

NOTES TO THE FINANCIAL STATEMENTS

December 31, 2005

(Amount expressed in Hong Kong dollars unless otherwise stated)

1 GROUP ORGANIZATION

PCCW Limited (the “Company”) was incorporated in the Hong Kong Special Administrative Region (“Hong Kong”) and its securities have been listed on The Stock Exchange of Hong Kong Limited (the “Stock Exchange”) since October 18, 1994. The address of its registered office is 39th Floor, PCCW Tower, TaiKoo Place, 979 King’s Road, Quarry Bay, Hong Kong. The principal activities of the Company and its subsidiaries (the “Group”) are the provision of local, mobile and international telecommunications services, Internet and interactive multimedia services, the sale and rental of telecommunications equipment, and the provision of computer, engineering and other technical services, mainly in Hong Kong; investment in, and development of, systems integration and technology-related businesses; and investment in, and development of, infrastructure and properties in Hong Kong and elsewhere in mainland China.

a. Subscription by China Network Communications Group Corporation (“China Netcom Group”)

On January 19, 2005, China Netcom Group, a state-owned enterprise established under the laws of the People’s Republic of China (the “PRC”), and China Netcom Group Corporation (BVI) Limited (“CNC (BVI)”), a company incorporated in the British Virgin Islands which is a wholly-owned subsidiary of China Netcom Group, entered into a conditional subscription agreement (the “Subscription Agreement”) with the Company. Pursuant to the Subscription Agreement, CNC (BVI) conditionally agreed to subscribe for 1,343,571,766 new ordinary shares of the Company of HK\$0.25 each at a price of HK\$5.90 per share (the “Subscription”), representing approximately 20% of the Company’s issued share capital as enlarged by the allotment and issue of the subscription shares. CNC (BVI) directed the Company to allot and issue those subscription shares to China Netcom Corporation (BVI) Limited (“China Netcom (BVI)”), a wholly-owned subsidiary of CNC (BVI). The proceeds of the Subscription were approximately HK\$7,927 million (before deduction of expenses). Subject to the Group’s capital investment procedures and the identification of appropriate investment opportunities, the Company intends to invest up to HK\$5,000 million of these proceeds in telecommunications opportunities in the PRC. The remainder will be used for reducing the Group’s debt and general corporate purposes. The Subscription Agreement and related matters were approved by the Company’s shareholders pursuant to an ordinary resolution passed at an extraordinary general meeting of the Company held on March 16, 2005. On April 1, 2005, the Subscription was completed and China Netcom (BVI) became a substantial shareholder and connected person (as defined in the Rules Governing the Listing of Securities on the Stock Exchange (the “Listing Rules”)) of the Company.

b. Conversion of Tranche A Convertible Note due 2011 issued by Pacific Century Premium Developments Limited (“PCPD”)

On February 24, 2005, the Company elected to convert Tranche A Convertible Note due 2011 with the principal amount of HK\$1,170 million, which was issued by PCPD, an indirect non wholly-owned subsidiary of the Company, to the Company on May 10, 2004, into new shares of PCPD of HK\$0.10 each at HK\$2.25 per PCPD share. Upon the exercise of conversion rights by the Company effective March 1, 2005, PCPD allotted and issued 520,000,000 new PCPD shares to Asian Motion Limited (“Asian Motion”), a wholly-owned subsidiary of the Company, as directed by the Company, which rank *pari passu* in all respects with the existing shares of PCPD. Immediately after the conversion and as at December 31, 2005, the Company, through Asian Motion, holds an equity interest of approximately 61.66% in the issued share capital of PCPD.

c. Establishment of a new operating model for Reach Ltd. (“REACH”) and restructuring of REACH’s debt

On April 16, 2005, the Company agreed with Telstra Corporation Limited (“Telstra”) and REACH on a new operating model under which REACH would operate as an outsourcer of telecommunications network services for the Group and Telstra and its subsidiaries (the “Telstra Group”). To implement this new operating model, PCCW Global (Singapore) Pte. Ltd. (formerly PCCW Communications (Singapore) Pte Ltd) (“PCCW Global (Singapore)”), an indirect wholly-owned subsidiary of the Company, and Telstra each agreed to acquire indefeasible rights to use international undersea cable capacity of REACH and its subsidiaries (“Reach Group”) (the “IRU”), for which PCCW Global (Singapore) and Telstra each paid Reach Global Networks Limited, a wholly-owned subsidiary of REACH, US\$157 million (approximately HK\$1,225 million) which was settled by way of set-off against, in the case of the Group and pursuant to the Reach Debt and Asset Restructure Deed dated April 16, 2005 between certain members of the Group, the Telstra Group and the Reach Group, the outstanding loan of approximately US\$600 million plus interest of US\$8 million owed to the Group by the Reach Group (“Shareholder Loan”), and not by way of new cash injections.

PCCW Global (Singapore) and Telstra also each assumed one half of certain of REACH’s committed payments in order to support growth in their own retail services. PCCW Global (Singapore)’s share of these payments over the next 17-year period from March 2005 to 2022 is expected to be approximately US\$106 million. PCCW Global (Singapore) and Telstra will only assume any additional future payments if it is approved by both parties.

1 GROUP ORGANIZATION *(CONTINUED)*

c. Establishment of a new operating model for Reach Ltd. (“REACH”) and restructuring of REACH’s debt *(continued)*

For accounting purposes, the IRU has been recognized as “Property, plant and equipment” in the amount of HK\$1,576 million. It consists of an offset against an existing shareholder loan of US\$157 million (approximately HK\$1,225 million) and the assumption of one half of REACH’s future capital expenditure payments relating to the IRU totaling approximately US\$45 million (approximately HK\$351 million). The remaining committed payments relate to purchases of plant and equipment of HK\$74 million and operating expenses of HK\$402 million which will be capitalized as “Property, plant and equipment” and written off as and when these payments are made respectively. A total of US\$9 million (approximately HK\$70 million) was paid during the year.

In addition, interest of US\$6 million due by REACH to the Group was waived and US\$290 million of the remaining balance of the Shareholder Loan and the amount owed by REACH of US\$155 million under the capacity prepayment agreement was capitalized by way of the issue of 445,000,000 shares in REACH to Pacific Century Cable Holdings Limited, a wholly-owned subsidiary of the Company and holder of the Group’s interest in REACH since its formation. Following the set-off and capitalization referred to above, REACH’s aggregate indebtedness to the Group was reduced to US\$155 million.

The subscription of additional shares in REACH and waiver of interest payable would have no impact on the financial statements of the Group as the carrying value of the Shareholder Loan and the outstanding amount under the capacity prepayment agreement entered into on April 15, 2003, together with their accrued interest, had been written off entirely in prior years.

Further, pursuant to the Reach Network Services Agreement dated April 16, 2005 between certain members of the Group, the Telstra Group and the Reach Group (“Reach Network Services Agreement”), REACH will provide to the Group and the Telstra Group certain outsourcing services in relation to the international undersea cable capacity allocated by way of the grant of the IRU.

As part of the arrangements relating to the establishment of the new operating model for REACH, the International Services Agreement was terminated pursuant to the provisions of the Reach Network Services Agreement and the Group’s obligations under the capacity prepayment agreement have been satisfied under the Reach Debt and Asset Restructure Deed.

d. Acquisition of SUNDAY Communications Limited (“SUNDAY”)

On June 13, 2005, the Company entered into a conditional sale and purchase agreement (“First Agreement”) with Distacom Hong Kong Limited (“Distacom HK”) and Distacom Communications Limited, whereby the Company conditionally agreed to purchase (or procure the purchase by one of its wholly-owned subsidiaries) and Distacom HK conditionally agreed to sell an aggregate of 1,380,000,000 ordinary shares of HK\$0.10 each (“SUNDAY Shares”) of SUNDAY, a company incorporated in the Cayman Islands with limited liability whose shares are listed on the Stock Exchange and whose American depository shares are quoted on the NASDAQ National Market in the United States of America, representing approximately 46.15% of the issued share capital of SUNDAY, for the consideration of HK\$897,000,000 in cash, being a price of HK\$0.65 per SUNDAY Share. On the same date, the Company entered into a separate conditional sale and purchase agreement (“Second Agreement”) with Townhill Enterprises Limited (“Townhill”) and USI Holdings Limited, whereby the Company conditionally agreed to purchase (or procure the purchase by one of its wholly-owned subsidiaries) and Townhill conditionally agreed to sell an aggregate of 410,134,000 SUNDAY Shares, representing approximately 13.72% of the issued share capital of SUNDAY, for the consideration of HK\$266,587,100 in cash, being a price of HK\$0.65 per SUNDAY Share. Upon the completion of both the First Agreement and the Second Agreement on June 22, 2005, the Company, through PCCW Mobile Holding No. 2 Limited (“PCCW Mobile”), was interested in an aggregate of 1,790,134,000 SUNDAY Shares, representing approximately 59.87% of the then issued share capital of SUNDAY, and as a result, SUNDAY became a subsidiary of the Company.

On July 8, 2005, PCCW Mobile made a mandatory unconditional cash offer (the “Offer”), through Citigroup Global Markets Asia Limited, to acquire all the SUNDAY Shares other than those owned by PCCW Mobile pursuant to Rule 26.1 of the Takeovers Code. The offer price was at HK\$0.65 per SUNDAY Share, which was the same as the price payable by PCCW Mobile for each SUNDAY Share purchased under the First Agreement and the Second Agreement. Upon the closure of the Offer on September 9, 2005, PCCW Mobile owned in aggregate of 2,372,672,256 SUNDAY Shares, representing approximately 79.35% of the issued share capital of SUNDAY.

The Stock Exchange granted waivers to SUNDAY for the period between September 9, 2005 and 15 April, 2006 relating to the compliance with the 25% minimum public float requirement for SUNDAY Shares.

1 GROUP ORGANIZATION (CONTINUED)

e. Disposal of gaming business in Japan

On July 22, 2005, a sale and purchase agreement was signed to dispose of the Group's 79.72% interest in JALECO LTD. ("JALECO") held by an indirect wholly-owned subsidiary of the Company. The disposal was completed on August 19, 2005 for a consideration of approximately US\$48.3 million and the Group recognized a disposal gain of approximately HK\$159 million.

f. Disposal of interest in MobileOne Ltd

On August 17, 2005, the Company announced that a conditional agreement had been signed to dispose of approximately 12.1% interest in MobileOne Ltd, one of the three mobile telephone operators in Singapore, by Great Eastern Telecommunications Limited ("GET"), an associate of the Group, for a consideration of approximately S\$260.8 million. The disposal was completed on October 28, 2005. As a 49% shareholder of GET, the Group recognized approximately HK\$52 million as its share of the disposal gain recognized by GET.

2 BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES

a. Statement of compliance

These financial statements have been prepared in accordance with applicable Hong Kong Financial Reporting Standards ("HKFRSs"), which collective term includes all applicable individual Hong Kong Financial Reporting Standards, Hong Kong Accounting Standards ("HKASs") and Interpretations issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA"), accounting principles generally accepted in Hong Kong and the requirements of the Hong Kong Companies Ordinance. A summary of the principal accounting policies adopted by the Group is set out below.

The HKICPA has issued a number of new and revised HKFRSs that are effective or available for early adoption for accounting periods beginning on or after January 1, 2005. Information on the changes in accounting policies resulting from initial application of these new and revised HKFRSs for the current and prior accounting periods reflected in these financial statements is provided in note 4.

b. Basis of preparation of the financial statements

The consolidated financial statements for the year ended December 31, 2005 comprise the Company and its subsidiaries, other than those unconsolidated subsidiaries acquired exclusively with a view for resale, and the Group's interest in jointly controlled companies and associates.

The measurement basis used in the preparation of the financial statements is historical cost basis, except that the following assets and liabilities are stated at fair value as explained in the accounting policies set out below:

- investment properties (see note 2(g));
- financial instruments classified as financial assets at fair value through profit or loss (see note 2(n)(i)) and available-for-sale financial assets (see note 2(n)(iii)); and
- derivative financial instruments (see note 2(p)).

The investment in unconsolidated subsidiaries held for sale is stated at the lower of carrying amount and fair value less costs to sell (see note 2(t)).

The preparation of financial statements in conformity with HKFRSs requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets, liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Judgements made by management in the application of HKFRSs that have significant effect on the financial statements and estimates with a significant risk of material adjustments in the next year are discussed in note 3.

2 BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES (CONTINUED)

c. Subsidiaries and controlled entities

A subsidiary, in accordance with the Hong Kong Companies Ordinance, is a company in which the Company, directly or indirectly, holds more than half of the issued share capital or controls more than half the voting power, or controls the composition of the board of directors. Subsidiaries are considered to be controlled if the Company has the power, directly or indirectly, to govern its financial and operating policies, so as to obtain benefits from their activities.

An investment in a controlled subsidiary is consolidated into the consolidated financial statements from the date that control commences until the date that control ceases.

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest. The excess of the cost of acquisition over the fair value of the Group's share of identifiable net assets acquired is recorded as goodwill (see note 2(l)).

Where the Group increases its interest in a subsidiary, its incremental interest gives rise to additional goodwill in the subsidiary. The goodwill is determined as the difference between the consideration given and the interest acquired in the subsidiary's net assets and contingent liabilities at their carrying values on the Group's consolidated balance sheet. No fair value exercise is performed because HKFRS 3 allows a step-up to fair values only at the date control is gained. Where the Group decreases its interest in a subsidiary without losing control, any gain or loss on the partial disposal is recognized as "Other gains, net" in the consolidated income statement.

Intra-group balances and transactions and any unrealized profits arising from intra-group transactions are eliminated in full in preparing the consolidated financial statements. Unrealized losses resulting from intra-group transactions are eliminated in the same way as unrealized gains but only to the extent that there is no evidence of impairment.

Minority interests in the balance sheet, being the portion of the net assets of subsidiaries attributable to equity interests that are not owned by the Company, whether directly or indirectly through subsidiaries, are presented in the consolidated balance sheet and statement of changes in equity within equity, separately from equity attributable to the equity holders of the Company. Minority interests in the results of the Group are presented on the face of the consolidated income statement as an allocation of the total profit or loss for the year between minority interests and the equity holders of the Company.

Where losses applicable to the minority exceed the minority's interest in the equity of a subsidiary, the excess, and any further losses applicable to the minority, are charged against the Group's interest except to the extent that the minority has a binding obligation to, and is able to, make additional investment to cover the losses. If the subsidiary subsequently reports profits, the Group's interest is allocated all such profits until the minority's share of losses previously absorbed by the Group has been recovered.

For subsidiaries which have accounting year ends different from the Group, the subsidiaries prepare, for the purpose of consolidation, financial statements up to and as at the same date as the Group.

In the Company's balance sheet, an investment in a subsidiary is stated at cost less impairment losses (see note 2(o)). The results of subsidiaries are accounted for by the Company on the basis of dividends received and receivable.

d. Associates

An associate is an entity in which the Group or the Company has significant influence, but not control or joint control, over its management, including participating in the financial and operating policy decisions.

Investments in associates are accounted for in the consolidated financial statements under the equity method and are initially recorded at cost and adjusted thereafter for the post-acquisition change in the Group's share of the associates' net assets. The consolidated income statement includes the Group's share of post-acquisition, post-tax results of the associates for the year.

When the Group's share of losses exceeds its interest in the associate, the Group's interest is reduced to nil and recognition of further losses is discontinued except to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of the associate. For this purpose, the Group's interest in the associate is the carrying amount of the investment under the equity method together with the Group's long-term interests that in substance form part of the Group's net investment in the associate.

2 BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES (CONTINUED)

d. Associates (continued)

Unrealized profits and losses resulting from transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associate, except where unrealized losses provide evidence of an impairment of the asset transferred, in which case they are recognized immediately in profit or loss.

In the Company's balance sheet, investments in associates are stated at cost less impairment losses (see note 2(o)). The results of associates are accounted for by the Company on the basis of dividends received and receivable.

e. Joint ventures and jointly controlled companies

A joint venture or a jointly controlled company is an entity which operates under a contractual arrangement between the Group or the Company and other parties, where the contractual arrangement establishes that the Group or the Company and one or more of the other parties share joint control over the economic activity of the entity. The Group has made investments in joint ventures in the People's Republic of China (the "PRC") in respect of which the partners' profit-sharing ratios during the joint venture period and share of net assets upon the expiration of the joint venture period may not be in proportion to their equity ratios, but are as defined in the respective joint venture contracts.

Investments made by means of joint venture structures where the Group or the Company controls the composition of the board of directors or equivalent governing body and/or is in a position to exercise control over the financial and operating policies of the joint ventures are accounted for as subsidiaries.

Investments in jointly controlled companies or joint ventures are accounted for in the consolidated financial statements under the equity method, as described in note 2(d) above.

In the Company's balance sheet, investments in joint ventures and jointly controlled companies are stated at cost less impairment losses (see note 2(o)). The results of joint ventures and jointly controlled companies are accounted for by the Company on the basis of dividends received and receivable.

f. Property, plant and equipment

The following items of property, plant and equipment are stated in the balance sheet at cost less accumulated depreciation and impairment losses (see note 2(o)):

- buildings held for own use which are situated on leasehold land, where the fair value of the building could be measured separately from the fair value of the leasehold land at the inception of the lease (see note 2(h)); and
- other items of plant and equipment.

The cost of an item of property, plant and equipment comprises (i) its purchase price, (ii) any directly attributable costs of bringing the asset to its working condition and location for its intended use, and (iii) the initial estimate at the time of installation and during the period of use, where relevant, of the costs of dismantling and removing the items and restoring the site on which they are located.

Subsequent costs are included in the carrying amount of an item of property, plant and equipment or recognized as a separate item of property, plant and equipment, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other costs, such as repairs and maintenance and overhaul costs, are recognized in the income statement as an expense in the period in which they are incurred.

Gains or losses arising from the retirement or disposal of an item of property, plant and equipment are determined as the difference between the net disposal proceeds and the carrying amount of the item and are recognized in the income statement on the date of retirement or disposal.

2 BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES (CONTINUED)

f. Property, plant and equipment (continued)

Freehold land is not depreciated. Depreciation on other property, plant and equipment is calculated to write off the cost of items of property, plant and equipment, less their expected residual value, if any, using the straight line method over their estimated useful lives as follows:

Land and buildings	Over the shorter of the unexpired term of land lease and the estimated useful lives
Exchange equipment	5 to 15 years
Transmission plant	5 to 25 years
Other plant and equipment	Over the shorter of 2 to 17 years and the term of lease

Both the useful life of an asset and its residual value, if any, are reviewed, and adjusted if appropriate, at each balance sheet date.

g. Investment properties

Investment properties are land and/or buildings which are owned or held under a leasehold interest (see note 2(h)) to earn rental income and/or for capital appreciation, and which are not occupied by the companies in the consolidated Group.

Investment properties are stated in the balance sheet at fair value, based on active market prices, adjusted, if necessary, for any difference in the nature, location or condition of the specific asset, determined annually by independent qualified valuers. The fair value of investment properties reflects, among other things, rental income from current leases and assumptions about rental income from future leases in the light of current market conditions. Any gain or loss arising from a change in fair value or from the retirement or disposal of an investment property is recognized in the income statement. Rental income from investment properties is accounted for as described in note 2(z)(iv).

When the Group holds a property interest under an operating lease to earn rental income and/or for capital appreciation, the interest is classified and accounted for as an investment property on a property-by-property basis. Any such property interest which has been classified as an investment property is accounted for as if it were held under a finance lease (see note 2(h)), and the same accounting policies are applied to that interest as are applied to other investment properties leased under finance leases. Lease payments are accounted for as described in note 2(h).

When an item of property, plant and equipment is transferred to investment property following a change in its use, any differences between the carrying amount and the fair value of the item arising at the date of transfer is recognized directly in equity if it is a gain. Upon disposal of the item the gain is transferred to retained earnings. Any loss arising in this manner is recognized immediately in the income statement.

If an investment property becomes owner-occupied, it is reclassified as property, plant and equipment and its fair value at the date of reclassification becomes its cost for accounting purposes. Investment property, that is being redeveloped for continued future use as investment property, continues to be measured at fair value and is not reclassified as property, plant and equipment during the redevelopment.

Property that is being constructed or developed for future use as investment property is classified as property, plant and equipment and stated at cost until construction or development is complete, at which time it is reclassified as investment property at fair value. Any difference between the fair value of the property at that date and its previous carrying amount is recognized in the income statement.

h. Leased assets

i. Classification of assets leased to the Group

Leases which do not transfer substantially all the risks and rewards of ownership to the Group are classified as operating leases, except for property held under operating leases that would otherwise meet the definition of an investment property, which is classified as an investment property on a property-by-property basis and, if classified as investment property, is accounted for as if held under a finance lease (see note 2(g)).

ii. Assets held for use in operating leases

Where the Group leases out assets under operating leases, the assets are included in the balance sheet according to their nature and, where applicable, are depreciated in accordance with the Group's depreciation policies, as set out in note 2(f). Impairment losses are accounted for in accordance with the accounting policy as set out in note 2(o). Revenue arising from operating leases is recognized in accordance with the Group's revenue recognition policies, as set out in note 2(z)(iv).

2 BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES (CONTINUED)

h. Leased assets (continued)

iii. Operating lease charges

Where the Group has the use of assets held under operating leases, payments made under the leases are charged to the income statement in equal instalments over the accounting periods covered by the lease term, except where an alternative basis is more representative of the pattern of benefits to be derived from the leased asset. Lease incentives received are recognized in the income statement as an integral part of the aggregate net lease payments made. Contingent rentals are charged to the income statement in the accounting period in which they are incurred.

The cost of acquiring land held under an operating lease is stated in the balance sheet as "Interests in leasehold land held for own use under operating leases" and is amortized to the income statement on a straight-line basis over the period of the lease term except where the property is classified as an investment property.

i. Properties held for development

Properties held for development represent interests in land where construction has not yet commenced. Properties held for development are stated at cost less impairment losses. Costs include original land acquisition costs, costs of land use rights, and any direct development costs incurred attributable to such properties.

j. Properties under development

Properties under development represent interests in land and buildings under construction. Properties under development for long-term retention purposes are stated at cost less impairment losses.

Properties under development for sale, for which pre-sales have commenced and pre-sale contracts were entered before January 1, 2005 are stated at cost plus attributable profits less any foreseeable losses, sale deposits received and instalments received and receivable (see note 2(z)(iii)).

Properties under development for sale where the pre-sales have not yet commenced or pre-sale contracts were entered on or after January 1, 2005 are carried at the lower of cost and the estimated net realizable value.

Cost includes original land acquisition costs, costs of land use rights, prepayment of leasehold land, construction expenditure incurred and other direct development costs attributable to such properties, including amortization of leasehold land and interest incurred on loans directly attributable to the development prior to the completion of construction.

The net realizable value is determined by reference to sale proceeds of properties sold in the ordinary course of business less all estimated selling expenses after the balance sheet date, or by management estimates based on prevailing market conditions.

Properties under development for long-term retention purpose, on completion, are transferred to property, plant and equipment or investment properties.

Properties under development for sale with the development expected to be completed within one year from the balance sheet date, which have either been pre-sold or are intended for sale, are classified under current assets.

k. Properties for sale

Completed properties for sale are classified under current assets and stated at the lower of cost and net realizable value. Cost is determined by apportionment of the total land and development costs attributable to the unsold properties. Net realizable value represents the estimated selling price less costs to be incurred in selling the properties.

l. Goodwill

Goodwill represents the excess of the cost of a business combination or an investment in jointly controlled companies or associates over the Group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities.

Goodwill is stated in the consolidated balance sheet at cost less accumulated impairment losses. Goodwill is allocated to cash-generating units ("CGUs") and is tested annually for impairment (see note 2(o)). In respect of jointly controlled companies and associates, the carrying amount of goodwill is included in the carrying amount of the interest in jointly controlled companies or associates.

On disposal of a CGU, a jointly controlled company or an associate during the year, any attributable amount of purchased goodwill is included in the calculation of the profit or loss on disposal.

2 BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES (CONTINUED)

m. Intangible assets (other than goodwill)

Intangible assets that are acquired by the Group are stated in the balance sheet at cost less accumulated amortization (where the estimated useful life is other than indefinite) and impairment losses (see note 2(o)). Expenditure on internally generated goodwill and brands is recognized as an expense in the period in which it is incurred.

Subsequent expenditure on an intangible asset after its purchase or its completion is recognized as an expense when it is incurred unless it is probable that this expenditure will enable the asset to generate future economic benefits in excess of its originally assessed standard of performance and this expenditure can be measured and attributed to the asset reliably. If these conditions are met, the subsequent expenditure is added to the cost of the intangible assets.

Amortization of intangible assets is charged to the income statement on a straight-line basis over the assets' estimated useful lives unless such lives are indefinite. Intangible assets with an indefinite useful life are tested systematically for impairment at each balance sheet date. The following intangible assets with finite useful lives are amortized from the date they are available for use and their estimated useful lives are as follows:

Trademarks	2 – 20 years
Content licence	10 years
Wireless broadband licence	Over the term of licence
Mobile carrier licence for third generation ("3G") services ("3G licence")	Over the term of licence, commencing from the date of launch of the 3G services
Customer base	2 years

Both the useful life and method of amortization and any conclusion that the useful life of an intangible asset is indefinite are reviewed annually.

n. Investments in debt and equity securities

The Group classifies its investments in debt and equity securities, other than investments in subsidiaries, associates, joint ventures and jointly controlled companies, in the following categories:

i. Financial assets at fair value through profit or loss

This category comprises financial assets held for trading and those designated as fair value through profit or loss at inception. A financial asset is classified as held for trading if acquired principally for the purpose of selling in the short term or if so designated by management.

Financial assets at fair value through profit or loss are classified as current assets, if they are either held for trading or are expected to be realized within 12 months of the balance sheet date, and are initially stated at fair value. At each balance sheet date, the fair value is remeasured, with any unrealized holding gains or losses arising from the changes in fair value being recognized in the income statement in the period in which they arise.

ii. Held-to-maturity investments

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Group has the positive ability and intention to hold to maturity. They are included in non-current assets, except for those with maturities less than 12 months from the balance sheet date, which are classified as current assets.

Held-to-maturity investments are initially recognized in the balance sheet at fair value plus transaction costs. Subsequently, they are stated in the balance sheet at amortized cost less impairment losses (see note 2(o)).

iii. Available-for-sale financial assets

Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories. They are included in non-current assets unless the Group intends to dispose of the investment within 12 months from the balance sheet date.

2 BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES (CONTINUED)**n. Investments in debt and equity securities (continued)****iii. Available-for-sale financial assets (continued)**

Available-for-sale financial assets are initially recognized at fair value plus transaction costs. At each balance sheet date the fair value is remeasured, with any unrealized holding gains or losses arising from the changes in fair value being recognized directly in the available-for-sale financial assets reserve under equity, except for impairment losses (see note 2(o)) and, in the case of monetary items such as debt securities, foreign exchange gains and losses which are recognized directly in the income statement. Where these investments are interest-bearing, interest calculated using the effective interest method is recognized in the income statement. When the investments are derecognized, the cumulative gain or loss previously recognized directly in the equity is recognized in the income statement.

The fair value of quoted investments are based on bid price at the balance sheet date. For unlisted securities or financial assets without an active market, the Group establishes the fair value by using valuation techniques including the use of recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis, and option pricing models, making maximum use of market inputs and relying as little as possible on entity-specific inputs. If none of the valuation techniques results in a reasonable estimate on the fair value, the investment is stated at cost less impairment losses (see note 2(o)).

Investments are recognized or derecognized on the date the Group commits to purchase or sell the investments or they expire.

o. Impairment of assets**i. Impairment of investments in debt and equity securities and other receivables**

Investments in debt and equity securities and other current and non-current receivables that are stated at cost or amortized cost or are classified as available-for-sale financial assets are reviewed at each balance sheet date to determine whether there is objective evidence of impairment. If such evidence exists, any impairment loss is determined and recognized as follows:

- For unquoted equity securities and current receivables that are carried at cost, the impairment loss is measured as the difference between the carrying amount of the financial asset and the estimated future cash flows, discounted at the current market rate of return for a similar financial asset where the effect of discounting is material, and recognized in the income statement. Impairment losses for current receivables are reversed through the income statement if in a subsequent period the amount of the impairment loss decreases. Impairment losses for unquoted equity securities are not reversed.
- For financial assets carried at amortized cost, the impairment loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition of these assets), and recognized in the income statement.

If in a subsequent period the amount of an impairment loss decreases and the decrease can be linked objectively to an event occurring after the impairment loss was recognized, the impairment loss is reversed through the income statement. A reversal of an impairment loss shall not result in the asset's carrying amount exceeding that which would have been determined had no impairment loss been recognized in prior years.

- For available-for-sale financial assets, when there is an impairment, the cumulative loss, if any, that had been recognized directly in the available-for-sale financial assets reserve under equity is removed from equity and is recognized in the income statement. The amount of the cumulative loss that is recognized in the income statement is the difference between the acquisition cost (net of any principal repayment and amortization) and current fair value, less any impairment loss on that asset previously recognized in the income statement.

Impairment losses recognized in the income statement in respect of the available-for-sale financial assets are not reversed through the income statement. Any subsequent increase in the fair value of such assets is recognized directly in the available-for-sale financial assets reserve under equity.

Impairment losses in respect of the available-for-sale financial assets are reversed if the subsequent increase in fair value can be objectively related to an event occurring after the impairment loss was recognized. Reversals of impairment losses in such circumstances are recognized in the income statement.

2 BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES (CONTINUED)

o. Impairment of assets *(continued)*

ii. Impairment of other assets

Internal and external sources of information are reviewed at each balance sheet date to identify indications that the following assets may be impaired or, except in the case of goodwill, an impairment loss previously recognized no longer exists or may have decreased:

- property, plant and equipment;
- interests in leasehold land held for own use classified as being held under an operating lease;
- intangible assets;
- investments in subsidiaries, jointly controlled companies and associates; and
- goodwill.

If any such indication exists, the asset's recoverable amount is estimated. In addition, for goodwill, intangible assets that are not yet available for use and intangible assets that have indefinite useful lives, the recoverable amount is estimated annually whether or not there is any indication of impairment.

– Calculation of recoverable amount

The recoverable amount of an asset is the greater of its net selling price and its value in use. Net selling price is the amount obtainable from the sale of an asset in an arm's length transaction between knowledgeable, willing parties, less the costs of disposal. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Where an asset does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the smallest group of assets that generates cash inflows independently (i.e. a CGU).

– Recognition of impairment losses

An impairment loss is recognized in the income statement whenever the carrying amount of an asset, or the CGU to which it belongs, exceeds its recoverable amount. Impairment losses recognized in respect of CGUs are allocated first to reduce the carrying amount of any goodwill allocated to the CGU and then, to reduce the carrying amount of the other assets in the CGU on a pro rata basis, except that the carrying value of an asset will not be reduced below its individual fair value less costs to sell, or value in use, if determinable.

– Reversals of impairment losses

In respect of assets other than goodwill, an impairment loss is reversed if there has been a favourable change in the estimates used to determine the recoverable amount. An impairment loss in respect of goodwill is not allowed to be reversed.

A reversal of an impairment loss is limited to the asset's carrying amount that would have been determined had no impairment loss been recognized in prior years. Reversals of impairment losses are credited to the income statement in the period in which the reversals are recognized.

p. Derivative financial instruments

Derivative financial instruments are initially recognized at fair value on the date a derivative contract is entered into. At each balance sheet date the fair value is remeasured. The gain or loss on remeasurement to fair value is recognized immediately in the income statement, except where the derivatives qualify for hedge accounting, in which case recognition of any resultant gain or loss depends on the nature of the item being hedged.

q. Inventories

Inventories consist of trading inventories, work-in-progress and consumable inventories.

