NOTES TO THE FINANCIAL STATEMENTS

December 31, 2006 (Amount expressed in Hong Kong dollars unless otherwise stated)

1. GENERAL INFORMATION

Pacific Century Premium Developments Limited (the "Company") and its subsidiaries (together the "Group") are principally engaged in the development and management of property and infrastructure and investment in properties in Hong Kong and mainland China.

The Company is a limited liability company incorporated in Bermuda and its securities are listed on The Stock Exchange of Hong Kong Limited (the "Stock Exchange"). The address of its registered office is Clarendon House, 2 Church Street, Hamilton HM 11, Bermuda.

At December 31, 2006, the directors consider the parent company of the Group to be Asian Motion Limited, a company incorporated in British Virgin Islands, and the ultimate holding company of the Group to be PCCW Limited ("PCCW"), a company incorporated in Hong Kong. PCCW produces financial statements available for public use.

The financial statements set out on pages 54 to 133 were approved by the board of directors (the "Board") on March 28, 2007.

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 ("HKFRS") issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA") and the disclosure requirements of the Hong Kong Companies Ordinance. The principal accounting policies applied in the preparation of these financial statements are set out below. These policies have been consistently applied to the years presented, unless otherwise stated.

b. Basis of preparation of the financial statements

The measurement basis used in the preparation of the financial statements is the historical cost convention, as modified by the revaluation of financial assets and financial liabilities at fair value through profit or loss and investment properties, which are carried at fair value.

The preparation of financial statements in conformity with HKFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements, are disclosed in note 3.

The HKICPA has issued certain new and revised HKFRS that are first effective or available for early adoption for the current accounting period of the Group. The following sets out the changes in accounting policies for the current and prior accounting periods reflected in these financial statements.

December 31, 2006 (Amount expressed in Hong Kong dollars unless otherwise stated)

2. BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES - CONTINUED

b. Basis of preparation of the financial statements - Continued

Amendments to published standards effective from January 1, 2006

HKAS 39 and HKFRS 4 Amendments, Financial instruments: Recognition and Measurement and Insurance Contract - Financial Guarantee Contracts

In prior years, financial guarantees issued by the Group were disclosed as contingent liabilities in accordance with HKAS 37 "Provisions, Contingent Liabilities and Contingent Assets". No provision was made in respect of these guarantees unless it was more likely than not that an outflow of resources will be required to settle the obligation and a reliable estimate can be made. With effect from January 1, 2006, in order to comply with the amendments to HKAS 39 in respect of financial guarantee contracts, the Group has changed its accounting policy for financial guarantees issued. Under the new policy, financial guarantees issued are accounted for as financial liabilities under HKAS 39 and measured initially at fair value, where the fair value can be reliably measured. There was no impact on the Group's consolidated financial statements for the current and prior years due to the adoption of the new accounting policy.

Standards, amendments and interpretations effective from January 1, 2006 adopted by the Group but have no impact on the Group's financial statements

HKAS 19 Amendment	Employee Benefits - Actuarial Gains and Losses, Group Plans and Disclosures
HKAS 21 Amendment	The Effects of Changes in Foreign Exchange Rates - Net Investment in a Foreign Operation
HKAS 39 Amendment	Financial Instruments: Recognition and Measurement - Cash Flow Hedge Accounting of Forecast Intragroup Transactions
HKAS 39 Amendment	Financial Instruments: Recognition and Measurement - The Fair Value Option
HKFRS 6	Exploration for and Evaluation of Mineral Resources
HKFRSs 1 & 6 Amendments	First-time Adoption of Hong Kong Financial Reporting Standards and Exploration for and Evaluation of Mineral Resources
HKFRS-Int 4	Determining whether an Arrangement contains a Lease
HKFRS-Int 5	Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds
HK(IFRIC)-Int 6	Liabilities arising from Participating in a Specific Market - Waste Electrical and Electronic Equipment

2. BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES - CONTINUED

b. Basis of preparation of the financial statements - Continued

The following standards and interpretations to existing standards have been published but not yet effective for the year ended December 31, 2006 and which the Group has not early adopted:

HKAS 1 Amendment	Presentation of Financial Statements - Capital Disclosures (effective for annual periods beginning on or after January 1, 2007)
HKFRS 7	Financial Instruments: Disclosures (effective for annual periods beginning on or after January 1, 2007)
HK(IFRIC)-Int 7	Applying the Restatement Approach under HKAS 29 Financial Reporting in Hyperinflationary Economies (effective for annual periods beginning on or after March 1, 2006)
HK(IFRIC)-Int 8	Scope of HKFRS 2 (effective for annual periods beginning on or after May 1, 2006)
HK(IFRIC)-Int 9	Reassessment of Embedded Derivatives (effective for annual periods beginning on or after June 1, 2006)
HK(IFRIC)-Int 10	Interim Financial Reporting and Impairment (effective for annual periods beginning on or after November 1, 2006)
HK(IFRIC)-Int 11	HKFRS 2 - Group and Treasury Share Transactions (effective for annual periods beginning on or after March 1, 2007)
HK(IFRIC)-Int 12	Service Concession Arrangements (effective for annual periods beginning on or after January 1, 2008)

The Group has already commenced an assessment of the impact of these new HKFRS but is not yet in a position to state whether these new HKFRS would have a significant impact on its results of operations and financial position.

2. BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES - CONTINUED

c. Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and all of its subsidiaries other than those unconsolidated subsidiaries acquired exclusively with a view for resale, made up to December 31 each year. Intra-group balances and transactions, and any unrealised profits arising from intra-group transactions, are eliminated in full in preparing the consolidated financial statements. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

In the Company's balance sheet, the investment in subsidiaries are stated at cost less provision for impairment losses (note 2(h)). The results of subsidiaries are accounted for by the Company on the basis of dividend received and receivable.

As stated in note 19 to the 2005 Financial Statements, considering that certain subsidiaries of the Company were acquired and held by the Group exclusively with a view to their subsequent disposal in the near future, the investment in these subsidiaries was accounted for as a disposal group held for sale and stated at the lower of carrying amount and fair value less costs to sell as at December 31, 2005. The investment in these subsidiaries was recorded as "Investment in unconsolidated subsidiaries held for sale" under current assets in the consolidated balance sheet with a carrying value of approximately HK$45 million as at December 31, 2005. These unconsolidated subsidiaries have been disposed during the year.

2. BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES - CONTINUED

d. Revenue recognition

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

(i) Sales of properties

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

For pre-completion contracts for the sale of development properties for which legally binding unconditional sales contracts were entered into on or after January 1, 2005, revenue and profits are recognised upon completion of the development and when significant risks and rewards of ownership have been transferred. Deposits and instalments received from purchasers prior to this stage are included in current liabilities.

If the pre-completion contracts for the sale of development properties 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 – Pre-completion Contracts for the Sale of Development Properties”, revenues and profits continue to be recognised 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 realisation of profit can be reasonably determined and on the basis that the total estimated profits 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.

(ii) Rental income from operating leases

Rental income receivable from investment properties under operating leases is recognised in 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 granted are recognised in the income statement as an integral part of the aggregate net lease payments receivable. Contingent rentals are recognised as income in the accounting period in which they are earned.

2. BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES – CONTINUED

d. Revenue recognition - Continued

(iii) Contract revenue

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

(iv) Interest income

Interest income from bank deposits is accrued on a time-apportioned basis using the effective interest method by reference to the principal outstanding and the rates applicable.

e. Operating leases

Leases of assets under which the lessor has not transferred all the risks and benefits of ownership are classified as operating leases.

(i) Assets held for use in operating leases (as lessor)

Where the Group leases out assets under operating leases, the assets are included in the balance sheet according to their nature as set out in note 2(g). Revenue arising from operating leases is recognised in accordance with the Group's revenue recognition policies, as set out in note 2(d)(ii).

(ii) Operating lease charges

Leases in which a significant portion of the risks and rewards of ownership retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are expensed in the income statement on a straight-line basis over the period of the lease.

Up-front payments made for leasehold land held under operating leases are presented in the balance sheet as prepayments for operating leases and are amortised in the income statement on a straight-line basis over the period of the lease or where there is impairment, the impairment is expensed in the income statement.

When a definite intention to develop the leasehold land is clear and action initiated, the net book value of leasehold land held under operating lease for sale is reclassified as properties under development.

2. BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES - CONTINUED

f. Property, plant and equipment and depreciation

Property, plant and equipment are stated in the balance sheet at cost less accumulated depreciation and impairment losses (note 2(h)). The cost of an asset comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use, including qualifying borrowing costs. Subsequent expenditure relating to property, plant and equipment that has already been recognised is added to the carrying amount of the asset and is depreciated over the original remaining useful life of the asset when it is probable that future economic benefits, in excess of the originally assessed standard of performance of the existing asset, will flow to the Group. All other subsequent expenditure, such as repairs and maintenance and overhaul costs, is recognised as an expense in the period in which it is incurred.

Depreciation is calculated to write off the cost on a straight-line basis over the estimated useful lives as follows:

Other plant and equipment	2 to 10 years

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

g. Investment properties

A property that is held for long-term rental yields or for capital appreciation or both, and that is not occupied by the companies in the consolidated Group, is classified as investment property.

Investment properties comprise land held under operating leases and buildings held under finance leases. Land held under operating leases are classified and accounted for as an investment property when the rest of the definition of investment property is met. The operating lease is accounted for as if it were a finance lease.

Investment properties are initially measured at their cost, including directly attributable construction costs, borrowing costs and other related transaction costs. After initial recognition, investment properties are stated in the balance sheet at fair value. Fair value is based on active market prices, adjusted, if necessary, for any difference in the nature, location or condition of the specific asset. If this information is not available, the Group uses alternative valuation methods such as recent prices on less active markets or discounted cash flow projections. These valuations are performed in accordance with the guidance issued by the International Valuation Standards Committee and are prepared or reviewed annually by independent external 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. The fair value also reflects, on a similar basis, any cash outflows that could be expected in respect of the properties. Changes in fair value arising on the revaluation of investment properties are recognised in the income statement.

2. BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES - CONTINUED

g. Investment properties - Continued

Subsequent expenditure is charged to the asset's carrying amount 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 repairs and maintenance costs are expensed in the income statement during the financial period in which they are incurred.

h. Impairment of assets

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

— interest in leasehold land;

— property, plant and equipment;

— goodwill; and

— investment in subsidiaries.

If any such indication exists, the asset's recoverable amount is estimated. An impairment loss is recognised in the income statement whenever the carrying amount of an asset exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purpose of assessing impairment, assets are grouped at the lowest level for which there are separately identifiable cash inflows (a cash-generating unit).

(i) Calculation of recoverable amount

The recoverable amount of an asset is the greater of its fair value less costs to sell and its value in use. Fair value less costs to sell 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.

2. BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES - CONTINUED

h. Impairment of assets - Continued

(ii) Reversals of impairment losses

An impairment loss of an asset other than goodwill is reversed if there has been a change in the estimates used to determine the recoverable amount.

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

i. Properties under development/held for sale

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

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 receivables (note 2(d)(i)).

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 realisable value. Cost includes original land acquisition costs, costs of land use rights, construction expenditure incurred and other direct development costs attributable to such properties, including amortisation of leasehold land and interest incurred on loans directly attributable to the development prior to the completion of construction. The net realisable value is determined by reference to estimated sales proceeds of properties sold in the ordinary course of business less all estimated selling expenses.

Up-front payments for leasehold land and land use rights included in properties under development are measured at amortised cost less accumulated impairment losses.

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.

Properties held for sale represent completed properties available for sales which are stated at the lower of cost and the estimated net realisable value. They are classified under current assets.

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

2. BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES - CONTINUED

j. Goodwill

Goodwill represents the excess of the cost of an acquisition over the Group's share of the fair value of the net identifiable assets and liabilities acquired at the date of acquisition.

Goodwill is stated at cost less accumulated impairment losses. Goodwill is allocated to cash-generating units for the purpose of impairment testing and is tested annually for impairment or whenever there is an indication of impairment. Impairment losses on goodwill are not reversed. Gains and losses on the disposal of an entity or business unit include the carrying amount of goodwill relating to the entity or business unit sold.

k. Financial instruments and derivatives

The fair value of the liability portion of convertible notes is determined using a market interest rate for an equivalent non-convertible debt. This amount is recorded as a liability on an amortised cost basis until extinguished on conversion or maturity of the debt. The remainder of the proceeds is allocated to the conversion option, which is recognised and included in shareholders' equity, net of income tax effects. The carrying amount of the financial liability is measured on the amortised cost basis using effective interest method minus principal repayments. The conversion option is an equity instrument that is recognised in the convertible notes reserve in equity until either the note is converted or redeemed. If the note is converted, the convertible notes reserve, together with the carrying amount 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 note is redeemed, the convertible notes reserve is transferred directly to retained earnings.

2. BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES – CONTINUED

l. Financial guarantees issued

Financial guarantees are contracts that require the issuer (i.e. the guarantor) to make specified payments to reimburse the beneficiary of the guarantee (the "holder") for a loss the holder incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument.

A financial guarantee contract issued by the Group and not designated as at fair value through profit or loss is recognised initially at its fair value less transaction costs that are directly attributable to the issue of the financial guarantee contract. Subsequent to initial recognition, the Group measures the value of financial guarantee contract at the higher of: (i) the amount determined in accordance with HKAS 37 "Provisions, Contingent Liabilities and Contingent Assets"; and (ii) the amount initially recognised less, when appropriate, cumulative amortisation recognised in accordance with HKAS 18 "Revenue".

Rental guarantee contract of the Group is categorised as a financial liability at fair value through profit or loss at inception and is initially recognised at fair value on the date on which a contract is entered into and subsequently re-measured at its fair value at each balance sheet date. Changes in fair value of the financial liability are recognised in the income statement.

m. Subsidiaries

Subsidiaries are entities controlled by the Group. Control exists when the Group has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that presently are exercisable are taken into account. An investment in a subsidiary is consolidated into the consolidated financial statements from the date that control commences until the date that control ceases.

In the Company's balance sheet, investment in subsidiaries are stated at cost less any impairment loss (note 2(h)). The results of subsidiaries are recognised by the Company to the extent of dividends received and receivable at the balance sheet date.

n. 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 their 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 is still undergoing the selling of the unconsolidated subsidiaries. The investment in unconsolidated subsidiaries held for sale is stated at the lower of carrying amount and fair value less costs to sell.

2. BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES – CONTINUED

o. Construction contracts

The accounting policy for contract revenue is set out in note 2(d)(iii) above and construction costs are recognised when incurred. When the outcome of a construction contract can be estimated reliably, contract costs are recognised as expenses by reference to the stage of completion of the contract activity at the balance sheet date. When it is probable that total contract costs will exceed total contract revenue, the expected loss is recognised as an expense immediately. When the outcome of a construction contract cannot be estimated reliably, revenue is recognised only to the extent that it is probable the contract costs incurred will be recoverable and contract costs are recognised 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 recognised profits less recognised losses, estimated value of work performed including progress billings, and are presented in the balance sheet as the "Gross amounts due from customers for contract work" (as an asset) or the "Gross amounts 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".

p. Cash and cash equivalents

Cash and cash equivalents comprise cash at bank and on hand, demand deposits with banks and other financial institutions, and other 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.

q. Accounts and other payables

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

2. BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES – CONTINUED

r. Provisions and contingent liabilities

Provisions are recognised for liabilities of uncertain timing or amount when the Company or the Group has a present obligation (legal or constructive) as a result of a past event, it is more likely than not that an outflow of resources will be required to settle the obligation and a reliable estimate can be made. Provisions are reviewed at each balance sheet date and adjusted to reflect the current best estimate of the amount required to settle the obligation. Where the time value of money is material, provisions are stated at the present value of the expenditures expected to settle the obligation.

Where it is not probable that an outflow of resources 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.

s. 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 capitalised 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 capitalisation of borrowing costs as part of the cost of a qualifying asset commences when expenditures for the asset are 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. Capitalisation 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 completed.

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 recognised as expenses over the period of the borrowing.

2. BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES – CONTINUED

t. Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the Group provides money, goods or services directly to a debtor with no intention of trading the receivable. They are included in current assets, except for maturities greater than twelve months after the balance sheet date. These are classified as non-current assets. Loans and receivables are included in accounts receivable and prepayments, deposits and other current assets.

Loans and receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of loans and receivables is established when there is objective evidence that the Group will not be able to collect amounts due according to the original terms of receivables. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the effective interest rate. The amount of the provision is recognised in the income statement.

u. Income tax

Income tax for the year comprises current tax and movements in deferred tax assets and liabilities. Income tax is recognised in the income statement.

(i) 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 years.

(ii) Deferred tax assets and liabilities arise from deductible and taxable temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the tax bases respectively. 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 utilised, are recognised.

The amount of deferred tax provided is based on the expected manner of realisation 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.

2. BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES – CONTINUED

v. Employee benefits

(i) Salaries, annual bonuses, annual leave entitlements, leave passage and the cost to the Group of non-monetary benefits are accrued in the year in which the associated services are rendered by employees of the Group. Where payment or settlement is deferred and the effect would be material, provisions are made for the estimated liability as a result of services rendered by employees up to the balance sheet date.

(ii) Defined benefit and defined contribution retirement schemes (including the Mandatory Provident Fund) are offered to employees of the Group. The schemes are operated by PCCW and the assets of such schemes are generally held in separate trustee-administered funds. The schemes are generally funded by payments from the relevant companies of the PCCW Group including the Group and, in some cases, employees themselves, taking into account of the recommendations of independent qualified actuaries.

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

The Group bears its attributable share of retirement costs of the defined benefit retirement schemes operated by PCCW. 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 per cent of the greater of the present value of the defined benefit obligations and the fair value of the scheme assets, are recognised in the income statement over the expected average remaining service lives of the participating employees. Past service costs are recognised as an expense on a straight-line basis over the average period until the benefits become vested.

2. BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES – CONTINUED

v. Employee benefits - Continued

(iii) The Group and PCCW operate share option schemes where employees (including directors) are granted options to acquire shares of the Company or PCCW at specified exercise prices. The fair value of the employee services received in exchange for the grant of the options is recognised 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. At each balance sheet date, the Group revises its estimates of the number of share options that is expected to become vested. The impact of the revision of original estimates, if any, is recognised in the income statement with a corresponding adjustment to the employee share-based compensation reserve over the remaining vesting period. On vesting date, the amount recognised 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 recognised 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). 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.

