fulfillment of the arrangement is dependent on the use of a specific asset or assets or the arrangement conveys a right to use the asset. If contracts contain a lease arrangement, the leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

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Telesat Holdings Inc.

Notes to the 2011 Consolidated Financial Statements

(all amounts in thousands of Canadian dollars, except for per share amounts and where otherwise noted)

4. CRITICAL ACCOUNTING JUDGMENTS AND ESTIMATES (continued)

Critical accounting estimates and assumptions

The Company makes accounting estimates and assumptions that affect the carrying value of assets and liabilities, reported net income and disclosure of contingent assets and liabilities. Estimates and assumptions are based on historical experience, current events and other relevant factors, therefore, actual results will differ and could be material. The accounting estimates and assumptions critical to the determination of the amounts reported in the financial statements are as follows:

Derivative financial instruments measured at fair value

Derivative financial assets and liabilities measured at fair value were $134.4 million and $213.5 million at December 31, 2011 (December 31, 2010 $72.4 million and $244.5 million, January 1, 2010 $15.9 million and $185.3 million). Quoted market values are unavailable for the Company s financial instruments and in the absence of an active market, the Company determines fair value for financial instruments based on prevailing market rates (bid and ask prices, as appropriate) for instruments with similar characteristics and risk profiles or internal or external valuation models, such as option pricing models and discounted cash flow analysis, using observable market-based inputs. The determination of fair value is affected significantly by the assumptions used for the amount and timing of estimated future cash flows and discount rates. As a result, the fair value of financial assets and liabilities and the amount of gains or losses on changes in fair value recorded to net income could vary.

Impairment of goodwill

Goodwill represents approximately $2.4 billion of total assets at December 31, 2011 and at each of the prior balance sheet dates. Determining whether goodwill is impaired requires an estimation of the Company s value. The Company s value requires management to estimate the future cash flows expected to arise from operations and to make assumptions regarding economic factors, tax rates, and annual growth rates. Actual operating results and the related cash flows of the Company could differ from the estimates used for the impairment analysis.

Impairment of intangible assets

Intangible assets represent approximately $896 million of total assets at December 31, 2011 (December 31, 2010 $946 million, January 1, 2010 $926 million). Impairment of intangible assets is tested annually or more frequently if indicators of impairment exist. The impairment analysis requires the Company to estimate the future cash flows expected to arise from operations and to make assumptions regarding economic factors, discount rates, tax rates, and annual growth rates. Actual operating results and the related cash flows of the Company could differ from the estimates used for the impairment analysis.

Where an impairment loss subsequently reverses, the carrying amount of the CGU or individual asset is increased to the revised estimate of its recoverable amount, so long as the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the CGU or individual asset in prior years.

The reversal of an impairment requires management to re-assess several indicators that led to the impairment. It requires the valuation of the recoverable amount by estimating the future cash flows expected to arise from the CGU or individual asset and the determination of a suitable discount rate in order to calculate its present value. Significant judgment is made in establishing these assumptions.

Employee Benefit

The cost of defined benefit pension plans and other post employment medical benefits and the present value of the pension obligation are determined using actuarial valuations. An actuarial valuation involves making various assumptions which may differ from actual developments in the future. These include the determination of the discount rate, future salary increases, mortality rates, future pension increases and return on plan assets. Due to the complexity of the valuation, the underlying assumptions, and its long term nature, a defined benefit obligation is highly sensitive to changes in these assumptions. All assumptions are reviewed at each reporting date.

Telesat Holdings Inc.

Notes to the 2011 Consolidated Financial Statements

(all amounts in thousands of Canadian dollars, except for per share amounts and where otherwise noted)

4. CRITICAL ACCOUNTING JUDGMENTS AND ESTIMATES (continued)

Determination of useful life of satellites and finite life intangible assets

The estimated useful life and depreciation method for satellites and finite life intangible assets are reviewed at the end of each reporting period, with the effect of any changes in estimate being accounted for on a prospective basis. Any change in these estimates may have a significant impact on the amounts reported.

Income taxes

Management assesses the recoverability of deferred tax assets based upon an estimation of the Company s projected taxable income using existing tax laws, and its ability to utilize future tax deductions before they expire. Actual results could differ from expectations.

5. TRANSITION TO IFRS

The Company adopted IFRS on January 1, 2011 with a transition date of January 1, 2010 (the opening balance sheet). Prior to the adoption of IFRS the Company prepared its consolidated financial statements in accordance with previous Canadian GAAP and applied Part V of the Canadian Institute of Chartered Accountants handbook. The Company s consolidated financial statements for the year ended December 31, 2011 are the first annual consolidated financial statements that comply with IFRS and these consolidated financial statements were prepared as described in note 2, including the application of IFRS 1. IFRS 1 provides for certain mandatory exceptions and provides for certain elective exemptions for first time adopters. These consolidated financial statements have been prepared in accordance with those IFRS standards and International Financial Reporting Interpretation Committee (IFRIC) interpretations issued and effective or issued and early adopted as at the timing of preparing these consolidated financial statements.

Initial elections upon adoption of IFRS 1

The basic principles of IFRS 1 assume that on the initial adoption of IFRS standards, these will be applied retrospectively as if the standards had been applied and effective from the date of inception. However, the IASB has determined that retrospective application in certain situations cannot be performed with sufficient reliability or significant cost. Therefore, IFRS 1 offers mandatory exceptions and elective exemptions to facilitate conversion from Canadian GAAP to IFRS. Below are the mandatory exceptions and elective exemptions applicable to the Company.

A. Mandatory exceptions

Estimates

The estimates made in the opening IFRS balance sheet reflect conditions that existed at the date of the underlying transaction or January 1, 2010, as required by each specific IFRS standard. Hindsight was not used to create or revise estimates. All estimates used in the preparation of the opening balance sheet reflect the facts and circumstances at the date of the underlying transaction or January 1, 2010, as may be the case.

B. Elective exemptions

Business combinations

IFRS 1 provides the Company with the option to apply IFRS 3R, *Business Combinations* , retrospectively or prospectively from the transition date of January 1, 2010. The retrospective application requires the restatement of business combinations that occurred prior to the transition date. The Company elected to apply IFRS 3R prospectively to business combinations that occurred on or after the date of transition of January 1, 2010.

Telesat Holdings Inc.

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5. TRANSITION TO IFRS (continued)

Fair value or revaluation as deemed cost

IFRS 1 provides an exemption to measure property, plant and equipment, intangible assets, and investment property at its fair value and use that fair value as its deemed cost at that date and an exemption to use a previous Canadian GAAP revaluation as deemed cost if it is comparable to fair value or reflects the cost or depreciated cost under IFRS. If no election is made, retrospective application is required in accordance with IAS 16, *Property, Plant and Equipment* , IAS 38, *Intangible Assets* , and IAS 40, *Investment Property* . The Company has elected to use a previous Canadian GAAP revaluation as deemed cost. The previous revaluation was required as part of the October 31, 2007 acquisition of Telesat Canada and Loral Skynet. This election had no impact on the Company s opening balance sheet.

Employee benefits

IFRS 1 provides the option to retrospectively apply the corridor approach under IAS 19, *Employee Benefits* , for the recognition of actuarial gains and losses, or alternatively recognize all cumulative actuarial gains and losses deferred under Canadian GAAP in opening accumulated deficit at the transition date. The Company has elected to recognize all cumulative actuarial gains and losses in opening accumulated deficit for all of its employee benefit plans at the date of transition. This election resulted in a decrease to other long-term assets of $15.4 million, a decrease to deferred tax liability of $3.5 million, a decrease to other long-term liabilities of $1.4 million and an increase to accumulated deficit of $10.5 million.

Cumulative currency translation differences

IFRS 1 permits cumulative translation gains and losses to be reset to zero at the transition date. The Company has elected to reset all cumulative translation gains and losses to zero in opening accumulated deficit at January 1, 2010. The impact was a decrease in accumulated other comprehensive loss of $7.4 million and an increase to accumulated deficit of $7.4 million after adjusting for changes in functional currency as determined under IAS 21, *The Effects of Changes in Foreign Exchange Rates* . There was no impact to the shareholders equity.

Borrowing costs

IAS 23, *Borrowing Costs* , requires an entity to capitalize the borrowing costs related to all qualifying assets. IFRS 1 allows the Company the option to apply this standard retrospectively or prospectively from the date of transition. The Company has elected to apply IAS 23 prospectively.

Leases

IFRS 1 provides the option to apply the transitional provisions under IFRIC 4, *Determining whether an Arrangement contains a Lease* , to determine whether an arrangement contains a lease on the basis of facts and circumstances existing at the date of transition. The Company has made this election in its evaluation of contracts existing at the transition date. As a result of the application of IFRIC 4, management determined that certain agreements were incorrectly accounted for as leases under Canadian GAAP. These immaterial errors were corrected as part of the IFRS transition as permitted under IFRS 1 with prior periods adjusted in these financial statements and the agreements are now accounted for as service agreements which do not contain a lease under IFRIC 4. The impact to the opening balance sheet was a decrease in satellite, property and other equipment of $19.5 million, a decrease to other current liabilities of $3.5 million, a decrease to other long-term liabilities of $17.8 million, a decrease to deferred tax liability of $6.1 million and a decrease to opening accumulated deficit of $7.9 million.

C. Reconciliation of Canadian GAAP to IFRS

The following represents the reconciliations from Canadian GAAP to IFRS for the respective periods noted for shareholders equity, net income and total comprehensive income. The first-time adoption of IFRS did not have a material impact on total operating, investing or financing cash flows.

Telesat Holdings Inc.

Notes to the 2011 Consolidated Financial Statements

(all amounts in thousands of Canadian dollars, except for per share amounts and where otherwise noted)

5. TRANSITION TO IFRS (continued)

Reconciliation of Shareholders Equity

As at	September 30, December 31, 2010	September 30, January 1, 2010
Shareholders equity under Canadian GAAP	1,132,325	897,296
Differences increasing (decreasing) reported shareholders equity[(a)] :		
1. Impairment Tangible assets		(5,921)
2. Impairment Intangible assets	365,183	312,725
3. Employee benefits	(20,100)	(10,489)
4. Foreign currency translation	1,634	3,745
5. Share based compensation		
6. Leases	5,821	7,911
Total shareholder s equity under IFRS	**1,484,863**	**1,205,267**

(a) Differences increasing (decreasing) reported shareholders equity are disclosed net of tax.

Reconciliation of Net Income

	September 30, For the year ended December 31, 2010
Net income under Canadian GAAP	228,191
Differences increasing (decreasing) reported net income:	
1. Impairment Tangible assets	7,924
2. Impairment Intangible assets	71,269
3. Employee benefits	(192)
4. Foreign currency translation	(32)
5. Share based compensation	987
6. Leases	68
7. Income taxes	(22,114)
Total net income under IFRS	**286,101**

Reconciliation of Comprehensive Income

	September 30, For the year ended December 31, 2010
Comprehensive income under Canadian GAAP	229,406
Differences increasing (decreasing) reported comprehensive income:	
Differences in net income	57,910
Foreign currency translation adjustment	(2,907)
Actuarial loss on defined benefit plans	(9,450)
Comprehensive income under IFRS	274,959

D. Changes in accounting policies from Canadian GAAP to IFRS

In addition to the mandatory exceptions and elective exemptions for retrospective application of IFRS, the following narratives explain the significant differences, as identified in the tables above, between previously adopted Canadian GAAP accounting policies and the current IFRS accounting policies adopted by the Company.

(1) Impairment Tangible assets

A recoverability test, under Canadian GAAP, is a two step process whereby the first test is performed by comparing the undiscounted cash flows expected to be generated from the asset to its carrying amount. If the asset does not recover its carrying value, an impairment loss is determined as the excess of the asset s carrying amount over its fair value. Fair value is calculated as the present value of expected cash flows derived from the asset.

Telesat Holdings Inc.

Notes to the 2011 Consolidated Financial Statements

(all amounts in thousands of Canadian dollars, except for per share amounts and where otherwise noted)

5. TRANSITION TO IFRS (continued)

The impairment test under IAS 36, *Impairment of Assets* , is a one step process whereby impairment is calculated as the excess of the asset s carrying amount over its recoverable amount. The recoverable amount is the higher of the asset s fair value less cost to sell and its value in use. Value in use is defined as the present value of the future cash flows expected to be derived from the asset. As a result of the differences in measurement, the Company recognized an impairment under IFRS, on the transition date, as the carrying amount of a certain satellite was in excess of its value in use.

The impairment resulted in the following adjustments to the opening IFRS balance sheet: a reduction to satellites, property and other equipment of $7.9 million, a reduction to deferred tax liability of $2.0 million and an increase in opening accumulated deficit of $5.9 million. The impairment recorded on the transition date was subsequently reversed in 2010 due to changes in revenue assumptions.

(2) Impairment Intangible assets

Impairment losses cannot be reversed under Canadian GAAP.

IFRS requires impairment losses other than those related to goodwill, to be reversed if certain criteria are met in accordance with IAS 36, *Impairment of Assets* . As a result, the Company reversed an impairment relating to its orbital slot intangible assets at the transition date. The reversal of the impairment was mainly the result of the variations in the discount rate applied. The reversal resulted in an increase to intangible assets of $411.6 million, an increase to deferred tax liability of $98.9 million and a decrease to opening accumulated deficit of $312.7 million on the opening IFRS balance sheet.

At the end of 2010 the impairment reversal resulted in an increase to intangible assets of $483.0 million, an increase to deferred tax liability of $117.8 million and an increase in accumulated earnings of $365.2 million. In the 2010 statement of income under IFRS compared to Canadian GAAP an additional $71.3 million of other operating gains was recorded, reduced by additional tax expense of $18.8 million.

(3) Employee benefits actuarial gains and losses

Under Canadian GAAP actuarial gains and losses arising from the calculation of the present value of the defined benefit obligation and the fair value of plan assets are recognized on a systematic and consistent basis, subject to a minimum required amortization based on a corridor approach. The corridor was 10% of the greater of the accrued benefit obligation and the fair value of plan assets at the beginning of the year. The excess of 10% is amortized as a component of pension expense on a straight-line basis over the expected average remaining service period of active participants. Actuarial gains and losses below the 10% corridor are deferred.

Under IFRS, the Company elected to recognize all actuarial gains and losses immediately in other comprehensive income without recycling to the income statement in subsequent periods. As a result, actuarial gains and losses are not amortized to the statement of income but instead recorded directly to other comprehensive income at the end of each period.

The recognition of actuarial gains and losses as per the opening IFRS balance sheet date resulted in a decrease to other long-term assets of $15.4 million, a decrease of $1.4 million to other long-term liabilities, a decrease to deferred tax liabilities of $3.5 million and a corresponding increase to accumulated deficit of $10.5 million. The change in accounting policy regarding the recognition of actuarial gains and losses had the following impact on the December 31, 2010 balance sheet: a decrease to other long-term assets of $29.5 million, a decrease of $2.6 million to other long-term liabilities, a decrease to deferred tax liabilities of $6.8 million and a corresponding decrease to accumulated earnings of $20.1 million. The operating expense increased by $0.2 million in 2010 under IFRS compared to Canadian GAAP as a result of the different accounting policies. The impact on the 2010 other comprehensive income resulted in a decrease of $9.5 million.