Trading inventories are carried at the lower of cost and net realizable value. Net realizable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

Work-in-progress is stated at cost, which comprises labor, materials and overheads where appropriate.

Consumable inventories, held for use in the maintenance and expansion of the Group's telecommunications systems, are stated at cost less provision for deterioration and obsolescence.

2 BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES (CONTINUED)**q. Inventories (continued)**

Cost is calculated using the weighted average cost formula and comprises all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.

r. Construction contracts

The accounting policy for contract revenue is set out in note 2(z)(v) below. When the outcome of a construction contract can be estimated reliably, contract costs are recognized as an expense by reference to the stage of completion of the contract at the balance sheet date. When it is probable that total contract costs will exceed total contract revenue, the expected loss is recognized as an expense immediately. When the outcome of a construction contract cannot be estimated reliably, contract costs are recognized as an expense in the period in which they are incurred.

Construction contracts in progress at the balance sheet date are recorded in the balance sheet at the net amount of costs incurred plus recognized profit less recognized losses and estimated value of work performed, including progress billing, and are presented in the balance sheet as the "Gross amount due from customers for contract work" (as an asset) or the "Gross amount due to customers for contract work" (as a liability), as applicable. Progress billings for work performed on a contract not yet paid by customers are included in the balance sheet under "Prepayments, deposits and other current assets".

s. Trade and other receivables

Trade and other receivables are initially recognized at fair value and thereafter stated at amortized cost using the effective interest method, less impairment losses for bad and doubtful debts (see note 2(o)), except where the receivables are interest-free loans made to related parties without any fixed repayment terms or the effect of discounting would be immaterial. In such cases, the receivables are stated at cost less impairment losses for bad and doubtful debts (see note 2(o)).

t. Unconsolidated subsidiaries held for sale

A subsidiary that is acquired and held exclusively with a view to resale is not consolidated and is classified as unconsolidated subsidiary held for sale in the consolidated balance sheet. Unconsolidated subsidiaries held for sale are classified as current assets because the sale is expected to be completed generally within one year or a further period if events or circumstances beyond the Group's control occur but the Group has initiated and is committed to a plan to sell the assets. The investment in unconsolidated subsidiaries held for sale is stated at the lower of carrying amount and fair value less costs to sell.

u. Cash and cash equivalents

Cash and cash equivalents comprise cash at bank and on hand, demand deposits with banks and other financial institutions (other than restricted cash), and short-term, highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value, having been within three months of maturity at acquisition, less bank overdrafts that are repayable on demand and form an integral part of the Group's cash management, and also advances from banks repayable within three months from the dates of advances.

v. Trade and other payables

Trade and other payables are initially recognized at fair value and thereafter stated at amortized cost using the effective interest method unless the effect of discounting would be immaterial, in which case they are stated at cost.

w. Borrowings

Borrowings are recognized initially at fair value less attributable transaction costs. Subsequent to initial recognition, borrowings are stated at amortized cost with any difference between the proceeds (net of transaction costs) and the redemption value being recognized in the income statement over the period of the borrowings using the effective interest method.

x. Convertible notes and bonds**i. Convertible notes and bonds issued**

Convertible notes and bonds that can be converted to share capital of the Company at the option of the holder, where the number of shares issued does not vary with changes in their fair value, are accounted for as compound financial instruments. At initial recognition the liability component of the convertible notes and bonds is calculated as the present value of the future interest and principal payments, discounted at the market rate of interest applicable at the time of initial recognition to similar liabilities that do not have a conversion option. Any excess of proceeds over the amounts initially recognized as the liability component is recognized as the equity component and included in the convertible note and bonds reserve under equity.

Transaction costs that relate to the issue of a compound financial instrument are allocated to the liability and equity components in proportion to the allocation of proceeds.

2 BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES (CONTINUED)

x. Convertible notes and bonds (continued)

i. Convertible notes and bonds issued (continued)

The liability component is subsequently stated at amortized cost until extinguished on conversion or maturity of the notes and bonds, with any difference between the amount initially recognized and the redemption value being recognized in the income statement over the period of the notes and bonds using the effective interest method.

If the notes and bonds are converted, the respective equity component in the convertible note and bonds reserve, together with the carrying value of the liability component at the time of conversion, is transferred to share capital and share premium as consideration for the shares issued. If the notes and bonds are redeemed, the respective equity component in the convertible note and bonds reserve is released directly to deficit.

ii. Convertible notes held

Convertible notes held on a continuing basis for an identifiable long-term purpose, are split into their derivative assets and assets components at initial recognition by recognizing the derivative asset component at its fair value and attributing to the asset component the difference between the proceeds of the convertible notes and the fair value of the derivative asset component.

The asset component is subsequently stated at amortized cost, with any difference between the fair value initially recognized and the redemption value being recognized in the income statement over the period of the convertible notes using the effective interest method. The derivative asset component is recognized at fair value with any change in fair value recognized in the income statement.

y. Provisions and contingent liabilities

Provisions are recognized for liabilities of uncertain timing or amount when the Group or the Company has a present legal or constructive obligation arising as a result of a past event, it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made. Where the time value of money is material, provisions are stated at the present value of the expenditure expected to settle the obligation.

Where it is not probable that an outflow of economic benefits will be required, or the amount cannot be estimated reliably, the obligation is disclosed as a contingent liability, unless the probability of outflow of economic benefits is remote. Possible obligations, whose existence will only be confirmed by the occurrence or non-occurrence of one or more future events, are also disclosed as contingent liabilities unless the probability of outflow of economic benefits is remote.

z. Revenue recognition

Provided it is probable that the economic benefits will flow to the Group and the revenue and costs, if applicable, can be measured reliably, revenue is recognized in the income statement as follows:

i. Telecommunications and other services

Telecommunications services comprise the fixed line and mobile telecommunications network services, and equipment businesses mainly in Hong Kong.

Telecommunications service revenue based on usage of the Group's network and facilities is recognized when the services are rendered. Telecommunications revenue for services provided for fixed periods is recognized on a straight-line basis over the applicable fixed period.

Up-front fees received for installation of equipment and activation of customer service are deferred and recognized over the expected customer relationship period, which is estimated based on the expected stabilized churn rate.

Other service income is recognized when services are rendered to customers.

ii. Sales of goods

Revenue from sale of goods is recognized when goods are delivered to customers which generally coincides with the time when the customer has accepted the goods and the related risks and rewards of ownership. Revenue is recorded after deduction of any trade discounts.

2 BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES (CONTINUED)

z. Revenue recognition (continued)

iii. Sales of properties

Revenue and profits arising from sales of completed properties is recognized upon execution of legally binding unconditional sales contracts upon which the beneficial interest in the property passes to the purchasers together with the significant risks and rewards of ownership.

Revenue and profits arising from the pre-completion contracts for the sale of properties under development is accounted for as follows:

- for pre-completion contracts for the sale of properties under development for which legally binding unconditional sales contracts were entered into before January 1, 2005, as permitted by the transitional provisions of HK-Int 3, revenue and profits continue to be recognized on the percentage of construction completion basis commencing when these contracts are signed and exchanged, provided that the construction work has progressed to a stage where the ultimate realization of profit can be reasonably determined and on the basis that the total estimated profit is apportioned over the entire period of construction to reflect the progress of the development. Deposits and instalments received from purchasers are netted off from properties under development.
- for pre-completion contracts for the sale of properties under development for which legally binding unconditional sales contracts were entered into on or after January 1, 2005, as required by HK-Int 3, revenue and profits are recognized upon completion of the development and when significant risks and reward of ownership have been transferred. Deposits and instalments received from purchasers prior to this stage are included in current liabilities.

iv. Rental income from operating leases

Rental income receivable under operating leases is recognized in the income statement in equal instalments over the periods covered by the lease term, except where an alternative basis is more representative of the pattern of benefits to be derived from the use of leased asset. Lease incentives granted are recognized in the income statement as an integral part of the aggregate net lease payments receivable. Contingent rentals are recognized as income in the accounting period in which they are earned.

v. Contract revenue

Revenue from a fixed price contract is recognized using the percentage of completion method, measured by reference to the percentage of estimated value of work performed to date to total contract revenue.

vi. Interest income

Interest income is recognized on a time-apportioned basis using the effective interest method.

vii. Commission income

Commission income is recognized when entitlement to the income is ascertained.

viii. Dividend income

Dividend income is recognized when the shareholder's right to receive payment is established.

aa. Borrowing costs

Borrowing costs are expensed in the income statement in the period in which they are incurred, except to the extent that they are capitalized as being directly attributable to the acquisition, construction or production of an asset which necessarily takes a substantial period of time to get ready for its intended use or sale.

The capitalization of borrowing costs as part of the cost of a qualifying asset commences when expenditure for the asset is being incurred, borrowing costs are being incurred and activities that are necessary to prepare the asset for its intended use or sale are in progress. Capitalization of borrowing costs is suspended or ceases when substantially all the activities necessary to prepare the qualifying asset for its intended use or sale are interrupted or complete.

Discounts or premiums relating to borrowings, ancillary costs incurred in connection with arranging borrowings and exchange differences arising from foreign currency borrowings, to the extent that they are regarded as adjustments to interest costs, are recognized as expenses over the period of the borrowing using the effective interest method.

2 BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES (CONTINUED)

bb. Income tax

- i. Income tax for the year comprises current tax and movements in deferred tax assets and liabilities. Current tax and movements in deferred tax assets and liabilities are recognized in the income statement except to the extent that they relate to items recognized directly in equity, in which case they are recognized in equity.
- ii. Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous year.
- iii. Deferred tax assets and liabilities arise from deductible and taxable temporary differences respectively, being the differences between the carrying amounts of assets and liabilities for financial reporting purposes and the tax bases. Deferred tax assets also arise from unused tax losses and unused tax credits.

All deferred tax liabilities, and all deferred tax assets to the extent that it is probable that future taxable profits will be available against which the asset can be utilized, are recognized.

The amount of deferred tax recognized is measured based on the expected manner of realization or settlement of the carrying amount of the assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date. Deferred tax assets and liabilities are not discounted.

cc. Employee benefits

i. Short term employee benefits

Salaries, annual bonuses, paid annual leave and the cost of non-monetary benefits are accrued in the year in which the associated services are rendered by employees. Where payment or settlement is deferred and the effect would be material, these amounts are stated at their present values.

ii. Retirement benefits

The Group operates both defined benefit and defined contribution retirement schemes (including the Mandatory Provident Fund) for its employees, the assets of which are generally held in separate trustee – administered funds. The schemes are generally funded by payments from the relevant Group companies and, in some cases, employees themselves, taking account of the recommendations of independent qualified actuaries.

The Group's contributions to the defined contribution schemes are recognized as an expense in the income statement in the period to which the contributions relate.

Retirement costs under defined benefit retirement schemes are assessed using the projected unit credit method. Under this method, the cost of providing defined benefits is charged to the income statement so as to spread the regular cost over the service lives of employees in accordance with the advice of the actuaries who carry out a full valuation of the schemes on an annual basis. The defined benefit obligation is measured as the present value of the estimated future cash outflows using interest rates determined by reference to market yields at the balance sheet date based on Exchange Fund Notes, which have terms to maturity approximating the terms of the related liability. Scheme assets are measured at fair value. Actuarial gains and losses, to the extent that the amount is in excess of 10% of the greater of the present value of the defined benefit obligations and the fair value of the scheme assets, are recognized in the income statement over the expected average remaining service lives of the participating employees. Past service costs are recognized as an expense on a straight-line basis over the vesting period until the benefits become vested.

2 BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES (CONTINUED)**cc. Employee benefits (continued)****iii. Share-based payments**

The Group operates share option schemes where employees (and including directors) are granted options to acquire shares of the Company at specified exercise prices. The fair value of the employee services received in exchange for the grant of the options is recognized as staff costs in the income statement with a corresponding increase in an employee share-based compensation reserve under equity. The fair value of the options granted is measured at grant date using the trinomial option pricing model, taking into account the terms and conditions upon which the options were granted, and spread over the respective vesting period during which the employees become unconditionally entitled to the options. During the vesting period, the number of share options that is expected to vest is reviewed. Any adjustment to the cumulative fair value recognized in prior years is charged or credited in the income statement for the year of the review, unless the original staff costs qualify for recognition as an asset, with a corresponding adjustment to the employee share-based compensation reserve. On vesting date, the amount recognized as staff costs is adjusted to reflect the actual number of share options that vest (with a corresponding adjustment to the employee share-based compensation reserve). The equity amount is recognized in the employee share-based compensation reserve until either the share options are exercised (when it is transferred to the share premium account) or the share options expires (when it is released directly to retained profits). Share options granted before November 7, 2002 or vested on or before December 31, 2004 are not expensed as they are not subject to the requirements of HKFRS 2. When the share options are exercised, the proceeds received, net of any directly attributable transaction cost, are credited to share capital (nominal value) and share premium.

The Group also grants employees (but not directors) shares of the Company at nil consideration under its share award schemes, under which the awarded shares are either newly issued at par value (the "Subscription Scheme") or are purchased from the open market (the "Purchase Scheme"). For the Subscription Scheme, the fair value of the employee services received in exchange for the grant of shares newly issued is recognized as staff costs in the income statement with a corresponding increase in an employee share-based compensation reserve under equity. The fair value of the awarded shares is measured by the quoted market price of the shares at grant date and is charged to the income statement over the respective vesting period. During the vesting period, the number of awarded shares that is expected to vest is reviewed. Any adjustment to the cumulative fair value recognized in prior years is charged or credited in the income statement for the year of the review, unless the original staff costs qualify for recognition as an asset, with a corresponding adjustment to the employee share-based compensation reserve. On vesting date, the amount recognized as staff costs is adjusted to reflect the actual number of awarded shares that vest (with a corresponding adjustment to the employee share-based compensation reserve). Shares awarded under the Subscription Scheme before November 7, 2002 or awarded after November 7, 2002 but vested on or before December 31, 2004 are not expensed as they are not subject to the requirements of HKFRS 2. On the other hand, for the Purchase Scheme, the cost of shares purchased from the open market is recognized in the balance sheet as prepaid expenses at the date of grant and amortized over the respective vesting period and recognized in the income statement as staff costs.

Shares of the Company granted to employees of the Group by the principal shareholder of the Company are accounted for in accordance with the same policy for the awarded shares under the Subscription Scheme as described above. The fair value of the shares granted by principal shareholder is measured by the quoted market price of the shares at grant date and is charged to the income statement over the respective vesting period.

iv. Termination benefits

Termination benefits are recognized only after either an agreement is in place with the appropriate employee representatives specifying the terms of redundancy and the numbers of employees affected, or, after individual employees have been advised of the specific terms.

2 BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES (CONTINUED)

dd. Foreign currencies

Foreign currencies transactions during the year are translated at the foreign exchange rates ruling at the transaction dates. Monetary assets and liabilities denominated in foreign currencies are translated at the foreign exchange rates ruling at the balance sheet date. Exchange gains and losses are recognized in the income statement.

Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the foreign exchange rates ruling at the transaction dates. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated using the foreign exchange rates ruling at the dates the fair value was determined. Exchange differences arising on translation of non-monetary assets and liabilities, such as financial assets at fair value through profit or loss, are reported as part of the fair value gain or loss in the income statement. Exchange differences arising on translation of non-monetary assets and liabilities, such as available-for-sale financial assets, are included in the fair value gain or loss in the available-for-sale financial assets reserve under equity.

The results of foreign operations are translated into Hong Kong dollars at the exchange rates approximating the foreign exchange rates ruling at the dates of transactions. Balance sheet items of foreign operations, including goodwill arising on consolidation of foreign operations acquired on or after January 1, 2005, are translated into Hong Kong dollars at the foreign exchange rates ruling at the balance sheet date. Goodwill arising on consolidation of a foreign operation acquired before January 1, 2005 is translated at the foreign exchange rate that applied at the date of acquisition of the foreign operation. The resulting exchange differences are recognized directly in the currency translation reserve under equity.

On consolidation, exchange differences arising from the translation of the net investment in foreign operations, and of borrowings and other currency instruments designated as hedges of such investments, if any, are taken to currency translation reserve under equity. On disposal of a foreign operation, the cumulative amount of the exchange differences recognized in the currency translation reserve under equity which relate to that foreign operation is included in the calculation of the profit or loss on disposal.

ee. Segment reporting

A segment is a distinguishable component of the Group that is engaged either in providing products or services (business segment), or in providing products or services within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those of other segments.

In accordance with the Group's internal financial reporting system, the Group has chosen business segment information as the primary reporting format and geographical segment information as the secondary reporting format for the purposes of these financial statements.

Segment revenue, expenses, results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis to that segment. Segment revenue, expenses and segment performance include transactions between segments. Inter-segment pricing is based on similar terms as those available to other external parties for similar services. These transactions are eliminated upon consolidation.

Segment capital expenditure is the total cost incurred during the year to acquire segment assets (both tangible and intangible) that are expected to be used for more than one year.

Unallocated items mainly comprise financial and corporate assets and liabilities, interest-bearing loans, borrowings, corporate and financing expenses.

3 CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

a. Key sources of estimation uncertainty

The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. Notes 21, 32(a), 33 and 40 contain information about the assumptions and their risk factors relating to goodwill impairment, defined benefit liability, fair value of share options or shares granted and financial instruments. Other key sources of estimation uncertainty are discussed below.

i. Useful lives of property, plant and equipment and intangible assets (other than goodwill)

The Group has significant property, plant and equipment and intangible assets (other than goodwill) acquired through the purchases of various subsidiaries. The Group is required to estimate the useful lives of property, plant and equipment and intangible assets (other than goodwill) in order to ascertain the amount of depreciation and amortization charges for each reporting period. A significant amount of these assets have estimated useful lives that extend beyond 10 years.

The useful lives are estimated at the time of purchase of these assets after considering future technology changes, business developments and the Group's strategies. The Group performs an annual review to assess the appropriateness of the estimated useful lives. Such review takes into account any unexpected adverse changes in circumstances or events, including declines in projected operating results, negative industry or economic trends, rapid advancement in technology and significant downturns in the Company's stock price. The Group extends or shortens the useful lives and/or makes impairment provisions according to the results of the review.

ii. Impairment of assets

At each balance sheet date, the Group reviews internal and external sources of information to identify indications that the following assets may be impaired or, except in the case of goodwill, an impairment loss previously recognized no longer exists or may have decreased:

- property, plant and equipment;
- interests in leasehold land held for own use classified as being held under an operating lease;
- intangible assets;
- investments in subsidiaries, jointly controlled companies and associates (except for those classified as held for sale or included in a disposal group that is classified as held for sale); and
- goodwill.

If any such indication exists, the asset's recoverable amount is estimated. In addition, for goodwill, intangible assets that are not yet available for use and intangible assets that have indefinite useful lives, the recoverable amount is estimated annually whether or not there is any indication of impairment. An impairment loss is recognized in the income statement whenever the carrying amount of an asset exceeds its recoverable amounts.

The sources utilized to identify indications of impairment are often subjective in nature and the Group is required to use judgement in applying such information to its business. The Group's interpretation of this information has a direct impact on whether an impairment assessment is performed as at any given balance sheet date. Such information is particularly significant as it relates to the Group's telecommunications services and infrastructure businesses in Hong Kong.

If an indication of impairment is identified, such information is further subjected to an exercise that requires the Group to estimate the recoverable value, representing the greater of the net selling price of such asset or its value in use. Depending on the Group's assessment of the overall materiality of the asset under review and complexity of deriving reasonable estimates of the recoverable value, the Group may perform such assessment utilizing internal resources or the Group may engage external advisors to counsel the Group in making this assessment. Regardless of the resources utilized, the Group is required to make many assumptions to make this assessment, including the utilization of such asset, the cash flows to be generated, appropriate market discount rates and the projected market and regulatory conditions. Changes in any of these assumptions could result in a material change to future estimates of the recoverable value of any asset.

3 CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS (CONTINUED)

a. Key sources of estimation uncertainty (continued)

iii. Revenue recognition

Telecommunications service revenue based on usage of the Group's network and facilities is recognized when the services are rendered. Telecommunications revenue for services provided for fixed periods is recognized on a straight-line basis over the respective period. In addition, up-front fees received for installation of equipment and activation of customer service are deferred and recognized over the expected customer relationship period. The Group is required to exercise considerable judgement in revenue recognition particularly in the areas of customer discounts, billing reserves for pricing changes, customer disputes, revenue reserve for special customer agreements and stabilized churn rate. Significant changes in management estimates may result in material revenue adjustments.

Revenue and profits arising from the pre-completion contracts for the sale of properties under development for which legally binding unconditional sales contracts were entered into before January 1, 2005 are recognized on the percentage of construction completion basis commencing when these contracts are signed and exchanged, provided that the construction work has progressed to a stage where the ultimate realization of profit can be reasonably determined and on the basis that the total estimated profit is apportioned over the entire period of construction to reflect the progress of the development. In this regard, the pre-sales of the residential portion of the Cyberport project commenced in early 2003. The Group has made certain estimates concerning the stage of completion of properties subject to pre-sale, the estimated costs to be incurred to completion, and the estimated total sales and cost of sales in applying the percentage of construction completion method. Significant changes in these estimates could result in material changes to revenues and profit recognized for pre-completion contracts for sales of properties under development.

iv. Provisions

The Group recognizes provisions when it has a present legal or constructive obligation arising as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made. The recording of provisions requires the application of judgements about the ultimate resolution of these obligations. At a result, provisions are reviewed at each balance sheet date and adjusted to reflect the Group's current best estimate.

Pursuant to the agreement in respect of the Cyberport project as set out in note 20(a), the Government of Hong Kong (the "Government") is entitled to receive payments of approximately 65% from the surplus cashflow as stipulated under certain terms and conditions of the Cyberport Project Agreement arising from the sales of the residential portion of the Cyberport project. Provision for payment to the Government is included as a cost within properties under development. The provision is based on estimated sales proceeds of the residential portion of the Cyberport project and the estimated development costs of the Cyberport project and forms part of the development costs for the Cyberport project. In case there are any changes to the Group's estimates of projected future sales proceeds and the developments costs, this would impact on the provisions to be made and the Group's profit to be derived from the Cyberport project.

v. Deferred taxation

While deferred tax liabilities are provided in full on all taxable temporary differences, deferred tax assets are recognized only to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilized. In assessing the amount of deferred tax assets that need to be recognized, the Group considers future taxable income and ongoing prudent and feasible tax planning strategies. In the event that the Group's estimates of projected future taxable income and benefits from available tax strategies are changed, or changes in current tax regulations are enacted that would impact the timing or extent of the Group's ability to utilize the tax benefits of net operating loss carryforwards in the future, adjustments to the recorded amount of net deferred tax assets and taxation expense would be made.

vi. Current tax

The Group makes provision for current tax based on estimated income tax liabilities. The estimated income tax liabilities are primarily computed based on the tax computation as prepared by the Group. Nevertheless, from time to time, there are cases of disagreements with the tax authorities of Hong Kong and elsewhere on the tax treatments of items included in the tax computations. If the Group considers it probable that these disputes would result in additional tax payments, the most likely amount of the payment will be estimated and adjustments to the tax expenses and tax liabilities will be made accordingly.

3 CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS (CONTINUED)**b. Critical accounting judgements in applying the Group's accounting policies**

Certain critical accounting judgements in applying the Group's accounting policies are described below.

i. Distinction between investment properties and owner-occupied properties

The Group determines whether a property qualifies as investment property, and has developed criteria in making its judgement. Investment property is a property held to earn rentals and/or for capital appreciation. Therefore, the Group considers whether the property generates cash flows largely independently of the other assets held by the entity.

Some properties comprise a portion that is held to earn rentals or for capital appreciation and another portion that is held for use in the production or supply of goods or services or for administrative purposes. If these portions can be sold separately (or leased out separately under a finance lease), the Group's financial statements account for the portions separately. If the portions cannot be sold separately, the property is accounted for as investment property only if an insignificant portion is held for use in the production or supply of goods or services or for administrative purposes. Judgement is applied in determining whether ancillary services are so significant that a property does not qualify as investment property. The Group considers each property separately in making its judgement.

ii. Held-to-maturity investments

The Group follows the guidance of HKAS 39 on classifying non-derivative financial assets with fixed or determinable payments and fixed maturities as held-to-maturity investments. In making its judgment on this classification, the Group evaluates its intention and ability to hold such investments to maturity.

If the Group fails to keep these investments to maturity other than for specific circumstances explained in HKAS 39, it will be required to reclassify the whole class as available-for-sale financial assets. The investments would therefore be measured at fair value but not amortized cost.

iii. Accounting for the IRU

The Group acquired an IRU from the Reach Group to use certain international undersea cables and determined to recognize it as transmission plant under "Property, plant and equipment". The Group believes that the period covered by the IRU represents the major part of the economic lives of the underlying assets and the Group bears all costs and receives all the benefits from the utilization of the undersea cables. Accordingly, the Group believes the risks and rewards incidental to ownership have been transferred to the Group and has treated the transaction as an acquisition of property, plant and equipment.

iv. Disposal of PCCW Tower

The disposal of PCCW Tower, the Group's headquarters in Hong Kong, was completed on February 7, 2005. Under the formal property sale and purchase agreement dated December 21, 2004, on completion of the disposal, the Group, through PCPD, has guaranteed to the purchaser a net monthly rental of approximately HK\$13.3 million for a period of 5 years commencing from the date following completion of the disposal. The Group considers that the significant risks and rewards associated with the ownership of the property have been transferred to the purchaser as the net potential shortfall in rental to be received by the Group over the guaranteed net monthly rental payments for the 5-year-period, if any, will be insignificant as compared to the total sales proceeds of HK\$2,808 million.

4 CHANGES IN ACCOUNTING POLICIES

The HKICPA has issued a number of new and revised HKFRSs that are effective for accounting periods beginning on or after January 1, 2005.

The principal accounting policies of the Group after the adoption of these new and revised HKFRSs have been summarized in note 2. The following sets out information on the significant changes in accounting policies for the current and prior accounting periods reflected in these financial statements.

The Group has not adopted any new standard or interpretation that is not effective for the current accounting period, details of which are set out in note 47.

a. Adoption of new and revised HKFRSs

The Group has adopted the new and revised HKFRSs below, which are relevant to its operations, in the preparation of the financial statements. The 2004 comparatives have been amended as required, in accordance with the relevant requirements.

HKAS 1	Presentation of Financial Statements
HKAS 2	Inventories
HKAS 7	Cash Flow Statements
HKAS 8	Accounting Policies, Changes in Accounting Estimates and Errors
HKAS 10	Events after the Balance Sheet Date
HKAS 11	Construction Contracts
HKAS 12	Income Taxes
HKAS 14	Segment Reporting
HKAS 16	Property, Plant and Equipment
HKAS 17	Leases
HKAS 18	Revenue
HKAS 19	Employee Benefits
HKAS 21	The Effects of Changes in Foreign Exchange Rates
HKAS 23	Borrowing Costs
HKAS 24	Related Party Disclosures
HKAS 27	Consolidated and Separate Financial Statements
HKAS 28	Investment in Associates
HKAS 31	Interests in Joint Ventures
HKAS 32	Financial Instruments: Disclosure and Presentation
HKAS 33	Earnings per Share
HKAS 36	Impairment of Assets
HKAS 37	Provisions, Contingent Liabilities and Contingent Assets
HKAS 38	Intangible Assets
HKAS 39	Financial Instruments: Recognition and Measurement
HKAS 40	Investment Property
HKAS-Int 12	Consolidation – Special Purpose Entities
HKAS-Int 15	Operating Leases – Incentives
HKAS-Int 21	Income Taxes – Recovery of Revalued Non-Depreciable Assets
HKFRS 2	Share-based Payment
HKFRS 3	Business Combinations
HKFRS 5	Non-current Assets Held for Sale and Discontinued Operations
HK-Int 3	Revenue – Pre-completion Contracts for the Sale of Development Properties
HK-Int 4	Leases – Determination of the Length of Lease Term in respect of Hong Kong Land Leases

The adoption of HKASs 2, 7, 8, 10, 11, 12, 14, 16, 19, 21, 23, 27, 28, 31, 33, 37, 38, HKAS-Ints 12 and 15, HKFRS 5 and HK-Int 4 had no material effect on the accounting policies. The effect of the adoption of certain new and revised HKFRSs, which results in substantial changes to the accounting policies, is set out below.

i. Changes in presentation (HKAS 1)

HKAS 1 has affected the presentation of share of net after-tax results of jointly controlled companies and associates, and minority interests.

4 CHANGES IN ACCOUNTING POLICIES (CONTINUED)**a. Adoption of new and revised HKFRSs (continued)****i. Changes in presentation (HKAS 1) (continued)**

- Presentation of shares of jointly controlled companies' and associates' taxation
In prior years, the Group's share of taxation of jointly controlled companies and associates accounted for using the equity method was included as part of the Group's income tax in the consolidated income statement. With effect from January 1, 2005, in accordance with the implementation guidance in HKAS 1, the Group has changed the presentation and includes the share of taxation of jointly controlled companies and associates accounted for under equity method in the respective shares of results of jointly controlled companies and associates reported in the consolidated income statement before arriving at the Group's profit or loss before taxation.
- Minority interests
In prior years, minority interests in the results of the Group for the year were separately presented in the income statement as a deduction before arriving at the profit attributable to shareholders (the equity holders of the Company). With effect from January 1, 2005, in order to comply with HKAS 1, the Group has changed its accounting policy relating to the presentation of minority interests. Under the new policy, minority interests are presented in the consolidated income statement as an allocation of the total profit or loss for the year between minority interests and equity holders of the Company, and are presented as part of equity, separately from interests attributable to the equity holders of the Company on the consolidated balance sheet, details of which are set out in note 2(c).

These changes in presentation have been applied retrospectively with comparatives restated as shown in notes 4(b) and 4(c) below.

ii. Leasehold land and buildings held for own use (HKAS 17)

In prior years, leasehold land and buildings held for own use were stated at cost less accumulated depreciation and impairment losses. Depreciation was calculated to write off the cost on a straight-line basis over the shorter of the lease term and the estimated useful lives of the buildings.

With effect from January 1, 2005, in order to comply with HKAS 17, the Group has adopted a new policy for leasehold land and buildings held for own use. Under the new policy, the interest in leasehold land held for own use is accounted for as being held under an operating lease where the fair value of the interest in any buildings situated on the leasehold land could be measured separately from the fair value of the interest in leasehold land at the time the lease was first entered into by the Group, or taken over from the previous lessee, or at the date of construction of those buildings, if later. Any buildings held for own use which are situated on such land leases continue to be presented as part of property, plant and equipment. Any pre-paid cost of acquiring the land leases is amortized in the income statement on a straight-line basis over the period of the lease term or where there is impairment, the impairment is expensed in the income statement. Details of the new policy are set out in notes 2(f) and 2(h).

This new accounting policy has been adopted retrospectively and comparative amounts have been restated accordingly. The adjustments for each financial statement line item affected for the years ended December 31, 2004 and 2005 are set out in notes 4(b) and 4(c) below.

iii. Recognition of up-front installation fees (HKAS 18)

In prior years, up-front fees received for installation of equipment and activation of customer service were recognized when installation and activation were completed.

Upon the adoption of HKAS 18 as from January 1, 2005, as set out in note 2(z)(i), up-front fees received for installation of equipment and activation of customer service are deferred and recognized over the expected customer relationship period, which is estimated based on the expected stabilized churn rate.

This new accounting policy has been adopted retrospectively and comparative amounts have been restated accordingly. The adjustments for each financial statement line item affected for the years ended December 31, 2004 and 2005 are set out in notes 4(b) and 4(c) below.