2. BASIS OF PREPARATION AND PRINCIPAL ACCOUNTING POLICIES – CONTINUED

w. Foreign currency translations

Companies comprising the Group maintain their books and records in the primary currencies of their operations (the "functional currencies"). The consolidated financial statements are presented in Hong Kong dollars, which is the Company's functional and presentation currency.

In the financial statements of individual companies, transactions in other currencies during the year are translated into the respective functional currencies at the exchange rates prevailing at the transaction dates. Monetary assets and liabilities denominated in other currencies are translated into the respective functional currencies at the exchange rates ruling at the balance sheet date. Exchange gains and losses are dealt with in the income statement.

For the purposes of preparing consolidated financial statements, the financial statements of the individual companies with functional currencies other than Hong Kong dollars are translated into Hong Kong dollars as follows:

(i) assets and liabilities for each company's balance sheet are translated at the closing rate at the date of that balance sheet;

(ii) income and expenses for each company's income statement are translated at average exchange rates for the year; and

(iii) all resulting exchange differences are recognised as a separate component of equity.

On consolidation, exchange differences arising from the translation of the net investment in foreign entities are taken to the currency translation reserve under equity. When a foreign operation is sold, such exchange differences are recognised in the consolidated income statement as part of the gain or loss on sale.

x. Segment reporting

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

Consistent with the Group's internal management and financial reporting, the Group has chosen business segment information as the primary reporting format and geographical segment information as the secondary reporting format.

y. Dividend distribution

Dividend distribution to the Company's shareholders is recognised as a liability in the financial statements in the period in which the dividends are approved by the Company's shareholders.

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. The management have made judgements in applying the Group's accounting policies. The judgements that have the most significant effect on the amounts recognised in the financial statements are discussed below:

(i) Financial instruments

The fair value of the liability portion of a convertible debt was determined by using a market interest rate for an equivalent non-convertible debt at the date the convertible notes was issued in May 2004. This amount is recorded as a financial liability and is measured on the amortised cost basis using effective interest method minus principal repayment. Had management determined that a different market interest rate of an equivalent non-convertible debt was appropriate at the date the convertible notes was issued in May 2004, this would have caused different amount of finance costs charged to the income statement for each accounting period.

(ii) Unconsolidated subsidiaries held for sale

The Group has made the judgement that it is appropriate not to consolidate those subsidiaries which were acquired by the Group and held exclusively with a view for resale. Management had the intention, at the time of acquisition, to dispose those subsidiaries within one year of their acquisition or to undergo the sale of those subsidiaries if the purchaser fails to perform according to the sales and purchase agreement. Such subsidiaries have been excluded from the Group's consolidation for both 2005 and 2006. An agreement was entered during the year and the unconsolidated subsidiaries were disposed as at December 31, 2006 (see note 19 for further details).

(iii) Disposal of PCCW Tower

Under the formal property sales and purchase agreement (the "Property Sales and Purchase Agreement") dated December 21, 2004 for the disposal of the property known as PCCW Tower, on completion of the disposal, the Group has guaranteed to the purchaser a net monthly rental of approximately HK$13.3 million for a period of 5 years up to February 7, 2010. The Group derecognised the property as at February 7, 2005 on the basis that the Group considered that the significant risks and rewards associated with the ownership of PCCW Tower were transferred to the purchaser as of that date as the potential shortfall in covering the guaranteed net monthly rental, if any, was expected to be insignificant as compared to the total sales proceeds of HK$2,808 million. The Property Sales and Purchase Agreement was completed on February 7, 2005 (see note 13 for further details).

3. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS - CONTINUED

b. The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below:

(i) Cost of sales and provisions

The recognition of cost of sales for the Cyberport project, including the payments to the Government of the Hong Kong Special Administrative Region ("HKSAR") pursuant to the Cyberport Project Agreement (note 15a), is based on the estimated total sales proceeds of the residential portion of the Cyberport project and the estimated total development costs, enabling appropriate margins to be recorded at each phase. The Government of the HKSAR is entitled to receive approximately 65 per cent from the surplus cash flow earned from the Cyberport project and forms part of the development costs for the Cyberport project. Significant variations in estimating the future sales proceeds and development costs would affect the amount of the cost of sales and the required provision to the Government of the HKSAR.

The Group has also made certain assumptions when significant risks and rewards of ownership of properties are transferred to purchasers. The estimation on the transfer of risks and reward of ownership of properties would affect the Group's profits for the year and the carrying value of properties under developments.

(ii) Estimated valuation of investment properties

The best evidence of fair value is current prices in an active market for similar leases and other contracts. In the absence of such information, the Group determines the amount within a range of reasonable fair values estimates. In making its estimates, the Group considers both (i) information from the valuations of investment properties performed by external professional valuers by using the open market value approach and (ii) other principal assumptions including the receipt of contractual rentals, expected future market rentals and discount rates to determine the fair value of the investment properties. Had the Group used different future market rentals, discount rates and other assumptions, the fair value of the investment properties would be different and thus caused impact to the consolidated income statement. As at December 31, 2006, the fair value of the investment properties was HK$3,861 million.

3. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS - CONTINUED

(iii) Estimated provision for rental guarantee

The rental guarantee in relation to PCCW Tower is accounted for as a financial liability at fair value through profit or loss. The best evidence of fair value is current prices in an active market for similar leases and other contracts. In the absence of such information, the Group determines the amount within a range of reasonable fair values estimates. The Group's estimate of fair value is based on estimates of receipt of contractual rentals, future market rentals, occupancy rates, maintenance costs and appropriate discount rates. In making its judgement, the Group considers valuations performed by the external professional valuers to determine the fair value of the rental guarantee using discounted cash flow valuation techniques. Had the estimated future market rentals changed or a different discount rate been used, adjustments to the provision for rental guarantee would be made. As at December 31, 2006, the provision for rental guarantee was HK$3 million (see note 31a for further details).

(iv) Goodwill impairment

The Group tests annually whether goodwill has suffered any impairment. The recoverable amounts of cash-generating units have been determined based on value-in-use calculations. These calculations require the use of estimates related to future cash flows of the cash generating units to which the goodwill is attached and appropriate discount rates. As at December 31, 2006, goodwill balance recognised in the consolidated balance sheet was HK$81 million.