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Notes to the 2011 Consolidated Financial Statements

(all amounts in thousands of Canadian dollars, except for per share amounts and where otherwise noted)

5. TRANSITION TO IFRS (continued)

(4) Foreign currency translation

Under Canadian GAAP, foreign currency translation of subsidiaries depends on the criteria provided in determining self-sustaining foreign operations and integrated foreign operations.

IFRS requires each entity in a consolidated group to determine its functionally currency in isolation in accordance with primary and secondary indications. As a result of this difference, certain subsidiaries that were previously accounted for as integrated foreign operations under Canadian GAAP were revised to have their functional currency as a foreign currency. The impact on the transition date was an increase to satellites, property and other equipment of $0.1 million, a $3.6 million increase to intangible assets, a $0.8 million reduction in accumulated other comprehensive loss and a $2.9 million reduction of accumulated deficit. The resulting foreign currency translation adjustment was then cleared to accumulated deficit using the IFRS 1 exemption for IAS 21.

The impact on the December 31, 2010 balance sheet was an increase to satellites, property and other equipment of $0.1 million, a $1.5 million increase to intangible assets, a $0.8 million reduction in accumulated other comprehensive loss and a $0.8 million increase of accumulated earnings. The difference in foreign currency translation of subsidiaries between IFRS and Canadian GAAP resulted in a decrease of gain (loss) on foreign exchange of $0.03 million in the 2010 statement of income. Other comprehensive income decreased by $2.9 million as a result of the foreign currency translation difference.

(5) Share-based compensation

The Company has equity-settled share-based compensation transactions with certain key employees. The vesting conditions embedded in these compensation plans are time and performance based. Under Canadian GAAP, the total fair value of these awards is recognized on a straight line basis throughout the vesting period.

Under IFRS, each tranche of the option grant is considered a separate grant and fair value is determined for each tranche of the option grant. As a result of this difference, the Company recorded a transitional adjustment to its opening IFRS balance sheet which resulted in an increase to reserves of $8.8 million and an increase to accumulated deficit of $8.8 million, with no overall impact on net equity. The Company recorded an adjustment to its December 31, 2010 balance sheet which resulted in an increase to reserves of $7.8 million and a decrease to accumulated earnings of $7.8 million, with no overall impact on net equity. The operating expense decreased by $1.0 million in the 2010 statement of income under IFRS compared to Canadian GAAP.

(6) Leases

As a result of the application of IFRIC 4, management determined that certain agreements were incorrectly accounted for as leases under Canadian GAAP. These immaterial errors were corrected as part of the IFRS transition as permitted under IFRS 1 with prior periods adjusted in these consolidated financial statements and the agreements are now accounted for as service agreements under IFRIC 4. The impact to the opening balance sheet was a decrease in satellites, property and other equipment of $19.5 million, a decrease to other current liabilities of $3.5 million, a decrease to other long-term liabilities of $17.8 million, a decrease to deferred tax liability of $6.1 million and a decrease to opening accumulated deficit of $7.9 million. The impact to the December 31, 2010 balance sheet was a decrease in satellites, property and other equipment of $15.4 million, a decrease to other current liabilities of $3.6 million, a decrease to other long-term liabilities of $13.2 million, a decrease to deferred tax liability of $4.4 million and an increase to accumulated earnings of $5.8 million. The difference between IFRS and Canadian GAAP resulted in an increase of $5.2 million of operating expenses, decrease of $3.4 million of depreciation, decrease of $1.7 million of net interest expense and an increase of tax expense of $1.2 million in the 2010 statement of income.

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Telesat Holdings Inc.

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(all amounts in thousands of Canadian dollars, except for per share amounts and where otherwise noted)

5. TRANSITION TO IFRS (continued)

(7) Income taxes

Differences for income taxes represent the effect of recording, where applicable, the deferred tax impact of other differences between Canadian GAAP and IFRS.

E. Presentation and Reclassification Differences

Consolidated Balance Sheet

Aggregation / disaggregation of balance sheet line items

i. Under Canadian GAAP, common shares, preferred shares, accumulated other comprehensive loss, and contributed surplus were presented separately. Under IFRS, common shares and preferred shares have been aggregated into the line item share capital while accumulated other comprehensive loss and contributed surplus have been aggregated into the line item reserves.

ii. For Canadian GAAP presentation, various balance sheet accounts were aggregated. IFRS has certain minimum presentation requirements for the balance sheet and as a result additional balance sheet line items were presented.

Reclassification of pension asset / liability

Under Canadian GAAP there was an asset recorded related to the post employment benefit plans. Upon transition to IFRS, all cumulative actuarial gains or losses deferred under Canadian GAAP were recognized in opening accumulated deficit as of the date of transition to IFRS and subsequently recognized in other comprehensive income. As a result of this accounting difference, the net amount related to the post employment benefit plans represents a liability under IFRS.

Tax reclassification

Under Canadian GAAP, deferred taxes were classified as current and non-current on the basis of either the underlying asset or the liability or the expected reversal of items not related to an asset or liability. For IFRS purposes, all deferred tax assets and liabilities are classified as non-current. All deferred tax assets and liabilities are netted.

Reclassification of Derivatives

Under Canadian GAAP the derivatives were categorized between current and non-current based on maturity. For IFRS purposes derivatives are separated into a current and non-current portion based on an assessment of the facts and circumstances (i.e. the underlying contracted cash flows).

Consolidated Statement of Income

Aggregation / disaggregation of statement of income line items

i. Under Canadian GAAP, revenue was presented for service revenue and equipment sales revenue. Under IFRS, the revenue streams are presented as a single line revenue.

ii. Under Canadian GAAP, the consolidated statement of income presented amortization for the depreciation of satellites, property and other equipment and intangible assets as one line item. For IFRS the expenses were disaggregated to present 1) depreciation of satellites, property and other equipment (depreciation) and 2) amortization of intangible assets (amortization).

iii. Under Canadian GAAP, cost of equipment sales and other income were presented separately from operations and administration expenses. Under IFRS, the consolidated statement of income combines those expenses and presents one line item operating expenses.

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Notes to the 2011 Consolidated Financial Statements

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5. TRANSITION TO IFRS (continued)

iv. Under Canadian GAAP, interest income and expenses were presented as one line item interest expense. For IFRS presentation interest expense is disaggregated to present 1) interest expense and 2) interest and other income.

F. Adjusted Telesat Holdings Inc. financial statements

The following are reconciliations of the financial statements previously presented under Canadian GAAP to the consolidated financial statements prepared under IFRS.

Reconciliation of Consolidated Balance Sheet as of December 31, 2010

Canadian GAAP accounts	Canadian GAAP balance	IFRS adjustments	IFRS reclassifications	IFRS balance	IFRS accounts
Current assets					**Assets**
Cash and cash equivalents	220,295			220,295	Cash and cash equivalents
Accounts receivable, net	44,109		(26)	44,083	Trade and other receivables
Current future tax asset	1,900		5,044	6,944	Other current financial assets
Other current assets	26,476		(5,539)	20,937	Prepaid expenses and other current assets
Total current assets	**292,780**		**(521)**	**292,259**	**Total current assets**
Satellites, property and other equipment, net	1,994,122	(15,333		1,978,789	Satellites, property and other equipment
			78,631	78,631	Other long-term financial assets
Other long-term assets	112,816	(29,487)	(71,302)	12,027	Other long-term assets
Intangible assets, net	461,060	484,487		945,547	Intangible assets
Goodwill	2,446,603			2,446,603	Goodwill
Total assets	**5,307,381**	**439,667**	**6,808**	**5,753,856**	**Total assets**
Liabilities					**Liabilities**
Current liabilities					
Accounts payable and accrued liabilities	49,906	68		49,974	Trade and other payables
			104,082	104,082	Other current financial liabilities
Other current liabilities	128,296	(3,657)	(61,994)	62,645	Other current liabilities
Debt due within one year	96,848			96,848	Current indebtedness
Total current liabilities	**275,050**	**(3,589)**	**42,088**	**313,549**	**Total current liabilities**
Debt financing	2,771,802			2,771,802	Long-term indebtedness
Future tax liability	310,552	106,565	(2,400)	414,717	Deferred tax liabilities
			265,629	265,629	Other long-term financial liabilities
Other long-term liabilities	676,217	(15,847)	(298,509)	361,861	Other long-term liabilities
Senior preferred shares	141,435			141,435	Senior preferred shares
Total liabilities	**4,175,056**	**87,129**	**6,808**	**4,268,993**	**Total liabilities**
Shareholders equity					**Shareholders Equity**

Common shares	756,414		541,764	1,298,178	Share capital
Preferred shares	541,764		(541,764)		
	1,298,178			1,298,178	
Accumulated deficit	(176,396)	340,200		163,804	Accumulated earnings (deficit)
Accumulated other comprehensive loss	(6,207)	6,207			
	(182,603)	346,407		163,804	
Contributed surplus	16,750	6,131		22,881	Reserves
Total shareholders equity	**1,132,325**	**352,538**		**1,484,863**	**Total shareholders equity**
Total liabilities and shareholders equity	**5,307,381**	**439,667**	**6,808**	**5,753,856**	**Total liabilities and shareholders equity**

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5. TRANSITION TO IFRS (continued)

Reconciliation of Consolidated Balance Sheet as of January 1, 2010

Canadian GAAP accounts	Canadian GAAP balance	IFRS adjustments	IFRS reclassifications	IFRS balance	IFRS accounts
Current assets					**Assets**
Cash and cash equivalents	154,189			154,189	Cash and cash equivalents
Accounts receivable, net	70,203		(3)	70,200	Trade and other receivables
Current future tax asset	2,184		5,133	7,317	Other current financial assets
Other current assets	29,018		(6,017)	23,001	Prepaid expenses and other current assets
Total current assets	**255,594**		**(887)**	**254,707**	**Total current assets**
Satellites, property and other equipment, net	1,926,190	(27,292)		1,898,898	Satellites, property and other equipment
			21,733	21,733	Other long-term financial assets
Other long-term assets	56,924	(15,560)	(22,333)	19,031	Other long-term assets
Intangible assets, net	510,675	415,246		925,921	Intangible assets
Goodwill	2,446,603			2,446,603	Goodwill
Total assets	**5,195,986**	**372,394**	**(1,487)**	**5,566,893**	**Total assets**
Liabilities					**Liabilities**
Current liabilities					
Accounts payable and accrued liabilities	43,413			43,413	Trade and other payables
			102,124	102,124	Other current financial liabilities
Other current liabilities	127,704	(3,527)	(52,056)	72,121	Other current liabilities
Debt due within one year	23,602			23,602	Current indebtedness
Total current liabilities	**194,719**	**(3,527)**	**50,068**	**241,260**	**Total current liabilities**
Debt financing	3,021,820			3,021,820	Long-term indebtedness
Future tax liability	269,193	87,162	(2,718)	353,637	Deferred tax liabilities
			239,825	239,825	Other long-term financial liabilities
Other long-term liabilities	671,523	(19,212)	(288,662)	363,649	Other long-term liabilities
Senior preferred shares	141,435			141,435	Senior preferred shares
Total liabilities	**4,298,690**	**64,423**	**(1,487)**	**4,361,626**	**Total liabilities**
Shareholders equity					**Shareholders Equity**
Common shares	756,414		541,764	1,298,178	Share capital
Preferred shares	541,764		(541,764)		
	1,298,178			1,298,178	
Accumulated deficit	(404,557)	291,740		(112,817)	Accumulated earnings (deficit)
Accumulated other comprehensive loss	(7,422)	7,422			

	(411,979)	299,162		(112,817)	
Contributed surplus	11,097	8,809		19,906	Reserves
Total shareholders equity	**897,296**	**307,971**		**1,205,267**	**Total shareholders equity**
Total liabilities and shareholders equity	**5,195,986**	**372,394**	**(1,487)**	**5,566,893**	**Total liabilities and shareholders equity**

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5. TRANSITION TO IFRS (continued)

Reconciliation of Consolidated Statement of Income for the year ended December 31, 2010

Canadian GAAP accounts	Canadian GAAP balance	IFRS adjustments	IFRS reclassifications	IFRS balance	IFRS accounts
Operating revenues					
Service revenues	801,144		20,217	821,361	Revenue
Equipment sales revenues	20,217		(20,217)		
Total operating revenues	821,361				
		(4,422)	(202,042)	(206,464)	Operating expenses
		3,543	(205,726)	(202,183)	Depreciation
Amortization	(251,194)		205,726	(45,468)	Amortization
Operations and administration	(186,467)		186,467		
Cost of equipment sales	(15,575)		15,575		
Total operating expenses	(453,236)				
		79,192	3,826	83,018	Other operating gains (losses), net
				450,264	Operating income
Earnings (loss) from operations	368,125				
Interest expense	(253,086)	1,743	(5,239)	(256,582)	Interest expense
			5,752	5,752	Interest and other income
Loss on changes in fair value of financial instruments	(11,168)			(11,168)	Loss on changes in fair value of financial instruments
Gain (loss) on foreign exchange	163,998	(32)		163,966	Gain (loss) on foreign exchange
Other income (expense)	4,339		(4,339)		
Earnings (loss) before income taxes	272,208			352,232	Income before tax
Income tax expense	(44,017)	(22,114)		(66,131)	Tax expense
Net earnings	**228,191**	**57,910**		**286,101**	**Net income**

Reconciliation of Consolidated Statement of Comprehensive Income for the year ended December 31, 2010

Canadian GAAP accounts	September 30, Canadian GAAP	September 30, IFRS adjustments	September 30, IFRS balance	September 30,	IFRS accounts

	balance			
Net earnings	228,191	57,910	286,101	Net income
Other comprehensive income (loss):				Other comprehensive income (loss):
Unrealized foreign currency translation gains (losses) of self sustaining foreign operations net of related taxes	1,215	(2,907)	(1,692)	Foreign currency translation adjustments, net of tax
		(9,450)	(9,450)	Actuarial gains (losses) on defined benefit plans, net of tax
	1,215	(12,357)	(11,142)	Other comprehensive income (loss)
Comprehensive income (loss)	**229,406**	**45,553**	**274,959**	**Total comprehensive income**

G. Adjustments to previously reported unaudited comparative figures under IFRS

The Company has adjusted its comparative consolidated financial statements and the reconciliation of equity as at January 1, 2010 and December 31, 2010 and the reconciliation of comprehensive income for the year ended December 31, 2010 to reflect the correction of amounts recorded for the reversal of impairments on tangible and intangible assets.

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5. TRANSITION TO IFRS (continued)

Intangible assets

These adjustments impacted intangible assets, deferred tax liabilities and accumulated earnings (deficit) and were identified through the completion of the Company s transition to IFRS as a basis of accounting. The comparative amounts had been previously disclosed in the Company s unaudited 2011 interim condensed consolidated financial statements.