4 CHANGES IN ACCOUNTING POLICIES (CONTINUED)

a. Adoption of new and revised HKFRSs (continued)

iv. Definition of related parties (HKAS 24)

As a result of the adoption of HKAS 24, the definition of related parties as disclosed in note 5 has been expanded to clarify that related parties include entities that are under the significant influence of a related party that is an individual (i.e. key management personnel, significant shareholders and/or their close family members) and post-employment benefit plans which are for the benefit of employees of the Group or of any entity that is a related party of the Group. The clarification of the definition of related parties has not resulted in any material changes to the previously reported disclosures of related party transactions nor has it had any material effect on the disclosures made in the current period, as compared to those that would have been reported had the Statement of Standard Accounting Practice 20 "Related party disclosures" still been in effect.

v. Financial instruments (HKAS 32 and HKAS 39)

With effect from January 1, 2005, in order to comply with HKAS 32 and HKAS 39, the Group has changed its accounting policies relating to financial instruments to those as set out in notes 2(n) to (p), 2(s) and 2(v) to (x). Further details of the changes are as follows:

– Investments in debt and equity securities

In prior years, equity investments, other than investments in subsidiaries, associates, joint ventures and jointly controlled companies, were classified as (i) investment securities, where the investments were held on a continuing basis for an identifiable long-term purpose were classified as investment securities and were stated at cost less provisions for diminution in value; and (ii) other investments, where the investments were other than investment securities and held-to-maturity securities and were stated at fair value with changes in fair value recognized in the income statement as they arose.

With effect from January 1, 2005, and in accordance with HKAS 39, all non-trading investments, other than investments in subsidiaries, associates, joint ventures and jointly controlled companies, are classified as available-for-sale financial assets and carried at fair value. Changes in fair value are recognized in the available-for-sale financial assets reserve under equity, unless there is objective evidence that an individual investment has been impaired. There are no material adjustments arising from the adoption of the new policies to the carrying value of trading investments, held-to-maturity investments and unquoted available-for-sale financial assets not carried at fair value. Details of the new accounting policies are set out in note 2(n).

– Derivative financial instruments

In prior years, the notional amounts of derivative financial instruments, including interest rate and currency swaps, forward interest rate agreements, interest rate options and equity options, entered into by the Group were not reflected in the balance sheet. The related interest flows were accounted for on an accrual basis and the premiums received or paid on written or purchased options were amortized over the terms of the respective options.

With effect from January 1, 2005, and in accordance with HKAS 39, all derivative financial instruments entered into by the Group are stated at fair value. Changes in fair value are recognized in the income statement as they arise. Details of the new accounting policies are set out in note 2(p).

– Convertible notes and bonds

In prior years, convertible notes and bonds issued were stated at amortized cost (including transaction costs), with any difference between the cost and redemption value being recognized in the income statement over the period of the convertible notes and bonds on a straight-line basis. Convertible notes held on a continuing basis for an identifiable long-term purpose were classified as loans receivable and stated at cost plus premium.

With effect from January 1, 2005, and in accordance with HKAS 32, convertible notes and bonds issued, that are convertible into a fixed number of shares of the Company, are split into their liability and equity components at initial recognition. The liability component is subsequently carried at amortized cost (including transaction costs) using the effective interest rate method. The equity component is recognized in the convertible note and bonds reserve until the note or bond is either converted (in which case it is transferred to share premium) or the note or bond is redeemed (in which case it is released directly to retained profits). For convertible notes held on a continuing basis for an identifiable long-term purpose, they are split into their derivative assets and asset components at initial recognition. The asset component is subsequently carried at amortized cost, while the derivative asset component is stated at fair value with the change in fair value recognized in the income statement. Details of the new accounting policies are set out in note 2(x).

4 CHANGES IN ACCOUNTING POLICIES (CONTINUED)

a. Adoption of new and revised HKFRSs (continued)

v. Financial instruments (HKAS 32 and HKAS 39) (continued)

- Amounts due from/to subsidiaries

In prior years, amounts due from subsidiaries of the Company are stated at cost less impairment losses while amounts due to subsidiaries of the Company are stated at cost.

With effect from January 1, 2005, and in accordance with HKAS 39, amounts due from subsidiaries are initially recognized at fair value and thereafter stated at amortized cost less impairment losses, except where the amounts due from subsidiaries are interest-free without any fixed repayment terms or the effect of discounting would be immaterial. In such cases, the amounts due from subsidiaries are stated at cost less impairment losses. For amounts due to subsidiaries, they are initially recognized at fair value and thereafter stated at amortized cost unless the effect of discounting would be immaterial, in which case they are stated at cost. Details of the new accounting policies are set out in notes 2(s) and 2(v) respectively.

The above changes in accounting policies were adopted by way of an adjustment to the opening balance of deficit as at January 1, 2005 in accordance with the transitional arrangements in HKAS 39, except for the change in accounting policy relating to the splitting of the convertible notes and bonds issued into their liability and equity components at initial recognition in accordance with HKAS 32, in which case it has been adopted retrospectively. The adjustments for each financial statement line item affected for the years ended December 31, 2004 and 2005 are set out in notes 4(b) and 4(c) below.

vi. Amortization of goodwill (HKFRS 3 and HKAS 36)

In prior periods, goodwill, arising on consolidation for acquisitions:

- occurring before January 1, 2001 was taken directly to reserves at the time it arose, and was not recognized in the income statement until disposal or impairment of the acquired business, and was subject to annual impairment testing; and
- occurring on or after January 1, 2001 was amortized on a straight-line basis over its useful life and was subject to impairment testing when there were indications of impairment.

With effect from January 1, 2005, in order to comply with HKFRS 3 and HKAS 36, the Group has changed its accounting policies relating to goodwill. Under the new policy, the Group no longer amortizes goodwill but tests it at least annually for impairment. Details of the new accounting policies are set out in note 2(l).

The new policy in respect of the cessation of amortization of goodwill has been applied prospectively in accordance with the transitional arrangements under HKFRS 3. Also, goodwill which had previously been taken directly to reserves (i.e. goodwill which arose before January 1, 2001) will not be recognized in the income statement on disposal or impairment of the acquired business, or under any other circumstances. The adjustments for each financial statement line item affected for the year ended December 31, 2005 are set out in note 4(c) below.

vii. Investment property (HKAS 40)

Changes in accounting policies relating to investment properties are as follows:

- Recognition of movements in fair value in the income statement

In prior years, changes arising on the revaluation of the Group's investment properties were recognized directly in the property revaluation reserve except when, on a portfolio basis, the reserve was insufficient to cover a deficit on the portfolio, or when a deficit previously recognized in the income statement had been reversed, or when an individual investment property was disposed of. In these limited circumstances, changes arising on the revaluation were recognized in the income statement.

Upon the adoption of HKAS 40 as from January 1, 2005, as set out in note 2(g), all changes in the fair value of investment properties are recognized directly in the income statement in accordance with the fair value model in HKAS 40.

There is no requirement for the Group to restate the comparative information and accordingly, any adjustment relating to the treatment of the property revaluation surplus has been made to the deficit as at January 1, 2005, including the reclassification of any amount held in the property revaluation reserve.

4 CHANGES IN ACCOUNTING POLICIES (CONTINUED)

a. Adoption of new and revised HKFRSs (continued)

vii. Investment property (HKAS 40) (continued)

– Dual use properties

In prior years, for dual use properties, the parts held for own use and used as investment properties were accounted for separately if a significant portion of the property was occupied by members of the Group.

HKAS 40 states that dual use properties can only be classified as investment properties if (i) the portion used as investment properties can be separately sold or leased out under finance lease; or (ii) the portion occupied by members of the Group is insignificant.

Upon the adoption of HKAS 40 as from January 1, 2005, part of the properties being accounted for as investment properties in prior years is treated as properties held for own use and hence is accounted for in accordance with HKAS 16 under the accounting policy as set out in note 2(f). The change in accounting policy has been adopted retrospectively and comparative amounts have been restated accordingly.

The adjustments for each financial statement line item affected for the years ended December 31, 2004 and 2005 are set out in notes 4(b) and 4(c) below.

viii. Deferred tax on movements in fair value of investment properties (HKAS-Int 21)

In prior years, the Group was required to apply the tax rate that would be applied for recovery of the carrying value of the investment properties through sale to determine whether any amounts of deferred tax liabilities should be recognized on the revaluation of investment properties.

As from January 1, 2005, in order to comply with HKAS-Int 21, the Group recognizes deferred tax liabilities on movements in the fair value of an investment property using tax rates that are applied for recovery of the carrying value of the investment properties through use, if the Group has no intention to sell it and the property would have been depreciable had the Group not adopted the fair value model. Details of the accounting policy for deferred tax are set out in note 2(bb).

The change in accounting policy has been adopted retrospectively and comparative amounts have been restated accordingly. The adjustments for each financial statement line item affected for the years ended December 31, 2004 and 2005 are set out in notes 4(b) and 4(c) below.

ix. Equity-settled share-based payments (HKFRS 2)

In prior years, no amounts were recognized for the equity-settled share-based payment transactions in the Group, including:

- share options granted to employees or directors of the Group to acquire shares of the Company at specified exercise prices under the share option schemes operated by the Group;
- shares of the Company awarded to employees (but not directors) of the Group under the Subscription Scheme operated by the Group; and
- shares of the Company granted to employees of the Group by the principal shareholder of the Company.

If the employees or directors of the Group chose to exercise the share options, the nominal amount of share capital and share premium were credited only to the extent of the share option's exercise price receivable.

With effect from January 1, 2005, in order to comply with HKFRS 2, the Group has adopted a new policy for the above equity-settled share-based payment transactions. Under the new policy, the Group recognizes the fair value of such share options or shares as an expense in the income statement according to the vesting schedule, with a corresponding increase recognized in the employee share-based compensation reserve under equity. Further details of the new policy are set out in note 2(cc)(iii).

4 CHANGES IN ACCOUNTING POLICIES (CONTINUED)

a. Adoption of new and revised HKFRSs (continued)

ix. Equity-settled share-based payments (HKFRS 2) (continued)

The new accounting policy has been applied retrospectively with comparatives restated, except that the Group has taken advantage of the transitional provisions set out in HKFRS 2, under which the new recognition and measurement policies have not been applied to the following grants of share options or shares:

- all share options or shares granted to employees or directors on or before November 7, 2002; and
- all share options or shares granted to employees or directors after November 7, 2002 but which had vested before January 1, 2005.

The adjustments for each financial statement line item affected for the years ended December 31, 2004 and 2005 are set out in notes 4(b) and 4(c) below.

x. Revenue arising from pre-sales of properties under development (HK-Int 3)

In prior years, revenue arising from the pre-sales of properties under development was recognized on the percentage of construction completion basis.

Upon the adoption of HK-Int 3 as from January 1, 2005, revenue arising from the pre-completion contracts for the sale of properties under development entered into on or after January 1, 2005 is recognized when the property is completed. Further details of the new policy are set out in note 2(z)(iii).

The new accounting policy has been applied prospectively in accordance with the transitional arrangements under HK-Int 3. The adjustments for each financial statement line item affected for the year ended December 31, 2005 are set out in note 4(c) below.

b. Restatement of prior periods

The following tables disclose the adjustments that have been made in accordance with the transitional provisions of the respective new and revised HKFRSs or the provisions of HKAS 8 to each of the line items in the consolidated income statement and balance sheet and the Company's balance sheet and other significant related disclosure items as previously reported for the year ended December 31, 2004.

4 CHANGES IN ACCOUNTING POLICIES (CONTINUED)

b. Restatement of prior periods (continued)

i. Effect on the consolidated financial statements

Consolidated income statement for the year ended December 31, 2004

In HK\$ million (except for earnings per share)	2004 (as previously reported)	Effect of new policy (increase/(decrease) in profit for the year)						Sub-total	2004 (as restated)
		HKAS 1	HKAS 17	HKAS 18	HKAS 32	HKAS-	HKFRS 2		
		(Note 4(a)(i))	(Note 4(a)(ii))	(Note 4(a)(iii))	(Note 4(a)(v))	Int 21 (Note 4(a)(viii))	(Note 4(a)(ix))		
Turnover	22,895	-	-	107	-	-	-	107	23,002
Cost of sales	(10,531)	-	-	-	-	-	-	-	(10,531)
General and administrative expenses	(8,298)	-	7	-	-	-	(93)	(86)	(8,384)
Other gains, net	461	-	-	-	-	(52)	-	(52)	409
Provisions for impairment losses	(40)	-	-	-	-	-	-	-	(40)
Restructuring costs	(51)	-	-	-	-	-	-	-	(51)
Interest income	57	-	-	-	-	-	-	-	57
Finance costs	(1,986)	-	-	-	(32)	-	-	(32)	(2,018)
Share of results of jointly controlled companies	(4)	-	-	-	-	-	-	-	(4)
Share of results of associates	152	(1)	-	-	-	-	-	(1)	151
Impairment losses on interests in jointly controlled companies and associates	(16)	-	-	-	-	-	-	-	(16)
Profit before taxation	2,639	(1)	7	107	(32)	(52)	(93)	(64)	2,575
Income tax	(981)	1	-	(19)	-	-	-	(18)	(999)
Profit after taxation	1,658	-	7	88	(32)	(52)	(93)	(82)	1,576
Minority interests	(20)	20	-	-	-	-	-	20	-
Profit for the year	1,638	20	7	88	(32)	(52)	(93)	(62)	1,576
Attributable to:									
Equity holders of the Company	1,638	-	7	88	(32)	(52)	(93)	(82)	1,556
Minority interests	-	20	-	-	-	-	-	20	20
Profit for the year	1,638	20	7	88	(32)	(52)	(93)	(62)	1,576
Earnings per share (in HK cents)									
Basic	30.50	-	0.13	1.64	(0.59)	(0.97)	(1.73)	(1.52)	28.98
Diluted	30.26	-	0.13	1.60	(0.58)	(0.95)	(1.69)	(1.49)	28.77
Increase/(Decrease) in other significant disclosure items:									
Staff costs	2,903	-	-	-	-	-	93	93	2,996
Depreciation	2,379	-	(22)	-	-	-	-	(22)	2,357
Amortization of land lease premium	-	-	15	-	-	-	-	15	15

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2005

(Amount expressed in Hong Kong dollars unless otherwise stated)

4 CHANGES IN ACCOUNTING POLICIES (CONTINUED)

b. Restatement of prior periods (continued)

i. Effect on the consolidated financial statements (continued)

Consolidated balance sheet as at December 31, 2004

In HK\$ million	2004 (as previously reported)	Effect of new policy (increase/(decrease) in net assets)						Sub-total	2004 (as restated)
		HKAS 17 (Note 4(a)(ii))	HKAS 18 (Note 4(a)(iii))	HKAS 32 (Note 4(a)(v))	HKAS 40 (Note 4(a)(vii))	HKAS- Int 21 (Note 4(a)(viii))	HKFRS 2 (Note 4(a)(ix))		
Non-current assets									
Property, plant and equipment	15,062	(1,157)	–	–	116	–	–	(1,041)	14,021
Investment properties	5,184	–	–	–	(108)	–	–	(108)	5,076
Interests in leasehold land held for own use under operating leases	–	1,189	–	–	(3)	–	–	1,186	1,186
Other non-current assets	11,198	–	–	–	–	–	–	–	11,198
	31,444	32	–	–	5	–	–	37	31,481
Current assets									
	13,524	–	–	–	–	–	–	–	13,524
Current liabilities									
Short-term borrowings	(9,031)	–	–	19	–	–	–	19	(9,012)
Accruals, other payables and deferred income	(6,617)	–	–	(15)	–	–	–	(15)	(6,632)
Advances from customers	(1,052)	–	(231)	–	–	–	–	(231)	(1,283)
Other current liabilities	(3,967)	–	–	–	–	–	–	–	(3,967)
	(20,667)	–	(231)	4	–	–	–	(227)	(20,894)
Net current liabilities	(7,143)	–	(231)	4	–	–	–	(227)	(7,370)
Total assets less current liabilities	24,301	32	(231)	4	5	–	–	(190)	24,111
Non-current liabilities									
Long-term liabilities	(20,663)	–	–	183	–	–	–	183	(20,480)
Deferred tax liabilities	(2,613)	–	213	–	–	88	–	301	(2,312)
Deferred income	(9)	–	(987)	–	–	–	–	(987)	(996)
Other long-term liabilities	(704)	–	–	(107)	–	–	–	(107)	(811)
Other non-current liabilities	(5,212)	–	–	–	–	–	–	–	(5,212)
	(29,201)	–	(774)	76	–	88	–	(610)	(29,811)
Net liabilities	(4,900)	32	(1,005)	80	5	88	–	(800)	(5,700)
CAPITAL AND RESERVES									
Share capital	1,344	–	–	–	–	–	–	–	1,344
Share premium	18	–	–	–	–	–	11	11	29
Employee share-based compensation reserve	–	–	–	–	–	–	137	137	137
Property revaluation reserve	25	–	–	–	8	97	–	105	130
Convertible note and bonds reserve	–	–	–	202	–	–	–	202	202
Deficit	(28,039)	32	(1,005)	(122)	(3)	(52)	(148)	(1,298)	(29,337)
Other reserves	19,936	–	–	–	–	–	–	–	19,936
Equity attributable to equity holders of the Company	(6,716)	32	(1,005)	80	5	45	–	(843)	(7,559)
Minority interests	1,816	–	–	–	–	43	–	43	1,859
Total equity	(4,900)	32	(1,005)	80	5	88	–	(800)	(5,700)

4 CHANGES IN ACCOUNTING POLICIES (CONTINUED)

b. Restatement of prior periods (continued)

ii. Effect on the Company's balance sheet

Balance sheet as at December 31, 2004

In HK\$ million	2004 (as previously reported)	Effect of new policy (increase/(decrease) in net assets)			2004 (as restated)
		HKAS 32 (Note 4(a)(v))	HKFRS 2 (Note 4(a)(ix))	Sub-total	
Non-current assets					
Property, plant and equipment	3	–	–	–	3
Investments in subsidiaries	20,721	(2,483)	148	(2,335)	18,386
Amounts due from a subsidiary	–	3,621	–	3,621	3,621
Loan due from a jointly controlled company of a subsidiary	1,214	–	–	–	1,214
Other non-current assets	307	–	–	–	307
	22,245	1,138	148	1,286	23,531
Current assets					
Amounts due from subsidiaries	–	66,370	–	66,370	66,370
Other current assets	337	–	–	–	337
	337	66,370	–	66,370	66,707
Current liabilities					
	(565)	–	–	–	(565)
Net current (liabilities)/assets	(228)	66,370	–	66,370	66,142
Total assets less current liabilities	22,017	67,508	148	67,656	89,673
Non-current liabilities					
Amounts due to subsidiaries	–	(67,508)	–	(67,508)	(67,508)
Net assets	22,017	–	148	148	22,165
CAPITAL AND RESERVES					
Share capital	1,344	–	–	–	1,344
Share premium	18	–	11	11	29
Special capital reserve	19,980	–	–	–	19,980
Employee share-based compensation reserve	–	–	137	137	137
Retained profits	675	–	–	–	675
Total equity	22,017	–	148	148	22,165

c. Estimated effect of changes in accounting policies for the current period

The following tables provide estimates of the extent to which each of the line items in the consolidated income statement and balance sheet and the Company's balance sheet and other significant related disclosure items for the year ended December 31, 2005 is higher or lower than it would have been had the previous policies still been applied in the year, where it is practicable to make such estimates. In addition, the adjustments that have been made to the opening balances at January 1, 2005, which are the aggregate effect of retrospective adjustments as at December 31, 2004 and the opening balance adjustments made as at January 1, 2005 to each of the line items in the consolidated balance sheet and the Company's balance sheet are also included.

4 CHANGES IN ACCOUNTING POLICIES (CONTINUED)
c. Estimated effect of changes in accounting policies for the current period (continued)
i. Effect on the consolidated financial statements

Estimated effect on the consolidated income statement for the year ended December 31, 2005:

In HK\$ million (except for earnings per share)	Estimated effect of new policy (increase/(decrease) in profit for the year)								Total
	HKAS 1 (Note 4(a)(i))	HKAS 17 (Note 4(a)(ii))	HKAS 18 (Note 4(a)(iii))	HKASs 32 & 39 (Note 4(a)(v))	HKFRS 3 & HKAS 36 (Note 4(a)(vi))	HKAS 40 (Note 4(a)(vii))	HKFRS 2 (Note 4(a)(ix))	HK-Int 3 (Note 4(a)(x))	
Turnover	-	-	147	-	-	-	-	(672)	(525)
Cost of sales	-	-	-	-	-	-	-	571	571
General and administrative expenses	-	7	-	25	105	73	(100)	-	110
Other gains, net	-	-	-	345	-	2	-	-	347
Provisions for impairment losses	-	-	-	-	-	-	-	-	-
Interest income	-	-	-	-	-	-	-	-	-
Finance costs	-	-	-	(2)	-	-	-	-	(2)
Share of results of jointly controlled companies	-	-	-	-	-	-	-	-	-
Share of results of associates	(1)	-	-	-	-	-	-	-	(1)
Impairment losses on interests in jointly controlled companies and associates	-	-	-	-	-	-	-	-	-
Profit before taxation	(1)	7	147	368	105	75	(100)	(101)	500
Income tax	1	-	(26)	-	-	-	-	18	(7)
Profit for the year	-	7	121	368	105	75	(100)	(83)	493
Attributable to:									
Equity holders of the Company	-	7	121	368	105	47	(98)	(50)	500
Minority interests	-	-	-	-	-	28	(2)	(33)	(7)
Profit for the year	-	7	121	368	105	75	(100)	(83)	493
Earnings per share (in HK cents)									
Basic	-	0.11	1.89	5.76	1.65	0.73	(1.53)	(0.78)	7.83
Diluted	-	0.11	1.89	5.75	1.64	0.73	(1.53)	(0.78)	7.81
Increase/(Decrease) in other significant disclosure items:									
Staff costs	-	-	-	-	-	-	100	-	100
Depreciation	-	(23)	-	-	-	-	-	-	(23)
Amortization of goodwill	-	-	-	-	(105)	-	-	-	(105)
Amortization of land lease premium	-	16	-	-	-	-	-	-	16

4 CHANGES IN ACCOUNTING POLICIES (CONTINUED)

c. Estimated effect of changes in accounting policies for the current period (continued)

i. Effect on the consolidated financial statements (continued)

Estimated effect on the consolidated balance sheet as at December 31, 2005:

In HK\$ million	Estimated effect of new policy (increase/(decrease) in net assets)								Total
	HKAS 17 (Note 4(a)(ii))	HKAS 18 (Note 4(a)(iii))	HKASs 32 & 39 (Note 4(a)(v))	HKFRS 3 & HKAS 36 (Note 4(a)(vi))	HKAS 40 (Note 4(a)(vii))	HKAS- Int 21 (Note 4(a)(viii))	HKFRS 2 (Note 4(a)(ix))	HK-Int 3 (Note 4(a)(x))	
Non-current assets									
Property, plant and equipment	(1,157)	-	-	-	116	-	-	-	(1,041)
Investment properties	-	-	-	-	(108)	-	-	-	(108)
Interests in leasehold land held for own use under operating leases	1,196	-	-	-	(3)	-	-	-	1,193
Goodwill	-	-	-	105	8	8	-	-	121
Properties held for/under development	-	-	-	-	-	-	-	721	721
Other non-current assets	-	-	(118)	-	-	-	-	-	(118)
	39	-	(118)	105	13	8	-	721	768
Current assets									
Derivative financial instruments	-	-	102	-	-	-	-	-	102
Available-for-sale financial assets	-	-	89	-	-	-	-	-	89
Financial assets at fair value through profit or loss	-	-	(55)	-	-	-	-	-	(55)
Prepayments, deposits and other current assets	-	-	26	-	-	-	-	(822)	(796)
	-	-	162	-	-	-	-	(822)	(660)
Current liabilities									
Derivative financial instruments	-	-	(62)	-	-	-	-	-	(62)
Accruals, other payables and deferred income	-	(215)	(80)	-	-	-	-	18	(277)
	-	(215)	(142)	-	-	-	-	18	(339)
Net current liabilities	-	(215)	20	-	-	-	-	(804)	(999)
Total assets less current liabilities	39	(215)	(98)	105	13	8	-	(83)	(231)
Non-current liabilities									
Long-term liabilities	-	-	(213)	-	-	-	-	-	(213)
Deferred tax liabilities	-	187	-	-	-	88	-	-	275
Deferred income	-	(856)	9	-	-	-	-	-	(847)
Other long-term liabilities	-	-	382	-	-	-	-	-	382
	-	(669)	178	-	-	88	-	-	(403)
Net assets/(liabilities)	39	(884)	80	105	13	96	-	(83)	(634)
CAPITAL AND RESERVES									
Share premium	-	-	-	-	-	-	25	-	25
Employee share-based compensation reserve	-	-	-	-	-	-	223	-	223
Property revaluation reserve	-	-	-	-	(120)	97	-	-	(23)
Convertible note and bonds reserve	-	-	183	-	-	-	-	-	183
Available-for-sale financial assets reserve	-	-	89	-	-	-	-	-	89
Deficit	39	(884)	(192)	105	133	(52)	(246)	(50)	(1,147)
Equity attributable to equity holders of the Company	39	(884)	80	105	13	45	2	(50)	(650)
Minority interests	-	-	-	-	-	51	(2)	(33)	16
Total equity	39	(884)	80	105	13	96	-	(83)	(634)

4 CHANGES IN ACCOUNTING POLICIES (CONTINUED)**c. Estimated effect of changes in accounting policies for the current period (continued)****ii. Effect on the Company's balance sheet**

Estimated effect on the balance sheet as at December 31, 2005:

In HK\$ million	Estimated effect of new policy (increase/(decrease) in net assets)		
	HKASs 32 & 39 (Note 4(a)(v))	HKFRS 2 (Note 4(a)(ix))	Total
Non-current assets			
Investments in subsidiaries	(8,531)	247	(8,284)
Current assets			
Amounts due from subsidiaries	76,039	–	76,039
Current liabilities			
Derivative financial instruments	(15)	–	(15)
Amounts due to subsidiaries	(67,620)	–	(67,620)
	(67,635)	–	(67,635)
Net current assets	8,404	–	8,404
Total assets less current liabilities	(127)	247	120
Net assets	(127)	247	120
CAPITAL AND RESERVES			
Share premium	–	25	25
Employee share-based compensation reserve	–	222	222
Retained profits	(127)	–	(127)
Total equity	(127)	247	120

5 RELATED PARTY TRANSACTIONS

For the purposes of these financial statements, parties are considered to be related to the Group if the Group has the ability, directly or indirectly, to control the party or exercise significant influence over the party in making financial and operating decisions, or vice versa, or where the Group and the party are subject to common control or common significant influence. Related parties may be individuals (being members of key management personnel, significant shareholders and/or their close family members) or other entities and include entities which are under the significant influence of related parties of the Group where those parties are individuals, and post-employment benefit plans which are for the benefit of employees of the Group or of any entity that is a related party of the Group.

During the year, the Group had the following significant transactions with related parties:

In HK\$ million	Note(s)	The Group	
		2005	2004
Convertible bond interest paid or payable to a substantial shareholder	a	276	293
Telecommunications service fees, rental charges, facility management services and subcontracting charges received or receivable from a jointly controlled company	a & c	135	135
System integration charges received or receivable from a shareholder of a PRC subsidiary	a	404	387
Telecommunications service fees and system integration charges received or receivable from a substantial shareholder	a	34	–
Telecommunications service fees, outsourcing fees and rental charges paid or payable to a jointly controlled company	a & c	765	905
Telecommunications service fees paid or payable to a substantial shareholder	a	14	–
Key management compensation	b	164	170

5 RELATED PARTY TRANSACTIONS (CONTINUED)

a. These transactions were carried out after negotiations between the Group and the related parties in the ordinary course of business and on the basis of estimated market value as determined by the directors. In respect of transactions for which the price or volume has not yet been agreed with the relevant related parties, the directors have determined the relevant amounts based on their best estimation.

b. Details of key management compensation

In HK\$ million	The Group	
	2005	2004
Salaries and other short-term employee benefits	117	127
Post-employment benefits	4	4
Share-based compensation	43	39
	164	170

c. Details of transactions with a jointly controlled company of a subsidiary ("JV")

An indirect wholly-owned subsidiary of the Company and a wholly-owned subsidiary of the JV have entered into a Hong Kong Domestic Connectivity Agreement and an International Services Agreement for the provision of domestic and international connectivity services in Hong Kong and between Hong Kong and other countries. Pursuant to the International Services Agreement, for the first five years of operations subsequent to the formation of the JV, the Group is required to acquire 90%, 90%, 80%, 70% and 60% per annum, respectively, of its total annual purchases of "Committed Services" (being international public switched telephone network terminating access, international transmission capacity and Internet gateway access services) from the wholly-owned subsidiary of the JV. The Hong Kong Domestic Connectivity Agreement contemplates a reciprocal arrangement, whereby the Group will provide local connectivity services in Hong Kong to the wholly-owned subsidiary of the JV under similar terms and conditions. These agreements were subsequently amended on January 31, 2001 and further amended on April 15, 2003 such that each of the Group and Telstra have agreed to purchase 90% per annum of the Group's and Telstra's respective Committed Services from the JV and its subsidiaries until repayment of the outstanding portion of US\$1,200 million (approximately HK\$9,360 million) of the debt under the amended US\$1,500 million syndicated term loan facility (the "Reach Term Facility") to a wholly-owned subsidiary of the JV on December 31, 2010 or earlier at rates benchmarked at least annually to prevailing market prices. The wholly-owned subsidiary of the JV similarly must acquire 90% per annum of its local connectivity services from the Group under the amended agreement for domestic connectivity services, similarly extended for the same period. The International Services Agreement was terminated as part of the arrangements relating to the establishment of the new operating model for the JV on April 16, 2005, details of which are set out in note 1(c).

Purchases made by the Group from the JV for the year ended December 31, 2005 were HK\$163 million (2004: HK\$855 million).

On June 17, 2004, the Company and Telstra agreed to purchase from the syndicate of banks the entire outstanding portion of US\$1,200 million of the debt under the Reach Term Facility for approximately US\$310.9 million (approximately HK\$2,425 million). The Company's share of the purchased debt was 50%, or approximately US\$155.45 million (approximately HK\$1,213 million). The purchase was completed on June 18, 2004. This loan receivable from the wholly-owned subsidiary of the JV is secured and will be repayable in a single payment on December 31, 2010. Interest on the loan receivable was suspended for six months from June 18, 2004 and agreed to be at London Interbank Offered Rate ("LIBOR") plus 250 basis points following such period. As at December 31, 2004, the loan receivable from the wholly-owned subsidiary of the JV was approximately HK\$1,214 million and was included in "Loan due from a jointly controlled company of a subsidiary" in the balance sheet of the Company (see note 24). This loan receivable was subsequently set-off pursuant to the arrangements relating to the establishment of the new operating model for the JV on April 16, 2005, details of which are set out in note 1(c).

5 RELATED PARTY TRANSACTIONS (CONTINUED)

c. Details of transactions with a jointly controlled company of a subsidiary ("JV") (continued)

In addition, on June 17, 2004, the Company and Telstra agreed to provide the JV with a revolving working capital loan facility with each of the Company and Telstra contributing up to US\$25 million (approximately HK\$195 million) to this facility. As at December 31, 2005, no draw down has been made by the JV under this facility (2004: Nil). This amount has been disclosed as the Group's commitment as at December 31, 2005 with details set out in note 41(c).