(v) Deferred taxation

While deferred tax liabilities are provided in full on all taxable temporary differences, deferred tax assets are recognised only to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised. In assessing the amount of deferred tax assets that need to be recognised, 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 utilise the tax benefits of net operating loss carried forward in the future, adjustments to the recorded amount of net deferred tax assets and taxation expense would be made. As at December 31, 2006, the total deferred tax assets recognised was HK$15 million, with HK$14 million deferred tax assets netted off against the deferred tax liabilities recognised in the consolidated balance sheet (note 28a).

4. TURNOVER

Turnover comprises revenues recognised in respect of the following businesses:

	The Group	
HK$ million	**2006**	2005
Property development	**6,953**	4,821
Property investment	**228**	233
Other businesses	**82**	73
	7,263	5,127

5. SEGMENT INFORMATION

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

a. Business segments

The Group comprises the following main business segments:

— Property development includes property development projects in Hong Kong and Beijing.

— Property investment is the investment in properties in Hong Kong and Beijing.

— Other businesses include the property management division providing services of property management, facilities management, corporate services and asset management.

December 31, 2006 (Amount expressed in Hong Kong dollars unless otherwise stated)

5. SEGMENT INFORMATION - CONTINUED

a. Business segments - Continued

	Property development		Property investment		Other businesses		Elimination		Consolidated	
HK$ million	**2006**	2005	**2006**	2005	**2006**	2005	**2006**	2005	**2006**	2005
REVENUE										
External revenue	**6,953**	4,821	**228**	233	**82**	73	**—**	—	**7,263**	5,127
Inter-segment revenue	**—**	—	**—**	—	**36**	37	**(36)**	(37)	**—**	—
Total revenue	**6,953**	4,821	**228**	233	**118**	110	**(36)**	(37)	**7,263**	5,127
RESULT										
Segment results	**822**	548	**143**	104	**2**	2	**—**	—	**967**	654
Unallocated corporate expenses									**(28)**	(33)
Finance costs									**(130)**	(127)
Interest income									**376**	222
Impairment loss									**(25)**	(6)
Profit before taxation									**1,160**	710
Taxation									**(195)**	(113)
Profit attributable to equity holders of the Company									**965**	597

5. SEGMENT INFORMATION - CONTINUED

a. Business segments - Continued

HK$ million	Property development 2006	Property development 2005	Property investment 2006	Property investment 2005	Other businesses 2006	Other businesses 2005	Elimination 2006	Elimination 2005	Consolidated 2006	Consolidated 2005
OTHER INFORMATION										
Capital expenditure incurred during the year	**12**	—	**134**	7	**1**	6	**—**	—	**147**	13
Depreciation and amortisation	**6**	—	**10**	8	**4**	3	**—**	—	**20**	11
Surplus on revaluation of investment properties credited to the income statement	**—**	—	**2**	16	**—**	—	**—**	—	**2**	16
Impairment loss recognised in the income statement	**—**	—	**—**	—	**25**	6	**—**	—	**25**	6
Provision for doubtful debts	**—**	—	**—**	—	**—**	7	**—**	—	**—**	7
Value of employee services under employee share option scheme	**—**	—	**—**	—	**2**	5	**—**	—	**2**	5
ASSETS										
Segment assets	**8,801**	13,417	**4,014**	3,804	**39**	72	**—**	—	**12,854**	17,293
Investment in unconsolidated subsidiaries held for sale									**—**	45
Unallocated corporate assets									**2,568**	3,306
Consolidated total assets									**15,422**	20,644
LIABILITIES										
Segment liabilities	**6,286**	12,534	**431**	437	**36**	52	**—**	—	**6,753**	13,023
Unallocated corporate liabilities									**1,986**	1,864
Consolidated total liabilities									**8,739**	14,887

5. SEGMENT INFORMATION - CONTINUED

b. Geographical segments

The Group's businesses are managed and operated in two principal economic environments, Hong Kong and mainland China. In presenting information on the basis of geographical segments, segment revenue is based on the geographical location of operations. Segment assets and capital expenditure are based on the geographical location of the assets.

	Revenue from external customers		Segment assets		Capital expenditure incurred during the year	
HK$ million	**2006**	2005	**2006**	2005	**2006**	2005
Hong Kong	**7,038**	4,915	**10,890**	16,877	**13**	6
Mainland China	**225**	212	**4,532**	3,767	**134**	7
	7,263	5,127	**15,422**	20,644	**147**	13

6. FINANCE COSTS

	The Group	
HK$ million	**2006**	2005
Interest expense:		
Convertible notes wholly repayable after 5 years (note 21)	**125**	127
Other finance costs	**5**	—
	130	127

7. PROFIT BEFORE TAXATION

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

	The Group	
HK$ million	**2006**	2005
Crediting:		
Gross rental income from investment properties	**228**	233
Other rental income	**3**	—
Less: outgoings	**(16)**	(21)
Surplus on revaluation of investment properties	**2**	16
Gain on disposal of an investment property	**—**	8
Charging:		
Cost of properties sold	**5,987**	4,119
Depreciation, included in:		
- cost of sales	**1**	1
- general and administrative expenses	**14**	10
Amortisation of leasehold land	**5**	—
Staff costs, included in:		
- cost of sales	**45**	43
- general and administrative expenses	**91**	86
Contributions to defined contribution retirement scheme, included in:		
- cost of sales	**3**	3
- general and administrative expenses	**5**	3
Contributions to defined benefit retirement scheme, included in cost of sales	**—**	1
Auditors' remuneration	**2**	2
Operating lease rental		
- land and buildings	**4**	3
- equipment	**3**	2
Value of employee services under employee share option scheme	**2**	5
Provision for doubtful debts	**—**	7
Net foreign exchange loss	**3**	—