The impact on the Company s comparative consolidated balance sheet as at January 1, 2010 was a decrease of intangible assets of $71.3 million, a decrease of deferred tax liabilities of $18.8 million, and an increase of accumulated deficit of $52.5 million.

The impact of the Company s comparative consolidated balance sheet as at December 31, 2010 was a decrease of intangible assets of $0.1 million, a decrease of deferred tax liabilities of a nominal amount, and a decrease of accumulated earnings of $0.1 million.

The impact on the Company s comparative consolidated statement of income for the year ended December 31, 2010 was an increase in operating income of $71.3 million and an increase in net income of $52.5 million.

Tangible assets

This adjustment impacted satellites, property and other equipment, deferred tax liabilities and accumulated earnings (deficit) and was identified through the completion of the Company s transition to IFRS as a basis of accounting. The comparative amounts had been previously disclosed in the Company s unaudited 2011 interim condensed consolidated financial statements.

The impact on the Company s comparative consolidated balance sheet as at December 31, 2010 was an increase of satellite, property and other equipment of $6.9 million, an increase of deferred tax liabilities of $1.8 million, and an increase of accumulated earnings of $5.1 million.

The impact on the Company s comparative consolidated statement of income for the year ended December 31, 2010 was an increase in operating income of $6.9 million and an increase in net income of $5.1 million.

6. SEGMENT INFORMATION

Telesat operates in a single industry segment, in which it provides satellite-based services to its broadcast, enterprise and consulting customers around the world.

The Company derives revenue from the following services:

Broadcast distribution or collection of video and audio signals in the North American and International markets which include television transmit and receive services, occasional use, bundled Digital Video Compression and radio services.

Enterprise provision of satellite capacity and ground network services for voice, data, and image transmission and internet access around the world.

Consulting and other all consulting services related to space and earth segments, government studies, satellite control services and R&D.

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6. SEGMENT INFORMATION (continued)

Revenue derived from the above service lines were as follows:

Revenue **Year ended December 31**	**September 30,** **2011**	**September 30,** **2010**
Broadcast	436,676	454,216
Enterprise	341,884	334,983
Consulting and Other	29,801	32,162
Total revenue	808,361	821,361

Geographic Information

Revenue by geographic region was based on the point of origin of the revenue (destination of the billing invoice), allocated as follows:

Revenue **Year ended December 31**	**September 30,** **2011**	**September 30,** **2010**
Canada	411,185	419,032
United States	247,924	261,136
Europe, Middle East & Africa	75,887	77,031
Asia & Australia	19,254	16,268
Latin America & Caribbean	54,111	47,894
Total revenue	808,361	821,361

Telesat s satellites are in geosynchronous orbit. For disclosure purposes, the satellites have been classified based on ownership. Satellites, property and other equipment and intangible assets by geographic region are allocated as follows:

Satellites, property and other equipment	**September 30,** **December 31,** **2011**	**September 30,** **December 31,** **2010**	**September 30,** **January 1,** **2010**
Canada	1,809,152	1,644,049	1,519,663
United States	276,211	327,608	370,664
All others	66,552	7,132	8,571

Total satellites, property and other equipment	2,151,915	1,978,789	1,898,898

Intangible assets	**September 30, December 31, 2011**	**September 30, December 31, 2010**	**September 30, January 1, 2010**
Canada	848,898	909,744	886,965
United States	33,257	33,094	36,066
All others	13,923	2,709	2,890
Total intangible assets	896,078	945,547	925,921

Goodwill was not allocated to geographic regions in any of the periods.

Major Customers

For the year ended December 31, 2011, there were two significant customers each representing more than 10% of consolidated revenue (December 31, 2010 two customers).

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Telesat Holdings Inc.

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7. OPERATING EXPENSES

The Company s operating expenses are comprised of the following:

Year ended December 31	September 30, 2011	September 30, 2010
Compensation and employee benefits [a]	61,755	66,438
Other operating expenses [b]	48,110	52,341
Cost of sales [c]	77,900	87,685
Total	187,765	206,464

a) Compensation and employee benefits include salaries, commission, post-employment benefits and charges arising from share-based payments.

b) Other operating expenses include general and administrative expense, marketing expense, in-orbit insurance expense, professional fees and facility costs.

c) Cost of sales includes the rental of third-party capacity, the cost of equipment sales and costs directly attributable to the facilitation of customer contracts.

8. OTHER OPERATING GAINS

Year ended December 31	September 30, 2011	September 30, 2010
Insurance proceeds [a]	135,019	
Impairment (loss) reversal on intangible assets (note 15)	(19,468)	71,269
Impairment reversal on satellites, property and other equipment		7,923
(Loss) gain on disposal of assets	(1,483)	3,826
Total	114,068	83,018

(a) The Company has insurance policies that provide coverage for a total, constructive total, or partial loss of Telstar 14R /Estrela do Sul 2. Following the launch of the satellite in May 2011, the Company determined that the north solar array failed to fully deploy and promptly filed a notice of loss with its insurers. During the third quarter of 2011, the Company filed a claim under its policies to its insurers. In December 2011, the Company received insurance proceeds of U.S. $132.7 million from its insurers with respect to the claim. Based on

management s best estimate and assumptions, there was no impairment in Telstar 14R/Estrela do Sul 2.

9. INTEREST EXPENSE

The components of interest expense are as follows:

Year ended December 31	September 30, 2011	September 30, 2010
Interest expense on indebtedness	182,719	192,829
Interest expense on derivative instruments	62,124	60,818
Interest expense on performance incentive payments	4,361	5,016
Interest expense on senior preferred shares (note 20)	9,869	12,339
Other expenses		224
Capitalized interest	(32,022)	(14,644)
Interest expense	227,051	256,582

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Telesat Holdings Inc.

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10. INCOME TAXES

Year ended December 31	September 30, 2011	September 30, 2010
Current tax expense	132	2,279
Deferred tax expense	51,854	63,852
Tax expense	51,986	66,131

A reconciliation of the statutory income tax rate, which is a composite of Canadian federal and provincial rates, to the effective income tax rate is as follows:

Year ended December 31	September 30, 2011	September 30, 2010
Income before tax	289,261	352,232
Multiplied by the statutory income tax rate of 28.11% (2010 30.49%)	81,311	107,396
Income tax recorded at rates different from the Canadian tax rate	(408)	179
Permanent differences	(9,316)	(17,811)
Origination and reversal of temporary differences	(10,145)	(24,880)
Previously unrecognized tax losses and credit	(8,977)	
Other	(479)	1,247
Total tax expense in the statement of income	51,986	66,131
Effective income tax rate	17.97%	18.77%

The tax effects of temporary differences between the carrying amounts of assets and liabilities for accounting purposes and the amounts used for tax purposes are presented below:

	September 30, December 31, 2011	September 30, December 31, 2010	September 30, January 1, 2010
Deferred tax assets			
Investment tax credit	2,702	556	661
Foreign tax credit	11,289	26	3
Financing charges	5,439	5,495	5,465
Deferred revenue	4,065	2,063	2,455
Loss carry forwards	25,538	53,344	76,900
Employee benefit	15,250	5,860	4,441
Other	471	585	956

Total deferred tax assets	64,754	67,929	90,881
Deferred tax liabilities			
Capital assets	(276,158)	(230,094)	(206,404)
Intangibles	(226,855)	(238,258)	(223,577)
Finance charges	(9,359)	(8,933)	(8,174)
Reserves	(4,278)	(5,361)	(6,363)
Total deferred tax liabilities	(516,650)	(482,646)	(444,518)
Deferred tax liabilities, net	(451,896)	(414,717)	(353,637)

Losses and tax credits

At December 31, 2011, the Company had Canadian tax losses carried forward of $101.5 million and U.S. tax losses carried forward of $26.7 million. The deferred tax asset not recognized in respect of the U.S. losses was $9.1 million. The Canadian and U.S. losses will expire between 2027 and 2030.

Telesat Holdings Inc.

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10. INCOME TAXES (continued)

The Company has $25.5 million of Canadian capital losses carried forward which may only be used against future capital gains. The deferred tax asset not recognized in respect of these losses was $3.3 million. These losses may be carried forward indefinitely.

In addition, the Company has $14.0 million of investment tax credits and foreign tax credits which may only be used to offset taxes payable. The deferred tax assets not recognized in respect of these credits is $3.2 million. They will begin to expire in 2017.

Investments in subsidiaries

As at December 31, 2011 the Company had temporary differences of $31.0 million associated with investments in subsidiaries for which no deferred tax liabilities have been recognized, as the Company is able to control the timing of the reversal of these temporary differences and it is not probable that these differences will reverse in the foreseeable future.

11. TRADE AND OTHER RECEIVABLES

	September 30, December 31, 2011	September 30, December 31, 2010	September 30, January 1, 2010
Trade receivables	49,936	50,456	62,499
Trade receivables due from related parties	386	428	1,509
Less: Allowance for doubtful accounts	(3,740)	(7,128)	(8,708)
Net trade receivables	46,582	43,756	55,300
Other receivables [(a)]	207	327	14,900
Trade and other receivables	46,789	44,083	70,200

(a) The January 1, 2010 balance consists of the main following items:
$7.2 million receivable related to the sale of Telstar 10, $3.7 million receivable relating to the Company s tenancy arrangement and a $2.0 million receivable relating to a basis swap payment that was scheduled to settle on December 31, 2009 but was received in the first week of January 2010.

Allowance for doubtful accounts

The movement in the allowance for doubtful accounts was as follows:

	September 30, December 31, 2011	September 30, December 31, 2010	September 30, January 1, 2010
Allowance for doubtful accounts, at the beginning of the year	7,128	8,708	5,410
Provisions (reversal) for impaired receivables	(136)	(1,134)	4,067
Receivables written off during the period	(3,050)	(256)	(769)
Foreign currency exchange differences	(202)	(190)	
Allowance for doubtful accounts, end of year	3,740	7,128	8,708

12. PREPAID EXPENSES AND OTHER CURRENT ASSETS

	September 30, December 31, 2011	September 30, December 31, 2010	September 30, January 1, 2010
Prepaid expenses [(a)]	10,302	10,762	10,231
Current tax asset	5,902	4,988	5,448
Inventory [(b)]	4,259	2,985	5,214
Deferred charges [(c)]	1,663	1,996	2,108
Other		206	
	22,126	20,937	23,001

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Telesat Holdings Inc.

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(all amounts in thousands of Canadian dollars, except for per share amounts and where otherwise noted)

12. PREPAID EXPENSES AND OTHER CURRENT ASSETS (continued)

a) Prepaid expenses are primarily comprised of prepaid satellite in-orbit insurance, prepaid interest on long-term indebtedness, and prepaid license fees.

b) At December 31, 2011, inventory consists of $4.1 million of finished goods (December 31, 2010 $2.4 million, January 1, 2010 $2.9 million) and $0.2 million of work in process (December 31, 2010 $0.6 million, January 1, 2010 $2.3 million). During the period, $18.3 million was recognized as cost of equipment sales and recorded as an operating expense (December 31, 2010 $15.6 million).

c) Deferred charges include deferred financing charges relating to the revolving facility and Canadian term loan facility (see note 19).

13. OTHER LONG-TERM ASSETS

	September 30, December 31, 2011	September 30, December 31, 2010	September 30, January 1, 2010
Prepaid expenses [(a)]	4,921	9,785	13,233
Deferred charges	87	1,751	5,244
Other	528	491	554
	5,536	12,027	19,031

a) Prepaid expenses consist of prepaid satellite in-orbit insurance.

14. SATELLITES, PROPERTY AND OTHER EQUIPMENT

	000000 Satellites	000000 Property and other equipment	000000 Assets under construction	000000 Total
Cost at January 1, 2010	2,018,872	199,923	72,366	2,291,161
Additions		6,184	282,376	288,560
Disposals/retirements		(21,501)		(21,501)
Impact of currency translation		(690)		(690)
Cost at December 31, 2010	2,018,872	183,916	354,742	2,557,530
Additions		1,368	371,997	373,365
Disposals/retirements	(26,502)	(16,336)		(42,838)

Reclassifications and transfers from assets under construction	321,743	24,791	(346,534)	
Impact of currency translation		(276)		(276)
Cost at December 31, 2011	2,314,113	193,463	380,205	2,887,781
Accumulated depreciation and impairment at January 1, 2010	(331,659)	(60,604)		(392,263)
Reversal of impairment	7,923			7,923
Depreciation	(181,872)	(20,311)		(202,183)
Disposals/retirements		7,654		7,654
Impact of currency translation		128		128
Accumulated depreciation and impairment at December 31, 2010	(505,608)	(73,133)		(578,741)
Depreciation	(181,658)	(16,968)		(198,626)
Disposals/retirements	26,502	14,769		41,271
Impact of currency translation		230		230
Accumulated depreciation and impairment at December 31, 2011	(660,764)	(75,102)		(735,866)
Net carrying values				
At January 1, 2010	1,687,213	139,319	72,366	1,898,898
At December 31, 2010	1,513,264	110,783	354,742	1,978,789
At December 31, 2011	1,653,349	118,361	380,205	2,151,915

Telesat Holdings Inc.

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14. SATELLITES, PROPERTY AND OTHER EQUIPMENT (continued)

Substantially all of the Company s satellites, property and other equipment have been pledged as security as a requirement of our senior secured credit facilities (note 19).

Borrowing costs of $32.0 million arising on financing were capitalized for the year ended December 31, 2011 ($14.6 million December 31, 2010) and are included in Assets under construction. The average capitalization rate was 8.0%, representing the Company s weighted average cost of borrowing.

The Company assesses impairment of its satellites, property and other equipment on a quarterly basis, or more frequently if events or changes in circumstances indicate that the carrying values may not be recoverable. The Company s CGUs hold a combination of certain satellites, property and other equipment and finite life intangible assets. Indefinite life intangible assets and goodwill have not been allocated to the CGUs. No impairment was recognized for the periods ended December 31, 2011 and December 31, 2010.