As set out in note 1(c), the Group entered into a new operating model with the JV on April 16, 2005. During the year ended December 31, 2005, the outsourcing fees paid or payable by the Group to the JV under the new operating model, determined on a cost plus basis, were HK\$552 million (2004: Nil). Details of other transactions pursuant to the agreements with the JV on April 16, 2005 are set out in note 1(c).

d. Amounts due from/(to) related companies

Other than as specified in this note, notes 24 and 25 and a loan to the parent company of a substantial shareholder in the amount of HK\$98 million at a fixed interest rate of 4% per annum and with fixed terms of repayment up to 2010, balances with related parties are unsecured, non-interest bearing and have no fixed repayment terms.

6 TURNOVER

In HK\$ million	The Group	
	2005	2004 (Restated) (Note 46)
Telecommunications and other service revenues	15,703	15,720
Amounts received and receivable in respect of goods sold	1,727	1,532
Amounts received and receivable in respect of properties sold	4,821	5,415
Amounts received and receivable from the rental of investment properties	248	335
	22,499	23,002

7 SEGMENT INFORMATION

Segment information is presented in respect of the Group's business and geographical segments. Business segment information is chosen as the primary reporting format because this is consistent with the Group's internal financial reporting.

a. Business segments

The Group comprises the following main business segments:

Telecommunications Services ("TSS") is the leading provider of telecommunications services, wholesale and retail consumer broadband, mobile, multimedia and NOW TV services and related equipment in Hong Kong.

Business eSolutions offers Information and Communications Technologies ("ICT") services, business broadband services, hosting and facilities management services and directories businesses within Hong Kong and mainland China.

Infrastructure and Property ("Infrastructure") covers the Group's property portfolio in Hong Kong and mainland China including the Cyberport development in Hong Kong.

Others include the Group's other businesses in Taiwan, United Kingdom and Japan and together with the corporate support functions.

In HK\$ million	TSS		Business eSolutions		Infrastructure		Others		Elimination		Consolidated	
	2005 (Restated) (Note 46)	2004	2005 (Restated) (Note 46)	2004	2005 (Restated) (Note 46)	2004	2005 (Restated) (Note 46)	2004	2005 (Restated) (Note 46)	2004	2005 (Restated) (Note 46)	2004
REVENUE												
External revenue	15,143	14,698	1,945	2,174	5,099	5,767	312	363	-	-	22,499	23,002
Inter-segment revenue	788	636	509	527	55	96	-	9	(1,352)	(1,268)	-	-
Total revenue	15,931	15,334	2,454	2,701	5,154	5,863	312	372	(1,352)	(1,268)	22,499	23,002
RESULT												
Segment results	4,471	4,728	(83)	(63)	539	1,274	(102)	(635)	-	-	4,825	5,304
Unallocated corporate expenses											(271)	(899)
Interest income											533	57
Finance costs											(2,234)	(2,018)
Share of results of jointly controlled companies and associates	120	162	-	(4)	-	-	1	(11)	-	-	121	147
Impairment losses on interests in jointly controlled companies and associates	-	-	(4)	(16)	-	-	-	-	-	-	(4)	(16)
Profit before taxation											2,970	2,575
Income tax											(1,103)	(999)
Profit for the year											1,867	1,576

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2005

(Amount expressed in Hong Kong dollars unless otherwise stated)

7 SEGMENT INFORMATION (CONTINUED)

a. Business segments (continued)

In HK\$ million	TSS		Business eSolutions		Infrastructure		Others		Elimination		Consolidated	
	2005	2004	2005	2004	2005	2004	2005	2004	2005	2004	2005	2004
		(Restated)		(Restated)		(Restated)		(Restated)		(Restated)		(Restated)
		(Note 46)		(Note 46)		(Note 46)		(Note 46)		(Note 46)		(Note 46)
OTHER INFORMATION												
Capital expenditure (including property, plant and equipment, investment properties, interests in leasehold land held for own use under operating leases, intangible assets and goodwill) incurred during the year	6,810	1,532	136	42	100	104	177	366				
Depreciation and amortization	2,267	2,061	96	135	119	140	122	112				
Impairment losses recognized in income statement	33	28	21	16	6	5	20	7				
Significant non-cash expenses (excluding depreciation, amortization and impairment losses)	109	99	4	4	41	-	11	212				
ASSETS												
Segment assets	21,839	17,202	1,348	1,508	17,247	18,577	1,731	1,507	-	-	42,165	38,794
Interests in jointly controlled companies and associates	697	1,858	-	2	-	-	8	14	-	-	705	1,874
Unallocated corporate assets											10,413	4,337
Consolidated total assets											53,283	45,005
LIABILITIES												
Segment liabilities	5,557	4,759	845	904	9,463	8,496	738	693	-	-	16,603	14,852
Unallocated corporate liabilities											33,948	35,853
Consolidated total liabilities											50,551	50,705

7 SEGMENT INFORMATION (CONTINUED)

b. Geographical segments

The Group's businesses are managed on a worldwide basis, but operate in three principal economic environments. In presenting information on the basis of geographical segments, segment revenue is based on the geographical location of customers. Segment assets and capital expenditure are based on the geographical location of the assets.

In HK\$ million	Revenue from external customers		Segment assets		Capital expenditure incurred during the year	
	2005	2004 (Restated) (Note 46)	2005	2004 (Restated) (Note 46)	2005	2004
Hong Kong	20,613	21,212	35,048	33,388	5,394	1,651
Mainland China (excluding Hong Kong) and Taiwan	1,498	1,468	4,956	4,780	110	46
Others	388	322	2,161	626	1,744	370
	22,499	23,002	42,165	38,794	7,248	2,067

8 OTHER GAINS, NET

In HK\$ million	The Group	
	2005	2004 (Restated) (Note 46)
Net realized gains on disposals of investments in subsidiaries, an associate, available-for-sale financial assets and financial assets at fair value through profit or loss	264	–
Net unrealized gains on financial assets at fair value through profit or loss	73	–
Impairment loss on investment in unconsolidated subsidiaries held for sale	(6)	–
Net unrealized holding losses on other investments	–	(25)
Net realized gains on disposals of investments in jointly controlled companies and associates, investment securities and other investments	–	22
Provision for impairment of investments	(18)	(187)
Loss on rental guarantee (note a)	(69)	–
Net realized and unrealized fair value gains on derivative financial instruments	319	–
Fair value gains on investment properties	2	–
Amortization of premium received from equity options	–	5
Gain on deemed disposal of interest in subsidiaries (note b)	–	59
Gain on placement of PCPD shares, net of expenses (note c)	–	524
Dividend income	10	11
Unclaimed dividend payable by a subsidiary written back	27	–
Others	24	–
	626	409

8 OTHER GAINS, NET (CONTINUED)

- a.** Under the formal property sale and purchase agreement dated December 21, 2004 in respect of the disposal of PCCW Tower, on completion of the disposal, there is a rental guarantee pursuant to which Partner Link Investments Limited, an indirect wholly-owned subsidiary of PCPD, will undertake to the purchaser that it will pay a guaranteed net monthly rental of approximately HK\$13.3 million to the purchaser for a period of 5 years commencing from February 8, 2005, i.e. the date following completion of the disposal of PCCW Tower. During the period from February 8, 2005 to December 31, 2005, the Group recorded a net loss of approximately HK\$28 million, representing the net cash outflow under the rental guarantee. In addition, the Group has also made a provision of approximately HK\$41 million in relation to the rental guarantee over the remaining term of the rental guarantee.
- b.** On March 5, 2004, the Company and DFG, a company incorporated in Bermuda and whose shares are listed on the Stock Exchange, entered into an agreement, under which DFG conditionally agreed to purchase the Company's interest in certain investment properties, the Cyberport project and related property and facilities management companies for an aggregate consideration of HK\$6,557 million. Such consideration was satisfied by the issuance of the then 93.42% of the increased share capital of DFG of approximately HK\$2,967 million to Asian Motion, and the issuance of convertible notes of HK\$3,590 million to the Company respectively. The agreement became unconditional on May 10, 2004 and DFG was subsequently renamed Pacific Century Premium Developments Limited. As the Company became the controlling shareholder (as defined under the Listing Rules) of DFG on completion of the transaction, the transaction was accounted for as a reverse acquisition and the Company was treated as acquiring a 93.42% interest in DFG. The Group recorded a deemed disposal gain of approximately HK\$36 million for the year ended December 31, 2004 as a result of the injection of its interests in certain investment properties to acquire the 93.42% interest in DFG. In addition, on October 28, 2004, Asian Motion agreed to sell, through Lehman Brothers Asia Limited, 118,000,000 PCPD shares at a price of HK\$2.18 per PCPD share. On the same date, Asian Motion also entered into a subscription agreement with PCPD for the subscription of 118,000,000 new PCPD shares at the price of HK\$2.18 per PCPD share. The net proceeds from the subscription were used for general working capital purposes. As a result, the Group recorded another deemed disposal gain of approximately HK\$36 million for the year ended December 31, 2004. Upon the adoption of new and revised HKFRSs effective January 1, 2005, the net assets of PCPD at the date of the deemed disposals were increased due to decreases of deferred tax liabilities (see note 4(a)(viii) above). Accordingly, the deemed disposal gains were restated to approximately HK\$28 million and HK\$31 million respectively to reflect the effect of the increased net assets of PCPD at the date of the deemed disposals.
- c.** On April 30, 2004, the Company and Asian Motion agreed to sell, through Citigroup Global Markets Hong Kong Futures and Securities Limited, 237,000,000 PCPD shares at a price of HK\$2.65 per PCPD share. The Group's gain (net of expenses) from the share placing was approximately HK\$252 million for the year ended December 31, 2004 and the net proceeds were used for the general working capital purposes of Asian Motion. In addition, on November 30, 2004, Asian Motion agreed to sell, through Deutsche Bank AG, Hong Kong Branch, 450,000,000 PCPD shares at a price of HK\$2.48 per PCPD share. The Group's gain (net of expenses) from this disposal was approximately HK\$311 million for the year ended December 31, 2004 and the net proceeds were used for general corporate purposes. Upon the adoption of new and revised HKFRSs effective January 1, 2005, these gains on placement of PCPD shares were restated to approximately HK\$238 million and HK\$286 million respectively.

9 PROVISIONS FOR IMPAIRMENT LOSSES

In HK\$ million	The Group	
	2005	2004
Provisions for impairment of:		
Property, plant and equipment (<i>note a</i>)	50	29
Others	2	11
	52	40

- a.** Due to technology and market changes in the sectors in which the Group operates, certain of the Group's property, plant and equipment became obsolete or impaired. Accordingly, the Group recognized an impairment loss of approximately HK\$50 million (2004: HK\$29 million) in the consolidated income statement for the year ended December 31, 2005.

10 PROFIT BEFORE TAXATION

Profit before taxation is stated after crediting and charging the following:

a. Staff costs

In HK\$ million	The Group	
	2005	2004 (Restated) (Note 46)
Retirement costs for directors	4	4
Retirement costs for other staff		
– pension income for defined benefit retirement schemes (note 32(a)(iii))	(240)	(129)
– contributions to defined contribution retirement scheme	151	170
	(85)	45
Equity-settled share-based payment expenses	100	93
Salaries, bonuses and other benefits	2,662	2,858
	2,677	2,996

b. Other items

In HK\$ million	The Group	
	2005	2004 (Restated) (Note 46)
Crediting:		
Dividend income from		
– listed investments	9	–
– unlisted investments	1	11
Realized gains on disposal of investments in a subsidiary and associates included in other gains, net	166	3
Realized gains on disposal of investment securities included in other gains, net	–	19
Realized gains on disposal of available-for-sale financial assets and financial assets at fair value through profit or loss included in other gains, net	98	–
Gain on disposal of property, plant and equipment, investment properties and interests in leasehold land held for own use under operating leases	24	56
Exchange gains, net	211	34
Gross rental income	248	335
Less: Outgoings	(21)	(54)
Charging:		
Provision for impairment of property, plant and equipment	50	29
Impairment loss for doubtful debts	137	45
Provision for inventory obsolescence	17	9
Depreciation of property, plant and equipment	2,543	2,357
Amortization of land lease premium	16	15
Amortization of intangible assets	135	97
Amortization of goodwill	–	63
Cost of inventories	1,692	1,473
Cost of properties sold	4,119	4,665
Auditors' remuneration	16	14
Operating lease rental		
– equipment	89	86
– other assets (including property rentals)	260	231

11 FINANCE COSTS

In HK\$ million	The Group	
	2005	2004 (Restated) (Note 46)
Interest paid/payable for:		
Overdrafts and bank loans wholly repayable within 5 years	153	113
Bank loans not wholly repayable within 5 years	–	5
Other loans wholly repayable within 5 years	943	927
Other loans not wholly repayable within 5 years	1,166	993
	2,262	2,038
Interest capitalized in fixed assets	(28)	(20)
Finance costs	2,234	2,018

During the year, the capitalization rates used to determine the amount of interest eligible for capitalization ranged from 5.37% to 7.75% (2004: 3.9% to 5.5%).

12 DIRECTORS' AND SENIOR EXECUTIVES' EMOLUMENTS

Details of directors' emoluments are set out below:

a. Directors' emoluments – cash and cash equivalents paid by the Company

In HK\$ million	The Group			
	2005			
	Directors' fees	Salaries, allowances and benefits in kind	Bonuses ¹	Retirement scheme contributions
Executive directors				
Li Tzar Kai, Richard	–	4.29 ²	–	–
So Chak Kwong, Jack	–	15.00	8.00	0.63
Yuen Tin Fan, Francis	–	4.28	7.30	0.64
Peter Anthony Allen	–	2.70 ³	3.00	0.19
Alexander Anthony Arena	–	11.48	8.83	0.81
Chung Cho Yee, Mico	–	5.00	13.09	0.54
Lee Chi Hong, Robert	–	11.00	7.90	0.90
Dr Fan Xingcha ⁴	0.05	2.80	2.05 ⁵	0.24
Non-executive directors				
Sir David Ford	–	2.54	0.12	0.20
Zhang Chunjiang ⁶	0.15	–	–	–
Dr Tian Suning ⁷	0.15	–	–	–
Independent non-executive directors				
Prof Chang Hsin-kang	0.20	–	–	–
Dr Fung Kwok King, Victor	0.20	–	–	–
Dr The Hon Sir Li Kwok Po, David	0.20	–	–	–
Sir Roger Lobo	0.30 ⁸	–	–	–
Aman Mehta	0.20	0.40	–	–
The Hon Raymond George Hardenbergh Seitz ⁹	0.30 ¹⁰	0.40	–	–
	1.75	59.89	50.29	4.15

12 DIRECTORS' AND SENIOR EXECUTIVES' EMOLUMENTS (CONTINUED)

a. Directors' emoluments – cash and cash equivalents paid by the Company (continued)

Notes:

- 1 Bonuses in respect of 2005, paid in 2005 and in 2006.
- 2 Benefit of accommodation provided.
- 3 Excludes remuneration for duties performed for associates.
- 4 Appointed as a Non-executive Director on April 1, 2005 and redesignated as an Executive Director on July 1, 2005.
- 5 Includes sign-on bonus.
- 6 Appointed as Non-executive Director on April 1, 2005.
- 7 Appointed as Non-executive Director on April 1, 2005.
- 8 Includes HK\$100,000 fee as Chairman of Audit Committee.
- 9 Redesignated as Independent Non-executive Director on February 1, 2005.
- 10 Includes HK\$100,000 fee as Chairman of Remuneration Committee.

In HK\$ million	The Group			
	2004			
	Directors' fees	Salaries, allowances and benefits in kind	Bonuses ¹	Retirement scheme contributions
Executive directors				
Li Tzar Kai, Richard	–	4.26 ²	–	–
So Chak Kwong, Jack	–	15.00	8.20	0.63
Yuen Tin Fan, Francis	–	4.28	13.69	0.64
Peter Anthony Allen	–	2.89 ³	3.94	0.07
Alexander Anthony Arena	–	4.00	14.18	0.45
Chung Cho Yee, Mico	–	5.00	13.12	0.52
Lee Chi Hong, Robert	–	10.00	7.80	0.83
Michael John Butcher ⁴	–	5.32	3.90	0.35
Cheung Wing Lam, Linus ⁵	–	1.25	–	0.13
Non-executive directors				
Sir David Ford	–	2.45	0.22	0.20
The Hon Raymond George Hardenbergh Seitz	0.30 ⁶	0.40	–	–
Independent non-executive directors				
Prof Chang Hsin-kang	0.20	–	–	–
Dr Fung Kwok King, Victor	0.20	–	–	–
Dr The Hon Sir Li Kwok Po, David	0.20	–	–	–
Sir Roger Lobo	0.30 ⁷	–	–	–
Aman Mehta ⁸	0.18	0.30	–	–
	1.38	55.15	65.05	3.82

Notes:

- 1 Includes bonuses in respect of 2003 (paid in 2003 and 2004) and 2004 (paid in 2004 and 2005).
- 2 Benefit of accommodation provided.
- 3 Excludes remuneration for duties performed for associates.
- 4 Resigned as Executive Director on August 26, 2004.
- 5 Resigned as Executive Director on February 29, 2004.
- 6 Includes HK\$100,000 fee as Chairman of Remuneration Committee.
- 7 Includes HK\$100,000 fee as Chairman of Audit Committee.
- 8 Appointed as Independent Non-Executive Director on February 10, 2004.

12 DIRECTORS' AND SENIOR EXECUTIVES' EMOLUMENTS (CONTINUED)

b. Directors' emoluments – share-based compensation

The Group 2005								
Grant date	Exercise price of share options	Number of share options/ shares outstanding at beginning of year	Number of share options exercised/ shares transferred	Number of share options/ shares outstanding at end of year	Number of share options vested	Share-based compensation charged to income statement (Note ii)	Value of shares transferred (Note i)	
Executive directors								
So Chak Kwong, Jack	July 25, 2003	4.3500	12,000,000	-	12,000,000	8,000,000	6.59	-
	February 8, 2005	4.4750	3,500,000	-	3,500,000	-	2.31	-
	May 15, 2003	N/A	4,322,000	2,161,000	2,161,000	N/A	5.71	11.13
Yuen Tin Fan, Francis	July 25, 2003	4.3500	8,534,000	-	8,534,000	5,689,333	4.68	-
	February 8, 2005	4.4750	3,000,000	-	3,000,000	-	1.98	-
Peter Anthony Allen	July 25, 2003	4.3500	2,000,000	-	2,000,000	1,333,333	1.10	-
	February 8, 2005	4.4750	2,000,000	-	2,000,000	-	1.32	-
Alexander Anthony Arena	July 25, 2003	4.3500	6,400,000	-	6,400,000	4,266,666	3.51	-
	February 8, 2005	4.4750	3,000,000	-	3,000,000	-	1.98	-
Chung Cho Yee, Mico	July 25, 2003	4.3500	5,695,200	-	5,695,200	3,796,800	3.13	-
	February 8, 2005	4.4750	3,000,000	-	3,000,000	-	1.98	-
Lee Chi Hong, Robert	July 25, 2003	4.3500	5,000,000	-	5,000,000	3,333,333	2.74	-
	February 8, 2005	4.4750	1,000,000	-	1,000,000	-	0.66	-
Dr Fan Xingcha	September 1, 2005	5.2500	7,000,000	-	7,000,000	-	1.42	-
Non-executive director								
Sir David Ford	July 25, 2003	4.3500	2,000,000	-	2,000,000	1,333,333	1.10	-
	February 8, 2005	4.4750	2,000,000	-	2,000,000	-	1.32	-
						41.53	11.13	

12 DIRECTORS' AND SENIOR EXECUTIVES' EMOLUMENTS (CONTINUED)

b. Directors' emoluments – share-based compensation (continued)

The Group 2004									
	Grant date	Exercise price of share options HK\$	Number of share options/ shares outstanding at beginning of year	Number of share options exercised/ shares transferred	Number of share options/ shares outstanding at end of year	Number of share options vested	Share-based compensation charged to income statement (Note ii) HK\$ million	Value of shares transferred (Note i) HK\$ million	
Executive directors									
So Chak Kwong, Jack	July 25, 2003	4.3500	12,000,000	–	12,000,000	4,000,000	8.94	–	
	May 15, 2003	N/A	6,483,000	2,161,000	4,322,000	N/A	7.68	11.78	
Yuen Tin Fan, Francis	July 25, 2003	4.3500	8,534,000	–	8,534,000	2,844,666	6.36	–	
Peter Anthony Allen	July 25, 2003	4.3500	2,000,000	–	2,000,000	666,666	1.49	–	
Alexander Anthony Arena	July 25, 2003	4.3500	6,400,000	–	6,400,000	2,133,333	4.77	–	
Chung Cho Yee, Mico	July 25, 2003	4.3500	5,695,200	–	5,695,200	1,898,400	4.24	–	
Lee Chi Hong, Robert	July 25, 2003	4.3500	5,000,000	–	5,000,000	1,666,666	3.72	–	
Non-executive director									
Sir David Ford	July 25, 2003	4.3500	2,000,000	–	2,000,000	666,666	1.49	–	
							38.69	11.78	

i. Value of shares transferred

The value of shares transferred represents the market value of relevant shares granted by the principal shareholder to a director at the date of transfer. No director exercised share options in 2005 or 2004. Had there been any exercise of share options by directors, the value of shares transferred would include the market value of the relevant shares at the date of exercise less the corresponding exercise price.

ii. Share-based compensation charged to income statement

Share-based compensation is a trinomial option pricing model calculation of the fair value of share options, and also the estimated fair value of the Company's shares granted as estimated at the date of grant. Share-based compensation is amortized in the income statement over the vesting period of the related share options or shares granted. These values do not represent realizable gains which are affected by a combination of a number of factors, including, performance of the Company's share price, vesting period, timing of exercise etc. The details of these share options and awards are disclosed under the section "Share Option Schemes" in the Report of the Directors and notes 33(a) and 33(c) to the financial statements.

Total directors' emoluments for the year ended December 31, 2005, including amortized share-based compensation, were HK\$157.61 million (2004: HK\$164.09 million).

No directors waived the right to receive emoluments during the year.

Of the five highest paid individuals in the Group, all (2004: all) are directors of the Company whose emoluments are stated above.

13 INCOME TAX

a. Taxation in the consolidated income statement represents:

In HK\$ million	The Group	
	2005	2004 (Restated) (Note 46)
Hong Kong profits tax		
– provision for current year	1,105	1,305
– under/(over) provision in respect of prior years	77	(76)
Overseas tax		
– provision for current year	5	10
Recovery of deferred taxation (note 35(a))	(84)	(240)
	1,103	999

Hong Kong profits tax has been provided at the rate of 17.5% (2004: 17.5%) on the estimated assessable profits for the year.

Overseas taxation has been calculated on the estimated assessable profits for the year at the rates prevailing in the respective jurisdictions.

b. Reconciliation between tax expense and accounting profit at applicable tax rate:

In HK\$ million	The Group	
	2005	2004 (Restated) (Note 46)
Profit before taxation	2,970	2,575
Notional tax on profit before taxation, calculated at applicable tax rates	520	451
Income not subject to taxation	(177)	(76)
Expenses not deductible for taxation purposes	348	353
Tax losses not recognized	444	456
Under/(Over) provision in prior years, net	13	(142)
Utilization of tax losses	(29)	(27)
Income not subject to taxation for jointly controlled companies and associates	(21)	(26)
Tax provision of overseas operations	5	10
Tax expense	1,103	999

14 PROFIT/(LOSS) ATTRIBUTABLE TO EQUITY HOLDERS OF THE COMPANY

Profit of HK\$2,809 million (2004: Loss of HK\$548 million) attributable to equity holders of the Company was dealt with in the financial statements of the Company.

15 DIVIDENDS

a. Dividends payable to equity holders of the Company attributable to the year

In HK\$ million	2005	2004
Interim dividend declared and paid of 6.5 HK cents (2004: 5.5 HK cents) per ordinary share	437	295
Final dividend proposed after the balance sheet date of 12 HK cents (2004: 9.6 HK cents) per ordinary share	807	645
	1,244	940

The final dividend proposed after the balance sheet date has not been recognized as a liability at the balance sheet date.

b. Dividends payable to equity holders of the Company attributable to the previous financial year, approved and paid during the year

In HK\$ million	2005	2004
Final dividend in respect of the previous financial year, approved and paid during the year, of 9.6 HK cents (2004: Nil) per ordinary shares	645	–

16 EARNINGS PER SHARE

The calculations of basic and diluted earnings per share are based on the following data:

	2005	2004 (Restated) (Note 46)
Earnings (in HK\$ million)		
Earnings for the purpose of basic earnings per share	1,595	1,556
Effective interest on liability component of convertible bonds (net of tax)	–	23
Earnings for the purpose of diluted earnings per share	1,595	1,579
Number of shares		
Weighted average number of ordinary shares for the purpose of basic earnings per share	6,388,671,140	5,369,998,643
Effect of deemed issue of shares under the Company's share option scheme for nil consideration	12,760,758	21,928,842
Effect of conversion of convertible bonds	–	96,864,195
Weighted average number of ordinary shares for the purpose of diluted earnings per share	6,401,431,898	5,488,791,680

The US\$450 million 1% guaranteed convertible bonds due 2007 of the Group outstanding as at December 31, 2005 has an anti-dilutive effect on the basic earnings per share for the year ended December 31, 2005. Both the US\$450 million 1% guaranteed convertible bonds due 2007 and the US\$1,100 million 3.5% guaranteed convertible bonds due 2005 of the Group outstanding as at December 31, 2004 have anti-dilutive effect on the basic earnings per share for the year ended December 31, 2004.

17 PROPERTY, PLANT AND EQUIPMENT

In HK\$ million	The Group 2005					
	Land and buildings	Exchange equipment	Transmission plant	Other plant and equipment	Projects under construction	Total
Cost						
Beginning of year, as previously stated	3,200	8,331	7,884	7,040	642	27,097
Prior period adjustment arising from adoption of new accounting standard for leases (<i>note 4(a)(ii)</i>)	(1,244)	–	–	(4)	–	(1,248)
Opening balances, as restated	1,956	8,331	7,884	7,036	642	25,849
Additions						
– through acquisition of a subsidiary	–	229	382	147	518	1,276
– others	–	600	1,916	553	999	4,068
Transfers	(11)	221	39	130	(379)	–
Disposals	(738)	(46)	(1)	(235)	–	(1,020)
Exchange differences	–	–	–	(6)	(34)	(40)
End of year	1,207	9,335	10,220	7,625	1,746	30,133
Accumulated depreciation and impairment						
Beginning of year, as previously stated	341	4,025	3,019	4,650	–	12,035
Prior period adjustment arising from adoption of new accounting standard for leases	(204)	–	–	(3)	–	(207)
Opening balances, as restated	137	4,025	3,019	4,647	–	11,828
Charge for the year	46	1,010	645	842	–	2,543
Provision for impairment in value	–	–	–	50	–	50
Disposals	(84)	(45)	(1)	(165)	–	(295)
Exchange differences	–	2	–	(7)	–	(5)
End of year	99	4,992	3,663	5,367	–	14,121
Net book value						
End of year	1,108	4,343	6,557	2,258	1,746	16,012
Beginning of year, as restated	1,819	4,306	4,865	2,389	642	14,021

17 PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

In HK\$ million	The Group 2004					
	Land and buildings	Exchange equipment	Transmission plant	Other plant and equipment	Projects under construction	Total
Cost						
Beginning of year, as previously stated	3,365	7,398	8,304	5,374	1,141	25,582
Prior period adjustment arising from adoption of new accounting standard for leases (<i>note 4(a)(ii)</i>)	(1,249)	–	–	(4)	–	(1,253)
Opening balances, as restated	2,116	7,398	8,304	5,370	1,141	24,329
Additions	13	418	337	575	629	1,972
Transfers	177	656	(757)	1,234	(1,128)	182
Disposals	(103)	(141)	–	(180)	–	(424)
Exchange differences	–	–	–	37	–	37
Valuation adjustment	(247)	–	–	–	–	(247)
End of year	1,956	8,331	7,884	7,036	642	25,849
Accumulated depreciation and impairment						
Beginning of year, as previously stated	278	3,268	2,490	3,886	–	9,922
Prior period adjustment arising from adoption of new accounting standard for leases	(185)	–	–	(2)	–	(187)
Opening balances, as restated	93	3,268	2,490	3,884	–	9,735
Charge for the year	60	898	500	899	–	2,357
Provision for impairment in value	–	–	29	–	–	29
Disposals	(16)	(141)	–	(166)	–	(323)
Exchange differences	–	–	–	30	–	30
End of year	137	4,025	3,019	4,647	–	11,828
Net book value						
End of year	1,819	4,306	4,865	2,389	642	14,021
Beginning of year, as restated	2,023	4,130	5,814	1,486	1,141	14,594

Land and buildings with an aggregate carrying value of approximately HK\$31 million were pledged as security for certain bank borrowings of the Group as at December 31, 2005 (2004: HK\$33 million).

17 PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

The carrying amount of land and buildings of the Group is analyzed as follows:

In HK\$ million	The Group	
	2005	2004 (Restated) (Note 46)
Held in Hong Kong		
On long lease (over 50 years)	93	767
On medium-term lease (10-50 years)	930	966
Held outside Hong Kong		
Freehold	40	41
Leasehold		
On medium-term lease (10-50 years)	45	45
	1,108	1,819

During the year ended December 31, 2005, the Group performed an annual review to reassess the useful lives of certain exchange equipment, transmission plant, and other plant and equipment of the Group, based on the experience from the Group's operational management, certification from equipment suppliers, technological trend research and future economic trend. The reassessment has resulted in a change in the estimated useful lives of these assets as the current switching network will be migrated to a full Internet Protocol network which will prolong the lives of certain assets in other parts of the network. The Group considers this to be a change in accounting estimate and has therefore accounted for the change prospectively from July 1, 2005. As a result of this change in accounting estimate, the Group's profit for the year and the net assets as at the year end have both been increased by HK\$110 million.

In HK\$ million	The Company 2005	
	Other plant and equipment	Total
Cost		
Beginning of year	5	5
Additions	–	–
End of year	5	5
Accumulated depreciation and impairment		
Beginning of year	2	2
Charge for the year	–	–
End of year	2	2
Net book value		
End of year	3	3
Beginning of year	3	3

17 PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

In HK\$ million	The Company 2004	
	Other plant and equipment	Total
Cost		
Beginning of year	2	2
Additions	3	3
End of year	5	5
Accumulated depreciation and impairment		
Beginning of year	2	2
Charge for the year	–	–
End of year	2	2
Net book value		
End of year	3	3
Beginning of year	–	–

18 INVESTMENT PROPERTIES

In HK\$ million	The Group	
	2005	2004
Beginning of year, as previously stated	5,184	5,880
Prior period adjustment arising from adoption of new accounting standard for investment properties (<i>note 4(a)(vii)</i>)	(108)	(92)
Opening balances, as restated	5,076	5,788
Transfers	–	(182)
Disposals	(1,765)	(179)
Exchange differences	77	(13)
Fair value gains/(losses)	2	(338)
End of year	3,390	5,076

Investment properties held in and outside Hong Kong were revalued as at December 31, 2005 by an independent valuer, CB Richard Ellis Limited. The basis of valuation for investment properties was open market value.

18 INVESTMENT PROPERTIES (CONTINUED)

The carrying amount of investment properties of the Group is analyzed as follows:

In HK\$ million	The Group	
	2005	2004 (Restated) (Note 46)
Held in Hong Kong		
On long lease (over 50 years)	–	1,765
On medium-term lease (10-50 years)	4	2
Held outside Hong Kong		
On long lease (over 50 years)	696	681
On medium-term lease (10-50 years)	2,690	2,628
	3,390	5,076

The Group leases out properties under operating leases. The leases typically run for an initial period of 1 to 9 years. None of the leases include contingent rentals.