8. DIRECTORS' EMOLUMENTS

a. Cash and cash equivalents paid by the Group during the year

HK$ '000	The Group 2006 Directors' fee	Salaries, allowances, other allowances and benefits in kind	Bonuses	Retirement scheme contributions	The Group 2005 Directors' fee	Salaries, allowances, other allowances and benefits in kind	Bonuses	Retirement scheme contributions
Executive Directors								
Li Tzar Kai, Richard (note i)	—	—	—	—	—	—	—	—
Lee Chi Hong, Robert	—	11,000	7,270	904	—	11,000	7,904	904
Alexander Anthony Arena (note i)	—	—	—	—	—	—	—	—
Hubert Chak (note i)	—	—	—	—	—	—	1,600	—
James Chan	—	3,068	1,600	258	—	2,891	2,379	243
Gan Kim See, Wendy	—	3,068	2,565	322	—	2,891	4,216	253
Independent Non-executive Directors								
Ronald James Blake, OBE, JP (note ii)	42	—	—	—	200	—	—	—
Cheung Kin Piu, Valiant	200	—	—	—	200	—	—	—
Tsang Link Carl, Brian	150	—	—	—	150	—	—	—
Prof Wong Yue Chim, Richard, SBS, JP	200	—	—	—	200	—	—	—
Dr Allan Zeman, GBS, JP (note iii)	175	—	—	—	150	—	—	—
	767	17,136	11,435	1,484	900	16,782	16,099	1,400

8. DIRECTORS' EMOLUMENTS - CONTINUED

a. Cash and cash equivalents paid by the Group during the year - Continued

i. The remuneration of executive directors employed by PCCW, the ultimate holding company of the Group, is borne by PCCW except a bonus was paid to Hubert Chak by the Company in 2005.

ii. Resigned as independent non-executive director on March 17, 2006.

iii Re-designated as independent non-executive director effective July 18, 2006.

iv. The total directors' emoluments for the year ended December 31, 2006, including the amortised share-based compensation, were HK$31 million (2005: HK$39 million).

v. No directors waived the right to receive emoluments during the current and prior years.

December 31, 2006 (Amount expressed in Hong Kong dollars unless otherwise stated)

8. DIRECTORS' EMOLUMENTS - CONTINUED

b. Share-based compensation

For executive directors employed by PCCW, the values of their services under PCCW's share option scheme borne by PCCW, are excluded from the analysis below.

	Grant date	Exercise price of share options HK$	Number of share options/ shares outstanding at beginning of year	Number of 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$'000	Realised benefits (note i) HK$'000
		The Group 2006						
Executive Directors								
Lee Chi Hong, Robert	July 25, 2003	4.35	5,000,000	—	5,000,000	5,000,000	841	—
	February 8, 2005	4.475	1,000,000	—	1,000,000	500,000	299	—
James Chan	July 25, 2003	4.35	210,000	—	210,000	210,000	105	—
Gan Kim See, Wendy	July 25, 2003	4.35	240,000	—	240,000	240,000	121	—
							1,366	—

8. DIRECTORS' EMOLUMENTS - CONTINUED

b. Share-based compensation - Continued

	Grant date	Exercise price of share options	Number of share options/ shares outstanding at beginning of year	Number of 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)	Realised benefits (note i)
		The Group 2005						
		HK$					HK$'000	HK$'000
Executive Directors								
Lee Chi Hong, Robert	July 25, 2003	4.35	5,000,000	—	5,000,000	3,333,333	2,745	—
	February 8, 2005	4.475	1,000,000	—	1,000,000	—	660	—
James Chan	July 25, 2003	4.35	210,000	—	210,000	140,000	188	—
Gan Kim See, Wendy	July 25, 2003	4.35	240,000	—	240,000	160,000	215	—
							3,808	—

i. Realised benefits

No director exercised share options in 2006 and 2005. The realised benefits represent the market value of the relevant shares at the date of transfer.

8. DIRECTORS' EMOLUMENTS - CONTINUED

b. Share-based compensation - Continued

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 at the date of grant. Share-based compensation is amortised in the income statement over the vesting period of the related share options. These values do not represent realisable gains which are affected by a combination of a number of factors, including, performance of PCCW's share price, vesting period and timing of exercise. The details of these share options are disclosed under the section "Share Options and Directors' Right to Acquire Shares or Debentures" in the Report of the Directors and note 25 to the consolidated financial statements.

9. FIVE TOP-PAID EMPLOYEES

a. Of the five highest paid individuals in the Group, three (2005: three) are directors whose emoluments are set out in note 8. Details of the emoluments of the other two highest paid individuals (2005: two) were as follows:

	The Group	
HK$ million	**2006**	2005
Salaries and other short-term employee benefits	**8**	7
Bonuses	**2**	3
Post-employment benefits	**1**	1
	11	11

9. FIVE TOP-PAID EMPLOYEES - CONTINUED

b. The emoluments of the remaining two individuals (2005: two) are within the emolument ranges as set out below:

	The Group Number of individuals	
	2006	2005
HK$4,200,001 - HK$4,300,000	**1**	—
HK$5,100,001 - HK$5,200,000	**—**	1
HK$5,700,001 - HK$5,800,000	**—**	1
HK$6,000,001 - HK$6,100,000	**1**	—
	2	2

The employees, whose emoluments are disclosed above, include senior executives who were also directors of the subsidiaries during the year. No directors waived the right to receive emoluments during the current and prior years.

10. TAXATION

Hong Kong profits tax has been provided at the rate of 17.5 per cent (2005: 17.5 per cent) on the estimated assessable profits for the year.

Mainland China income tax has been calculated on the estimated assessable profits for the year at the rates prevailing in the respective jurisdiction.

	The Group	
HK$ million	**2006**	2005
Hong Kong profits tax		
- Provision for current year	**146**	95
- Over provision in respect of prior years	**(1)**	(1)
Mainland China income tax		
- Provision for current year	**4**	—
- Under provision in respect of prior years	**1**	—
Deferred taxation relating to the origination and reversal of temporary differences (note 28)	**45**	19
	195	113

10. TAXATION - CONTINUED

Reconciliation between taxation charge and the Group's accounting profit at applicable tax rates is set out below:

	The Group	
HK$ million	**2006**	2005
Profit before taxation	**1,160**	710
Notional tax on profit before taxation, calculated at 17.5 per cent	**203**	124
Income not subject to taxation	**(65)**	(40)
Expenses not deductible for taxation purposes	**32**	34
Utilisation of tax losses not previously recognised	**—**	(21)
Tax losses not recognised	**2**	—
Over provision in respect of prior years	**—**	(1)
Effect of different tax rate of subsidiaries operating in mainland China	**23**	17
Taxation charge	**195**	113