In 2010, an impairment loss of $7.9 million was reversed on the satellites. The reversal of impairment was mainly due to changes in revenue assumptions. The recoverable amount is calculated using the following assumptions:

	September 30, 2011	September 30, 2010
Discount rate	10.75%	10.0%

15. INTANGIBLE ASSETS

	000000	000000	000000	000000	000000	000000	000000	000000
	Indefinite life				Finite life			
	Orbital slots	Trade name	Revenue backlog	Customer relationships	Customer contract	Transponder rights	Other	Total Intangibles
Cost at January 1, 2010	599,549	17,000	268,433	199,070		29,550	4,453	1,118,055
Disposals						(999)	(2,966)	(3,965)
Impact of currency translation	(1,711)		(166)	(1,044)		(54)	(29)	(3,004)
Cost at December 31, 2010	597,838	17,000	268,267	198,026		28,497	1,458	1,111,086
Additions					12,618			12,618
Impact of currency translation	615		70	51			(123)	613
Cost at December 31, 2011	598,453	17,000	268,337	198,077	12,618	28,497	1,335	1,124,317
Accumulated amortization and impairment at January 1, 2010	(71,370)		(77,309)	(34,087)		(7,493)	(1,875)	(192,134)
Amortization			(32,952)	(11,021)		(4,387)	(797)	(49,157)
Retirements						999	2,468	3,467

Reversal of impairment	71,269							71,269
Impact of currency translation			34	937		38	7	1,016
Accumulated amortization and impairment at December 31, 2010	(101)		(110,227)	(44,171)		(10,843)	(197)	(165,539)
Amortization			(27,930)	(11,005)	(39)	(4,109)	(86)	(43,169)
Impairment	(19,468)							(19,468)
Impact of currency translation	1		(55)	(22)			13	(63)
Accumulated amortization and impairment at December 31, 2011	(19,568)		(138,212)	(55,198)	(39)	(14,952)	(270)	(228,239)
Net carrying values								
At January 1, 2010	528,179	17,000	191,124	164,983		22,057	2,578	925,921
At December 31, 2010	597,737	17,000	158,040	153,855		17,654	1,261	945,547
At December 31, 2011	578,885	17,000	130,125	142,879	12,579	13,545	1,065	896,078

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15. INTANGIBLE ASSETS (continued)

The orbital slots represent a right to operate satellites in a given longitudinal coordinate in space, where geostationary orbit may be achieved. They are limited in availability and represent a scarce resource. Usage of orbital slots is licensed through the International Telecommunications Union. Satellite operators can generally expect, with a relatively high level of certainty, continued occupancy of an assigned orbital slot either during the operational life of an existing orbiting satellite or upon replacement by a new satellite once the operational life of the existing orbiting satellite is over. As a result of the expectancy right to maintain the once awarded orbital slots, an indefinite life is typically associated with orbital slots.

The Company s trade name has a long and established history, a strong reputation and has been synonymous with quality and growth within the satellite industry. It has been assigned an indefinite life because of expected ongoing future use.

The following are the remaining useful lives of significant intangible assets:

Revenue backlog	1 13 years
Customer relationships	7 17 years
Transponder rights	1 10 years
Customer contract	15 years
Concession rights	12 years
Patent	14 years

Substantially all of the Company s intangible assets have been pledged as security as a requirement of our senior secured credit facilities.

Impairment

Finite life intangible assets are assessed annually and are included with the Company s CGUs (see note 3). Indefinite life intangible assets are tested for impairment at the individual asset level (see note 3). The annual impairment test was performed in the fourth quarter of 2011 and 2010, and at the IFRS transition date.

In 2010, an impairment loss of $71.3 million was reversed on the orbital slots. The impairment was originally recorded in 2008 when discount rates were high due to liquidity issues in the credit markets. The subsequent decrease in discount rates, as well as changes in revenue projections and gross margin assumption positively impacted the valuation of the orbital slots in 2010. In 2011, an impairment loss of $19.5 million was recognized on the orbital slots (2010 no impairment loss) mainly due to an increase in discount rates.

The recoverable amount is calculated using the following assumptions

	September 30, 2011	September 30, 2010
Discount rate	10.75%	10.0%

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16. GOODWILL

The Company carries goodwill at its cost of $2,446.6 million with no accumulated impairment losses since acquisition.

Impairment

Goodwill is tested for impairment at the entity level because that represents the lowest level at which goodwill supports the Company s operations and is monitored internally. The annual impairment test on goodwill was performed in the fourth quarter of 2011 and 2010 in accordance with the policy described in note 3. In addition, goodwill was tested for impairment for purposes of the opening IFRS balance sheet. No impairment was recognized. The Company s recoverable amount exceeded the carrying value therefore, no impairment was recognized for the period. The most significant assumptions used in the impairment test were as follows:

	September 30, December 31, 2011	September 30, December 31, 2010	September 30, January 1, 2010
Discount rate	10.75%	10.0%	9.5%
Terminal year growth rate	3.0%	3.0%	3.0%

Some of the more sensitive assumptions used including the forecasted cash flows and the discount rate could have yielded different estimates of recoverable amount. Actual operating results and the related cash flows of the Company could differ from the estimated operating results and related cash flows used in the impairment analysis. Had different estimates been used, it could have resulted in a lower fair value and there could have been a risk of failing the goodwill impairment test.

17. OTHER CURRENT LIABILITIES

	September 30, December 31, 2011	September 30, December 31, 2010	September 30, January 1, 2010
Deferred revenue	66,588	61,732	70,109
Decommissioning liabilities	151	166	1,024
Other	1,138	747	988
	67,877	62,645	72,121

18. OTHER LONG-TERM LIABILITIES

	September 30, December 31, 2011	September 30, December 31, 2010	September 30, January 1, 2010
Deferred revenue	342,281	315,583	322,384
Net defined benefit plan obligations (see note 25)	67,605	30,801	23,664
Uncertain tax positions	6,795	7,585	7,086

Unfavorable backlog	1,785	3,922	7,145
Unfavorable leases	769	969	1,174
Decommissioning liabilities	1,461	1,367	14
Other	1,806	1,634	2,182
	422,502	361,861	363,649

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19. INDEBTEDNESS

	September 30, December 31, 2011	September 30, December 31, 2010	September 30, January 1, 2010
Senior secured credit facilities [a] :			
Revolving facility			
The Canadian term loan facility	80,000	170,000	185,000
The U.S. term loan facility (December 31, 2011 USD $1,684,800, December 31, 2010 USD $1,702,350, January 1, 2010 USD $1,719,900)	1,720,686	1,698,945	1,811,399
The U.S. term loan II facility (December 31, 2011 USD $144,725, December 31, 2010 USD $146,225, January 1, 2010 USD $147,725)	147,808	145,933	155,584
Senior Notes (USD $692,825) [b]	707,582	691,439	729,683
Senior Subordinated Notes (USD $217,175) [c]	221,801	216,741	228,729
	2,877,877	2,923,058	3,110,395
Less: deferred financing costs and prepayment options [d]	(43,251)	(54,408)	(64,973)
	2,834,626	2,868,650	3,045,422
Less: current portion (net of deferred financing costs)	(86,495)	(96,848)	(23,602)
Long-term portion	2,748,131	2,771,802	3,021,820

(a) The senior secured credit facilities are secured by substantially all of Telesat s assets. Under the terms of these facilities, Telesat is required to comply with certain covenants including financial reporting, maintenance of certain financial covenant ratios for leverage and interest coverage, a requirement to maintain minimum levels of satellite insurance, restrictions on capital expenditures, a restriction on fundamental business changes or the creation of subsidiaries, restrictions on investments, restrictions on dividend payments, restrictions on the incurrence of additional debt, restrictions on asset dispositions, and restrictions on transactions with affiliates. The financial covenant ratios include total debt to EBITDA for covenant purposes (earnings before interest, taxes, depreciation, amortization and other charges) and EBITDA for covenant purposes to interest expense. Both financial covenant ratios tighten over the term of the credit facility. At December 31, 2011, Telesat was in compliance with all of the required covenants.

Each tranche of the credit facility is subject to mandatory principal repayment requirements, which, in the initial years, are generally an annual amount representing 1% of the initial aggregate principal amount, payable quarterly. The senior secured credit facility has several tranches which are described below:

(i) A revolving Canadian dollar denominated credit facility (the revolving facility) of up to $153 million is available to Telesat. This revolving facility matures on October 31, 2012 and is available to be drawn at any time. The drawn loans bear interest at the prime rate or LIBOR or Bankers Acceptance plus an applicable margin of 125 to 225 basis points per annum. Undrawn amounts under the facility are subject to a commitment fee. As of December 31, 2011, other than approximately $0.2 million in drawings related to letters of credit, there were no borrowings under this facility.

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19. INDEBTEDNESS (continued)

(ii) The Canadian term loan facility was initially a $200 million facility denominated in Canadian dollars, with a maturity date of October 31, 2012. Loans under this facility bear interest at a floating rate of the Bankers Acceptance rate plus an applicable margin of 275 basis points per annum. The required repayments on the Canadian term loan facility are as follows:

	September 30, Principal Repayments
2012	80,000

The payments are generally made quarterly in varying amounts. The average interest rate was 4.13% for the year ended December 31, 2011 (December 31, 2010 3.63%). This facility had $80 million outstanding at December 31, 2011.

(iii) The U.S. term loan was initially a $1,755 million facility denominated in U.S. dollars, bears interest at LIBOR plus an applicable margin of 300 basis points per annum, and has a maturity of October 31, 2014. The weighted average effective interest rate was 3.72% for the year ended December 31, 2011 (December 31, 2010 3.76%). The loan had U.S. $1,685 million outstanding at December 31, 2011. Principal repayments of U.S. $4.4 million are made on a quarterly basis, with a lump sum repayment of the remaining balance payable on the maturity date.

(iv) The U.S. term loan II was initially a $150 million delayed draw facility denominated in U.S. dollars, bears interest at LIBOR plus an applicable margin of 300 basis points per annum, and has a maturity of October 31, 2014. The weighted average effective interest rate was 3.73% for the year ended December 31, 2011 (December 31, 2010 3.77%). The facility had U.S. $145 million outstanding at December 31, 2011. Principal repayments of U.S. $0.4 million are made on a quarterly basis, with a lump sum repayment of the remaining balance payable on the maturity date.

(b) The Senior Notes bear interest at an annual rate of 11.0% and are due November 1, 2015. The Senior Notes include covenants or terms that restrict Telesat s ability to, among other things, (i) incur additional indebtedness, (ii) incur liens, (iii) pay dividends or make certain other restricted payments, investments or acquisitions, (iv) enter into certain transactions with affiliates, (v) modify or cancel the Company s satellite insurance, (vi) effect mergers with another entity, and (vii) redeem the Senior Notes prior to May 1, 2012, in each case subject to exceptions provided in the Senior Notes indenture. The weighted average effective interest rate was 11.37% for the year ended December 31, 2011 (December 31, 2010 11.56%).

(c) The Senior Subordinated Notes bear interest at a rate of 12.5% and are due November 1, 2017. The Senior Subordinated Notes include covenants or terms that restrict Telesat s ability to, among other things, (i) incur additional indebtedness, (ii) incur liens, (iii) pay dividends or make certain other restricted payments, investments or acquisitions, (iv) enter into certain transactions with affiliates, (v) modify or cancel the Company s satellite insurance, (vi) effect mergers with another entity, and (vii) redeem the Senior Subordinated Notes prior to May 1, 2013, in each case subject to exceptions provided in the Senior Subordinated Notes indenture. The weighted average effective interest rate was 12.66% for the year ended December 31, 2011 (December 31, 2010 12.88%).

(d)

The U.S. term loan facilities, Senior Notes and Senior Subordinated Notes are presented on the balance sheet net of related deferred financing costs of $49.4 million (December 31, 2010 $61.6 million, January 1, 2010 $73.1 million). The indentures agreement for the Senior Notes and Senior Subordinated Notes contain provisions for certain prepayment options which were fair valued at the time of debt issuance (note 23). The initial fair value impact of the prepayment options on the Senior Notes and Senior Subordinated Notes was an increase to the liabilities of $6.5 million and $2.7 million, respectively. These liability amounts are subsequently amortized using the effective interest rate method with carrying amounts of $4.1 million and $2.1 million respectively, at December 31, 2011 (December 31, 2010 $4.9 million and $2.3 million, January 1, 2010 $5.6 million and $2.5 million).

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19. INDEBTEDNESS (continued)

The short-term and long-term portions of deferred financing costs and prepayment options are as follows:

		September 30, December 31, 2011	September 30, December 31, 2010	September 30, January 1, 2010
Short-term deferred financing costs		12,961	12,165	11,462
Long-term deferred financing costs		36,468	49,433	61,593
		49,429	61,598	73,055
Long-term prepayment option	Senior Notes	(4,133)	(4,928)	(5,631)
Long-term prepayment option	Senior Subordinated Notes	(2,045)	(2,262)	(2,451)
		(6,178)	(7,190)	(8,082)
Total deferred financing costs and prepayment options		43,251	54,408	64,973

The outstanding balance of indebtedness, excluding deferred financing costs and prepayment options, will be repaid as follows (in millions of Canadian dollars):

2012	September 30, 2013	September 30, 2014	September 30, 2015	September 30, Thereafter	September 30, Total
99.5	19.4	1,829.6	707.6	221.8	2,877.9

20. SENIOR PREFERRED SHARES

Telesat issued 141,435 senior preferred shares with an issue price of $1,000 per Senior Preferred Share on October 31, 2007. The Senior Preferred Shares rank in priority, with respect to the payment of dividends and return of capital upon liquidation, dissolution or winding-up, ahead of the shares of all other classes of Telesat stock which have currently been created, as well as any other shares that may be created that by their terms rank junior to the senior preferred shares. Senior Preferred Shares are entitled to receive cumulative preferential dividends at a rate of 7% per annum on the Liquidation Value, being $1,000 per Senior Preferred Share plus all accrued and unpaid dividends (8.5% per annum following a Performance Failure, being a failure to pay annual dividends in cash or in Holding PIK Preferred Stock in any year, while such failure is continuing, the failure to redeem the Holding PIK Preferred Stock when submitted for redemption on or after the twelfth anniversary of the date of issue, or the failure to redeem Holding PIK Preferred Stock for which an offer of redemption is accepted following a Change of Control). Such annual dividend may be paid in cash, subject to the requirements of the Canada Business Corporations Act (the CBCA), if such payment is permitted under the terms of (i) the senior secured credit facilities and (ii) the indentures governing the notes. If the cash payment is not permitted under the terms of the senior secured credit facilities, the dividends will be paid, subject to the requirements of the CBCA, in senior preferred shares based on an issue price of $1,000 per Senior Preferred Share. Dividends of $1.7 million have been accrued at December 31, 2011 (December 31, 2010 $2.1 million, January 1, 2010 $25.1 million).

The Senior Preferred Shares may be submitted by the holder for redemption on or after the twelfth anniversary of the date of issue, subject to compliance with law. Upon a change of control which occurs after the fifth anniversary of the issue of the Senior Preferred Shares, or on the fifth anniversary if a change of control occurs prior to the fifth anniversary of the issue, Telesat must make an offer of redemption to all holders of Senior Preferred Shares, and must redeem any Senior Preferred Shares for which the offer of redemption is accepted within 25 days of such offer. As a result, the Senior Preferred Shares have been classified as a liability on the consolidated balance sheet and dividends have been classified as interest expense on the statement of income (note 9).

The holders of the Senior Preferred Shares are not entitled to receive notice of or to vote at any meeting of shareholders of the Company except for meetings of the holders of the Senior Preferred Shares as a class, called to amend the terms of the Senior Preferred Shares, or otherwise as required by law.

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(all amounts in thousands of Canadian dollars, except for per share amounts and where otherwise noted)

21. SHARE CAPITAL

There was no change in share capital in the period of January 1, 2010 to December 31, 2011.