As at December 31, 2005, the total future minimum lease payments in respect of investment properties and the dual use properties being accounted for as land and buildings under non-cancellable operating leases are receivable as follows:

In HK\$ million	The Group	
	2005	2004 (Restated) (Note 46)
Within 1 year	208	191
After 1 year but within 5 years	333	333
After 5 years	45	96
	586	620

Total future minimum lease payments receivable under non-cancellable operating leases as at December 31, 2004 included minimum lease receipts from the tenants of PCCW Tower, the Group's headquarters in Hong Kong, up to February 7, 2005, i.e. the completion date of the disposal of PCCW Tower.

19 INTERESTS IN LEASEHOLD LAND HELD FOR OWN USE UNDER OPERATING LEASES

In HK\$ million	The Group	
	2005	2004
Cost		
Beginning of year, as previously stated	–	–
Prior period adjustment arising from adoption of new accounting standards for leases and investment properties (<i>notes 4(a)(ii) and (vii)</i>)	1,364	1,369
Opening balances, as restated	1,364	1,369
Transfer to properties under development	(224)	–
Disposals	(321)	(5)
End of year	819	1,364
Accumulated amortization		
Beginning of year, as previously stated	–	–
Prior period adjustment arising from adoption of new accounting standards for leases and investment properties	178	166
Opening balances, as restated	178	166
Charge for the year	16	15
Transfer to properties under development	(3)	–
Disposals	(33)	(3)
End of year	158	178
Net book value		
End of year	661	1,186
Beginning of year, as restated	1,186	1,203

The carrying amount of interests in leasehold land held for own use under operating leases of the Group is analyzed as follows:

In HK\$ million	The Group	
	2005	2004 (Restated) (<i>Note 46</i>)
Held in Hong Kong		
On long lease (over 50 years)	99	610
On medium-term lease (10-50 years)	550	562
Held outside Hong Kong		
On medium-term lease (10-50 years)	12	14
	661	1,186

20 PROPERTIES HELD FOR/UNDER DEVELOPMENT

In HK\$ million	The Group	
	2005	2004
Leasehold land, at cost:		
Located in Hong Kong	–	3
Properties held for development	–	3
Properties under development (<i>note a</i>)	7,473	6,548
Less: Properties under development classified as current assets	(5,538)	(469)
	1,935	6,079
Total	1,935	6,082

a. Pursuant to an agreement dated May 17, 2000 entered into with the Government (“Cyberport Project Agreement”), the Group was granted an exclusive right and obligation to design, develop, construct and market the Cyberport project at Telegraph Bay on the Hong Kong Island. The Cyberport project consists of commercial and residential portions. The completed commercial portion was transferred to the Government at no consideration. The associated costs incurred have formed part of the development costs of the residential portion. Pre-sales of the residential portion of the Cyberport project commenced in February 2003.

21 GOODWILL

In HK\$ million	The Group	
	2005	2004
Cost		
Beginning of year	1,625	1,535
Opening balance adjustment to eliminate accumulated amortization and impairment	(665)	–
Additions	1,701	90
End of year	2,661	1,625
Accumulated amortization and impairment		
Beginning of year	665	602
Eliminated against cost at January 1, 2005	(665)	–
Charge for the year	–	63
End of year	–	665
Carrying amount		
End of year	2,661	960
Beginning of year	960	933

In 2004, goodwill not already recognized directly in reserves was amortized on a straight-line basis over its estimated useful life ranging from 10 to 20 years. The amortization of goodwill for the year ended December 31, 2004 was included in “General and administrative expenses” in the consolidated income statement.

As explained further in note 4(a)(vi), with effect from January 1, 2005, the Group no longer amortizes goodwill. In accordance with the transitional provisions set out in HKFRS 3, the accumulated amortization of goodwill as at January 1, 2005 has been eliminated against the cost of goodwill as at that date.

21 GOODWILL (CONTINUED)

Impairment tests for cash-generating units containing goodwill

Goodwill is allocated to the Group's CGUs identified according to business segment as follows:

In HK\$ million	The Group	
	2005	2004
TSS		
BtN Access (note a)	–	585
PCCW Global (note a)	585	–
SUNDAY – Unallocated (note b)	1,538	–
	2,123	585
Business eSolutions		
PCCW Directories	162	162
ChinaBig	58	52
Omnilink	120	50
Others	6	6
	346	270
Infrastructure – PCPD	168	81
Others	24	24
Total	2,661	960

- During the year, the BtN Access CGU has merged with the International section of the Commercial Group of the TSS business segment to form a new CGU, PCCW Global. The goodwill related to the BtN Access CGU of HK\$585 million was re-allocated to the PCCW Global CGU accordingly.
- The goodwill of HK\$1,538 million arising from the acquisition of SUNDAY during the year is included in the TSS business segment. The Company is still in the process of assessing the synergistic effect that the acquisition of SUNDAY will bring to the respective CGUs of the Group and will allocate the goodwill to those respective CGUs after such assessment is completed in 2006.

The recoverable amounts of the CGUs are determined based on value-in-use calculations. These calculations use cash flow projections based on financial budgets approved by management covering a five-year period. Cash flows beyond the five-year period are extrapolated using the estimated growth rates stated below. The growth rate does not exceed the long-term average growth rate for the business in which the CGU operates.

Key assumptions used for value-in-use calculations:

	2005		
	Gross margin	Growth rate	Discount rate
PCCW Global	24.2%	4.0%	14.0%
SUNDAY – Unallocated	N/A	3.3%	10.5%
PCCW Directories	59.3%	2.0%	12.0%
ChinaBig	51.3%	5.8%	12.0%
Omnilink	18.4%	3.0%	17.0%
PCPD	18.0%	N/A	12.0%

21 GOODWILL (CONTINUED)**Impairment tests for cash-generating units containing goodwill (continued)**

These assumptions have been used for the analysis of each CGU within the business segment.

There was no evidence of impairment arising from this review. The only circumstances where a reasonably possible change in key assumptions might have caused an impairment loss to be recognized was in respect of PCCW Global where:

- a fall of 1.7% in the gross margin; or
- a decrease of 3.5% in the growth rate; or
- an increase of 2.0% in the discount rate

would have caused an impairment loss to be recognized.

Management determined budgeted gross margin based on past performance and its expectations for market development. The weighted average growth rates used are consistent with the forecasts included in industry reports. The discount rates used are pre-tax and reflect specific risks relating to the relevant CGUs.

22 INTANGIBLE ASSETS

In HK\$ million	The Group 2005						
	Trademarks	Content licence	Wireless broadband licence	3G licence (Note a)	Customer base	Others	Total
Cost							
Beginning of year	1,518	375	106	–	–	63	2,062
Additions							
– through acquisition of a subsidiary	10	–	–	101	65	7	183
– others	–	–	–	–	–	20	20
Exchange differences	–	–	(8)	–	–	–	(8)
End of year	1,528	375	98	101	65	90	2,257
Accumulated amortization and impairment							
Beginning of year	332	375	31	–	–	58	796
Charge for the year (note b)	78	–	20	–	16	21	135
End of year	410	375	51	–	16	79	931
Net book value							
End of year	1,118	–	47	101	49	11	1,326
Beginning of year	1,186	–	75	–	–	5	1,266

22 INTANGIBLE ASSETS (CONTINUED)

In HK\$ million	The Group 2004				Total
	Trademarks	Content licence	Wireless broadband licence	Others	
Cost					
Beginning of year	1,518	375	93	63	2,049
Additions	–	–	5	–	5
Exchange differences	–	–	8	–	8
End of year	1,518	375	106	63	2,062
Accumulated amortization and impairment					
Beginning of year	256	375	11	57	699
Charge for the year (note b)	76	–	20	1	97
End of year	332	375	31	58	796
Net book value					
End of year	1,186	–	75	5	1,266
Beginning of year	1,262	–	82	6	1,350

- The 3G licence will be amortized over the licence period, commencing from the date of launch of the 3G services. The 3G services have not been launched as at December 31, 2005.
- The amortization charge for the year is included in “General and administrative expenses” in the consolidated income statement.

23 INVESTMENTS IN SUBSIDIARIES

In HK\$ million	The Company	
	2005	2004 (Restated) (Note 46)
Unlisted shares, at cost	146,471	146,463
Capital contribution in respect of employee share-based compensation	247	148
	146,718	146,611
Less: Provision for impairment in value	(128,233)	(128,225)
	18,485	18,386

The provision for impairment in value of HK\$128,233 million (2004: HK\$128,225 million) relates to certain subsidiaries of the Company which hold the Group's investments in subsidiaries, jointly controlled companies, associates, investment securities and other investments.

23 INVESTMENTS IN SUBSIDIARIES (CONTINUED)

Dividends from the PRC joint ventures accounted for as subsidiaries will be declared based on the profits in the statutory financial statements of these PRC joint ventures which are prepared using accounting principles generally accepted in the PRC. Such profits are different from the amounts reported under HKFRSs.

As at December 31, 2005, particulars of the principal subsidiaries of the Company are as follows:

Company name	Place of incorporation/ operations	Principal activities	Nominal value of issued capital/ registered capital	Equity interest attributable to the Group	
				Directly	Indirectly
PCCW-HKT Limited	Hong Kong	Investment holding	HK\$6,092,100,052	–	100%
PCCW-HKT Telephone Limited ¹	Hong Kong	Telecommunications services	HK\$2,163,783,209	–	100%
PCCW-HKT Business Services Limited	Hong Kong	Provision of business customer premises equipment and ancillary business services	HK\$2	–	100%
PCCW-HKT Network Services Limited	Hong Kong	Provision of retail international data and value-added services, local value-added telecommunications services; consumer premises equipment, business customer premises equipment, computer products and ancillary services, marketing and selling satellite master antenna television and related equipment and products and provision of maintenance services in relation thereto, manages customer loyalty programs “No.1 Club” and “Partners” for members of the programs	HK\$3	–	100%
PCCW Teleservices (Hong Kong) Limited	Hong Kong	Provision of customer relationship management and customer contact management solutions and services	HK\$2	–	100%
PCCW-HKT Technical Services Limited	Hong Kong	Provision of technical support and maintenance services	HK\$500,002	–	100%
PCCW Media Limited	Hong Kong	Provision of pay television programme services and interactive multimedia services	HK\$3,500,000,100 (HK\$3,500,000,095 ordinary shares, HK\$1 “A” Class share and HK\$4 “B” Class shares)	–	100%

23 INVESTMENTS IN SUBSIDIARIES (CONTINUED)

Company name	Place of incorporation/ operations	Principal activities	Nominal value of issued capital/ registered capital	Equity interest attributable to the Group	
				Directly	Indirectly
PCCW Teleservices Operations (Hong Kong) Limited	Hong Kong	Provision of customer relationship management and customer contact management solutions and services	HK\$2	–	100%
Cascade Limited	Hong Kong	Design, build and operate network infrastructures including technical consultancy and operation outsourcing	HK\$10,000	–	100%
PCCW IMS Limited	Hong Kong	Provision of retail broadband and narrowband Internet access services under the “NETVIGATOR” brandname, international telecommunication services and the provision of support services to a fellow subsidiary	HK\$2	–	100%
Pacific Century Systems Limited	Hong Kong	Customer premises equipment related business	HK\$1,000,000	100%	–
Corporate Access Limited	Cayman Islands/ Asia Pacific	Transponder leasing	US\$10	–	100%
BtN Access (HK) Limited (now known as PCCW Global (HK) Limited)	Hong Kong	Provision of satellite based telecommunication services to third parties and satellite transponder capacity to a fellow subsidiary	HK\$10	–	100%
Beyond The Network Limited (now known as PCCW Global Limited)	Hong Kong	Global Internet Protocol based communication service	HK\$2	–	100%
PCCW Global (Singapore) Pte. Ltd.	Singapore	Telecommunication solutions resale services	S\$2	–	100%
電訊盈科(北京)有限公司 ²	The PRC	System integration, consulting and informatization project	US\$6,750,000	–	100%
Omnilink Technology Limited	British Virgin Islands	Investment holding	US\$14,850	–	100%
Unihub China Information Technology Company Limited	The PRC	Selling of hardware and software and information system consulting services	RMB200,000,000	–	38.2%
中盈優創資訊科技有限公司 ³					
Unihub Limited (now known as PCCW Solutions Limited)	Hong Kong/ Asia Pacific	Computer services and provision of IP/IT related value-added services to business customers	HK\$1,200	–	100%
PCCW Business eSolutions Limited	Hong Kong	Provision of IP/IT related value-added services to business customers	HK\$2	–	100%

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2005

(Amount expressed in Hong Kong dollars unless otherwise stated)

23 INVESTMENTS IN SUBSIDIARIES (CONTINUED)

Company name	Place of incorporation/ operations	Principal activities	Nominal value of issued capital/ registered capital	Equity interest attributable to the Group	
				Directly	Indirectly
PCCW Powerbase Data Center Services (HK) Limited	Hong Kong	Data center services	HK\$2	–	100%
Power Logistics Limited	Hong Kong	Delivery services	HK\$100,000	–	100%
PCCW Directories Limited ¹	Hong Kong	Sale of advertising in the Business White Pages, Yellow Pages for businesses and Yellow Pages for customers, publication of directories, provision of Internet directory services and sale of on-line advertising	HK\$10,000	–	100%
ChinaBiG Limited	Hong Kong	Production and distribution of trade directory	HK\$359,189	–	76.97%
Pacific Century Premium Developments Limited	Bermuda/ Hong Kong	Investment holding	HK\$240,245,987	–	61.66%
Cyber-Port Limited	Hong Kong	Property development	HK\$2	–	61.66%
Beijing Jing Wei House and Land Estate Development Co., Ltd. 北京京威房地產開發有限公司 ⁴	The PRC	Property development	US\$100,000,000	–	61.66%
Talent Master Investments Limited	British Virgin Islands/Hong Kong	Investment holding	US\$1	–	61.66%

Certain subsidiaries which do not materially affect the results or financial position of the Group are not included.

Notes:

- 1 The subsidiary has accounting year end date of March 31. These subsidiaries prepare, for the purpose of consolidation, financial statements as at the same date as the Group.
- 2 Represents a wholly foreign owned enterprise.
- 3 Represents a Sino-foreign equity joint venture.
- 4 Represents a Sino-foreign cooperative joint venture.

24 INTEREST IN JOINTLY CONTROLLED COMPANIES

In HK\$ million	The Group		The Company	
	2005	2004	2005	2004
Share of net assets of jointly controlled companies, net of unrecognized losses	2,815	2,815	–	–
Loans due from jointly controlled companies	8	2,361	–	2,353
Amounts due from jointly controlled companies	24	27	–	–
	2,847	5,203	–	2,353
Provision for impairment	(2,837)	(3,976)	–	(1,139)
	10	1,227	–	1,214
Investments at cost, unlisted shares	3,130	3,130	–	–

Balances with jointly controlled companies are unsecured, non-interest bearing and have no fixed terms of repayment except for the capacity prepayment to REACH of HK\$1,139 million and the loan receivable from the wholly-owned subsidiary of REACH of HK\$1,214 million in 2004, (see note 5(c)) as included in “Loans due from jointly controlled companies” above, both of which were settled as a result of the establishment of new operating model for REACH and restructuring of REACH’s debt as set out in note 1(c).

As at December 31, 2005, particulars of the principal jointly controlled company of the Group are as follows:

Company name	Place of incorporation/ operations	Principal activities	Nominal value of issued capital/ registered capital	Equity interest attributable to the Group	
				Directly	Indirectly
Reach Ltd.	Bermuda/Asia	Provision of international telecommunication services	US\$5,890,000,000	–	50%

Summarized unaudited financial information of the significant jointly controlled company, REACH, is as follows:

In HK\$ million	2005	2004
Condensed consolidated balance sheet information as at December 31		
Non-current assets	1,648	3,166
Current assets	2,240	2,121
Total assets	3,888	5,287
Non-current liabilities	(2,806)	(13,221)
Current liabilities	(2,927)	(3,720)
Net liabilities	(1,845)	(11,654)
Condensed consolidated income statement information for the year ended December 31		
Turnover	5,478	6,300
Expenses	(3,254)	(6,575)
Profit/(Loss) after taxation	2,224	(275)

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2005

(Amount expressed in Hong Kong dollars unless otherwise stated)

24 INTEREST IN JOINTLY CONTROLLED COMPANIES (CONTINUED)

An analysis of the Group's total interest in REACH as at December 31, 2005 is as follows:

In HK\$ million	2005	2004
Share of net assets, net of unrecognized losses	2,705	2,705
Capacity prepayment to REACH	–	1,139
Loan receivable from a wholly-owned subsidiary of REACH (note 5(c))	–	1,214
Goodwill previously eliminated against reserves	8,578	8,578
Total interest in REACH before provision for impairment	11,283	13,636
Provision for impairment	(11,283)	(12,422)
Total interest in REACH after provision for impairment	–	1,214

25 INTEREST IN ASSOCIATES

In HK\$ million	The Group		The Company	
	2005	2004	2005	2004
Share of net assets of associates, net of unrecognized losses	758	708	–	–
Loans due from an associate	78	78	–	–
Amounts due from an associate	34	39	1	4
	870	825	1	4
Provision for impairment	(175)	(178)	–	–
	695	647	1	4
Investments at cost, unlisted shares	975	1,000	–	–

Balances with associates are unsecured, non-interest bearing and have no fixed terms of repayment except for the loans due from an associate, which bear interest at commercial rates, are secured by part of its movable properties and have fixed terms of repayment ranging up to three years from the date of drawdown in 2000, and a full provision for impairment was made in 2003.

As at December 31, 2005, particulars of the principal associates of the Group are as follows:

Company name	Place of incorporation/ operations	Principal activities	Nominal value of issued capital/ registered capital	Equity interest attributable to the Group	
				Directly	Indirectly
Great Eastern Telecommunications Limited*	Cayman Islands	Non-trading	US\$43,112,715	–	49%
Abacus Distribution Systems (Hong Kong) Limited	Hong Kong	Provision of computer reservation systems and travel related services	HK\$15,600,000	–	37.04%
Petro-CyberWorks Information Technology Company Limited 石化盈科信息技術 有限責任公司	The PRC	Design and development of Enterprise Resource Planning systems, and customer relationship management systems	RMB50,000,000	–	45%

* The associate has accounting year end date of March 31. The associate prepares, for the purpose of consolidation, financial statements as at the same date as the Group.

25 INTEREST IN ASSOCIATES (CONTINUED)

Summarized unaudited financial information of the associates of the Group is as follows:

In HK\$ million	2005	2004
Total assets	1,674	1,725
Total liabilities	(230)	(218)
Turnover	497	487
Profit after taxation	447	279

During the year ended December 31, 2005, the Group has not recognized its share of losses of its associates amounting to approximately HK\$1 million (2004: HK\$1 million). As at December 31, 2005, the accumulated share of losses of the associates unrecognized by the Group was HK\$6 million (2004: HK\$5 million).

26 INVESTMENTS

Investments are analyzed as follows:

In HK\$ million	The Group	
	2005	2004
Held-to-maturity investments	18	31
Investment securities (note a)	–	388
Available-for-sale financial assets (note b)	526	–
Financial assets at fair value through profit or loss (note c)	312	–
Other investments (note d)	–	313
	856	732

a. Investment securities

In HK\$ million	The Group	
	2005	2004
Unlisted, at cost	–	1,765
Less: Provision for impairment in value	–	(1,377)
	–	388

In 2004, a listed security was transferred from investment securities to other investments. This transfer was effected at fair value. The aggregate unrealized holding loss at the date of transfer which had not been previously recognized of approximately HK\$0.5 million was recognized in the consolidated income statement at the date of transfer.

As at December 31, 2004, investment securities with an aggregate carrying value of approximately HK\$19 million were pledged as security for certain bank borrowings of the Group.

26 INVESTMENTS (CONTINUED)**b. Available-for-sale financial assets**

In HK\$ million	The Group	
	2005	2004
Listed		
Hong Kong	101	–
Overseas	1	–
	102	–
Unlisted	424	–
	526	–
Market value of listed securities	102	–

During the year, an available-for-sale financial asset with a carrying value of approximately HK\$87 million was sold at a realized gain of approximately HK\$67 million, which was included in “Other gains, net” in the consolidated income statement.

As at December 31, 2005, available-for-sale financial assets with an aggregate carrying value of approximately HK\$21 million were pledged as security for certain bank borrowings of the Group.

c. Financial assets at fair value through profit or loss

In HK\$ million	The Group	
	2005	2004
Listed		
Hong Kong	255	–
Unlisted	57	–
	312	–

In 2002, the Group entered into certain derivative contracts, in the form of equity swap and equity option contracts, with a third party with the effect of entering into forward sales of a portion of certain quoted investments plus written call options held by the counterparty for the remaining portion of those quoted investments (see note 30(c)). As at December 31, 2005, the underlying quoted investments with aggregate carrying value of approximately HK\$178 million (2004: HK\$224 million which was classified as “Other investments” in 2004) have been placed as collateral for the transaction.

d. Other investments

In HK\$ million	The Group	
	2005	2004
Listed, at quoted market value		
Hong Kong	–	242
Unlisted	–	71
	–	313

Upon adoption of HKAS 39 on January 1, 2005, investments held for trading were reclassified as “Financial assets at fair value through profit or loss” and there was no other investments as at December 31, 2005.

27 CURRENT ASSETS AND LIABILITIES

a. Sales proceeds held in stakeholders' accounts

The balance represents proceeds from the sales of the residential portion of the Cyberport project retained in bank accounts opened and maintained by stakeholders. These amounts will be transferred to specific bank accounts, which are restricted in use, pursuant to certain conditions and procedures as stated in the Cyberport Project Agreement and the legally binding pre-sale contracts entered with the purchasers.

b. Restricted cash

Pursuant to the Cyberport Project Agreement, the Group has a restricted cash balance of approximately HK\$1,332 million as at December 31, 2005 (2004: HK\$903 million) held in specific bank accounts. The uses of the funds are specified in the Cyberport Project Agreement.

In addition, the Group has a restricted cash balance of approximately HK\$259 million as at December 31, 2005 (2004: Nil) which represented a bank deposit placed by an indirect wholly-owned subsidiary of the Company as a security for a bank guarantee issued in favour of the Company in connection with the undertakings as set out in note 34(a)(iii).

The remaining HK\$1 million as at December 31, 2005 represented a bank deposit placed by an indirect subsidiary of the Company as a security for a bank guarantee issued in respect of the use of facilities at the Hong Kong International Airport for the provision of mobile services.

As at December 31, 2004, there was a bank deposit of HK\$1 million placed by an another indirect subsidiary of the Company as a security for a banking facility granted to that subsidiary of the Company (see note 43).

c. Inventories

In HK\$ million	The Group	
	2005	2004
Work-in-progress	417	351
Finished goods	103	86
Consumable inventories	14	33
	534	470

d. Investment in unconsolidated subsidiaries held for sale

In respect of the reverse acquisition of DFG as set out in note 8(b), considering that certain subsidiaries of DFG were acquired and held exclusively with a view to resale, the investment in those subsidiaries of PCPD is accounted for as investment in unconsolidated subsidiaries held for sale and stated at the lower of carrying amount and fair value less costs to sell, of approximately HK\$45 million as at December 31, 2005 (2004: HK\$51 million).

The formal conditional agreement with a buyer entered into in 2004 for the disposal of PCPD's entire interest in subsidiaries holding a gas operation expired during the year. A second buyer has been solicited to purchase these subsidiaries at the same consideration, payable in cash by instalments in 2006.

e. Accounts receivable, net

An aging analysis of accounts receivable is set out below:

In HK\$ million	The Group	
	2005	2004
0 – 30 days	1,247	1,055
31 – 60 days	354	253
61 – 90 days	110	108
91 – 120 days	107	88
Over 120 days	466	327
	2,284	1,831
Less: Impairment loss for doubtful debts	(228)	(192)
	2,056	1,639

27 CURRENT ASSETS AND LIABILITIES (CONTINUED)

e. Accounts receivable, net (continued)

The carrying amounts of the net accounts receivable are denominated in the following currencies:

In HK\$ million	The Group	
	2005	2004
Hong Kong Dollars	1,602	1,290
United States Dollars	230	154
Chinese Renminbi	185	151
New Taiwan Dollars	30	27
Others	9	17
	2,056	1,639

f. Short-term borrowings

In HK\$ million	The Group		The Company	
	2005	2004 (Restated) (Note 46)	2005	2004
Bank loans	6,500	2	–	–
Current portion of long-term borrowings (note 28(a))	–	12	–	–
Convertible note and bonds (note 28(b))	–	8,998	–	461
	6,500	9,012	–	461
Secured	–	473	–	461
Unsecured	6,500	8,539	–	–

The carrying amounts of the short-term borrowings are denominated following currencies:

In HK\$ million	The Group		The Company	
	2005	2004	2005	2004
Hong Kong Dollars	6,500	–	–	–
United States Dollars	–	8,998	–	461
Others	–	14	–	–
	6,500	9,012	–	461

Please refer to note 43 for details of the Group's banking facilities.

27 CURRENT ASSETS AND LIABILITIES (CONTINUED)

g. Accounts payable

An aging analysis of accounts payable is set out below:

In HK\$ million	The Group	
	2005	2004
0 – 30 days	648	636
31 – 60 days	82	67
61 – 90 days	43	22
91 – 120 days	49	41
Over 120 days	175	166
	997	932

The carrying amounts of the accounts payable are denominated in the following currencies:

In HK\$ million	The Group	
	2005	2004
Hong Kong Dollars	651	651
United States Dollars	110	90
Chinese Renminbi	204	154
New Taiwan Dollars	28	25
Others	4	12
	997	932

h. Gross amount due to customers for contract work

In HK\$ million	The Group	
	2005	2004
Contract costs incurred plus attributable profits less foreseeable losses	784	794
Less: Estimated value of work performed	(795)	(799)
	(11)	(5)

The total amount of progress billings, included in the estimated value of work performed as at December 31, 2005, is approximately HK\$782 million (2004: HK\$782 million).

Included in non-current assets at December 31, 2005 is approximately HK\$8 million (2004: Nil) representing retention receivable from customers in respect of construction contracts in progress.

28 LONG-TERM LIABILITIES

In HK\$ million	The Group		The Company	
	2005	2004 (Restated) (Note 46)	2005	2004
Long-term borrowings (note a)	18,885	17,163	–	–
Convertible note and bonds (note b)	3,972	3,317	–	–
	22,857	20,480	–	–

a. Long-term borrowings

In HK\$ million	The Group		The Company	
	2005	2004	2005	2004
Repayable within a period				
– not exceeding one year	–	12	–	–
– over five years	18,885	17,163	–	–
	18,885	17,175	–	–
Less: Amounts repayable within one year included under current liabilities (note 27(f))	–	(12)	–	–
	18,885	17,163	–	–
Representing:				
US\$456 million 7.88% guaranteed notes (note i)	3,508	3,547	–	–
US\$500 million 6% guaranteed notes (note ii)	3,847	3,900	–	–
JPY30,000 million 3.65% guaranteed notes (note iii)	–	1,950	–	–
US\$1,000 million 8% guaranteed notes (note iv)	7,701	7,766	–	–
US\$500 million 5.25% guaranteed notes (note v)	3,829	–	–	–
	18,885	17,163	–	–
Secured	–	–	–	–
Unsecured	18,885	17,163	–	–

28 LONG-TERM LIABILITIES (CONTINUED)

a. Long-term borrowings (continued)

Details of major long-term borrowings of HK\$18,885 million of the Group are presented below:

i. US\$456 million 7.88% guaranteed notes

On January 24, 2003, PCCW Capital No. 3 Limited, an indirect wholly-owned subsidiary of the Company, privately placed US\$456 million 7.88% guaranteed notes due 2013 to raise funds for general corporate purposes. The notes are listed on the Luxembourg Stock Exchange and were unconditionally and irrevocably guaranteed by the Company until May 12, 2004. On May 12, 2004, the noteholders approved the novation of the guarantee to PCCW-HKT Telephone Limited (“HKTC”), an indirect wholly-owned subsidiary of the Company, and amendments to certain terms of the notes.

ii. US\$500 million 6% guaranteed notes

On July 17, 2003, PCCW-HKT Capital No.2 Limited, an indirect wholly-owned subsidiary of the Company, issued US\$500 million 6% guaranteed notes due 2013 which are listed on the Luxembourg Stock Exchange. The notes are irrevocable and unconditionally guaranteed by HKTC and will rank pari passu with all other outstanding unsecured and unsubordinated obligations of HKTC. The proceeds are used for general corporate purposes.

iii. JPY30,000 million 3.65% guaranteed notes

On October 26, 2001, Profit Century Finance Limited (“PCF”), an indirect wholly-owned subsidiary of the Company, completed the placement of JPY30,000 million 3.65% guaranteed notes due 2031 (the “Yen Notes”). Interest was payable semi-annually in arrears. The Yen Notes were redeemable at the option of PCF on any interest payment date falling on or after October 27, 2006.

The Yen Notes were unconditionally and irrevocably guaranteed by HKTC and ranked pari passu with all other outstanding unsecured and unsubordinated obligations of HKTC. The Yen Notes were repurchased by PCF and cancelled in full on June 30, 2005.

iv. US\$1,000 million 8% guaranteed notes

In November 2001, PCCW-HKT Capital Limited, an indirect wholly-owned subsidiary of the Company, issued US\$1,000 million 7.75% guaranteed notes due 2011 (the “Notes due 2011”). Interest is payable semi-annually in arrears. The interest rate payable on the Notes due 2011 will be subject to adjustment from time to time if the relevant rating agencies downgrade the rating ascribed to the Notes due 2011 below a pre-agreed level. The interest rate payable on the Notes due 2011 has been adjusted to 8% based on the current ratings.

The Notes due 2011 are unconditionally and irrevocably guaranteed by HKTC and will rank pari passu with all other outstanding unsecured and unsubordinated obligations of HKTC.

v. US\$500 million 5.25% guaranteed notes

On July 20, 2005, PCCW-HKT Capital No.3 Limited, an indirect wholly-owned subsidiary of the Company, issued US\$500 million 5.25% guaranteed notes due 2015, which are listed on the Singapore Exchange Securities Trading Limited. Interest is payable semi-annually in arrears. The notes are irrevocable and unconditionally guaranteed by HKTC and will rank pari passu with all other outstanding unsecured and unsubordinated obligations of HKTC. The proceeds are used for general corporate purposes.

Please refer to note 43 for details of the Group’s banking facilities.

28 LONG-TERM LIABILITIES (CONTINUED)**b. Convertible note and bonds**

In HK\$ million	The Group		The Company	
	2005	2004 (Restated) (Note 46)	2005	2004
Repayable within a period				
– not exceeding one year	–	8,998	–	461
– over one year, but not exceeding two years	3,972	–	–	–
– over two years, but not exceeding five years	–	3,317	–	–
	3,972	12,315	–	461
Less: Amounts repayable within one year included under current liabilities (note 27(f)):				
US\$54 million 5% mandatory convertible note due 2005 (note ii)	–	(461)	–	(461)
US\$1,100 million 3.5% guaranteed convertible bonds due 2005 (note iii)	–	(8,537)	–	–
	–	(8,998)	–	(461)
	3,972	3,317	–	–
Representing:				
US\$450 million 1% guaranteed convertible bonds due 2007 (note i)	3,972	3,317	–	–
	3,972	3,317	–	–
Secured	–	–	–	–
Unsecured	3,972	3,317	–	–

Details of convertible note and bonds of HK\$3,972 million of the Group are presented below:

i. US\$450 million 1% guaranteed convertible bonds due 2007

On January 29, 2002, PCCW Capital No. 2 Limited, an indirect wholly-owned subsidiary of the Company, issued US\$450 million 1% guaranteed convertible bonds due 2007, which are unconditionally and irrevocably guaranteed on a joint and several basis by the Company and HKTC. The convertible bonds due 2007 are listed on the Luxembourg Stock Exchange. They are convertible, at the option of their holders, into ordinary shares of the Company at an initial conversion price of HK\$13.5836 (approximately US\$1.7415) per share at any time up to and including the close of business on January 15, 2007. The bonds bear interest at 1% per annum, payable semi-annually in arrears on January 29 and July 29 in each year and at maturity, commencing on July 29, 2002. Unless previously redeemed, converted or purchased and cancelled, these bonds will be redeemed in US dollars at 119.383% of their principal amount, plus accrued interest on January 29, 2007.