11. DIVIDENDS

HK$ million	**2006**	2005
Interim dividend of 1.5 Hong Kong cents per ordinary share (2005: 1.5 Hong Kong cents per ordinary share) paid	**36**	36
Final dividend proposed after the balance sheet date of 5.5 Hong Kong cents per ordinary share (2005: 5.5 Hong Kong cents per ordinary share)	**132**	132
	168	168

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

12. EARNINGS PER SHARE

The calculations of basic and diluted earnings per share based on the share capital of the Company are as follows:

	2006	2005
Earnings (HK$ million)		
Earnings for the purpose of calculating the basic earnings per share	965	597
Finance costs on convertible notes	125	126
Earnings for the purpose of calculating the diluted earnings per share	1,090	723

	2006	2005
Number of shares		
Weighted average number of ordinary shares for the purpose of calculating the basic earnings per share	2,402,459,873	2,318,405,078
Effect of dilutive potential ordinary shares on conversion of convertible notes and employee share option	672,222,222	756,277,017
Weighted average number of ordinary shares for the purpose of calculating the diluted earnings per share	3,074,682,095	3,074,682,095

13. INVESTMENT PROPERTIES

	The Group	
HK$ million	2006	2005
Balance at January 1,	3,607	6,316
Addition	127	—
Disposal	—	(2,800)
Surplus on revaluation of investment properties	2	16
Exchange differences	125	75
Balance at December 31,	3,861	3,607

13. INVESTMENT PROPERTIES - CONTINUED

Investment properties held in Hong Kong and mainland China were revalued as at December 31, 2006 by an independent valuer. The basis of valuation for investment properties was open market value. The fair value gain during the year amounted to HK$2 million (2005: HK$16 million) was credited to the consolidated income statement under surplus on revaluation of investment properties.

In the consolidated income statement, cost of sales includes HK$16 million (2005: HK$21 million) direct operating expenses that generate rental income while there was no direct operating expenses relating to investment properties that were unlet.

On December 21, 2004, Partner Link Investments Limited ("Partner Link"), an indirectly wholly-owned subsidiary of the Company, entered into the Property Sales and Purchase Agreement with Richly Leader Limited (the "Purchaser"), a third party, for the disposal of PCCW Tower for a consideration of HK$2,808 million in cash. The consideration was arrived at after arm's length negotiations. The Property Sales and Purchase Agreement was completed on February 7, 2005 and the Group had recorded a gain on disposal of HK$8 million for 2005 (see note 31a for details of guarantee to the Purchaser by the Group in relation to this transaction).

The carrying amount of investment properties is analysed as follows:

	The Group	
HK$ million	**2006**	2005
Held in Hong Kong		
On medium-term lease (10-50 years)	**35**	33
Held in mainland China		
On long lease (over 50 years)	**730**	696
On medium-term lease (10-50 years)	**3,096**	2,878
	3,861	3,607

14. PROPERTY, PLANT AND EQUIPMENT

HK$ million	The Group Other plant and equipment
At January 1, 2005	
At cost	53
Less : Accumulated depreciation	(18)
Net book value	35
Net book value at January 1, 2005	35
Additions	13
Depreciation	(11)
Net book value at December 31, 2005	37
At December 31, 2005	
At cost	67
Less: Accumulated depreciation	(30)
Net book value	37
Net book value at January 1, 2006	**37**
Additions	**20**
Depreciation	**(15)**
Exchange differences	**1**
Net book value at December 31, 2006	**43**
At December 31, 2006	
At cost	**89**
Less: Accumulated depreciation	**(46)**
Net book value	**43**

15. PROPERTIES UNDER DEVELOPMENT/HELD FOR SALE

	The Group	
HK$ million	**2006**	2005
Properties under development	**3,210**	7,413
Less: Properties under development classified as non-current assets	**(1,979)**	(1,875)
	1,231	5,538
Properties held for sale	**290**	131
Properties under development/held for sale	**1,521**	5,669

a. Pursuant to an agreement dated May 17, 2000 entered into with the Government of the HKSAR ("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 of the HKSAR at no consideration. The associated costs incurred have formed part of the development costs of the residential portion. Pre-sales of residential portion of the Cyberport project commenced in February 2003.

16. INTEREST IN LEASEHOLD LAND

The Group's interest in leasehold land represents prepaid operating lease payments and their net book value is analysed as follows:

	The Group		
HK$ million	Lease in Hong Kong over 50 years	Lease in mainland China over 50 years	Total
Balance at January 1, 2005	155	—	155
Transfer to properties under development	(155)	—	(155)
Balance at December 31, 2005	—	—	—
Balance at January 1, 2006	—	—	—
Addition	—	**495**	**495**
Amortisation	—	**(5)**	**(5)**
Exchange differences	—	**12**	**12**
Balance at December 31, 2006	—	**502**	**502**

The leasehold land transferred to properties under development in 2005 was subjected to amortisation over the period of the lease on a straight-line basis. The amount of amortisation charge of the leasehold land had been capitalised as part of the cost of properties under development. As at December 31, 2006, the net book value of leasehold land included in properties under development was approximately HK$155 million (2005: HK$155 million).

17. GOODWILL

HK$ million	The Group 2006	2005
Cost		
Balance at January 1,	**81**	84
Elimination of accumulated amortisation (note a)	—	(3)
Balance at December 31,	**81**	81
Accumulated amortisation		
Balance at January 1, (note a)	—	(3)
Elimination against cost of goodwill (note a)	—	3
Balance at December 31,	—	—
Net Book Value		
Balance at December 31,	**81**	81
Balance at January 1,	**81**	81

a. From January 1, 2005 onwards, the Group ceased amortisation of goodwill and the accumulated amortisation as at December 31, 2004 was eliminated with a corresponding decrease in the cost of goodwill.

18. INVESTMENT IN SUBSIDIARIES

	The Company	
HK$ million	**2006**	2005
Unlisted shares, at cost	**2,870**	2,870

Dividends from the mainland China entities accounted for as subsidiaries will be declared based on the profits in the statutory financial statements of these mainland China entities which are prepared using accounting principles generally accepted in The People's Republic of China. Such profits are different from the amounts reported under HKFRS.

As at December 31, 2006, the Group has financed the operations of certain of its entities in mainland China in the form of shareholder's loans amounting to approximately US$199 million (2005: US$199 million) which have not been registered with the State Administration of Foreign Exchange. As a result, remittances in foreign currency of these amounts outside mainland China may be restricted.