At December 31, 2011	September 30, Number of shares	September 30, Stated Value ($)
Common Shares	74,252,460	756,414
Voting Participating Preferred Shares	7,034,444	117,388
Non-Voting Participating Preferred Shares	35,953,824	424,366
Director Voting Preferred Shares	1,000	10
Total share capital		1,298,178

The authorized share capital of the Company is comprised of: (i) an unlimited number of common shares, of voting participating preferred shares, of non-voting participating preferred shares, of redeemable common shares, and of redeemable non-voting participating preferred shares, (ii) 1,000 director voting preferred shares, and (iii) 325,000 senior preferred shares (note 20). None of the redeemable common shares or redeemable non-voting participating preferred shares have been issued as at December 31, 2011. The Company s share based compensation plan has authorized the grant of up to 8,824,646 options to purchase non-voting participating preferred shares (see note 24).

Common Shares

The holders of the common shares are entitled to receive notice of and to attend all annual and special meetings of the shareholders of the Company and to one vote in respect of each common share held on all matters at all such meetings, except in respect of a class vote applicable only to the shares of any other class, in respect of which the common shareholders shall have no right to vote. The holders of the common shares are entitled to receive dividends as may be declared by the Board of Directors of the Company, and are entitled to share in the distribution of the assets of the Company upon liquidation, winding-up or dissolution, subject to the rights, privileges and conditions attaching to any other class of shares ranking in order of priority. The common shares are convertible at the holders option, at any time, into voting participating preferred shares or non-voting participating preferred shares, on a one-for-one basis. The common shares have no par value.

Voting Participating Preferred Shares

The rights, privileges and conditions of the voting participating preferred shares are identical in all respects to those of the common shares, except for the following:

The holders of voting participating preferred shares are not entitled to vote at meetings of the shareholders of the Company on resolutions electing directors.

For all other meetings of the shareholders of the Company, the holders of voting participating preferred shares are entitled to a variable number of votes per voting participating preferred share based on the number of voting participating preferred shares,

non-voting participating preferred shares and redeemable non-voting participating preferred shares outstanding on the record date of the given meeting of the shareholders of the Company.

The voting participating preferred shares are convertible, at any time, at the holders option into common shares or non-voting participating preferred shares on a one-for-one basis as long as the result of such conversion does not cause the Company to cease to be a qualified corporation within the meaning of the Canadian Telecommunication Common Carrier Ownership and Control Regulations pursuant to the Telecommunications Act (Canada).

The voting participating preferred shares have no par value.

Telesat Holdings Inc.

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21. SHARE CAPITAL (continued)

Non-Voting Participating Preferred Shares

The rights, privileges and conditions of the non-voting participating preferred shares are identical in all respects to those of the common shares, except for the following:

The holders of non-voting participating preferred shares are not entitled to vote on any matter at meetings of the shareholders of the Company, except in respect of a class vote applicable only to the non-voting participating preferred shares.

The non-voting participating preferred shares are convertible, at any time, at the holders option into common shares or voting participating preferred shares on a one-for-one basis as long as the result of such conversion does not cause the Company to cease to be a qualified corporation within the meaning of the Canadian Telecommunication Common Carrier Ownership and Control Regulations pursuant to the Telecommunications Act (Canada).

The non-voting participating preferred shares have no par value.

Director Voting Preferred Shares

The rights, privileges and conditions of the director voting preferred shares are identical in all respects to those of the common shares, except for the following:

The holders of director voting preferred shares are entitled to receive notice of and to attend all meetings of the shareholders of the Company at which directors of the Company are to be elected. The holders of the director voting preferred shares are not entitled to attend meetings of the shareholders of the Company and have no right to vote on any matter other than the election of directors of the Company.

The holders of director voting preferred shares are entitled to receive annual non-cumulative dividends of $10 per share if declared by the Board of Directors of the Company, in priority to the payment of dividends on the common shares, voting participating preferred shares, non-voting participating preferred shares, redeemable common shares, and redeemable non-voting participating preferred shares, but after payment of any accrued dividends on the senior preferred shares.

In the event of liquidation, wind-up or dissolution, the holders of director voting preferred shares are entitled to receive $10 per share in priority to the payment of dividends on the common shares, voting participating preferred shares, non-voting participating preferred shares, redeemable common shares, and redeemable non-voting participating preferred shares, but after payment of any accrued dividends on the senior preferred shares.

The director voting preferred shares are redeemable at the option of the Company, at any time, at a redemption price of $10 per share.

The director voting preferred shares have a nominal stated value.

22. CAPITAL DISCLOSURES

Telesat is a privately held company with registered debt in the United States. The Company s financial strategy is designed to maintain compliance with its financial covenants under its senior secured credit facility (see note 19), and to maximize returns to its shareholders and other stakeholders. Telesat meets these objectives through regular monitoring of its financial covenants and operating results on a quarterly basis. The Company s overall financial strategy remains unchanged from 2010.

Telesat Holdings Inc.

Notes to the 2011 Consolidated Financial Statements

(all amounts in thousands of Canadian dollars, except for per share amounts and where otherwise noted)

22. CAPITAL DISCLOSURES (continued)

Telesat defines its capital as shareholders equity (comprising issued share capital, accumulated earnings and excluding reserves) and debt financing (comprising indebtedness and excluding deferred financing costs and prepayment options as detailed in note 19).

The Company s capital at the end of the year was as follows:

	September 30, December 31, 2011	September 30, December 31, 2010	September 30, January 1, 2010
Shareholders equity (excluding reserves)	1,668,170	1,461,982	1,185,361
Debt financing (excluding deferred financing costs and prepayment options)	2,877,877	2,923,058	3,110,395

Telesat manages its capital by measuring the financial covenant ratios contained in its senior secured credit agreement (the credit agreement), dated October 31, 2007 and which terminates in October 2014. As of December 31, 2011, the Company was subject to three financial covenant compliance tests: a maximum Consolidated Total Debt to Consolidated Earnings Before Interest, Taxes, Depreciation and Amortization (EBITDA) for covenant purposes ratio test, a minimum Consolidated EBITDA for covenant purposes to Consolidated Interest Expense ratio test and a maximum Permitted Capital Expenditure Amount test. Compliance with financial covenants is measured on a quarterly basis, except for the maximum Permitted Capital Expenditure Amount which is only measured at the end of every fiscal year.

As of December 31, 2011, Telesat s Consolidated Total Debt to Consolidated EBITDA for covenant purposes ratio, for credit agreement compliance purposes, was 4.39:1 (December 31, 2010 4.59:1), which was less than the maximum test ratio of 6.25:1. The Consolidated EBITDA for covenant purposes to Consolidated Interest Expense ratio, for credit agreement compliance purposes, was 2.74:1 (December 31, 2010 2.63:1), which was greater than the minimum test ratio of 1.70:1. The compliance test ratios become more restrictive over the term of the credit agreement.

The maximum Permitted Capital Expenditure Amount varies in each fiscal year with the opportunity to carry forward or carry back unused amounts based on conditions specified in the credit agreement. An additional amount of U.S. $500 million is also available over the term of the credit agreement for the construction or acquisition of up to four new satellites. For the fiscal year ended December 31, 2011, the Company s Capital Expenditure Amount, as defined in the credit agreement, was $341.5 million and was in compliance with the credit agreement.

As part of the on-going monitoring of Telesat s compliance with its financial covenants, interest rate risk due to variable interest rate debt is managed through the use of interest rate swaps (note 23), and foreign exchange risk exposure arising from principal and interest payments on Telesat s debt is partially managed through a cross currency basis swap (note 23). In addition, the Company s operating results are tracked against budget on a monthly basis, and this analysis is reviewed by senior management.

23. FINANCIAL INSTRUMENTS

Measurement of Risks

The Company, through its financial assets and liabilities, is exposed to various risks. The following analysis provides a measurement of risks as at the balance sheet date of December 31, 2011.

Credit Risk

Credit risk is the risk that a counterparty to a financial asset will default, resulting in the Company incurring a financial loss. At December 31, 2011, the maximum exposure to credit risk is equal to the carrying value of the financial assets, $474 million (December 31, 2010 $350 million, January 1, 2010 $253 million). Cash and cash equivalents are invested with high quality investment grade financial institutions and are governed

by the Company s corporate investment policy, which aims to reduce credit risk by restricting investments to high-grade U.S. dollar and Canadian dollar denominated investments.

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23. FINANCIAL INSTRUMENTS (continued)

It is expected that the counterparties to the Company s financial assets will be able to meet their obligations as they are institutions with strong credit ratings. Telesat regularly monitors the credit risk and credit exposure.

Telesat has a number of diverse customers, which limits the concentration of credit risk with respect to trade receivables. The Company has credit evaluation, approval and monitoring processes intended to mitigate potential credit risks. Telesat s standard payment terms are 30 days. Interest at a rate of 1.5% per month, compounded monthly, is typically charged on balances remaining unpaid at the end of the standard payment terms. Telesat s historical experience with customer defaults has been minimal. As a result, Telesat considers the credit quality of its North American customers to be high; however due to the additional complexities of collecting from its International customers the Company considers the credit quality of its International customers to be lower than the North American customers. At December 31, 2011, North American and International customers made up 36% and 64% of the outstanding trade receivable balance, respectively (December 31, 2010 38% and 62%, January 1, 2010 39% and 61%). Anticipated bad debt losses have been provided for in the allowance for doubtful accounts. The allowance for doubtful accounts at December 31, 2011 was $3.7 million (December 31, 2010 $7.1 million, January 1, 2010 $8.7 million).

Foreign Exchange Risk

The Company s operating results are subject to fluctuations as a result of exchange rate variations to the extent that transactions are made in currencies other than Canadian dollars. The most significant impact of variations in the exchange rate is on the U.S. dollar denominated debt financing. At December 31, 2011, approximately $2,798 million of the $2,878 million total debt financing (before netting of deferred financing costs and prepayment options) is the Canadian dollar equivalent of the U.S. dollar denominated portion of the debt.

The Company has entered into a cross currency basis swap to economically hedge the foreign currency risk on a portion of its U.S. dollar denominated debt. At December 31, 2011, the Company had a cross currency basis swap of $1,175 million (December 31, 2010 $1,187 million, January 1, 2010 $1,200 million) which required the Company to pay Canadian dollars to receive U.S. $1,012 million (December 31, 2010 U.S. $1,022 million, January 1, 2010 U.S. $1,033 million). At December 31, 2011, the fair value of this derivative contract was a liability of $160.4 million (December 31, 2010 liability of $192.5 million, January 1, 2010 liability of $137.1 million). The non-cash loss will remain unrealized until the contract is settled. This contract is due on October 31, 2014.

Telesat uses forward contracts to hedge foreign currency risk on anticipated transactions, mainly related to the construction of satellites. At December 31, 2011, the Company had no outstanding foreign exchange contracts. At December 31, 2010, the Company had nine outstanding foreign exchange contracts which required the Company to pay $188.3 million Canadian dollars (January 1, 2010 $21.5 million) to receive U.S. $185.0 million (January 1, 2010 U.S. $20.0 million) for future capital expenditures and interest payments. At December 31, 2010, the fair value of the derivative contracts was a liability of $2.6 million (January 1, 2010 $0.4 million).

The Company s main currency exposures as at December 31, 2011 lie in its U.S. dollar denominated cash and cash equivalents, trade and other receivables, trade and other payables and indebtedness.

As at December 31, 2011, a 5 percent increase (decrease) in the Canadian dollar against the U.S. dollar would have increased (decreased) the Company s net income by approximately $158 million and increased (decreased) other comprehensive income by $1 million. This analysis assumes that all other variables, in particular interest rates, remain constant.

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Telesat Holdings Inc.

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(all amounts in thousands of Canadian dollars, except for per share amounts and where otherwise noted)

23. FINANCIAL INSTRUMENTS (continued)

Interest Rate Risk

The Company is exposed to interest rate risk on its cash and cash equivalents and its long term debt which is primarily variable rate financing. Changes in the interest rates could impact the amount of interest Telesat is required to pay. Telesat uses interest rate swaps to economically hedge the interest rate risk related to variable rate debt financing. At December 31, 2011, the Company had a series of three interest rate swaps to fix interest on $930 million of Canadian dollar denominated debt at average fixed rates ranging from 3.02% to 3.5%. As at December 31, 2011, the fair value of these derivative contracts was a liability of $53.1 million (December 31, 2010 liability of $49.4 million, January 1, 2010 liability of $47.7). The contracts mature by October 31, 2014.

If the interest rates on the unhedged variable rate debt change by 0.25% this would result in a change in the net income of approximately $2.0 million for the year ended December 31, 2011.

Liquidity Risk

The Company maintains credit facilities to ensure it has sufficient available funds to meet current and foreseeable financial requirements. The following are the contractual maturities of financial liabilities as at December 31, 2011:

	000000	000000	000000	000000	000000	000000	000000	000000
In millions of Canadian dollars	**Carrying amount**	**Contractual cash flows (undiscounted)**	**2012**	**2013**	**2014**	**2015**	**2016**	**After 2016**
Trade and other payables	45,156	45,156	45,156					
Customer and other deposits	4,822	4,822	2,882	907	999	34		
Deferred satellites performance incentive payments	69,898	98,594	15,661	8,416	8,414	8,435	8,481	49,187
Dividends payable on senior preferred shares (note 20)	1,650	1,650	1,650					
Promissory note payable to Loral (note 29)	21,141	21,141						21,141
Tax indemnification payable to Loral (note 29)	7,111	7,111		7,111				
Other financial liabilities	3,708	3,708	2,151	1,557				
Long-term indebtedness	2,905,023	3,552,922	289,933	186,635	1,985,962	813,141	27,725	249,526
Interest rate swaps	53,101	52,762	18,658	18,607	15,497			
Cross currency basis swap	160,373	76,604	27,247	26,907	22,450			
	3,271,983	3,864,470	403,338	250,140	2,033,322	821,610	36,206	319,854

The carrying value of the deferred satellites performance incentive payments includes $2.5 million interest payable. The carrying value of the long-term indebtedness includes $21.0 million of interest payable and excludes $49.4 million of financing costs.

Telesat Holdings Inc.