Upon adoption of HKAS 32, the convertible bonds due 2007 were split into the liability and equity components at initial recognition. With effect from January 1, 2005, and in accordance with HKAS 39, interest expense on the convertible bonds is calculated using the effective interest method by applying the effective interest rate of 5.3% to the liability component.

28 LONG-TERM LIABILITIES (CONTINUED)

b. Convertible note and bonds (continued)

ii. US\$54 million 5% mandatory convertible note due 2005

On June 28, 2002, the Company issued a US\$190 million 5% mandatory convertible note due 2005 (the "Telstra Note due 2005") to Telstra as part of the disposal of the Group's 40% interest in Joint Venture (Bermuda) No. 2 Limited. Unless previously redeemed or converted or purchased and cancelled, the Telstra Note due 2005 could be convertible into ordinary shares of the Company on June 30, 2005 or the date which was 30 days after the holder of the Telstra Note due 2005 had given notice to the Company declaring that, amongst other things, an event of default or potential event of default had occurred under the Reach Term Facility, or any financing agreement entered into for the purpose of refinancing all or a significant part of such facility; the Company had ceased to have a controlling interest in HKTC; or if HKTC and its subsidiaries had ceased to carry on as their principal business the provision of fixed line telecommunications services in Hong Kong ("Repayment Date"). Interest was payable at 5% per annum compounded on a quarterly basis.

On the Repayment Date, the Telstra Note due 2005, plus accrued interest thereon, could be redeemed through its mandatory conversion into ordinary shares of the Company at a conversion price determined by reference to the volume weighted average price of the ordinary shares of the Company as quoted on the Stock Exchange for the 20 dealing days immediately preceding the Repayment Date. The Company was entitled to early redeem the Telstra Note due 2005 in full by giving notice in writing to Telstra. The redemption amount could be the outstanding principal balance together with any unpaid interest accrued at the date of redemption. The Telstra Note due 2005 could be redeemed at the request of Telstra, if a resolution was passed or an order was made that the Company be wound up or dissolved. The Company's obligations to Telstra as the initial holder of the Telstra Note due 2005 were secured by the Group's equity interest in REACH.

On April 15, 2003, the Company redeemed US\$143 million (approximately HK\$1,115 million) of the Telstra Note due 2005 and issued an amended note in the principal amount of approximately US\$54 million ("Amended Telstra Note due 2005") to Telstra. The principal amount of the Amended Telstra Note due 2005 was equal to US\$190 million, being the initial principal amount of the Telstra Note due 2005, plus its accrued and capitalized interest until March 31, 2003 of approximately US\$7 million less US\$143 million. The terms of the Amended Telstra Note due 2005 were substantially the same as those of the Telstra Note due 2005.

On June 30, 2005, the Company redeemed the Amended Telstra Note due 2005 upon its scheduled maturity for US\$58,386,346.06 in cash, which was a 5% discount to the outstanding principal amount and accrued interest as at June 30, 2005 of US\$61,459,311.64 and not by the mandatory conversion into ordinary shares of the Company.

iii. US\$1,100 million 3.5% guaranteed convertible bonds due 2005

On December 5, 2000, guaranteed convertible bonds due 2005 with the principal amount of US\$1,100 million were issued by PCCW Capital Limited, a wholly-owned subsidiary of the Company. These bonds were listed on the Luxembourg Stock Exchange. They were convertible into ordinary shares of the Company at US\$4.9804 (approximately HK\$38.8471) subject to adjustments, per share at any time on or after January 5, 2001 and up to the close of business on November 21, 2005 and were interest-bearing at 3.5% per annum, payable annually in arrears. Unless previously cancelled, redeemed or converted, these bonds could be redeemed in US dollars at 120.12% of the principal amount together with accrued interest on December 5, 2005. If these bonds were fully converted, the Company would be required to issue approximately 221 million ordinary shares.

Upon adoption of HKAS 32, the guaranteed convertible bonds due 2005 were split into liability and equity components at initial recognition. With effect from January 1, 2005, and in accordance with HKAS 39, interest expense on the convertible bonds is calculated using the effective interest method by applying the effective interest rate of 6.57% to the liability component.

On December 5, 2005, these bonds were fully redeemed in cash, which represented 120.12% of the outstanding principal amount and accrued interest as at December 5, 2005, and not by conversion into ordinary shares of the Company.

Prior to the adoption of new accounting standards on financial instruments, the redemption premium of convertible bonds was being accrued on a straight-line basis from the date of issuance to the final redemption date. As at December 31, 2004, the total redemption premiums for the convertible bonds described in (i) and (iii) above were HK\$1,808 million, of which HK\$398 million and HK\$1,410 million were included in "Other long-term liabilities" and "Accruals, other payables and deferred income" respectively in the consolidated balance sheet.

28 LONG-TERM LIABILITIES (CONTINUED)**b. Convertible note and bonds (continued)****iii. US\$1,100 million 3.5% guaranteed convertible bonds due 2005 (continued)**

Upon the adoption of HKAS 32 in respect of splitting of the convertible notes and bonds into their liability and equity components at initial recognition, the total redemption premiums for the convertible bonds described in (i) and (iii) above were restated to HK\$1,930 million, of which HK\$413 million and HK\$1,517 million were included in "Other long-term liabilities" and "Accruals, other payables and deferred income" respectively in the consolidated balance sheet as at December 31, 2004 (see note 4(a)(v)).

With effect from January 1, 2005, and in accordance with HKAS 39, the liability components of convertible notes and bonds, including the redemption premium, are stated at amortized cost using the effective interest method in the consolidated balance sheet.

As at December 31, 2005, none of the above-mentioned convertible note and bonds had been converted into ordinary shares of the Company.

29 PROVISIONS

In HK\$ million	The Group 2005		
	Payment to the Government (Note a)	Others	Total
Beginning of year	6,380	88	6,468
Additional provisions made	–	12	12
Additional provisions included in properties under development	1,648	–	1,648
Provisions settled	(1,323)	(71)	(1,394)
End of year	6,705	29	6,734
Less: Amounts classified as current liabilities	(5,270)	(29)	(5,299)
	1,435	–	1,435

a. Pursuant to the Cyberport Project Agreement, the Government shall be entitled to receive payments of approximately 65% from the surplus cashflow arising from the sales of the residential portion of the Cyberport project, net of certain allowable costs incurred on the project, as stipulated under certain terms and conditions of the Cyberport Project Agreement. Provision for payment to the Government is included in properties under development as the amount is considered as a part of the development costs of the Cyberport project. The provision is based on estimated sales proceeds of the residential portion of the Cyberport project and the estimated development costs of the Cyberport project. The estimated amount to be paid to the Government during the forthcoming year is classified as current liabilities.

30 DERIVATIVE FINANCIAL INSTRUMENTS

In HK\$ million	The Group		The Company	
	2005	2004	2005	2004
Current assets				
Cross currency swaps (<i>note a</i>)	42	–	–	–
Interest rate option (<i>note b</i>)	–	–	–	–
Equity swap and equity option (<i>note c</i>)	60	–	–	–
	102	–	–	–
Current liabilities				
Cross currency swaps (<i>note a</i>)	(62)	–	(15)	–
Forward foreign exchange contracts (<i>note d</i>)	–	–	–	–
	(62)	–	(15)	–

a. As at December 31, 2005, the Group had outstanding cross currency swap contracts with notional amounts of US\$2,406 million (approximately HK\$18,767 million) (2004: US\$5,956 million and JPY30,000 million (a total of approximately HK\$48,407 million)) at various rates respectively, to manage the Group's exposure to foreign currencies and interest rate fluctuations. The Company had outstanding cross currency swap contracts with notional amounts of US\$450 million (approximately HK\$3,510 million) (2004: US\$2,500 million and JPY 30,000 million (a total of approximately HK\$21,450 million)) at various rates respectively.

The carrying amounts of the outstanding cross currency swap contracts represent either the fair value receivables, which are included in current assets, or the fair value payables, which are included in current liabilities, as at December 31, 2005. In accordance with the transitional provisions in HKAS 39, no fair value gains or losses are required to be recognized for the outstanding cross currency swap contracts as at December 31, 2004, but details of these fair values are set out in note 40(e).

b. The Group enters into interest rate options to manage its interest rate risk. As at December 31, 2005, the total notional amount of such instruments was HK\$38 million (2004: HK\$53 million) and the carrying amount of such instruments was nil (January 1, 2005: Nil).

c. In 2002, the Group entered into certain derivative contracts, in the form of equity swap and equity option contracts, with a third party with the effect of entering into forward sales of a portion of certain quoted other investments plus written call options held by the counterparty for the remaining portion of those quoted other investments. The deemed forward sales effectively eliminated the Group's exposure to market price fluctuation and accordingly, the underlying quoted other investments were carried at the deemed forward price as at December 31, 2002. An advance receipt of approximately HK\$187 million for the deemed forward sales was received in 2002. The amount was included in "Other long-term liabilities" in the consolidated balance sheet and is interest bearing at commercial rate. The Group recognized a gain of approximately HK\$10 million for marking the quoted other investments to the deemed forward price and the gain was reflected in "Net gains on investments" in the consolidated income statement for the year ended December 31, 2002. The Group also received premiums of approximately HK\$25 million for the written call options with notional amount of approximately HK\$71 million. The premiums received were recorded as deferred income and were being amortized into income on a straight-line basis over the life of the call options. The underlying quoted other investments were carried at market value at each balance sheet date and any unrealized holding gains or losses were recognized in the consolidated income statement in the period as it arose. The underlying quoted other investments for both the deemed forward sales and written call options have been placed as collateral for the above equity swap and equity option transactions (note 26(c)).

With effect from January 1, 2005, in order to comply with HKAS 39, it is considered that each of these equity swap contracts comprises a debt instrument (the host contract) and embedded derivatives that are indexed to the prices of the equity investments. The debt instrument is carried at amortized cost while the compound embedded derivatives are bifurcated from the host contract and are separately accounted for in the financial statements at their fair market value at each balance sheet date. As at December 31, 2005, the carrying amount of the debt instrument and the compound derivatives was HK\$206 million (January 1, 2005: HK\$202 million), which was included in "Other long-term liabilities", and HK\$60 million (January 1, 2005: HK\$57 million), which was included in "Derivative financial instruments" under current assets, respectively.

No new derivative contract of this nature was entered into by the Group in 2005 and 2004.

30 DERIVATIVE FINANCIAL INSTRUMENTS (CONTINUED)

d. As at December 31, 2004, the Group and the Company had outstanding forward foreign exchange contracts to buy US\$141 million and US\$61 million at various rates totaling approximately HK\$1,090 million and HK\$472 million respectively. These contracts had estimated losses of HK\$5 million and HK\$1 million respectively as at December 31, 2004. In accordance with the transitional provisions in HKAS 39, the balance sheets as at December 31, 2004 were not adjusted to reflect these losses (see note 4(a)(v)). There was outstanding forward foreign exchange contract as at December 31, 2005.

31 SHARE CAPITAL

	2005		2004	
	Number of shares	Nominal value HK\$ million	Number of shares	Nominal value HK\$ million
Authorized:				
Ordinary shares of HK\$0.25 each				
Beginning of year	6,400,000,000	1,600	6,400,000,000	1,600
Increase during the year (note a)	3,600,000,000	900	–	–
End of year	10,000,000,000	2,500	6,400,000,000	1,600
Issued and fully paid:				
Ordinary shares of HK\$0.25 each				
Beginning of year	5,374,263,061	1,344	5,368,754,074	1,343
Exercise of employee share options (note b)	5,185,663	1	5,508,987	1
Issued for cash (note c)	1,343,571,766	336	–	–
End of year	6,723,020,490	1,681	5,374,263,061	1,344

a. Pursuant to an ordinary resolution passed at an extraordinary general meeting of the Company held on March 16, 2005, the authorized share capital of the Company was increased from HK\$1,600,000,000 to HK\$2,500,000,000 by the creation of an additional 3,600,000,000 ordinary shares of HK\$0.25 each, ranking *pari passu* with the existing shares of the Company.

b. During the year, 5,185,663 employee share options were exercised by the eligible option holders at their respective subscription prices of HK\$4.35 for a total cash consideration of HK\$22,557,634 resulting in the issue of 5,185,663 new ordinary shares of HK\$0.25 each.

c. Upon the completion of the Subscription on April 1, 2005 as set out in note 1(a), China Netcom (BVI) subscribed for 1,343,571,766 new ordinary shares of the Company of HK\$0.25 each at a price of HK\$5.90 per share. The proceeds from the Subscription were approximately HK\$7,927 million (before deduction of expenses), of which up to HK\$5,000 million will be used for investing in telecommunications opportunities in the PRC and the remainder will be used for reducing the Group's debt and general corporate purposes.

All new ordinary shares issued during the year rank *pari passu* in all respects with the existing shares.

32 EMPLOYEE RETIREMENT BENEFITS**a. Defined benefit retirement schemes**

The Group operates defined benefit retirement schemes ("DB Schemes") that provide lump sum benefits for employees upon resignation and retirement. The DB Schemes are final salary defined benefit schemes. The scheme assets are administered by independent trustees and are maintained independently of the Group's finances.

The DB Schemes are funded by contributions from the Group and employees in accordance with qualified independent actuaries' recommendation from time to time on the basis of periodic valuations.

In December 2004, members of certain DB Schemes were offered an option to receive a commuted lump sum payment in respect of their future monthly pension benefit and 382 members elected this option. This pension buy-out event was considered as a settlement event under SSAP 34 "Employee benefits". A gain of HK\$131 million was recognized in the consolidated income statement for the year ended December 31, 2004.

32 EMPLOYEE RETIREMENT BENEFITS (CONTINUED)

a. Defined benefit retirement schemes (continued)

On October 31, 2005, all the benefits of active members in respect of service before July 1, 2003 (i.e. the date on which all active members of the DB Schemes were transferred to defined contribution schemes operated by the Group for future services, with their benefits prior to that date remaining unchanged) were transferred to defined contribution schemes operated by the Group ("Transfer of past DB benefits") effective November 1, 2005. The value of the benefits of each member transferred was calculated to be the benefit entitlement of such members as at October 31, 2005, plus enhancement, if any. Enhancement is 50% of the increase in vested benefits, if any, which would have accrued to such members during the period from October 31, 2005 to January 31, 2006, assuming the transfer did not occur until January 31, 2006. After the Transfer of past DB benefits, the DB Schemes no longer have a defined benefit obligation in respect of the active members. This Transfer of past DB benefits was considered as a curtailment and settlement event under HKAS 19. The Group has injected HK\$64 million to the DB Schemes to make up part of the funding deficit as at October 31, 2005. An one-off curtailment and settlement gain of HK\$197 million was recognized in the consolidated income statement for the year ended December 31, 2005.

The latest independent actuarial valuation of the DB Schemes, prepared in accordance with HKAS 19, was carried out on December 31, 2005 and was prepared by Mr Aaron Wong of Watson Wyatt Hong Kong Limited, fellow of the Canadian Institute of Actuaries and also fellow of the Society of Actuaries, USA, using the projected unit credit method. The actuary was of the opinion that the fair value of the scheme assets was sufficient to cover 92.5% (2004: 92.6%) of the present value of the defined benefit obligations as at December 31, 2005.

i. The net liability recognized in the consolidated balance sheet is as follows:

In HK\$ million	The Group	
	2005	2004
Present value of the defined benefit obligations	228	3,984
Fair value of scheme assets	(211)	(3,691)
	17	293
Unrecognized actuarial (losses)/gains	(4)	24
Defined benefit liability in the consolidated balance sheet	13	317

As at December 31, 2005, the scheme assets do not include any ordinary shares issued by the Company (2004: Nil).

ii. Movements in the net liability recognized in the consolidated balance sheet are as follows:

In HK\$ million	The Group	
	2005	2004
Beginning of year	317	446
Contributions paid	(64)	–
Income recognized in the consolidated income statement (note iii)	(240)	(129)
End of year	13	317

32 EMPLOYEE RETIREMENT BENEFITS (CONTINUED)**a. Defined benefit retirement schemes (continued)**

iii. (Income)/Expense recognized in the consolidated income statement is as follows:

In HK\$ million	The Group	
	2005	2004
Interest cost	131	235
Expected return on scheme assets	(174)	(233)
Gain on curtailment/settlement	(197)	(131)
	(240)	(129)
The (income)/expense is recognized in the following line item in the consolidated income statement:		
General and administrative expenses – retirement costs for other staff (note 10(a))	(240)	(129)
Actual return on scheme assets	80	296

iv. The principal actuarial assumptions used (expressed as weighted averages) are as follows:

	The Group	
	2005	2004
Discount rate	4.25%	4.00%
Expected rate of return on scheme assets	5.75%	5.75%
Future salary increases	N/A	3.50%

b. Defined contribution retirement scheme

The Group also operates defined contribution schemes, including the Mandatory Provident Fund Scheme (“the MPF scheme”) under the Hong Kong Mandatory Provident Fund Schemes Ordinance, for employees employed under the jurisdiction of the Hong Kong Employment Ordinance. The schemes are administered by independent trustees.

Under the defined contribution scheme, the employer is required to make contributions to the scheme at rates specified under the rules of the scheme. Where employees leave the scheme prior to the full vesting of the employer’s contributions, the amount of forfeited contributions is used to reduce the contributions payable by the Group.

Under the MPF scheme, the employer and its employees are each required to make contributions to the scheme at 5% of the employees’ relevant income, subject to a cap of monthly relevant income of HK\$20,000. Contributions to the scheme vest immediately upon the completion of the service in the relevant service period.

33 EQUITY COMPENSATION BENEFITS

a. Share option schemes of the Company

The Company has a share option scheme (the “1994 Scheme”) which was adopted in September 1994 and amended in May 2002 under which the board of directors (the “Board”) of the Company may, at its discretion, invite employees of the Group, including directors of any company in the Group, and other eligible persons, to take up options to subscribe for shares of the Company. The vesting period and exercise period of the options are determined by the Board but in any case no options can be exercised later than ten years from the date of grant. Each option gives the holder the right to subscribe for one share. The 1994 Scheme was due to expire in September 2004.

At the Company’s annual general meeting held on May 19, 2004, the shareholders of the Company approved the termination of the 1994 Scheme and the adoption of a new share option scheme (the “2004 Scheme”). Since May 19, 2004, the Board may, at its discretion, grant share options to any eligible person to subscribe for shares in the Company subject to the terms and conditions stipulated in the 2004 Scheme. The overall limit on the number of shares which may be issued upon exercise of all outstanding options granted and yet to be exercised under the 2004 Scheme and any other share option schemes including 1994 Scheme must not exceed 30% of the shares in issue from time to time. In addition, the maximum number of shares which may be granted under the 2004 Scheme must not exceed 10% of the Company’s issued share capital as at May 19, 2004 (or some other date if renewal of this limit is approved by shareholders). The exercise price of the options under the 2004 Scheme shall be determined by the Board in its absolute discretion but in any event shall not be less than the highest of (i) the closing price of the shares as stated in the daily quotations sheet of the Stock Exchange on the date of grant, (ii) the average closing price of the shares as stated in the daily quotations sheet of the Stock Exchange for the five days last preceding the date of grant on which days it has been possible to trade shares on the Stock Exchange, and (iii) the nominal value of a share on the date of grant. The vesting period and exercise period of the options are determined by the Board, but no option can be exercised later than the day last preceding the tenth anniversary of the date of grant in respect of such option. In general, the subscription price is determined by reference to the closing prices of the shares as stated in the daily quotations sheet of the Stock Exchange. The basis for determination of the subscription price and the total number of shares that can be granted to eligible persons are precisely specified in the rules of the 2004 Scheme. The 2004 Scheme does not specify a minimum period for which an option must be held nor a performance target which must be achieved before an option can be exercised. The Group has no legal or constructive obligation to repurchase or settle the options in cash.

i. Movements in the number of share options outstanding and their related weighted average exercise prices

	2005		2004	
	Weighted average exercise price HK\$	Number of options	Weighted average exercise price HK\$	Number of options
Beginning of year	11.26	178,742,716	10.87	222,177,528
Issued (<i>note iii</i>)	4.55	75,924,000	N/A	–
Exercised (<i>note iv</i>)	4.35	(5,185,663)	4.35	(5,508,987)
Cancelled/Lapsed (<i>note v</i>)	7.73	(17,982,980)	9.97	(37,925,825)
End of year (<i>note ii</i>)	9.49	231,498,073	11.26	178,742,716
Exercisable at end of year	13.62	123,852,906	14.75	93,379,227

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2005

(Amount expressed in Hong Kong dollars unless otherwise stated)

33 EQUITY COMPENSATION BENEFITS (CONTINUED)

a. Share option schemes of the Company (continued)

ii. Terms of unexpired and unexercised share options at balance sheet date

Date of grant	Vesting period	Exercise period	Exercise price HK\$	Number of options	
				2005	2004
August 17, 1999 to September 15, 1999	August 17, 2000 to August 17, 2004	August 17, 2000 to August 17, 2009	11.7800	16,412,125	18,872,390
October 25, 1999 to November 23, 1999	October 25, 2000 to October 25, 2004	October 25, 2000 to October 25, 2009	22.7600	3,370,400	3,432,400
February 8, 2000 to March 8, 2000	February 8, 2001 to February 8, 2003	February 8, 2001 to February 8, 2010	75.2400	86,700	86,700
August 26, 2000 to September 24, 2000	May 26, 2001 to May 26, 2005	May 26, 2001 to August 26, 2010	60.1200	9,887,200	9,946,600
October 27, 2000 to November 25, 2000	March 15, 2001 to March 15, 2005	March 15, 2001 to October 27, 2010	24.3600	9,989,790	11,085,070
January 22, 2001 to February 20, 2001	January 22, 2001 to January 22, 2005	January 22, 2001 to January 22, 2011	16.8400	16,368,452	17,195,318
February 20, 2001	February 8, 2002 to February 8, 2004	February 8, 2002 to February 8, 2011	18.7600	86,700	86,700
April 17, 2001 to May 16, 2001	May 26, 2001 to May 26, 2005	May 26, 2001 to April 17, 2011	10.3000	1,147,040	1,324,360
July 16, 2001 to September 15, 2001	July 16, 2002 to July 16, 2004	July 16, 2002 to July 16, 2011	9.1600	365,760	648,600
October 15, 2001 to November 13, 2001	October 15, 2002 to October 15, 2004	October 15, 2002 to October 15, 2011	8.6400	120,000	292,000
May 10, 2002	April 11, 2003 to April 11, 2007	April 11, 2003 to April 11, 2012	7.9150	86,700	231,700
June 19, 2002	June 19, 2002 to June 19, 2004	June 19, 2002 to May 21, 2012	10.0900	–	179,000
August 1, 2002	August 1, 2003 to August 1, 2005	August 1, 2003 to July 31, 2012	8.0600	200,000	200,000
October 11, 2002	October 11, 2002	October 11, 2002 to October 10, 2007	8.6165	1,200,000	1,200,000
November 13, 2002	November 13, 2003 to November 13, 2005	November 13, 2003 to November 12, 2012	6.1500	6,820,000	6,860,000
July 25, 2003	July 25, 2004 to July 25, 2006	July 25, 2004 to July 23, 2013	4.3500	92,568,206	105,911,878
September 16, 2003	September 16, 2004 to September 16, 2006	September 16, 2004 to September 14, 2013	4.9000	190,000	1,190,000
February 8, 2005	February 8, 2006 to February 8, 2007	February 8, 2006 to February 7, 2009	4.4750	65,599,000	–
September 1, 2005	September 1, 2006 to September 1, 2008	September 1, 2006 to August 31, 2010	5.2500	7,000,000	–
				231,498,073	178,742,716

33 EQUITY COMPENSATION BENEFITS (CONTINUED)

a. Share option schemes of the Company (continued)

ii. Terms of unexpired and unexercised share options at balance sheet date (continued)

The range of exercise prices and the weighted average remaining contractual life of the share options outstanding are as follows:

Range of exercise prices	2005		2004	
	Weighted average remaining contractual life (years)	Number of options	Weighted average remaining contractual life (years)	Number of options
HK\$ 4.01 to 5.04	5.71	158,357,206	8.57	107,101,878
5.05 to 7.54	5.76	13,820,000	7.87	6,860,000
7.55 to 11.29	4.10	3,119,500	5.50	4,075,660
11.30 to 16.79	3.63	16,412,125	4.63	18,872,390
16.80 to 25.04	4.84	29,815,342	5.85	31,799,488
55.05 to 70.04	4.65	9,887,200	5.65	9,946,600
70.05 to 85.00	4.10	86,700	5.11	86,700
		231,498,073		178,742,716

iii. Details of share options granted during the year

Vesting period	Exercise period	2005			2004	
		Exercise price HK\$	Consideration received HK\$	Number of options	Consideration received HK\$	Number of options
February 8, 2006 to February 8, 2007	February 8, 2006 to February 7, 2009	4.4750	–	68,924,000	–	–
September 1, 2006 to September 1, 2008	September 1, 2006 to August 31, 2010	5.2500	–	7,000,000	–	–
			–	75,924,000	–	–

The fair value of share options granted during the year is determined using the trinomial option pricing model. The weighted average fair value of share options granted and the respective weighted average inputs and assumptions to the model are as follows:

	2005	2004
Fair value at measurement date	HK\$0.99	N/A
Share price	HK\$4.55	N/A
Exercise price	HK\$4.55	N/A
Expected volatility	31.53%	N/A
Expected option life (in years)	4.09 years	N/A
Expected dividends	3.33%	N/A
Risk-free interest rate	2.54%	N/A

33 EQUITY COMPENSATION BENEFITS (CONTINUED)
a. Share option schemes of the Company (continued)
iii. Details of share options granted during the year (continued)

The expected volatility is based on statistical analysis of daily share prices over one year immediately preceding the grant date. Expected dividends are based on historical dividends. Risk-free interest rate is based on the market yield of Exchange Fund Notes with a term similar to the expected option life.

Share options were granted under a service condition. This condition has not been taken into account in the grant date fair value measurement of the services received. There were no market conditions associated with the share option grants.

iv. Details of share options exercised during the year

Exercise date	2005				2004	
	Exercise price HK\$	Market value per share at exercise date HK\$	Proceeds received HK\$	Number of options	Proceeds received HK\$	Number of options
July 26, 2004 to December 31, 2004	4.3500	4.75 to 5.50	–	–	23,964,093	5,508,987
January 3, 2005 to December 9, 2005	4.3500	4.48 to 5.35	22,557,634	5,185,663	–	–
			22,557,634	5,185,663	23,964,093	5,508,987

The weighted average share price at the date of exercise for share options exercised during the year was HK\$5.07 (2004: HK\$5.17).

v. Details of share options cancelled or lapsed during the year

Exercise period	Exercise price HK\$	Number of options	
		2005	2004
August 17, 2000 to August 17, 2009	11.7800	2,460,265	652,798
August 17, 2000 to October 25, 2009	22.7600	62,000	1,076,800
May 26, 2001 to August 26, 2010	60.1200	59,400	362,000
March 15, 2001 to October 27, 2010	24.3600	1,095,280	1,881,012
January 22, 2001 to January 22, 2011	16.8400	826,866	6,083,120
May 26, 2001 to April 17, 2011	10.3000	177,320	2,218,600
July 16, 2002 to July 16, 2011	9.1600	282,840	41,160
October 15, 2002 to October 15, 2011	8.6400	172,000	–
April 11, 2003 to April 11, 2012	7.9150	145,000	–
September 27, 2001 to September 7, 2011	6.8150	–	3,600,000
April 29, 2003 to April 29, 2012	9.9500	–	5,600,000
June 19, 2002 to May 21, 2012	10.0900	179,000	100,000
November 13, 2003 to November 12, 2012	6.1500	40,000	180,000
July 25, 2004 to July 23, 2013	4.3500	8,158,009	16,130,335
September 16, 2004 to September 14, 2013	4.9000	1,000,000	–
February 8, 2006 to February 7, 2009	4.4750	3,325,000	–
		17,982,980	37,925,825

33 EQUITY COMPENSATION BENEFITS (CONTINUED)

b. Share award schemes of the Company

In 2002, the Company established two employee share incentive award schemes under which awards of shares may be granted to employees of participating subsidiaries. Directors of the Company are not eligible to participate in either scheme. On June 10, 2002, the Company approved the establishment of the Purchase Scheme under which selected employees are awarded shares purchased in the market. On November 12, 2002, the Company approved the establishment of the Subscription Scheme under which selected employees are awarded newly issued shares. The purpose of both the Purchase Scheme and the Subscription Scheme is to recognize the contributions of certain employees of the Group, to retain them for the continued operation and development of the Group, and to attract suitable personnel for the further development of the Group. Under both schemes, following the making of an award to an employee, the relevant shares are held on trust for that employee and then vest over a period of time provided that the employee remains an employee of the Group at the relevant time and satisfies any other conditions specified at the time the award is made. The maximum aggregate number of shares that can be awarded under the two schemes is limited to 1% of the issued share capital of the Company (excluding shares that have already been transferred to employees on vesting).

A summary of movements in shares held under the share award schemes during the year is as follows:

	Number of shares	
	2005	2004
Beginning of year	3,692,400	5,771,000
Awards of vested shares to employees	(3,692,400)	(2,078,600)
End of year	–	3,692,400

In HK\$ million	2005	2004
Fair value of shares held as at December 31	N/A	18
Fair value of shares awarded to employees during the year	18	10
Amounts recognized in the consolidated balance sheet as prepaid expenses	–	7
Amounts recognized in the consolidated income statement as staff costs	7	10

The fair value of shares under the Subscription Scheme at the measurement date is measured by the quoted market price of the shares at grant date.

c. Shares granted by principal shareholder of the Company

Pursuant to an agreement made between the Chairman and a director in 2002, 387,600 shares of the Company were transferred by the Chairman personally to that director in April 2004, being the second of three annual installments of a total of 1,162,800 shares the Chairman agreed to transfer to that director. The transfer of the third (last) annual installment of 387,600 shares in April 2005 did not proceed as the director concerned resigned from the Company in September 2004. In addition, pursuant to another agreement made between the Chairman and another director in 2003, 2,161,000 shares (2004: 2,161,000 shares) of the Company were transferred by the Chairman personally to that director in July 2005, being the second of three annual installments of a total of 6,483,000 shares the Chairman agreed to transfer to that director. No new shares were issued by the Company.

The fair value of shares granted by principal shareholder is measured by the quoted market price of the shares at grant date.

d. Employees' rights to invest in shares of JALECO

In August 2000, the Group established an incentive scheme under which certain employees of the Group were granted options to acquire equity interests in JALECO. The exercise price of the options to the employees was set at a price not less than the fair value of the shares at the time of issue. Shares of JALECO have been trading below the cost of the options since the first exercise date. As at December 31, 2003 and up to November 8, 2004, a total number of 4,021,000 shares of JALECO were held by the incentive scheme which was operated under a limited partnership arrangement and no options were exercised by the employees. On November 8, 2004, the limited partnership was dissolved and the 4,021,000 shares of JALECO were transferred to Pacific Century CyberWorks Japan Limited, a wholly-owned subsidiary of the Company. These shares formed a part of the Group's 79.72% interest in JALECO and were disposed of by the Group in August 2005 as set out in note 1(e).

33 EQUITY COMPENSATION BENEFITS (CONTINUED)

e. Share option schemes of PCPD

PCPD approved and adopted a share option scheme on March 17, 2003 (the “2003 PCPD Scheme”), which was valid for 10 years after the date of adoption. In order to align the terms of the share option scheme of PCPD with those of the Company and in view of the limited number of shares capable of being issued under the 2003 PCPD Scheme relative to the current capital base of PCPD, the shareholders of PCPD approved the termination of the 2003 PCPD Scheme and the adoption of a new share option scheme (the “2005 PCPD Scheme”) at PCPD’s annual general meeting held on May 13, 2005. The 2005 PCPD Scheme became effective on May 23, 2005 following its approval by the shareholders of the Company. No further share options will be granted under the 2003 PCPD Scheme following its termination, but the provisions of such scheme will remain in full force and effect with respect to the options granted prior to its termination.

Under the 2005 PCPD Scheme, the board of directors of PCPD may, at its discretion, grant share options to any eligible person to subscribe for shares in PCPD subject to the terms and conditions stipulated in the 2005 PCPD Scheme. The exercise price of the options under the 2005 PCPD Scheme is determined by the board of directors of PCPD in its absolute discretion but in any event shall not be less than the highest of (i) the closing price of the shares of PCPD as stated in the daily quotations sheet of the Stock Exchange on the date of grant; (ii) the average closing price of the shares of PCPD as stated in the daily quotations sheet of the Stock Exchange for the five days last preceding the date of grant on which days it has been possible to trade shares on the Stock Exchange; and (iii) the nominal value of the share of PCPD on the date of grant. The overall limit on the number of shares which may be issued upon exercise of all outstanding options granted and yet to be exercised under the 2005 PCPD Scheme and other share option schemes of PCPD must not exceed 30% of the shares in issue from time to time. In addition, the maximum number of shares of PCPD in respect of which options may be granted under the 2005 PCPD Scheme shall not (when aggregated with any shares subject to any grants made after May 23, 2005 pursuant to any other share option schemes of PCPD) exceed 10% of the issued share capital of PCPD on May 23, 2005 (or some other date if renewal of this limit is approved by shareholders).

No share options have been granted under the 2005 PCPD Scheme during the year ended December 31, 2005 and no share options were outstanding at December 31, 2005 under such scheme.

Details of share options granted by PCPD pursuant to the 2003 PCPD Scheme and the share options outstanding, are as follows:

i. Movements in the number of share options outstanding and their related weighted average exercise prices

	2005		2004	
	Weighted average exercise price HK\$	Number of options	Weighted average exercise price HK\$	Number of options
Beginning of year	2.375	10,000,000	N/A	–
Issued (note iii)	N/A	–	2.375	10,000,000
End of year (note ii)	2.375	10,000,000	2.375	10,000,000
Exercisable at end of year	2.375	10,000,000	2.375	10,000,000

ii. Terms of unexpired and unexercised share options at balance sheet date

Date of grant	Vesting period	Exercise period	Exercise price HK\$	Number of options	
				2005	2004
December 20, 2004	December 20, 2004	December 20, 2004 to December 19, 2014	2.375	10,000,000	10,000,000
				10,000,000	10,000,000

33 EQUITY COMPENSATION BENEFITS (CONTINUED)

e. Share option schemes of PCPD (continued)

ii. Terms of unexpired and unexercised share options at balance sheet date (continued)

The options outstanding at December 31, 2005 had an exercise price of HK\$2.375 (2004: HK\$2.375) and a weighted average remaining contractual life of 9 years (2004: 10 years).

iii. Details of share options granted during the year

Vesting period	Exercise period	2005			2004	
		Exercise price HK\$	Consideration received HK\$	Number of options	Consideration received HK\$	Number of options
December 20, 2004	December 20, 2004 to December 19, 2014	2.375	–	–	2	10,000,000
			–	–	2	10,000,000

The fair value of share options granted during 2004 was determined using the trinomial option pricing model. The weighted average fair value of share options granted and the respective weighted average inputs and assumptions to the model were as follows:

	2004
Fair value at measurement date	HK\$1.29
Share price	HK\$2.375
Exercise price	HK\$2.375
Expected volatility	50%
Expected option life (in years)	10 years
Expected dividends	N/A
Risk-free interest rate	3.95%

As the share options were vested before January 1, 2005, there was no expenses recognized in the consolidated income statement.

f. Share option schemes of SUNDAY

On March 1, 2000, the shareholders of SUNDAY approved and adopted a share option scheme (the “2000 SUNDAY Scheme”). Subject to any earlier termination by SUNDAY in a general meeting of shareholders, the 2000 SUNDAY Scheme will remain in force for 10 years from its adoption date.

On May 22, 2002, the shareholders of SUNDAY approved the adoption of a new share option scheme (the “2002 SUNDAY Scheme”) and the termination of the 2000 SUNDAY Scheme. Upon the termination of the 2000 SUNDAY Scheme, no further options will be granted thereunder but the provisions of the 2000 SUNDAY Scheme will remain in full force and effect in respect of the existing options granted.

Under the 2002 SUNDAY Scheme, the board of directors of SUNDAY may, in its discretion, grant options to any director, employee, consultant, customer, supplier, agent, partner, shareholder or adviser of or contractor to SUNDAY and its subsidiaries (the “SUNDAY Group”) or a company in which the SUNDAY Group holds an interest or a subsidiary of such company. Each grant of options to a director, chief executive or substantial shareholder or any of their respective associates must be approved in accordance with the requirements of the Listing Rules.

The exercise price for any particular option under the 2002 SUNDAY Scheme will be determined by the board of directors of SUNDAY but will be not less than the highest of: (i) the closing price of shares of SUNDAY on the date of grant of the option; (ii) an amount equivalent to the average closing price of a share of SUNDAY for the five business days immediately preceding the date of grant of the option; and (iii) the nominal share value.

The maximum number of shares which may be issued upon exercise of all outstanding options granted and yet to be exercised under both the 2000 SUNDAY Scheme and the 2002 SUNDAY Scheme must not, in aggregate, exceed 30% of the shares of SUNDAY in issue.

33 EQUITY COMPENSATION BENEFITS (CONTINUED)

f. Share option schemes of SUNDAY (continued)

The total number of shares available for issue under options which may be granted under the 2002 SUNDAY Scheme (excluding those options that have been granted by SUNDAY prior to the date of approval of the 2002 SUNDAY Scheme) must not, in aggregate, exceed 10% of the issued share capital of SUNDAY as at the date of approval of the 2002 SUNDAY Scheme ("Scheme Mandate Limit"). The Scheme Mandate Limit may be refreshed by shareholders of SUNDAY in general meeting provided that the Scheme Mandate Limit so refreshed must not exceed 10% of the issued share capital of SUNDAY at the date of approval of refreshment by the shareholders. The board may also seek separate shareholders' approval in general meeting to grant options beyond the Scheme Mandate Limit (whether or not refreshed) provided that the options in excess of the Scheme Mandate Limit are granted only to the eligible participants specified by SUNDAY before such approval is sought.

No option may be granted under the 2002 SUNDAY Scheme to any eligible participant which, if exercised in full, would result in the total number of shares issued and to be issued upon exercise of the options already granted or to be granted to such eligible participant (including exercised, cancelled and outstanding options) in the 12-month period up to and including the date of such new grant exceeding 1% of the issued share capital of SUNDAY. As at the date of such new grant, any grant of further options above this limit will be subject to certain requirements provided under the Listing Rules, including the approval of shareholders at a general meeting.

No share options have been granted or exercised under the 2002 SUNDAY Scheme during the year ended December 31, 2005 (2004: Nil). All outstanding share options granted by SUNDAY under the 2000 SUNDAY Scheme had either been cancelled or had lapsed under the terms of the 2000 SUNDAY Scheme by August 9, 2005, being one month after the date on which the unconditional mandatory general cash offer made by PCCW Mobile became unconditional.

Details of share options granted by SUNDAY pursuant to the 2000 SUNDAY Scheme and the share options outstanding, are as follows:

i. Movements in the number of share options outstanding and their related weighted average exercise prices

	2005		2004	
	Weighted average exercise price HK\$	Number of options	Weighted average exercise price HK\$	Number of options
Beginning of year	1.97	28,630,089	1.96	30,072,503
Cancelled (note iii)	1.98	(26,998,431)	N/A	–
Lapsed (note iv)	1.84	(1,631,658)	1.76	(1,442,414)
End of year (note ii)	N/A	–	1.97	28,630,089
Exercisable at end of year	N/A	–	1.97	28,630,089

ii. Terms of unexpired and unexercised share options at balance sheet date

Date of grant	Vesting period	Exercise period	Exercise price HK\$	Number of options	
				2005	2004
March 23, 2000	March 23, 2001 to March 23, 2003	March 23, 2001 to March 22, 2010	3.05	–	13,194,076
May 31, 2000	May 31, 2001 to May 31, 2003	May 31, 2001 to May 30, 2010	1.01	–	13,737,971
May 31, 2000	May 31, 2001 to May 31, 2003	May 31, 2001 to May 30, 2010	3.05	–	255,844
January 19, 2001	January 19, 2002 to January 19, 2004	January 19, 2002 to January 18, 2011	1.01	–	1,442,198
				–	28,630,089

33 EQUITY COMPENSATION BENEFITS (CONTINUED)

f. Share option schemes of SUNDAY (continued)

ii. Terms of unexpired and unexercised share options at balance sheet date (continued)

The exercise prices and the weighted average remaining contractual life of the share options outstanding are as follows:

Exercise prices	2005		2004	
	Weighted average remaining contractual life (years)	Number of options	Weighted average remaining contractual life (years)	Number of options
HK\$ 1.01	N/A	–	5.48	15,180,169
3.05	N/A	–	5.23	13,449,920
		–		28,630,089

iii. Details of share options cancelled during the year

Exercise period	Exercise price HK\$	Number of options	
		2005	2004
March 23, 2001 to March 22, 2010	3.05	12,632,274	–
May 31, 2001 to May 30, 2010	1.01	12,976,337	–
May 31, 2001 to May 30, 2010	3.05	155,929	–
January 19, 2002 to January 18, 2011	1.01	1,233,891	–
		26,998,431	–

iv. Details of share options lapsed during the year

Exercise period	Exercise price HK\$	Number of options	
		2005	2004
March 23, 2001 to March 22, 2010	3.05	561,802	488,281
May 31, 2001 to May 30, 2010	1.01	761,634	570,281
May 31, 2001 to May 30, 2010	3.05	99,915	41,000
January 19, 2002 to January 18, 2011	1.01	208,307	342,852
		1,631,658	1,442,414

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2005

(Amount expressed in Hong Kong dollars unless otherwise stated)

34 RESERVES/(DEFICIT)

In HK\$ million	2005								Total
	Share premium	Special capital reserve	Employee share-based compensation reserve	Property revaluation reserve	Convertible note and bonds reserve	Currency translation reserve	Available-for-sale financial assets reserve	Deficit	
THE GROUP									
At January 1, 2005, as previously stated	18	19,980	-	25	-	(44)	-	(28,039)	(8,060)
Prior period adjustments in respect of:									
Employee share-based compensation	11	-	137	-	-	-	-	(148)	-
Restatement of deemed gain on disposal and placement of shares of subsidiaries	-	-	-	-	-	-	-	(52)	(52)
Deferred tax arising from the revaluation of investment properties	-	-	-	97	-	-	-	-	97
Deferral of up-front installation fees	-	-	-	-	-	-	-	(1,005)	(1,005)
Interests in leasehold land held for own use under operating leases	-	-	-	-	-	-	-	32	32
Restatement of investment properties to property, plant and equipment	-	-	-	8	-	-	-	(3)	5
Financial instruments	-	-	-	-	202	-	-	(122)	80
At January 1, 2005, as restated, before opening balance adjustments	29	19,980	137	130	202	(44)	-	(29,337)	(8,903)
Opening balance adjustments in respect of:									
Financial instruments	-	-	-	-	-	-	-	(438)	(438)
Transfer of property revaluation reserve to deficit	-	-	-	(130)	-	-	-	130	-
At January 1, 2005, as restated, after opening balance adjustments	29	19,980	137	-	202	(44)	-	(29,645)	(9,341)
Exercise of employee share options	21	-	-	-	-	-	-	-	21
Premium arising from exercise of employee share options	14	-	(14)	-	-	-	-	-	-
Employee share-based compensation	-	-	100	-	-	-	-	-	100
Issue of ordinary shares, net of issuing expenses	7,558	-	-	-	-	-	-	-	7,558
Transfer to special capital reserve (note d)	-	3,010	-	-	-	-	-	(3,010)	-
Elimination of losses for the period from January 1, 2005 to June 29, 2005 against special capital reserve (note e)	-	(496)	-	-	-	-	-	496	-
Redemption of convertible bonds	-	-	-	-	(19)	-	-	19	-
Translation exchange differences	-	-	-	-	-	(11)	-	-	(11)
Profit for the year	-	-	-	-	-	-	-	1,595	1,595
Dividend approved in respect of the previous year	-	-	-	-	-	-	-	(645)	(645)
Dividend declared and paid in respect of the current year (note f)	-	(239)	-	-	-	-	-	(198)	(437)
Fair value gains from available-for-sale financial assets	-	-	-	-	-	-	89	-	89
At December 31, 2005	7,622	22,255	223	-	183	(55)	89	(31,388)	(1,071)
Attributable to:									
The Company and subsidiaries	7,622	22,255	223	-	183	(55)	89	(31,811)	(1,494)
Jointly controlled companies	-	-	-	-	-	-	-	54	54
Associates	-	-	-	-	-	-	-	369	369
At December 31, 2005	7,622	22,255	223	-	183	(55)	89	(31,388)	(1,071)

34 RESERVES/(DEFICIT) (CONTINUED)

In HK\$ million	2005				
	Share premium	Special capital reserve	Employee share-based compen- sation reserve	Retained profit	Total
THE COMPANY					
At January 1, 2005, as previously stated	18	19,980	–	675	20,673
Prior period adjustment in respect of:					
Employee share-based compensation	11	–	137	–	148
At January 1, 2005, as restated, before opening balance adjustment	29	19,980	137	675	20,821
Opening balance adjustment in respect of:					
Financial instruments	–	–	–	47	47
At January 1, 2005, as restated, after opening balance adjustment	29	19,980	137	722	20,868
Exercise of employee share options	35	–	(14)	–	21
Issue of ordinary shares, net of issuing expenses	7,558	–	–	–	7,558
Transfer to special capital reserve (<i>note d</i>)	–	3,010	–	(3,010)	–
Elimination of losses for the period from January 1, 2005 to June 29, 2005 against special capital reserve (<i>note e</i>)	–	(496)	–	496	–
Employee share-based compensation	–	–	100	–	100
Dividend approved in respect of the previous year	–	–	–	(645)	(645)
Profit for the year	–	–	–	2,809	2,809
Dividend declared and paid in respect of the current year (<i>note f</i>)	–	(239)	–	(198)	(437)
At December 31, 2005	7,622	22,255	223	174	30,274

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

December 31, 2005

(Amount expressed in Hong Kong dollars unless otherwise stated)

34 RESERVES/(DEFICIT) (CONTINUED)

In HK\$ million	2004							
	Share premium	Special capital reserve	Employee share-based compensation reserve	Property revaluation reserve	Convertible note and bonds reserve	Currency translation reserve	Deficit	Total
THE GROUP								
At January 1, 2004, as previously stated	173,460	–	–	305	–	(97)	(182,850)	(9,182)
Prior period adjustments in respect of:								
Employee share-based compensation	11	–	44	–	–	–	(55)	–
Deferred tax arising from the revaluation of investment properties	–	–	–	106	–	–	–	106
Deferral of up-front installation fees	–	–	–	–	–	–	(1,093)	(1,093)
Interests in leasehold land held for own use under operating leases	–	–	–	–	–	–	25	25
Restatement of investment properties to property, plant and equipment	–	–	–	24	–	–	(3)	21
Financial instruments	–	–	–	–	202	–	(90)	112
At January 1, 2004, as restated	173,471	–	44	435	202	(97)	(184,066)	(10,011)
Prior period adjustments in respect of:								
Employee share-based compensation	–	–	93	–	–	–	–	93
Deferred tax arising from the revaluation of investment properties	–	–	–	(9)	–	–	–	(9)
Restatement of investment properties to property, plant and equipment	–	–	–	(16)	–	–	–	(16)
Exercise of employee share options	22	–	–	–	–	–	–	22
Elimination of accumulated deficit as at June 30, 2004 against share premium account (note a)	(152,932)	–	–	–	–	–	152,932	–
Transfer to special capital reserve (note a)	(20,532)	20,532	–	–	–	–	–	–
Reversal of excess provision for impairment loss as at June 30, 2004 to special capital reserve (note c)	–	14	–	–	–	–	(14)	–
Elimination of losses for the period from July 1, 2004 to December 30, 2004 against special capital reserve (note b)	–	(566)	–	–	–	–	566	–
Deficit on revaluation of investment properties, net of deferred taxation	–	–	–	(26)	–	–	–	(26)
Valuation adjustment	–	–	–	(254)	–	–	–	(254)
Translation exchange differences	–	–	–	–	–	53	–	53
Realization of negative goodwill on disposal of interest in subsidiaries	–	–	–	–	–	–	(16)	(16)
Profit for the year, as previously stated	–	–	–	–	–	–	1,638	1,638
Prior period adjustments in respect of:								
Employee share-based compensation	–	–	–	–	–	–	(93)	(93)
Restatement of deemed gain on disposal and placement of shares of subsidiaries	–	–	–	–	–	–	(52)	(52)
Deferral of up-front installation fees	–	–	–	–	–	–	88	88
Interests in leasehold land held for own use under operating leases	–	–	–	–	–	–	7	7
Financial instruments	–	–	–	–	–	–	(32)	(32)
Profit for the year, as restated	–	–	–	–	–	–	1,556	1,556
Dividend declared and paid in respect of the current year	–	–	–	–	–	–	(295)	(295)
At December 31, 2004, as restated	29	19,980	137	130	202	(44)	(29,337)	(8,903)
Attributable to:								
The Company and subsidiaries	29	19,980	137	130	202	(44)	(29,639)	(9,205)
Jointly controlled companies	–	–	–	–	–	–	53	53
Associates	–	–	–	–	–	–	249	249
At December 31, 2004, as restated	29	19,980	137	130	202	(44)	(29,337)	(8,903)

34 RESERVES/(DEFICIT) (CONTINUED)

In HK\$ million	2004				
	Share premium	Special capital reserve	Employee share-based compensation reserve	(Deficit)/ Retained profit	Total
THE COMPANY					
At January 1, 2004, as previously stated	173,460	–	–	(151,966)	21,494
Prior period adjustment in respect of:					
Employee share-based compensation	11	–	44	–	55
At January 1, 2004, as restated	173,471	–	44	(151,966)	21,549
Exercise of employee share options	22	–	–	–	22
Elimination of accumulated deficit as at June 30, 2004 against share premium account (<i>note a</i>)	(152,932)	–	–	152,932	–
Transfer to special capital reserve (<i>note a</i>)	(20,532)	20,532	–	–	–
Reversal of excess provision for impairment loss as at June 30, 2004 to special capital reserve (<i>note c</i>)	–	14	–	(14)	–
Elimination of losses for the period from July 1, 2004 to December 30, 2004 against special capital reserve (<i>note b</i>)	–	(566)	–	566	–
Prior period adjustments in respect of:					
Employee share-based compensation	–	–	93	–	93
Loss for the year	–	–	–	(548)	(548)
Dividend declared and paid in respect of the current year	–	–	–	(295)	(295)
At December 31, 2004, as restated	29	19,980	137	675	20,821

a. Pursuant to a special resolution passed at an extraordinary general meeting of the Company held on May 19, 2004 and the subsequent order of the High Court of Hong Kong (the “High Court”) made on August 3, 2004, the entire amount of HK\$173,464,615,915 then standing to the credit of the share premium account of the Company was cancelled in accordance with the provisions of the Hong Kong Companies Ordinance (the “Capital Reduction”).

Out of the credit arising from the Capital Reduction, HK\$152,932,345,321 was applied to eliminate the accumulated losses of the Company as at June 30, 2004. An undertaking was given by the Company in connection with the Capital Reduction. Pursuant to the undertaking, the balance of HK\$20,532,270,594 of the credit arising from the Capital Reduction and any sum received by the Company in respect of its investments against which provision for impairment loss or diminution in value had been made up to June 30, 2004 (or, in the case of a revaluation or disposal of any of such investment, sums revalued or realized in excess of the written down value of the relevant investment as at June 30, 2004) up to an aggregate amount of HK\$152,932,345,321 shall be credited to a special capital reserve in the accounting records of the Company. While any debt or liability of, or claim against, the Company at the date of the Capital Reduction remains outstanding and the person entitled to the benefit thereof has not agreed otherwise, the special capital reserve shall not be treated as realized profit and (for so long as the Company remains a listed company) shall be treated as an undistributable reserve for the purposes of section 79C of the Hong Kong Companies Ordinance. The undertaking, however, is subject to the following provisos:-

- i. the amount standing to the credit of the special capital reserve may be applied for the same purposes as a share premium account may be applied or may be reduced or extinguished by the aggregate of any increase in the Company’s issued share capital or share premium account resulting from an issue of shares for cash or other new consideration or upon a capitalization of distributable reserves after the date of the Capital Reduction;

34 RESERVES/(DEFICIT) (CONTINUED)

- ii. an amount of up to HK\$20,532,270,594 of the special capital reserve may be applied by the Company for the purpose of eliminating any loss sustained after June 30, 2004, provided that if subsequent to the elimination any of the Company's investments against which provision for impairment loss or diminution in value has been made for the period respecting the loss shall be revalued in excess of their written down value at the end of that period or realized for a sum in excess of such written down value, or any sum is received by the Company in respect of such investment, then a sum equal to the amount of the revaluation or the sum realized in excess of the written down value or the sum received by the Company in respect of such investment as aforesaid up to an aggregate amount of HK\$20,532,270,594 or the total amount of the non-permanent losses sought to be eliminated (whichever is less) shall be re-credited to the special capital reserve; and
- iii. upon the coming into force of one or more guarantees to be issued by Standard Chartered Bank (HK) Limited ("SCB") in the form scheduled to the undertaking, the Company will be released from the undertaking to the extent of an amount equal to the sum so guaranteed less the fees and expenses incurred in issuing the relevant guarantee(s), with the result that such amount of the special capital reserve would thereby become distributable.

Subsequent to the balance sheet date, the above undertaking was released as permitted by an order made by the High Court on January 10, 2006, details of which are set out in note 45(a).

- b. Pursuant to resolutions of the Board of the Company passed on September 29, 2004 and December 30, 2004, losses for the periods from July 1, 2004 to September 29, 2004 and from September 30, 2004 to December 30, 2004 in the amount of HK\$284,227,183 and HK\$281,932,052 respectively was eliminated against the special capital reserve by the Company.
- c. In 2004, a subsidiary of the Company, against which provision for impairment loss for diminution in value had been made in prior years, was liquidated. The amount realized from the liquidation exceeded the written down value by HK\$13,681,249. In accordance with the undertaking given by the Company to the High Court, as summarized in note (a) above, the Company is required to credit such amount to the special capital reserve.
- d. During the year, dividend income of HK\$3,011,014,502 from an indirect wholly-owned subsidiary of the Company was received. In accordance with the undertaking given by the Company to the High Court, as summarized in note (a) above, the Company is required to transfer such amount to the special capital reserve.
- e. Pursuant to resolutions of the Board of the Company passed on June 29, 2005, losses for the period from January 1, 2005 to June 29, 2005 in the amount of HK\$496,480,940 was eliminated against the special capital reserve by the Company.
- f. An interim dividend for the year ended December 31, 2005 of HK\$436,942,407 was paid to the shareholders on October 4, 2005. Pursuant to that part of the undertaking set out in note (a)(iii) above, as a result of the issue of guarantee by SCB on September 30, 2005 and after deduction of the fees and expenses amounting to HK\$19,372,284, a sum of HK\$239,142,407 was transferred from the special capital reserve for the payment of the dividend and the balance of HK\$197,800,000 was paid out of the retained profit of the Company.

35 DEFERRED TAXATION

a. Movement in deferred tax liabilities/(assets) during the year is as follows:

In HK\$ million	2005							
	Accelerated tax depreciation	Valuation adjustment resulting from acquisition of subsidiaries	Leasing partnership	Revaluation of properties	Deferred installation revenue	Derivative financial instruments	Others	Total
THE GROUP								
Beginning of year, as previously stated	1,554	460	317	325	-	-	(81)	2,575
Prior period adjustment arising from adoption of new and revised HKFRSs	-	-	-	(88)	(213)	-	-	(301)
Opening balances, as restated	1,554	460	317	237	(213)	-	(81)	2,274
Opening balance adjustment arising from adoption of new and revised HKFRSs	-	-	-	-	-	(53)	-	(53)
	1,554	460	317	237	(213)	(53)	(81)	2,221
Charged/(Credited) to consolidated income statement (<i>note 13</i>)	118	(66)	(93)	(171)	47	53	28	(84)
Reclassification of deferred tax assets previously provided	(41)	-	-	75	-	-	-	34
Exchange differences	3	-	-	3	-	-	-	6
End of year	1,634	394	224	144	(166)	-	(53)	2,177

In HK\$ million	2004							
	Accelerated tax depreciation	Valuation adjustment resulting from acquisition of subsidiaries	Leasing partnership	Revaluation of properties	Deferred installation revenue	Others	Total	
THE GROUP								
Beginning of year, as previously stated	1,725	490	469	471	-	(129)	3,026	
Prior period adjustment arising from adoption of new and revised HKFRSs	-	-	-	(106)	(232)	-	(338)	
Opening balances, as restated	1,725	490	469	365	(232)	(129)	2,688	
(Credited)/Charged to consolidated income statement (<i>note 13</i>)	(171)	(30)	(152)	42	19	52	(240)	
Credited to property revaluation reserve	-	-	-	(170)	-	-	(170)	
Exchange differences	-	-	-	-	-	(4)	(4)	
End of year	1,554	460	317	237	(213)	(81)	2,274	

In HK\$ million	The Group	
	2005	2004 (Restated) (<i>Note 46</i>)
Net deferred tax assets recognized in the consolidated balance sheet	(4)	(38)
Net deferred tax liabilities recognized in the consolidated balance sheet	2,181	2,312
	2,177	2,274

35 DEFERRED TAXATION (CONTINUED)

b. Deferred income tax assets are recognized for tax loss carry forwards to the extent that realization of the related tax benefit through utilization against future taxable profits is probable. The Group has unutilized estimated tax losses for which no deferred tax assets have been recognized of HK\$19,376 million (2004: HK\$14,846 million) to carry forward for deduction against future taxable income. Estimated tax losses of HK\$179 million (2004: HK\$1,916 million) and HK\$214 million (2004: HK\$125 million) will expire within 1-5 years and after 5 year from December 31, 2005 respectively. The remaining portion of the tax losses, mainly relating to Hong Kong companies, can be carried forward indefinitely.

36 3G LICENCE FEE LIABILITY

On October 22, 2001, SUNDAY 3G (Hong Kong) Limited, a wholly-owned subsidiary of SUNDAY, was granted a 3G licence in accordance with the provisions of the Telecommunications Ordinance, Chapter 106 of the Laws of Hong Kong. The 3G licence will be valid for 15 years from the date of grant to October 21, 2016, and requires SUNDAY to establish, maintain and use equipment for the 3G telecommunications network and to provide 3G services in Hong Kong. Pursuant to the terms of the 3G licence, prescribed minimum annual fees is payable to the Office of the Telecommunications Authority in arrears for each of the remaining 10 years from 2007 to 2016. The aggregate of such fees are HK\$1,056,838,000.

As set out in note 44, the Group, through PCCW Mobile, acquired approximately 59.87% of the interest in SUNDAY on June 22, 2005. Accordingly, the 3G licence and the 3G licence fee liability were acquired and were recorded at fair values at acquisition date of approximately HK\$101 million and HK\$529 million respectively.

As at December 31, 2005, the Group's 3G licence fee liability, representing the discounted value of the remaining minimum annual fees payable from 2007 to 2016, is repayable as follows:

In HK\$ million	The Group					
	2005			2004		
	Present value of the minimum annual fees	Interest expense relating to future periods	Total minimum annual fees	Present value of the minimum annual fees	Interest expense relating to future periods	Total minimum annual fees
Repayable within a period						
– over one year, but not exceeding two years	49	11	60	–	–	–
– over two years, but not exceeding five years	161	80	241	–	–	–
– over five years	321	435	756	–	–	–
	531	526	1,057	–	–	–

37 AMOUNTS DUE FROM/(TO) SUBSIDIARIES

During the year, the Company entered into transactions with certain subsidiaries in the ordinary course of business. Details of the amounts due from and due to subsidiaries are as follows:

a. Amounts due from subsidiaries

In HK\$ million	The Company	
	2005	2004 (Restated) (Note 46)
Current assets (note i)		
Amounts due from subsidiaries	95,320	85,657
Less: Provision for impairment	(19,281)	(19,287)
	76,039	66,370
Non-current assets		
Convertible notes due from a subsidiary (note ii)	–	3,621

37 AMOUNTS DUE FROM/(TO) SUBSIDIARIES (CONTINUED)

a. Amounts due from subsidiaries (continued)

- i. As at December 31, 2005, amounts due from subsidiaries are unsecured, non-interest bearing and repayable on demand. As at December 31, 2004, certain subsidiaries had borrowings from the Company of HK\$54 million, which were bearing interest at commercial rates throughout the terms of the borrowings.

As at December 31, 2005, the Group has financed the operations of certain of its PRC joint ventures accounted for as subsidiaries in the form of shareholder's loans amounting to approximately US\$199 million (2004: US\$198 million) which have not been registered with the State Administration of Foreign Exchange. As a result, remittances in foreign currency of these amounts outside the PRC may be restricted.

- ii. On February 24, 2005, the Company elected to convert Tranche A Convertible Note due 2011 with the principal amount of HK\$1,170 million, which was issued by PCPD to the Company on May 10, 2004, details of which are set out in note 1(b). In addition, on June 29, 2005, the Company transferred Tranche B Convertible Note due 2014 with the principal amount of HK\$2,420 million, which was also issued by PCPD to the Company on May 10, 2004, at a fair value of HK\$1,919 million to a wholly-owned subsidiary of the Company.

As at December 31, 2004, included in convertible notes due from a subsidiary were HK\$1,170 million Tranche A Convertible Note due 2011 which was non-interest bearing and HK\$2,451 million Tranche B Convertible Note due 2014 which was bearing interest at 1% per annum.

b. Amounts due to subsidiaries

In HK\$ million	The Company	
	2005	2004 (Restated) (Note 46)
Current liabilities		
Amounts due to subsidiaries	(67,508)	–
Non-current liabilities		
Amounts due to subsidiaries	–	(67,508)

As at December 31, 2005, amounts due from subsidiaries are unsecured, non-interest bearing and repayable on demand. As at December 31, 2004, certain subsidiaries had borrowings to the Company of HK\$4,966 million, which were bearing interest at commercial rates throughout the terms of the borrowings.

38 NET LEASE PAYMENTS RECEIVABLE

A company within the Group is a limited partner in a number of limited partnerships, which own and lease assets to third parties.