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23. FINANCIAL INSTRUMENTS (continued)

Financial assets and liabilities recorded in the balance sheet were as follows:

	000000	000000	000000	000000	000000
December 31, 2011	**Loans and receivables**	**Held for Trading FVTPL**	**Other financial liabilities**	**Total**	**Fair value**
Cash and cash equivalents	277,962			277,962	277,962
Trade and other receivables	46,789			46,789	46,789
Other financial assets current	7,010			7,010	7,010
Other financial assets long-term	7,977	134,431		142,408	142,408
Trade and other payables			(45,156)	(45,156)	(45,156)
Other financial liabilities current		(42,204)	(40,784)	(82,988)	(85,549)
Other financial liabilities long-term		(171,270)	(88,513)	(259,783)	(255,225)
Indebtedness (excluding deferred financing costs) (note 19)			(2,884,056)	(2,884,056)	(2,943,132)
Senior preferred shares (note 20)			(141,435)	(141,435)	(143,265)
Total	339,738	(79,043)	(3,199,944)	(2,939,249)	(2,998,158)

December 31, 2010	**Loans and receivables**	**Held for Trading FVTPL**	**Other financial liabilities**	**Total**	**Fair value**
Cash and cash equivalents	220,295			220,295	220,295
Trade and other receivables	44,083			44,083	44,083
Other financial assets current	6,944			6,944	6,944
Other financial assets long-term	6,226	72,405		78,631	78,631
Trade and other payables			(49,974)	(49,974)	(49,974)
Other financial liabilities current		(63,199)	(40,883)	(104,082)	(104,012)
Other financial liabilities long-term		(181,255)	(84,374)	(265,629)	(263,456)
Indebtedness (excluding deferred financing costs) (note 19)			(2,930,248)	(2,930,248)	(3,067,412)
Senior preferred shares (note 20)			(141,435)	(141,435)	(153,978)
Total	277,548	(172,049)	(3,246,914)	(3,141,415)	(3,288,879)

January 1, 2010	**Loans and receivables**	**Held for Trading FVTPL**	**Other financial liabilities**	**Total**	**Fair value**
Cash and cash equivalents	154,189			154,189	154,189
Trade and other receivables	70,200			70,200	70,200
Other financial assets current	7,317			7,317	7,317
Other financial assets long-term	5,819	15,914		21,733	21,733

Trade and other payables			(43,413)	(43,413)	(43,413)
Other financial liabilities current		(57,129)	(44,995)	(102,124)	(102,470)
Other financial liabilities long-term		(128,157)	(111,668)	(239,825)	(237,226)
Indebtedness (excluding deferred financing costs) (note 19)			(3,118,477)	(3,118,477)	(3,104,151)
Senior preferred shares (note 20)			(141,435)	(141,435)	(174,466)
Total	237,525	(169,372)	(3,459,988)	(3,391,835)	(3,408,287)

Telesat Holdings Inc.

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23. FINANCIAL INSTRUMENTS (continued)

Fair Value

Fair value is the amount that willing parties would accept to exchange a financial instrument based on the current market for instruments with the same risk, principal and remaining maturity. Where possible, fair values are based on the quoted market values in an active market. In the absence of an active market, we determine fair values based on prevailing market rates (bid and ask prices, as appropriate) for instruments with similar characteristics and risk profiles or internal or external valuation models, such as option pricing models and discounted cash flow analysis, using observable market-based inputs. The fair value hierarchy is as follows:

Level 1 based on quoted prices in active markets for identical assets or liabilities.

Level 2 based on observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

Estimates of fair values are affected significantly by the assumptions for the amount and timing of estimated future cash flows and discount rates, which all reflect varying degrees of risk. Potential income taxes and other expense that would be incurred on disposition of these financial instruments are not reflected in the fair values. As a result, the fair values are not necessarily the net amounts that would be realized if these instruments were actually settled.

The carrying amounts of cash and cash equivalents, trade and other receivables, and trade and other payables approximate fair value due to the short-term maturity of these instruments. Included in cash and cash equivalents are $66.5 million (December 31, 2010 $91.1 million, January 1, 2010 $64.5 million) of short-term investments classified as Level 2 in the fair value hierarchy. The fair value of the indebtedness is based on transactions and quotations from third parties considering market interest rates and excluding deferred financing costs. The indebtedness and senior preferred shares are classified as Level 2 in the fair value hierarchy.

Fair value of derivative financial instruments

The current and long term portions of the fair value of the Company s derivative assets and liabilities, at each of the balance sheet dates, and the fair value methodologies used to calculate those values were as follows:

December 31, 2011	000000 Long-term assets	000000 Current liabilities	000000 Long-term liabilities	000000 Total	000000 Fair value hierarchy
Cross currency basis swap		(23,637)	(136,736)	(160,373)	Level 2
Interest rate swaps		(18,567)	(34,534)	(53,101)	Level 2
Forward foreign exchange contracts					Level 2
Prepayment option embedded derivatives	134,431			134,431	Level 2

	134,431	(42,204)	(171,270)	(79,043)

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23. FINANCIAL INSTRUMENTS (continued)

December 31, 2010	000000 Long-term assets	000000 Current liabilities	000000 Long-term liabilities	000000 Total	000000 Fair value hierarchy
Cross currency basis swap		(29,349)	(163,107)	(192,456)	Level 2
Interest rate swaps		(31,279)	(18,148)	(49,427)	Level 2
Forward foreign exchange contracts		(2,571)		(2,571)	Level 2
Prepayment option embedded derivatives	72,405			72,405	Level 2
	72,405	(63,199)	(181,255)	(172,049)	

January 1, 2010	Long-term assets	Current liabilities	Long-term liabilities	Total	Fair value hierarchy
Cross currency basis swap		(16,763)	(120,343)	(137,106)	Level 2
Interest rate swaps		(39,930)	(7,814)	(47,744)	Level 2
Forward foreign exchange contracts		(436)		(436)	Level 2
Prepayment option embedded derivatives	15,914			15,914	Level 2
	15,914	(57,129)	(128,157)	(169,372)	

Reconciliation of fair value of derivative assets and liabilities	September 30,
Opening fair value, January 1, 2010	(169,372)
Unrealized losses on derivatives	(13,955)
Realized gains on derivatives:	
Cross currency basis swap	1,183
Interest rate swaps	
Forward foreign exchange contracts	1,604
Impact of foreign exchange	8,491
Fair value, December 31, 2010	(172,049)
Unrealized gains on derivatives	87,914
Realized gains on derivatives:	
Cross currency basis swap	1,895
Interest rate swaps	
Forward foreign exchange contracts	8,776
Impact of foreign exchange	(5,579)
Fair value, December 31, 2011	(79,043)

24. SHARE BASED COMPENSATION PLANS

Telesat Holdings Stock Option Incentive Plan

On September 19, 2008, Telesat adopted a stock option incentive plan (the stock option plan) for certain key employees of the Company and its subsidiaries. The stock option plan provides for the grant of up to 8,824,646 options to purchase non-voting participating preferred shares of Telesat Holdings Inc., convertible into common shares.

Two different types of stock options can be granted under the stock option plan: time-vesting options and performance-vesting options. The time-vesting options generally become vested and exercisable over a five year period by 20% increments on October 31 st of each year, starting in 2008. The vesting amount is prorated for optionees whose employment with the Company or its subsidiaries commenced after October 31, 2007. The performance-vesting options become vested and exercisable over a five year period starting March 31, 2009, provided the Company has achieved or exceeded an annual or cumulative target consolidated EBITDA established and communicated on the grant date by the Board of Directors.

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23. FINANCIAL INSTRUMENTS (continued)

The Company expenses the fair value of stock options that are expected to vest over the vesting period using the Black-Scholes option pricing model. The share-based compensation expense is included in operating expenses.

The exercise periods of the stock options expire ten years from the grant date. The exercise price of each share underlying the options will be the higher of a fixed price, established by the Board of Directors on the grant date, and the fair market value of a non-voting participating preferred share on the grant date.

The movement in the number of stock options outstanding and their related weighted-average exercise prices are as follows:

	000000	000000	000000	000000
	Time Vesting Option Plans		Performance Vesting Option Plan	
	Number of Options	Weighted-Average Exercise Price ($)	Number of Options	Weighted-Average Exercise Price ($)
Outstanding December 31, 2011	7,265,952	11.08	1,407,672	11.12
Options exercisable at December 31, 2011	5,666,287		687,698	
Weighted-average remaining life	6 years		6 years	
Outstanding December 31, 2010	7,265,952	11.08	1,407,672	11.12
Options exercisable at December 31, 2010	4,173,018		526,252	
Weighted-average remaining life	7 years		7 years	
Outstanding January 1, 2010	7,303,705	11.07	1,453,814	11.07
Options exercisable at January 1, 2010	2,740,969		162,091	
Weighted-average remaining life	8 years		8 years	

During 2011 no options were granted, forfeited, exercised or expired.

The compensation expense, number of stock options granted, weighted-average fair value per option granted and the assumptions used to determine the share-based compensation expense using the Black-Scholes option pricing model were as follows:

	September 30, December 31, 2011	September 30, December 31, 2010
Compensation expense (credited to equity-settled employee benefits reserve)	2,654	4,667
Number of stock options granted		22,372
Weighted-average fair value per option granted ($)		16.50
Weighted average assumptions:		
Dividend yield		
Expected volatility		31.10%

Risk-free interest rate	3.85%
Expected life (years)	10

Telesat Holdings Inc.

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25. EMPLOYEE BENEFIT PLANS

The Company s net defined benefit plan expense included in operating expense consisted of the following elements:

	September 30,	September 30,	September 30,	September 30,
	Defined benefit pension plans		Other post-employment benefit plans	
Year ended December 31,	2011	2010	2011	2010
Current service cost	3,844	2,630	299	232
Interest cost	9,687	9,655	1,183	1,237
Expected return on plan assets	(10,708)	(10,231)		
Net defined benefit plan expense	2,823	2,054	1,482	1,469

The Company s funding policy is to make contributions to its pension funds based on actuarial cost methods as permitted by pension regulatory bodies. Contributions reflect actuarial assumptions concerning future investment returns, salary projections and future service benefits. Plan assets are represented primarily by Canadian and foreign equity securities, fixed income instruments and short-term investments.

The Company provides certain health care and life insurance benefits for some of its retired employees and their dependents. Participants are eligible for these benefits generally when they retire from active service and meet the eligibility requirements for the pension plan. These benefits are funded primarily on a pay-as-you-go basis, with the retiree generally paying a portion of the cost through contributions, deductibles and coinsurance provisions.

	September 30,	September 30,	September 30,
	December 31, 2011	December 31, 2010	January 1, 2010
Balance sheet obligations for:			
Pension benefits	43,266	9,209	1,231
Other post-employment benefits	24,339	21,592	22,433
	67,605	30,801	23,664

The amounts recognized in the balance sheet are determined as follows:

	000000	000000	000000	000000	000000	000000
	December 31, 2011		December 31, 2010		January 1, 2010	
	Pension	Other	Pension	Other	Pension	Other
Present value of funded obligations	211,872		174,662		151,063	
Fair value of plan assets	169,808		166,235		150,746	

	42,064		8,427		317	
Present value of unfunded obligations	1,202	24,339	782	21,592	914	22,433
Liability in the balance sheet	43,266	24,339	9,209	21,592	1,231	22,433

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(all amounts in thousands of Canadian dollars, except for per share amounts and where otherwise noted)

25. EMPLOYEE BENEFIT PLANS (continued)

The changes in the defined benefit obligations and in the fair value of plan assets and the funded status of the defined benefit plans were as follows:

	September 30,	September 30, December 31, 2011	September 30,
Pension and other benefits	**Pension**	**Other**	**Total**
Change in benefit obligations			
Defined benefit obligation, January 1, 2011	175,444	21,592	197,036
Current service cost	3,844	299	4,143
Interest cost	9,687	1,183	10,870
Actuarial (gains) losses	30,541	2,222	32,763
Benefits paid	(7,825)	(990)	(8,815)
Contributions by plan participants	1,383	33	1,416
Plan amendments			
Defined benefit obligation, December 31, 2011	213,074	24,339	237,413

		December 31, 2011	
Pension and other benefits	**Pension**	**Other**	**Total**
Change in fair value of plan assets			
Fair value of plan assets, January 1, 2011	166,235		166,235
Expected return on plan assets	10,708		10,708
Actuarial gains (losses)	(8,800)		(8,800)
Benefits paid	(7,825)	(990)	(8,815)
Contributions by plan participants	1,383	33	1,416
Contributions by employer	8,107	957	9,064
Fair value of plan assets, December 31, 2011	169,808		169,808
Funded status			
Plan surplus (deficit)	(43,266)	(24,339)	(67,605)
Accrued benefit asset (liability)	(43,266)	(24,339)	(67,605)

		December 31, 2010	
Pension and other benefits	**Pension**	**Other**	**Total**
Change in benefit obligations			
Defined benefit obligation, January 1, 2010	151,977	22,433	174,410
Current service cost	2,630	232	2,862
Interest cost	9,665	1,237	10,902

Actuarial (gains) losses	19,165	(1,250)	17,915
Benefits paid	(9,379)	(856)	(10,235)
Contributions by plan participants	1,386	32	1,418
Plan amendments		(236)	(236)
Defined benefit obligation, December 31, 2010	175,444	21,592	197,036

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Telesat Holdings Inc.

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(all amounts in thousands of Canadian dollars, except for per share amounts and where otherwise noted)

25. EMPLOYEE BENEFIT PLANS (continued)

Pension and other benefits	September 30, Pension	September 30, December 31, 2010 Other	September 30, Total
Change in fair value of plan assets			
Fair value of plan assets, January 1, 2010	150,746		150,746
Expected return on plan assets	10,231		10,231
Actuarial gains (losses)	5,108		5,108
Benefits paid	(9,379)	(856)	(10,235)
Contributions by plan participants	1,386	32	1,418
Contributions by employer	8,143	824	8,967
Fair value of plan assets, December 31, 2010	166,235		166,235
Funded status			
Plan surplus (deficit)	(9,209)	(21,592)	(30,801)
Accrued benefit asset (liability)	(9,209)	(21,592)	(30,801)

The major categories of plan assets as a percentage of total plans assets and the expected rate of return on assets at the end of the reporting period for each category are as follows:

	September 30, Expected return	September 30,	September 30, Fair value of plan assets	September 30,
	December 31, 2011	December 31, 2010	December 31, 2011	December 31, 2010
Equity securities	8.4%	7.9%	59%	61%
Fixed income instruments	4.4%	4.6%	39%	36%
Short-term investments	3.4%	2.7%	2%	3%
Weighted average of expected return	6.7%	6.6%	100%	100%

Plan assets are valued as at the measurement date of December 31 each year. The overall expected rate of return is a weighted average of the expected returns of the various investment categories held in the asset portfolio. The Management Level Pension Fund Investment Committee and Investment Managers assessment of the expected returns is based on historical average return trends and market predictions.

The actual return on plan assets for the year ended December 31, 2011 was $1.9 million (December 31, 2010 $15.4 million).

The experience adjustments on plan liabilities for the year ended December 31, 2011 was a loss of $1.0 million (December 31, 2010 gain of $1.7 million). The experience adjustments on plan assets for the year ended December 31, 2011 was a loss of $8.8 million (December 31, 2010 gain of $5.1 million).

The significant weighted-average assumptions adopted in measuring the Company s pension and other benefit obligations were as follows:

	September 30, Pension	September 30, Other
	December 31, 2011	
Accrued benefit obligation		
Discount rate	4.5%	4.5%
Benefit costs for the periods ended		
Discount rate	5.5%	5.5%
Expected long-term rate of return on plan assets	6.5%	
Future salary increase	3.0%	
Pre and post retirement pension increase	1.1%	

Telesat Holdings Inc.

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(all amounts in thousands of Canadian dollars, except for per share amounts and where otherwise noted)

25. EMPLOYEE BENEFIT PLANS (continued)

For measurement purposes, the medical trend rate for drugs was assumed to be 10.5% for 2011, decreasing by 1% per annum, to a rate of 4.5% per annum in 2016. The health care cost trend rate was assumed to be 9% grading down to 5% in 2019. Other medical trend rates were assumed to be 4.5%.

Actuarial gains and losses recognized in other comprehensive income:

	000000	000000 2011	000000	000000	000000 2010	000000
	Pension	Other	Total	Pension	Other	Total
Cumulative amount at January 1	(10,505)	1,055	(9,450)			
Recognized during the year, net of taxes (2011 $10,486; 2010 $3,357)	(29,614)	(1,463)	(31,077)	(10,505)	1,055	(9,450)
Cumulative amount at December 31	(40,119)	(408)	(40,527)	(10,505)	1,055	(9,450)

Sensitivity of assumptions

The impact of a hypothetical 1% change in the health care cost trend rate on the other post-retirement benefit obligation and the aggregate of service and interest cost would have been as follows:

	September 30, Benefit obligation	September 30, Aggregate of service and interest cost
As reported	24,339	1,482
Impact of increase of 1% point	2,011	146
Impact of decrease of 1% point	(1,706)	(121)

The above sensitivities are hypothetical and should be used with caution. Changes in amounts based on a 1% point variation in assumptions generally cannot be extrapolated because the relationship of the change in assumption to the change in amounts may not be linear. The sensitivities have been calculated independently of changes in other key variables. Changes in one factor may result in changes in another, which could amplify or reduce certain sensitivities.

The Company expects to make contributions of $8.9 million to the defined benefit plans during the next fiscal year.

26. SUPPLEMENTAL CASH FLOW INFORMATION

	September 30, December 31, 2011	September 30, December 31, 2010	September 30, January 1, 2010

Cash and cash equivalents is comprised of:			
Cash	86,500	129,217	89,679
Short term investments, original maturity three months or less	66,547	91,078	64,510
Restricted cash [(a)]	124,915		
	277,962	220,295	154,189

(a) The insurance proceeds received for the settlement of the Telstar 14R/Estrela do Sul 2 claim are restricted in use, and will be used to repay a portion of the Company s Credit Facility or reinvested in satellite procurements in accordance with the terms and conditions of the Credit Agreement. The restricted amount is expected to be used within the next twelve months.

Telesat Holdings Inc.

Notes to the 2011 Consolidated Financial Statements

(all amounts in thousands of Canadian dollars, except for per share amounts and where otherwise noted)

26. SUPPLEMENTAL CASH FLOW INFORMATION (continued)

The net change in operating assets and liabilities shown in the consolidated statements of cash flows is comprised of the following:

At December 31	September 30, 2011	September 30, 2010
Trade and other receivables	(1,668)	21,884
Financial assets	(1,604)	(541)
Other assets	(4,335)	(1,295)
Trade and other payables	(196)	(22,484)
Financial liabilities	(2,061)	(20,249)
Other liabilities	(3,249)	(7,130)
	(13,113)	(29,815)

At December 31	September 30, 2011	September 30, 2010
Non-cash investing and financing activities are comprised of:		
Purchase of satellites, property and other equipment	24,441	24,775

27. COMMITMENTS AND CONTINGENT LIABILITIES

Off balance sheet commitments include operating leases, commitments for future capital expenditures and other future purchases.

Off balance sheet commitments	000000 2012	000000 2013	000000 2014	000000 2015	000000 2016	000000 Thereafter	000000 Total
Operating lease commitments	6,830	6,478	5,824	5,392	4,805	32,628	61,957
Other operating commitments	21,791	18,285	14,271	7,530	3,377	1,388	66,642
Capital commitments	156,096						156,096
Total off balance sheet commitments	**184,717**	**24,763**	**20,095**	**12,922**	**8,182**	**34,016**	**284,695**

Certain of the Company s offices, warehouses, earth stations, and office equipment are leased under various terms. The aggregate expense related to operating lease commitments for the year ended December 31, 2011 was $7 million (December 31, 2010 $8.0 million). The expiry terms range from January 2012 to January 2043.

Telesat has entered into contracts for the construction and launch of Nimiq 6 (targeted for launch in 2012) and Anik G1 (targeted for launch in 2012). The total outstanding commitments at December 31, 2011 are in U.S. dollars.

Cash and cash equivalents includes $124.9 million of restricted cash as at December 31, 2011 (December 31, 2010 zero, January 1, 2010 zero). The restricted cash can be used for capital expenditures of satellite projects. The restricted cash is as a result of insurance proceeds received for the claim filed in relation to Telstar 14R/Estrela do Sul 2. The insurance proceeds were given as the satellite s north solar array anomaly has diminished the amount of power available for the satellite s transponders and reduced the operational life expectancy of the satellite.

Telesat has agreements with various customers for prepaid revenue on several service agreements which take effect when the spacecraft is placed in service. Telesat is responsible for operating and controlling these satellites. Customer prepayments of $408.0 million (December 31, 2010 $377.1 million, January 1, 2010 $358.4 million), refundable under certain circumstances, are reflected in other financial liabilities, both current and long-term.

Telesat Holdings Inc.

Notes to the 2011 Consolidated Financial Statements

(all amounts in thousands of Canadian dollars, except for per share amounts and where otherwise noted)

27. COMMITMENTS AND CONTINGENT LIABILITIES (continued)

In the normal course of business, the Company has executed agreements that provide for indemnification and guarantees to counterparties in various transactions. These indemnification undertakings and guarantees may require the Company to compensate the counterparties for costs and losses incurred as a result of certain events including, without limitation, loss or damage to property, change in the interpretation of laws and regulations (including tax legislation), claims that may arise while providing services, or as a result of litigation that may be suffered by the counterparties. The nature of substantially all of the indemnification undertakings prevents the Company from making a reasonable estimate of the maximum potential amount the Company could be required to pay counterparties as the agreements do not specify a maximum amount and the amounts are dependent upon the outcome of future contingent events, the nature and likelihood of which cannot be determined at this time. Historically, the Company has not made any significant payments under such indemnifications.

Telesat and Loral have entered into an indemnification agreement whereby Loral will indemnify Telesat for any tax liabilities for taxation years prior to 2007 related to Loral Skynet operations. Likewise, Telesat will indemnify Loral for the settlement of any tax receivables for taxation years prior to 2007.

Legal Proceedings

The Company frequently participates in proceedings before national telecommunications regulatory authorities. In addition, the Company may also become involved from time to time in other legal proceedings arising in the normal course of its business.

Telesat Canada s Anik F1 satellite, built by Boeing and launched in November 2000, has defective solar arrays that have caused a drop in power output on the satellite and reduced its operational life. Telesat Canada filed a claim for Anik F1 as a constructive total loss under its insurance policies and received an amount from its insurers in settlement of that claim. In November 2006, Telesat Canada commenced arbitration proceedings against Boeing, alleging that Boeing was grossly negligent and/or engaged in willful misconduct in the design and manufacture of the Anik F1 satellite and in failing to warn Telesat Canada prior to the launch of a material deficiency in the power performance of a similar satellite previously launched. Telesat s claim seeks approximately $331 million plus costs and post-award interest, a portion of which was in respect of the subrogated rights of its insurers. Boeing has responded by alleging that Telesat Canada failed to obtain what it asserts to be contractually required waivers of subrogation rights such that, if Telesat Canada is successful in obtaining an award which includes an amount in respect of the subrogated rights of the insurers, Boeing is entitled to off-setting damages in that amount, which is approximately $176 million. Boeing also asserts that Telesat Canada owes Boeing performance incentive payments pursuant to the terms of the satellite construction contract in the amount of approximately U.S. $5.5 million plus interest. The arbitration hearing is scheduled to commence in November 2012. While it is not possible to determine the ultimate outcome of the arbitration, Telesat Canada intends to vigorously prosecute its claims and defend its position that no liability is owed Boeing in connection with the dispute and that, in the circumstances of this case, it was not contractually required to obtain waivers of the subrogation rights at issue.

Other than the above, the Company is not aware of any proceedings outstanding or threatened as of the date hereof by or against us or relating to its business which may have, or have had in the recent past, significant effects on Telesat Canada s financial position or profitability.

Telesat Holdings Inc.

Notes to the 2011 Consolidated Financial Statements

(all amounts in thousands of Canadian dollars, except for per share amounts and where otherwise noted)

28. SUBSIDIARIES

The list of significant companies included in the scope of consolidation is as follows:

Company	September 30, Country	September 30, Method of Consolidation	September 30, % voting rights December 31, 2011
Telesat Canada	Canada	Fully consolidated	100.00
Infosat Communications LP	Canada	Fully consolidated	100.00
Skynet Satellite Corporation	United States	Fully consolidated	100.00
Telesat Network Services, Inc.	United States	Fully consolidated	100.00
The SpaceConnection Inc.	United States	Fully consolidated	100.00
Telesat Satellite LP	United States	Fully consolidated	100.00
Infosat Able Holdings Inc.	United States	Fully consolidated	100.00
Able Infosat Communications, Inc.	United States	Fully consolidated	100.00
Telesat Brasil Capacidade de Satélites Ltda.	Brazil	Fully consolidated	100.00
Telesat (IOM) Limited	Isle of Man	Fully consolidated	100.00

The percentage of voting rights and interest were the same as at December 31, 2010 and January 1, 2010, respectively.

29. RELATED PARTY TRANSACTIONS

The Company s immediate shareholders are Red Isle Private Investment Inc. (Red Isle), a company incorporated in Canada, Loral Holdings Corporation (Loral Holdings), a company incorporated in the United States, Mr. John P. Cashman and Mr. Colin D. Watson, two Canadian citizens. Red Isle is wholly owned by the Public Sector Pension Investment Board (PSP Investments), a Canadian Crown corporation. Loral Holdings is a wholly owned subsidiary of Loral Space & Communications Inc. (Loral), a United States publically listed company.

Transactions with subsidiaries

The Company and its subsidiaries regularly engage in inter-group transactions. These transactions include the purchase and sale of satellite services and communication equipment, providing and receiving network and call centre services, access to orbital slots and management services. The transactions have been entered into over the normal course of operations. Balances and transactions between the Company and its subsidiaries have been eliminated on consolidation and therefore have not been disclosed.

Transactions with related parties

The Company and certain of its subsidiaries regularly engage in transactions with related parties. The Company s related parties include Loral, Red Isle, Space Systems/Loral (SSL), a satellite manufacturer and a wholly owned subsidiary of Loral, XTAR LLC (XTAR), a satellite operator and affiliate of Loral, and Loral Canadian Gateway Corporation (LCGC), a wholly owned subsidiary of Loral.

On April 11, 2011, Telesat acquired from Loral and LCGC all of its rights and obligations with respect to the Canadian payload on the ViaSat-1 satellite, which was manufactured by SSL, and all related agreements. On closing of the transaction, Telesat paid Loral U.S. $13 million ($12.6 million Canadian dollars) for the assumption of Loral s 15-year revenue contract with Xplornet Communications Inc. for ViaSat-1. In addition Telesat reimbursed Loral and LCGC approximately U.S. $48.2 million of net costs incurred through completion of the sale.

During the year, the Company and its subsidiaries entered into the following transactions with related parties.

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Telesat Holdings Inc.

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(all amounts in thousands of Canadian dollars, except for per share amounts and where otherwise noted)

29. RELATED PARTY TRANSACTIONS (continued)

	September 30, Sale of goods and services, interest income	September 30,	September 30, Purchase of goods and services, interest expense	September 30,
year ended ended	**December 31, 2011**	**December 31, 2010**	**December 31, 2011**	**December 31, 2010**
Loral				
Revenue	1	166		
Operating expenses			4,990	5,245
Interest expense			1,291	1,004
-Intangible asset			12,618	
Red Isle				
Interest expense			9,869	12,339
SSL				
Revenue	1,942	2,373		
Satellite, property and other equipment			180,853	168,040
Operating expenses			1,423	373
XTAR				
Revenue	927	1,017		
LCGC				
Revenue	324	442		
Satellite, property and other equipment			4,586	

The following balances were outstanding at the end of the year:

	September 30, Amounts owed by related parties	September 30,	September 30,	September 30, Amounts owed to related parties	September 30,	September 30,
At	**December 31, 2011**	**December 31, 2010**	**January 1, 2010**	**December 31, 2011**	**December 31, 2010**	**January 1, 2010**
Loral						
Trade receivables/payables					14	
Other long-term financial assets/liabilities	2,387	2,332	2,461	28,252	24,474	19,543
Red Isle						
Other current financial liabilities				1,650	2,075	
Other long-term financial liabilities						25,090
Senior preferred shares				141,435	141,435	141,435
SSL						
Trade receivable/payable	380	428	1,430	4,758	37	1,230

Other current financial liabilities		1,047	1,003	
Other long-term financial liabilities		15,018	15,469	8,068
XTAR				
Trade receivable/payable	79			

The amounts outstanding are unsecured and will be settled in cash. The related party transactions were made on terms equivalent to those that prevail in arm s length transactions.

Telesat Holdings Inc.

Notes to the 2011 Consolidated Financial Statements

(all amounts in thousands of Canadian dollars, except for per share amounts and where otherwise noted)

29. RELATED PARTY TRANSACTIONS (continued)

The Company has entered into contracts for the construction of Nimiq 6 and Anik G1 with SSL. The total outstanding commitments at December 31, 2011 were $50.9 million (December 31, 2010 $187.4 million, January 1, 2010 $225.1 million).

Other related party transactions

The Company funds certain defined benefit pension plans as described in note 25. Contributions made to the plans for the year ended December 31, 2011 were $8.1 million (December 31, 2010 $8.1 million).

Compensation of key management personnel

Key management personnel consists of Board level directors and senior management.

	September 30, Year ended 2011	September 30, Year ended 2010
Short-term benefits (including salary)	7,309	7,262
Post-employment benefits	720	557
Other-long term benefits		
Termination benefits		
Share-based payments	2,572	4,514
	10,601	12,333

There were no transactions with key management personnel in 2011 and 2010 other than compensation.

30. CONDENSED CONSOLIDATING FINANCIAL INFORMATION

The 11.0% Senior Notes and the 12.5% Senior Subordinated Notes were co-issued by Telesat LLC and Telesat Canada, (the Issuers) which are 100% owned subsidiaries of Telesat, and were guaranteed fully and unconditionally, on a joint and several basis, by Telesat and certain of its subsidiaries.

The condensed consolidating financial information below for the year ended December 31, 2011 and the year ended December 31, 2010 are presented pursuant to Article 3-10(d) of Regulation S-X. The information presented consists of the operations of Telesat Holdings Inc. Telesat Holdings Inc. primarily holds investments in subsidiaries and equity. Telesat LLC, a U.S. Delaware corporation, is a financing subsidiary that has no assets, liabilities or operations.

The condensed consolidating financial information reflects the investments of Telesat Holdings Inc. in the Issuers, of the Issuers in their respective Guarantor and Non-Guarantor subsidiaries and of the Guarantors in their Non-Guarantor subsidiaries using the equity method.