In HK\$ million	The Group	
	2005	2004
The net investment in relation to these finance leases comprises:		
Net lease payments receivable	264	377
Less: Current portion of net lease payments receivable (included in "Prepayments, deposits and other current assets" in the consolidated balance sheet)	(61)	(90)
	203	287

Non-recourse finance of HK\$876 million (2004: HK\$1,573 million) has been offset against net rentals receivable in arriving at the above net investment in finance leases.

39 NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT**a. Reconciliation of profit before taxation to net cash inflow from operating activities**

In HK\$ million	The Group	
	2005	2004 (Restated) (Note 46)
Profit before taxation	2,970	2,575
Adjustment for:		
Impairment losses on interests in jointly controlled companies and associates	4	16
Employee share-based compensation	100	93
Provision for inventory obsolescence	17	9
Interest income	(533)	(57)
Interest expense	2,048	1,884
Finance charges	186	124
Depreciation of property, plant and equipment	2,543	2,357
Net unrealized holding losses on other investments	–	25
Net unrealized gains on financial assets at fair value through profit or loss	(73)	–
Realized losses/(gains) on disposal of interests in jointly controlled companies and associates	4	(3)
Realized gains on disposal of financial assets at fair value through profit or loss	(8)	–
Realized gains on disposal of investment securities	–	(19)
Realized gains on disposal of available-for-sale financial assets	(90)	–
Gain on deemed disposal of interest in subsidiaries	–	(59)
Gain on disposal of interests in subsidiaries, net of expenses	(170)	(524)
Net realized and unrealized fair value gains on derivative financial instruments	(319)	–
Fair value gains on investment properties	(2)	–
Provision for impairment of investments	18	187
Provision for impairment of property, plant and equipment	50	29
Provision for impairment of other non-current assets	2	11
Provision for rental guarantee	41	–
Gain on disposal of property, plant and equipment, investment properties and interests in leasehold land held for own use under operating leases	(24)	(56)
Impairment loss for doubtful debts	137	45
Dividend income	(10)	(11)
Amortization of intangible assets	135	97
Amortization of goodwill	–	63
Amortization of land lease premium	16	15
Amortization of business development costs	–	3
Amortization of premium received from equity options	–	(5)
Amortization of up-front installation fees	(243)	(234)
Impairment loss on investment in unconsolidated subsidiaries held for sale	6	–
Share of results of jointly controlled companies and associates	(121)	(147)
Exchange gains	(195)	–
OPERATING PROFIT BEFORE CHANGES IN WORKING CAPITAL	6,489	6,418
Decrease/(Increase) in operating assets		
– properties under development	(836)	(2,480)
– inventories	(77)	58
– accounts receivable, net	(477)	(113)
– prepayments, deposits and other current assets	111	72
– sales proceeds held in stakeholders' accounts	125	(2,016)
– restricted cash	(687)	1,797
– amounts due from related companies	(56)	94
– amounts due from jointly controlled companies and associates	(8)	–
– other non-current assets	22	–
Increase/(Decrease) in operating liabilities		
– accruals, accounts payable, provisions, other payables and deferred income	121	2,499
– gross amount due to customers for contract work	6	5
– amounts due to related companies	(150)	(49)
– other long-term liabilities	(20)	–
– advances from customers	940	10
CASH GENERATED FROM OPERATIONS	5,503	6,295
Interest received	543	41
Tax paid		
– Hong Kong profits tax paid	(1,404)	(1,233)
– overseas tax paid	(3)	–
NET CASH INFLOW FROM OPERATING ACTIVITIES	4,639	5,103

39 NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT (CONTINUED)

b. Acquisition of subsidiaries

In HK\$ million	The Group	
	2005	2004
Net assets acquired:		
Property, plant and equipment	1,276	–
Intangible assets	183	5
Investment in unconsolidated subsidiaries	–	55
Inventories	13	–
Trade receivables, deposits, prepayments and other receivables	200	70
Restricted cash, cash and cash equivalents	113	–
Trade payables, other payables and accrued charges	(379)	–
Long-term loans	(850)	–
3G licence fee liability	(529)	–
Minority interests	(11)	–
	16	130
Goodwill on acquisition	1,148	89
	1,164	219
Satisfied by:		
Interest in certain subsidiaries	–	209
Cash from internal resources	1,164	10
	1,164	219
Analysis of the net outflow of cash and cash equivalents in respect of the acquisition of subsidiaries:		
Cash	(1,164)	(10)
Cash and cash equivalents acquired	112	–
Net cash outflow in respect of acquisition of subsidiaries	(1,052)	(10)

39 NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT (CONTINUED)**c. Disposal of subsidiaries**

In HK\$ million	The Group	
	2005	2004
Net assets disposed of:		
Property, plant and equipment	1	–
Inventories	9	–
Accounts receivables, prepayments, deposits and other assets	4	–
Cash and bank balances	277	–
Accounts payables, accruals and other payables	(15)	–
Minority interests	(58)	–
	218	–
Gain on disposal of subsidiaries	170	–
	388	–
Satisfied by:		
Cash	388	–
	388	–
Analysis of the net inflow of cash and cash equivalents in respect of the disposal of subsidiaries:		
Cash	388	–
Cash and bank balances disposed of	(277)	–
Net cash inflow in respect of disposal of subsidiaries	111	–

d. Analysis of cash and cash equivalents

In HK\$ million	The Group		The Company	
	2005	2004	2005	2004
Cash and bank balances	11,317	4,413	4,980	287
Bank loans and overdrafts	(46)	(15)	–	–
Restricted cash	(1,592)	(904)	–	–
Cash and cash equivalents as at December 31	9,679	3,494	4,980	287

The carrying amounts of cash and cash equivalents in the balance sheets are denominated in the following currencies:

In HK\$ million	The Group		The Company	
	2005	2004	2005	2004
Hong Kong Dollars	3,938	2,769	126	36
United States Dollars	5,531	441	4,854	251
Chinese Renminbi	200	–	–	–
Sterling Pound	10	–	–	–
Japanese Yen	–	284	–	–
	9,679	3,494	4,980	287

39 NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT (CONTINUED)

e. Major non-cash transaction

During the year, the Group acquired an IRU from the Reach Group which was settled in part by way of set-off against the Shareholder Loan of approximately US\$155 million plus interest of US\$2 million. Details of this transaction are set out in note 1(c).

40 FINANCIAL INSTRUMENTS

Exposure to credit, liquidity, and market (including foreign currency and interest rate) risks arises in the normal course of the Group's business. Exposures to these risks are controlled by the Group's financial management policies and practices described below.

a. Credit risk

The Group's credit risk is primarily attributable to trade and other receivables, investments, over-the-counter derivative transactions and cash transactions entered into for risk management purposes. Management has policies in place and exposures to these credit risks are monitored on an ongoing basis.

The normal credit period granted by the Group ranges up to 30 days from the date of invoice. In respect of trade and other receivables, credit evaluations are performed on all customers requiring credit over a certain amount. Debtors who have overdue payable are requested to settle all outstanding balances before any further credit is granted.

Investments, derivative and cash transactions are executed with counterparties with sound credit ratings. Given their high credit ratings, the Group does not expect any investment counterparty to fail to meet its obligations. Moreover, credit limits were set for individual counterparties and periodic reviews were conducted to ensure that the limits are strictly followed.

The Group does not have a significant exposure to any individual debtors or counterparties.

The maximum exposure to credit risk is represented by the carrying amount of each financial asset, including derivative financial instruments, in the balance sheet. Except for the guarantees given by the Group as disclosed in note 42, the Group does not provide any other guarantees which would expose the Group to credit risk.

b. Liquidity risk

The Group's policy is to regularly monitor current and expected liquidity requirements and its compliance with lending covenants, to ensure that it maintains sufficient reserves of cash and readily realizable marketable securities and adequate committed lines of funding from major financial institutions to meet its liquidity requirements in the short and longer term.

c. Market risk

Market risk composed of foreign currency exposure and interest rate exposure deriving from the Group's operation and funding activities. As a matter of policy, the Group enters into currency forwards, interest rate and currency swaps, forward rate agreements, options and other financial instruments to manage its exposure and reduce the market risk that is directly related to the Group's operations and financing. The Group does not undertake any speculative trading activities in connection with these financial instruments or enter into or acquire market risk sensitive instruments for trading purposes.

The Finance and Management Committee, a subcommittee of the Executive Committee of the Board, determines the appropriate risk management activities with the aim of prudently managing the market risk associated with transactions entered into in the normal course of the business.

All treasury risk management activities are carried out in accordance with policies and guidelines approved by the Finance and Management Committee and the Executive Committee, which are reviewed on a regular basis. Early termination and amendments to the terms of the transaction would typically occur when there are changes in the underlying assets or liabilities or in the risk management strategy of the Group.

In the normal course of business, the Group used the above-mentioned financial instruments to limit its exposure to adverse fluctuations in foreign currency exchange rates and interest rates. These instruments are executed with creditworthy financial institutions, and all contracts are denominated in currencies of major industrial countries.

As at 31 December 2005, all of the Group's foreign currency denominated long-term liabilities are either: (i) swapped into Hong Kong dollar by cross-currency swaps or (ii) hedged into Hong Kong dollar by currency forward contracts. In terms of interest rate exposure, most of the long-term liabilities are in fixed rate basis and will not be affected by future Hong Kong dollar interest rate fluctuations.

40 FINANCIAL INSTRUMENTS (CONTINUED)
d. Effective interest rates

The following table summarizes the carrying amounts, maturity and contract terms of income-earning financial assets and interest-bearing financial liabilities at the balance sheet date.

In HK\$ million, except for %	The Group					
	2005			2004		
	1 year or less	Over 5 years	Total	1 year or less	1-5 years	Total
Assets						
Cash and cash equivalent						
Fixed rate, HK\$	3,938	–	3,938	2,769	–	2,769
<i>Average interests rate (%)</i>	3.70%		3.70%	0.17%		0.17%
Fixed rate, US\$	5,531	–	5,531	441	–	441
<i>Average interests rate (%)</i>	4.25%		4.25%	2.17%		2.17%
Fixed rate, RMB	200	–	200	–	–	–
<i>Average interests rate (%)</i>	1.18%		1.18%			
Fixed rate, GBP	10	–	10	–	–	–
<i>Average interests rate (%)</i>	4.47%		4.47%			
Fixed rate, JPY	–	–	–	284	–	284
<i>Average interests rate (%)</i>				0.88%		0.88%
	9,679	–	9,679	3,494	–	3,494
Derivative financial instruments						
– Cross currency swaps						
Receive fixed US\$, pay floating HK\$						
Carrying amounts (<i>note i</i>)	–	–	–	–	71	71
Notional amounts	–	–	–	–	7,457	7,457
<i>Average receive rate (%)</i>					6.90%	6.90%
<i>Average pay rate (%)</i>					4.12%	4.12%
Receive fixed US\$, pay fixed HK\$						
Carrying amounts (<i>note i</i>)	–	42	42	–	–	–
Notional amounts	–	11,357	11,357	–	–	–
<i>Average receive rate (%)</i>		6.33%	6.33%			
<i>Average pay rate (%)</i>		6.05%	6.05%			
Receive fixed JPY, pay floating US\$						
Carrying amounts (<i>note i</i>)	–	–	–	–	391	391
Notional amounts	–	–	–	–	1,950	1,950
<i>Average receive rate (%)</i>					3.65%	3.65%
<i>Average pay rate (%)</i>					5.27%	5.27%
Carrying amounts (<i>note i</i>)	–	42	42	–	462	462
Notional amounts	–	11,357	11,357	–	9,407	9,407

40 FINANCIAL INSTRUMENTS (CONTINUED)

d. Effective interest rates (continued)

In HK\$ million, except for %	The Group							
	2005				2004			
	1 year or less	1-5 years	Over 5 years	Total	1 year or less	1-5 years	Over 5 years	Total
Liabilities								
Short-term borrowings								
Floating rate, HK\$	(6,500)	–	–	(6,500)	–	–	–	–
Average interest rate (%)	4.38%			4.38%				
Fixed rate, US\$	–	–	–	–	(8,998)	–	–	(8,998)
Average interest rate (%)					6.49%			6.49%
Others	–	–	–	–	(14)	–	–	(14)
Average interest rate (%)					2.95%			2.95%
	(6,500)	–	–	(6,500)	(9,012)	–	–	(9,012)
Long-term liabilities								
Fixed rate, US\$	–	(3,972)	(18,885)	(22,857)	–	(3,317)	(15,213)	(18,530)
Average interest rate (%)		5.30%	7.01%	6.72%		5.30%	7.46%	7.07%
Fixed rate, JPY	–	–	–	–	–	–	(1,950)	(1,950)
Average interest rate (%)							3.65%	3.65%
	–	(3,972)	(18,885)	(22,857)	–	(3,317)	(17,163)	(20,480)
Derivative financial instruments								
– Cross currency swaps								
Receive floating US\$, pay floating HK\$								
Carrying amounts (note i)	–	–	–	–	(7)	(6)	–	(13)
Notional amounts	–	–	–	–	1,950	1,950	–	3,900
Average receive rate (%)					5.27%	5.27%		5.27%
Average pay rate (%)					2.97%	3.44%		3.21%
Receive fixed US\$, pay fixed HK\$								
Carrying amounts (note i)	–	(15)	(47)	(62)	(254)	(209)	(125)	(588)
Notional amounts	–	3,510	3,900	7,410	12,090	7,800	11,700	31,590
Average receive rate (%)		1.00%	8.00%	4.68%	2.77%	8.00%	7.33%	5.75%
Average pay rate (%)		0.59%	7.70%	4.33%	2.77%	7.59%	6.46%	5.33%
Receive fixed US\$, receive fixed HK\$								
Carrying amounts (note i)	–	–	–	–	–	(50)	–	(50)
Notional amounts	–	–	–	–	–	3,510	–	3,510
Average receive rate (%)						1.00%		1.00%
Average receive rate (%)						0.50%		0.50%
Carrying amounts (note i)	–	(15)	(47)	(62)	(261)	(265)	(125)	(651)
Notional amounts	–	3,510	3,900	7,410	14,040	13,260	11,700	39,000

40 FINANCIAL INSTRUMENTS (CONTINUED)

d. Effective interest rates (continued)

In HK\$ million, except for %	The Company					
	2005			2004		
	1 year or less	1-5 years	Total	1 year or less	1-5 years	Total
Assets						
Cash and cash equivalent						
Fixed rate, HK\$	126	–	126	36	–	36
Average interest rate (%)	3.65%		3.65%	0.04%		0.04%
Fixed rate, US\$	4,854	–	4,854	251	–	251
Average interest rate (%)	4.23%		4.23%	1.96%		1.96%
	4,980	–	4,980	287	–	287
Derivative financial instruments						
– Cross currency swaps						
Receive fixed JPY, pay floating US\$						
Carrying amounts (note i)	–	–	–	–	391	391
Notional amounts	–	–	–	–	1,950	1,950
Average receive rate (%)					3.65%	3.65%
Average pay rate (%)					5.27%	5.27%
Carrying amounts	–	–	–	–	391	391
Notional amounts	–	–	–	–	1,950	1,950
Liabilities						
Short-term borrowings						
Fixed rate, US\$	–	–	–	(461)	–	(461)
Average interest rate (%)				5.00%		5.00%
	–	–	–	(461)	–	(461)
Derivative financial instruments						
– Cross currency swaps						
Receive fixed US\$, pay fixed HK\$						
Carrying amounts (note i)	–	(15)	(15)	(254)	–	(254)
Notional amounts	–	3,510	3,510	12,090	–	12,090
Average receive rate (%)		1.00%	1.00%	2.77%		2.77%
Average pay rate (%)		0.59%	0.59%	2.77%		2.77%
Receive fixed US\$, receive fixed HK\$						
Carrying amounts (note i)	–	–	–	–	(50)	(50)
Notional amounts	–	–	–	–	3,510	3,510
Average receive rate (%)					1.00%	1.00%
Average receive rate (%)					0.50%	0.50%
Receive floating US\$, pay floating HK\$						
Carrying amounts (note i)	–	–	–	(7)	(6)	(13)
Notional amounts	–	–	–	1,950	1,950	3,900
Average receive rate (%)				5.27%	5.27%	5.27%
Average pay rate (%)				2.97%	3.44%	3.21%
Carrying amounts (note i)	–	(15)	(15)	(261)	(56)	(317)
Notional amounts	–	3,510	3,510	14,040	5,460	19,500

- i. The carrying amounts of the outstanding cross currency swap contracts represent their fair values at the balance sheet date. In accordance with the transitional provisions in HKAS 39, the balance sheets as at December 31, 2004 were not adjusted to reflect the fair values of the cross currency swap contracts held at that date.

40 FINANCIAL INSTRUMENTS (CONTINUED)

e. Fair values

All financial instruments are carried at amounts not materially different from their fair values as at December 31, 2005 and 2004 except as follows:

In HK\$ million		2005		2004	
	Note	Carrying amount	Fair value	Carrying amount (Restated) (Note 46)	Fair value
THE GROUP					
Held-to-maturity investments	i	18	N/A	31	N/A
Derivative financial instruments					
– current assets					
Cross currency swaps	iii	42	42	–	462
Interest rate option	iii	–	–	–	–
Equity swap and equity option	iii	60	60	–	57
Short-term borrowings	ii	(6,500)	(6,500)	(10,529)	(10,714)
Derivative financial instruments					
– current liabilities					
Cross currency swaps	iii	(62)	(62)	–	(651)
Forward foreign exchange contracts	iii	–	–	–	(5)
Long-term borrowings		(18,885)	(20,084)	(17,163)	(19,282)
Convertible note and bonds	ii	(3,972)	(3,954)	(3,730)	(3,936)
THE COMPANY					
Derivative financial instruments					
– current assets					
Cross currency swaps	iii	–	–	–	391
Short-term borrowings	ii	–	–	(461)	(467)
Derivative financial instruments					
– current liabilities					
Cross currency swaps	iii	(15)	(15)	–	(317)
Forward foreign exchange contracts	iii	–	–	–	(1)

- i. Due to the nature of held-to-maturity investments, it is not practicable to estimate their fair value as such exercise would require excessive cost.
- ii. Balances as at December 31, 2004 include redemption premium on respective convertible note and bonds.
- iii. In accordance with the transitional provisions in HKAS 39, the balance sheets as at December 31, 2004 were not adjusted to reflect the fair value of derivative financial instruments held at that date (see note 4(a)(v)).

40 FINANCIAL INSTRUMENTS (CONTINUED)**f. Estimation of fair values**

Fair value of financial instruments is estimated as follows:

- i. The fair value of financial instruments traded in active markets (such as trading and available-for-sale financial assets, and listed long-term borrowings and convertible note and bonds) is based on quoted market prices at the balance sheet date.
- ii. The fair value of financial instruments that are not traded in an active market (for example, over-the-counter derivatives) is determined by using valuation techniques. The Group uses a variety of methods and makes assumptions that are based on market conditions existing at each balance sheet date. Quoted market prices or dealer quotes for similar instruments are used for long-term debt. Other techniques, such as estimated discounted cash flows, are used to determine the fair value for the remaining financial instruments. The fair value of cross currency swaps is calculated as the present value of the estimated future cash flows. The fair value of forward foreign exchange contracts is determined using quoted forward exchange rates at the balance sheet date.
- iii. The nominal value less impairment provision of trade receivables and payables are assumed to approximate their fair values. The fair value of financial liabilities for disclosure purposes is estimated by discounting the future contractual cash flows at the current market interest rate that is available to the Group for similar financial instruments.

41 COMMITMENTS**a. Capital**

In HK\$ million	The Group	
	2005	2004
Authorized and contracted for	2,920	1,909
Authorized but not contracted for	2,270	3,077
	5,190	4,986

An analysis of the above capital commitments by nature is as follows:

In HK\$ million	The Group	
	2005	2004
Investments	202	236
Investment properties	–	85
Property development (note i)	2,835	3,954
Acquisition of property, plant and equipment	2,151	707
Others	2	4
	5,190	4,986

- i. The capital commitment as disclosed above represented management's best estimate of total construction costs of the Cyberport project, which has been revised from the total construction costs since the Cyberport Project Agreement was entered into on May 17, 2000.

41 COMMITMENTS (CONTINUED)

b. Operating leases

As at December 31, 2005, the total future minimum lease payments under non-cancellable operating leases are payable as follows:

Land and buildings

In HK\$ million	The Group	
	2005	2004
Within 1 year	339	143
After 1 year but within 5 years	368	209
After 5 years	82	76
	789	428

Equipment

In HK\$ million	The Group	
	2005	2004
Within 1 year	179	144
After 1 year but within 5 years	41	56
After 5 years	1	10
	221	210

c. Others

As set out in note 5(c) above, on June 17, 2004, the Company agreed to provide REACH with a revolving working capital loan facility up to US\$25 million (approximately HK\$195 million). The facility is secured and will be repayable in full by REACH on December 31, 2007. The interest receivable under this facility is LIBOR plus 250 basis points. As at December 31, 2005, none of this working capital loan facility has been drawn down by REACH.

As at December 31, 2005, the Group has other outstanding commitment as follows:

In HK\$ million	The Group	
	2005	2004
Purchase of rights to broadcast certain TV content	811	586
Purchase commitment on telecommunications services	300	–
Operating expenditure commitment	378	–
	1,489	586

42 CONTINGENT LIABILITIES

In HK\$ million	The Group		The Company	
	2005	2004	2005	2004
Performance guarantee	403	129	311	–
Tender guarantee	2	1	–	–
Advance payment guarantee	10	6	10	–
Guarantees given for bonds/notes issued by subsidiaries	–	–	4,034	12,056
Guarantee in lieu of cash deposit	5	5	2	–
Staff mortgage loan guarantee	–	1	–	–
Employee compensation	6	3	6	3
Guarantee indemnity	11	11	–	–
Corporate guarantee	–	92	–	–
	437	248	4,363	12,059

On April 23, 2002, a writ of summons was issued against PCCW-HKT Limited (“HKT”), an indirect wholly-owned subsidiary of the Company, by New Century Infocomm Tech Co., Ltd. for HKT’s failure to purchase 6,522,000 shares of Taiwan Telecommunication Network Services Co., Ltd. (“TTNS”), an indirect subsidiary of the Company, pursuant to an option agreement entered into on July 24, 2000. The total claim against HKT amounted to approximately HK\$99 million (NT\$418 million), being the purchase price of shares in TTNS, contractual interest for the period from January 1, 2001 to January 2, 2002 at 6.725% per annum and interest on the due amount pursuant to Sections 48 and 49 of the High Court Ordinance, Chapter 4 of the Laws of Hong Kong. However, this figure should be reduced by the current market value of the shares in TTNS which would be transferred to HKT in the event that the claimants are successful in their claim. A defence was filed by HKT on May 29, 2002 and proceedings are ongoing. Based on legal advice received, the directors consider that HKT has valid defences and therefore no provision has been made.

HKTC is in dispute with Hong Kong’s Inland Revenue Department (the “IRD”) regarding the deductibility of certain finance expenses. The IRD had raised two assessments for part of the disputed finance expenses on April 21, 2005 and February 3, 2006. HKTC had lodged an objection to both assessments and successfully obtained a holdover of the tax assessed through the purchase of Tax Reserve Certificates in the amount of HK\$308 million. The estimated tax impact of the dispute may amount to HK\$322 million up to December 31, 2005. Based on the information available to the Group to date, HKTC has made a provision based on the best estimate of the amount that may ultimately be required to settle the dispute. The directors consider that the impact of any unprovided amounts which may materialize is immaterial.

The Group is subject to certain corporate guarantee obligations to guarantee performance of its wholly-owned subsidiaries in the normal course of their businesses. The amount of liabilities arising from such obligations, if any, cannot be ascertained but the directors are of the opinion that any resulting liability would not materially affect the financial position of the Group.

43 BANKING FACILITIES

Aggregate banking facilities as at December 31, 2005 were HK\$11,579 million (2004: HK\$11,300 million) of which the unused facilities amounted to HK\$5,079 million (2004: HK\$11,286 million).

A summary of major borrowings is set out in note 28(a).

Security pledged for certain banking facilities includes:

In HK\$ million	The Group	
	2005	2004
Land and buildings	31	33
Bank deposit	10	15
Investment securities	21	19
	62	67

As at December 31, 2005, an indirect subsidiary of the Company has been granted a banking facility amounting to approximately HK\$20 million (2004: HK\$20 million) from a bank for the purpose of providing guarantee to the Government. Such facility was secured by a bank deposit placed by that indirect subsidiary of the Company from time to time to secure the amount of guarantee issued by the bank. The bank deposit of HK\$1 million was included in "Restricted cash" in the consolidated balance sheet as at December 31, 2004, while no guarantee was issued by the bank and no such bank deposit was placed by the subsidiary as at December 31, 2005 (see note 27(b)).

In addition, the bank guarantee issued in favour of the Company in connection with the undertakings as set out in note 34(a)(iii) above was secured by a bank deposit placed by another indirect wholly-owned subsidiary of the Company amounting to approximately HK\$259 million as at December 31, 2005 (2004: Nil), which was included in "Restricted cash" in the consolidated balance sheet (see note 27(b)).

As at December 31, 2005, a bank guarantee was issued to another indirect subsidiary of the Company in respect of the use of facilities at the Hong Kong International Airport for the provision of mobile services. Such bank guarantee was pledged against a bank deposit placed by the indirect subsidiary of the Company amounting to approximately HK\$1 million, which was included in "Restricted cash" in the consolidated balance sheet (see note 27(b)).

44 BUSINESS COMBINATIONS

As set out in note 1(d), on June 22, 2005, the Group, through PCCW Mobile, acquired approximately 59.87% of the issued share capital of SUNDAY for a total cash consideration of HK\$1,163,587,100. SUNDAY Group is a developer and provider of wireless communications and data services in Hong Kong, and a 3G licence holder. The acquired business contributed revenue of HK\$598 million and loss before tax of HK\$136 million to the Group for the period from June 22, 2005 to December 31, 2005. If the acquisition had occurred on January 1, 2005, the estimated consolidated revenue for the Group would have been HK\$23,057 million, and profit before taxation would have been HK\$2,905 million.

Details of net assets acquired and goodwill are as follows:

	HK\$ million
Purchase consideration:	
Cash paid	1,164
Less: Fair value of net assets acquired	(16)
Goodwill on acquisition	1,148

The goodwill is attributable to the cost of entry into wireless communications market in Hong Kong, control premium of SUNDAY and the significant synergies expected to arise after the Group's acquisition of SUNDAY.

44 BUSINESS COMBINATIONS (CONTINUED)

Acquiree's net assets at the acquisition date are as follows:

In HK\$ million	Fair value	Carrying amounts
Property, plant and equipment	1,276	1,282
3G licence	101	812
Customer base	65	–
Trademark	10	–
Other intangible assets	7	7
Inventories	13	13
Trade receivables, deposits, prepayments and other receivables	200	199
Restricted cash, cash and cash equivalents	113	113
Trade payables, other payables and accrued charges	(379)	(370)
Long-term loans	(850)	(850)
3G licence fee liability	(529)	(557)
Net assets	27	649
Minority interests (40.13%)	(11)	
Net assets acquired	16	
		HK\$ million
Purchase consideration settled in cash		1,164
Cash and cash equivalents acquired		(112)
Net cash outflow on acquisition (note 39(b))		1,052

45 POST BALANCE SHEET EVENTS

The following events occurred subsequent to December 31, 2005 up to the date of approval of these financial statements by the Board:

a. On January 10, 2006, the High Court made an order permitting the release of the Company from its undertakings given to the High Court in connection with the Capital Reduction, details of which are set out in note 34(a). In summary, the undertakings required certain amounts to be credited to the special capital reserve created in connection with the Capital Reduction; that those amounts should not be treated as realized profit for the purposes of the Hong Kong Companies Ordinance; that the special capital reserve should be treated as undistributable for the purposes of the Hong Kong Companies Ordinance; and that the Company record a summary of the undertakings in its audited or interim financial statements. Following the release of the undertakings, the Company and the special capital reserve will cease to be subject to those restrictions and the Company will no longer be required to record a summary of the undertakings in its audited or interim financial statements.

The order of the High Court permits the undertakings to be released subject to the Company setting aside sums totalling approximately US\$544 million (approximately HK\$4,243 million) and HK\$106 million for the sole purpose of discharging certain debts or liabilities of the Company existing at the date of the Capital Reduction, principally being the aggregate amount of principal, accrued interest and redemption premium payable on maturity of the US\$450 million 1% guaranteed convertible bonds due 2007 issued by PCCW Capital No. 2 Limited. Those amounts were set aside, and the release of the undertakings thereby became effective, on March 27, 2006. The cash set aside will be recorded under "Restricted cash" in the balance sheet of the Company.

45 POST BALANCE SHEET EVENTS (CONTINUED)

b. On March 2, 2006, PCCW IMS China Development Limited (“PCCW IMS China”), an indirect wholly-owned subsidiary of the Company, entered into a sale and purchase agreement (the “Sale and Purchase Agreement”) with China Netcom Group and 中國網絡通信(控股)有限公司, a state-owned enterprise established under the laws of the PRC and a wholly-owned subsidiary of China Netcom Group, (as vendors), and 網通寬帶網絡有限責任公司 (“CNCBB”), a limited liability company established in the PRC and a subsidiary of China Netcom Group, (as the target company), whereby PCCW IMS China will acquire an aggregate of 50% of the registered capital of CNCBB after the completion of CNCBB’s group reorganization at a consideration of RMB318 million (approximately HK\$305.77 million), which will be funded by internal resources of the Company and is payable in a prescribed manner.

46 COMPARATIVE FIGURES

Certain comparative figures have been adjusted or re-classified as a result of the changes in accounting policies. Further details are disclosed in note 4.

47 POSSIBLE IMPACT OF AMENDMENTS, NEW STANDARDS AND INTERPRETATIONS ISSUED BUT NOT YET EFFECTIVE FOR THE ANNUAL ACCOUNTING PERIOD ENDED DECEMBER 31, 2005

Up to the date of approval of these financial statements, the HKICPA has issued the following amendments, new standards and interpretations which are not yet effective for the accounting period ended December 31, 2005 and which have not been adopted in these financial statements:

		Effective for accounting periods Beginning on or after
HKFRS 6	Exploration for and Evaluation of Mineral Resources	January 1, 2006
HKFRS-Int 4	Determining whether an Arrangement contains a Lease	January 1, 2006
HKFRS-Int 5	Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds	January 1, 2006
HK(IFRIC)-Int 6	Liabilities arising from participating in a specific market – Waste electrical and electronic equipment	December 1, 2005
Amendments to HKAS 19 Employee benefits – Actuarial Gains and Losses, Group Plans and Disclosures		January 1, 2006
Amendments to HKAS 39 Financial Instruments: Recognition and Measurement: – Cash Flow Hedge Accounting of Forecast Intragroup Transactions		January 1, 2006
– The Fair Value Option		January 1, 2006
– Financial Guarantee Contracts		January 1, 2006
Amendments, as a consequence of the Hong Kong Companies (Amendment) Ordinance 2005, to:		
– HKAS 1	Presentation of Financial Statements	January 1, 2006
– HKAS 27	Consolidated and Separate Financial Statements	January 1, 2006
– HKFRS 3	Business Combinations	January 1, 2006
HKFRS 7	Financial Instruments: Disclosures	January 1, 2007
Amendment to HKAS 1 Presentation of Financial Statements – Capital Disclosures		January 1, 2007

In addition, the Hong Kong Companies (Amendment) Ordinance 2005 came into effect on December 1, 2005 and would be first applicable to the Group’s financial statements for the period beginning January 1, 2006.

The Group is in the process of making an assessment of what the impact of these amendments, new standards and new interpretations would be in the period of initial application, but is not yet in a position to state whether these amendments, new standards and new interpretations would have a significant impact on the Group’s results of operations and financial position.