Condensed Consolidating Statement of Income (Loss)

For the year ended December 31, 2011

	Telesat Holdings	Telesat LLC	Telesat Canada	Guarantor Subsidiaries	Non-guarantor Subsidiaries	Adjustments	Consolidated
Revenue			742,728	110,203	20,286	(64,856)	808,361
Operating expenses			(134,137)	(95,827)	(22,657)	64,856	(187,765)
			608,591	14,376	(2,371)		620,596
Depreciation			(146,581)	(51,711)	(334)		(198,626)
Amortization			(42,480)	1,541	(82)		(41,021)
Other operating gains (losses), net			116,063	(1,989)	(6)		114,068
Operating income (loss)			535,593	(37,783)	(2,793)		495,017
Income (loss) from equity investments	247,144		(40,204)	(3,049)		(203,891)	
Interest (expense) income	(9,869)		(219,590)	2,421	(13)		(227,051)
Interest and other income			86	1,465	3		1,554
Gain on changes in fair value of financial instruments			98,585				98,585
(Loss) gain on foreign exchange			(75,155)	(6,084)	2,395		(78,844)
Income (loss) before tax	237,275		299,315	(43,030)	(408)	(203,891)	289,261
Tax (expense) benefit			(52,171)	106	79		(51,986)
Net income (loss)	237,275		247,144	(42,924)	(329)	(203,891)	237,275

Condensed Consolidating Statement of Income (Loss)

For the year ended December 31, 2010

	Telesat Holdings	Telesat LLC	Telesat Canada	Guarantor Subsidiaries	Non-guarantor Subsidiaries	Adjustments	Consolidated
Revenue			745,689	98,049	23,839	(46,216)	821,361
Operating expenses			(144,180)	(83,375)	(25,125)	46,216	(206,464)
			601,509	14,674	(1,286)		614,897
Depreciation			(147,892)	(53,948)	(343)		(202,183)
Amortization			(47,395)	2,126	(199)		(45,468)
Other operating losses, net			75,023	7,995			83,018
Operating income (loss)			481,245	(29,153)	(1,828)		450,264
Income (loss) from equity investments	298,439		(30,096)	(32,013)		(236,330)	
Interest (expense) income	(12,338)		(244,372)	125	3		(256,582)
Interest and other income (expense)			4,316	1,517	(81)		5,752
Loss on changes in fair value of financial instruments			(11,168)				(11,168)
Gain (loss) on foreign exchange			162,921	7,333	(6,288)		163,966
Income (loss) before tax	286,101		362,846	(52,191)	(8,194)	(236,330)	352,232
Tax expense			(64,407)	(1,169)	(555)		(66,131)
Net income (loss)	286,101		298,439	(53,360)	(8,749)	(236,330)	286,101

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Condensed Consolidating Balance Sheet

As at December 31, 2011

	Telesat Holdings	Telesat LLC	Telesat Canada	Guarantor Subsidiaries	Non-guarantor Subsidiaries	Adjustments	Consolidated
Assets							
Cash and cash equivalents			256,837	18,654	2,471		277,962
Trade and other receivables			27,010	18,670	1,109		46,789
Other current financial assets			26	255	6,729		7,010
Intercompany receivable			349,662	137,658	148,153	(635,473)	
Prepaid expenses and other current assets			14,052	8,019	55		22,126
Total current assets			647,587	183,256	158,517	(635,473)	353,887
Satellites, property and other equipment			1,808,997	340,992	1,926		2,151,915
Other long-term financial assets			141,084	896	428		142,408
Other long-term assets			3,010	2,526			5,536
Intangible assets			848,898	47,077	103		896,078
Investment in affiliates	1,878,938		1,184,893	1,495,142	260	(4,559,233)	
Goodwill			2,078,056	343,876	24,671		2,446,603
Total assets	1,878,938		6,712,525	2,413,765	185,905	(5,194,706)	5,996,427
Liabilities							
Trade and other payables			33,405	9,118	2,633		45,156
Other current financial liabilities	1,650		79,995	1,308	35		82,988
Intercompany payable	45,689		179,352	375,012	35,420	(635,473)	
Other current liabilities			64,393	3,111	373		67,877
Current indebtedness			86,494	1			86,495
Total current liabilities	47,339		443,639	388,550	38,461	(635,473)	282,516
Long-term indebtedness			2,748,131				2,748,131
Deferred tax liabilities			452,208	(312)			451,896
Other long-term financial liabilities			255,630	3,862	291		259,783
Other long-term liabilities			411,533	10,726	243		422,502
Senior preferred shares	141,435						141,435
Total liabilities	188,774		4,311,141	402,826	38,995	(635,473)	4,306,263
Shareholders Equity							
Share capital	1,298,178		2,320,730	1,898,682	104,434	(4,323,846)	1,298,178
Accumulated earnings (deficit)	369,992		35,415	176,382	42,071	(253,868)	369,992
Reserves	21,994		45,239	(64,125)	405	18,481	21,994
Total shareholders equity	1,690,164		2,401,384	2,010,939	146,910	(4,559,233)	1,690,164
Total liabilities and shareholders equity	1,878,938		6,712,525	2,413,765	185,905	(5,194,706)	5,996,427

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Condensed Consolidating Balance Sheet

As at December 31, 2010

	Telesat Holdings	Telesat LLC	Telesat Canada	Guarantor Subsidiaries	Non-guarantor Subsidiaries	Adjustments	Consolidated
Assets							
Cash and cash equivalents			196,682	21,135	2,478		220,295
Trade and other receivables			28,718	13,593	1,772		44,083
Other current financial assets			25	346	6,573		6,944
Intercompany receivable			219,035	202,459	112,436	(533,930)	
Prepaid expenses and other current assets			13,671	7,136	130		20,937
Total current assets			458,131	244,669	123,389	(533,930)	292,259
Satellites, property and other equipment			1,643,419	333,173	2,197		1,978,789
Other long-term financial assets			77,503	502	626		78,631
Other long-term assets			7,907	4,120			12,027
Intangible assets			909,744	35,617	186		945,547
Investment in affiliates	1,663,758		1,309,540	1,487,893	259	(4,461,450)	
Goodwill			2,078,056	343,876	24,671		2,446,603
Total assets	1,663,758		6,484,300	2,449,850	151,328	(4,995,380)	5,753,856
Liabilities							
Trade and other payables			31,667	15,164	3,143		49,974
Intercompany payable	35,385		124,484	374,061		(533,930)	
Other current financial liabilities	2,075		100,610	1,233	164		104,082
Other current liabilities			61,643	301	701		62,645
Current indebtedness			96,847	1			96,848
Total current liabilities	37,460		415,251	390,760	4,008	(533,930)	313,549
Long-term indebtedness			2,771,802				2,771,802
Deferred tax liabilities			416,069	(2,002)	650		414,717
Other long-term financial liabilities			265,346		283		265,629
Other long-term liabilities			348,873	12,750	238		361,861
Senior preferred shares	141,435						141,435
Total liabilities	178,895		4,217,341	401,508	5,179	(533,930)	4,268,993
Shareholders Equity							
Share capital	1,298,178		2,320,730	1,896,596	104,434	(4,321,760)	1,298,178
Accumulated earnings (deficit)	163,804		(128,079)	216,134	38,204	(126,259)	163,804
Reserves	22,881		74,308	(64,388)	3,511	(13,431)	22,881
Total shareholders equity	1,484,863		2,266,959	2,048,342	146,149	(4,461,450)	1,484,863
Total liabilities and shareholders equity	1,663,758		6,484,300	2,449,850	151,328	(4,995,380)	5,753,856

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Condensed Consolidating Balance Sheet

As at January 1, 2010

	Telesat Holdings	Telesat LLC	Telesat Canada	Guarantor Subsidiaries	Non-guarantor Subsidiaries	Adjustments	Consolidated
Assets							
Cash and cash equivalents			137,623	14,232	2,334		154,189
Trade and other receivables			51,444	15,591	3,165		70,200
Other current financial assets			101	267	6,949		7,317
Intercompany receivable			249,103	150,490	120,038	(519,631)	
Prepaid expenses and other current assets			14,957	7,967	77		23,001
Total current assets			453,228	188,547	132,563	(519,631)	254,707
Satellites, property and other equipment			1,446,613	449,801	2,484		1,898,898
Other long-term financial assets			20,545	529	659		21,733
Other long-term assets			13,311	5,720			19,031
Intangible assets			886,965	38,570	386		925,921
Investment in affiliates	1,371,792		1,346,054	1,477,459	261	(4,195,566)	
Goodwill			2,078,057	343,876	24,670		2,446,603
Total assets	1,371,792		6,244,773	2,504,502	161,023	(4,715,197)	5,566,893
Liabilities							
Trade and other payables			32,059	6,798	4,556		43,413
Intercompany payable			108,346	411,285		(519,631)	
Other current financial liabilities			100,685	1,304	135		102,124
Other current liabilities			70,523	1,093	505		72,121
Current indebtedness			23,601	1			23,602
Total current liabilities			335,214	420,481	5,196	(519,631)	241,260
Long-term indebtedness			3,021,820				3,021,820
Deferred tax liabilities			355,904	(2,266)	(1)		353,637
Other long-term financial liabilities	25,090		214,633	102			239,825
Other long-term liabilities			346,705	16,268	676		363,649
Senior preferred shares	141,435						141,435
Total liabilities	166,525		4,274,276	434,585	5,871	(519,631)	4,361,626
Shareholders Equity							
Share capital	1,298,178		2,320,730	1,896,596	104,434	(4,321,760)	1,298,178
Accumulated earnings (deficit)	(112,817)		(430,301)	237,247	46,953	146,101	(112,817)
Reserves	19,906		80,068	(63,926)	3,765	(19,907)	19,906
Total shareholders equity	1,205,267		1,970,497	2,069,917	155,152	(4,195,566)	1,205,267
Total liabilities and shareholders equity	1,371,792		6,244,773	2,504,502	161,023	(4,715,197)	5,566,893

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Condensed Consolidating Statement of Cash Flow

For the year ended December 31, 2011

	Telesat Holdings	Telesat LLC	Telesat Canada	Guarantor Subsidiaries	Non-guarantor Subsidiaries	Adjustments	Consolidated
Cash flows from (used in) operating activities							
Net income (loss)	237,275		247,144	(42,924)	(329)	(203,891)	237,275
Adjustments to reconcile net income (loss) to cash flows from operating activities:							
Amortization and depreciation			189,061	50,170	416		239,647
Deferred tax expense (benefit)			52,099	(145)	(100)		51,854
Unrealized foreign exchange loss (gain)			66,375	4,045	(2,714)		67,706
Unrealized gain on derivatives			(87,914)				(87,914)
Dividends on senior preferred shares	1,650						1,650
Share-based compensation			2,073	383	198		2,654
Income (loss) from equity investments	(247,144)		40,204	3,049		203,891	
Loss on disposal of assets			588	879	16		1,483
Impairment loss on intangible assets			18,368	1,100			19,468
Insurance proceeds			(135,019)				(135,019)
Other			(28,167)	(2,876)	242		(30,801)
Customer prepayments on future satellite services			55,268	2,500			57,768
Insurance proceeds			11,228				11,228
Operating assets and liabilities	(2,075)		1,944	(15,262)	2,280		(13,113)
Net cash from (used in) operating activities	(10,294)		433,252	919	9		423,886
Cash flows from (used in) investing activities							
Satellite programs			(302,193)	(54,006)			(356,199)
Purchases of other property and equipment			(16,137)	(1,374)	(55)		(17,566)
Purchase of intangible assets				(12,618)			(12,618)
Insurance proceeds			135,019				135,019
Proceeds from sale of assets			148				148
Business acquisitions			(9,264)	9,264			
Dividends received			8,633			(8,633)	
Net cash used in investing activities			(183,794)	(58,734)	(55)	(8,633)	(251,216)
Cash flows from (used in) financing activities							
Repayment of indebtedness			(108,741)				(108,741)
Dividends paid on preferred shares	(10)						(10)
Satellite performance incentive payments			(5,928)				(5,928)
Intercompany loan	10,304		(74,634)	64,330			
Dividends paid				(8,633)		8,633	
Net cash from (used in) financing activities	10,294		(189,303)	55,697		8,633	(114,679)
Effect of changes in exchange rates on cash and cash equivalents				(363)	39		(324)
Increase (decrease) in cash and cash equivalents			60,155	(2,481)	(7)		57,667
Cash and cash equivalents, beginning of year			196,682	21,135	2,478		220,295
Cash and cash equivalents, end of year			256,837	18,654	2,471		277,962

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Condensed Consolidating Statement of Cash Flow

For the year ended December 31, 2010

	Telesat Holdings	Telesat LLC	Telesat Canada	Guarantor Subsidiaries	Non-guarantor Subsidiaries	Adjustments	Consolidated
Cash flows from operating activities							
Net income (loss)	286,101		298,439	(53,360)	(8,749)	(236,330)	286,101
Adjustments to reconcile net income (loss) to cash flows from operating activities:							
Amortization and depreciation			195,287	51,822	542		247,651
Deferred tax expense			63,277	146	429		63,852
Unrealized foreign exchange (gain) loss			(168,787)	(7,502)	6,273		(170,016)
Unrealized loss on derivatives			13,955				13,955
Dividends on senior preferred shares	2,075						2,075
Share-based compensation			3,691	635	341		4,667
(Income) loss from equity investments	(298,439)		30,096	32,013		236,330	
Gain on disposal of assets			(3,754)	(72)			(3,826)
Reversal of impairment loss on intangible assets			(71,269)				(71,269)
Reversal of impairment loss on satellites, property and other equipment				(7,923)			(7,923)
Other			(24,600)	(315)	(15)		(24,930)
Customer prepayments on future satellite services			30,982				30,982
Operating assets and liabilities	10,293		(44,971)	2,867	1,996		(29,815)
Net cash from operating activities	30		322,346	18,311	817		341,504
Cash flows used in investing activities							
Satellite programs			(257,725)				(257,725)
Purchase of other property and equipment			(2,299)	(1,556)	(111)		(3,966)
Proceeds from sale of assets			26,782	144			26,926
Other			10,000			(10,000)	
Net cash used in investing activities			(223,242)	(1,412)	(111)	(10,000)	(234,765)
Cash flows from (used in) financing activities							
Repayment of indebtedness			(34,946)				(34,946)
Dividends paid on preferred shares	(30)						(30)
Satellite performance incentive payments			(5,099)				(5,099)
Dividends paid				(10,000)		10,000	
Net cash from (used in) financing activities	(30)		(40,045)	(10,000)		10,000	(40,075)
Effect of changes in exchange rates on cash and cash equivalents				4	(562)		(558)
Increase in cash and cash equivalents			59,059	6,903	144		66,106
Cash and cash equivalents, beginning of year			137,623	14,232	2,334		154,189
Cash and cash equivalents, end of year			196,682	21,135	2,478		220,295