The balances with subsidiaries are unsecured, non-interest bearing and have no fixed terms of repayment. The amounts due from subsidiaries as at December 31, 2006 were HK$2,423 million (2005: HK$4,039 million).

As at December 31, 2006, 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
ACCA Investment Limited	Hong Kong	Property holding	HK$2	—	100%
Atkins Developments Limited	British Virgin Islands	Investment holding	US$1	—	100%
Beijing Jing Wei House and Land Estate Development Co., Ltd. 北京京威房地產開發有限公司[1]	The People's Republic of China	Property development	US$100,000,000	—	100%

18. INVESTMENT 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	Equity interest attributable to the Group Indirectly
Beijing Jingwei Property Management Co., Ltd. 北京京威物業管理有限公司 [2]	The People's Republic of China	Property management	US$150,000	—	100%
北京啟夏房地產開發有限公司 [3]	The People's Republic of China	Property development	US$33,000,000	—	100%
Carlyle International Limited	Hong Kong	Entrustment work	HK$2	—	100%
Carmay Investment Limited	Hong Kong	Property holding	HK$2	—	100%
Cyber-Port Limited	Hong Kong	Property development	HK$2	—	100%
Cyber-Port Management Limited	Hong Kong	Provision of project management services	HK$2	—	100%
Excel Bright Properties Limited	British Virgin Islands	Investment holding	US$2	—	100%
Extra Lite International Limited	British Virgin Islands	Investment holding	US$1	—	100%
Gain Score Limited	British Virgin Islands	Investment holding	US$1	—	100%
Ipswich Holdings Limited	British Virgin Islands	Investment holding	US$2	100%	—
Island South Property Management Limited	Hong Kong	Property management	HK$2	—	100%
Madeline Investments Limited 盈科大衍地產發展有限公司	Hong Kong	Trademark registrant	HK$2	—	100%
Midgre Properties Limited	British Virgin Islands	Investment holding	US$2	—	100%
Pacific Century Paramount Real Estate Company Limited	Hong Kong	Estate agency	HK$1	—	100%

December 31, 2006 (Amount expressed in Hong Kong dollars unless otherwise stated)

18. INVESTMENT 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
Partner Link Investments Limited	British Virgin Islands/ Hong Kong	Investment holding	US$1	—	100%
PCPD Corporate Services Limited	Hong Kong	Corporate services	HK$1	—	100%
PCPD Facilities Management Limited	Hong Kong	Property management	HK$2	—	100%
PCPD Operations Limited	British Virgin Islands/ Hong Kong	Corporate services	US$1	—	100%
PCPD Property Management Limited	British Virgin Islands	Provision of management services	US$2	—	100%
PCPD Real Estate Agency Limited	Hong Kong	Property sales agency	HK$2	—	100%
PCPD Services Limited	Hong Kong	Provision of management services	HK$2	—	100%
PCPD Wealth Limited	Hong Kong	Investment holding	HK$1	—	100%
Pride Pacific Limited	Hong Kong	Financing	HK$2	—	100%
Prime Asset Investment Limited	Hong Kong	Investment holding	HK$1	—	100%
Smart Phoenix Limited	British Virgin Islands	Property development	US$1	—	100%
Talent Master Investments Limited	British Virgin Islands/ Hong Kong	Property development	US$1	—	100%
Toppest Class Limited	British Virgin Islands	Investment holding	US$1	—	100%
Wise Union Enterprises Limited	British Virgin Islands	Investment holding	US$1	—	100%

Notes:

1 Represents a Sino-foreign cooperative joint venture.

2 Represents a wholly foreign investment enterprise.

3 Represents a wholly foreign owned enterprise.

19. INVESTMENT IN UNCONSOLIDATED SUBSIDIARIES HELD FOR SALE

	The Group	
HK$ million	**2006**	2005
Unlisted shares, at cost	—	55
Less: Provision for impairment in value	—	(10)
	—	45

In respect of certain subsidiaries of the Company acquired and held exclusively with a view to resale, the investment in these subsidiaries of the Company was 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. The results of these unconsolidated subsidiaries were excluded from the consolidated income statement except that the Group had recorded impairment provision of HK$6 million in 2005.

An agreement was entered during the year with Asian Century Properties Limited, a British Virgin Islands company, for the disposal of the Company's entire interest in the gas operation, payable by instalments in 2006. The Group has received HK$10 million from Asian Century Properties Limited in 2006 and a provision of HK$25 million has been made against the outstanding sales consideration receivable. This provision has reduced the carrying value of the receivable to HK$10 million, which has been recovered in January 2007.

20. 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.

b. Restricted cash

Pursuant to the Cyberport Project Agreement, the Group has a restricted cash balance of approximately HK$826 million as at December 31, 2006 (2005: HK$1,332 million) held in specific bank accounts. The uses of the funds are specified in the Cyberport Project Agreement.

20. CURRENT ASSETS AND LIABILITIES – CONTINUED

c. Accounts receivable, net

An aging analysis of accounts receivable is set out below:

	The Group	
HK$ million	**2006**	2005
Current	**418**	172
One to three months	**—**	64
More than three months	**20**	3
	438	239

The normal credit period granted by the Group ranges up to 30 days from the date of the invoice unless there is separate mutual agreement on extension of the credit period.

d. Accounts payable

An aging analysis of accounts payable is set out below:

	The Group	
HK$ million	**2006**	2005
Current	**80**	181
One to three months	**5**	5
More than three months	**8**	—
	93	186

20. CURRENT ASSETS AND LIABILITIES – CONTINUED

e. Gross amounts due to customers for contract works

	The Group	
HK$ million	**2006**	2005
Contract costs incurred plus attributable profits less foreseeable losses	**779**	784
Less: Estimated value of work performed	**(786)**	(795)
	(7)	(11)

The total amount of progress billings, included in the estimated value of work performed as at December 31, 2006, was approximately HK$786 million (2005: HK$782 million).

21. LONG-TERM BORROWINGS

	The Group		
	2006		
HK$ million	**Long-term borrowings**	**Convertible notes reserve**	**Total**
Balance at January 1, 2006	**1,803**	**769**	**2,572**
Finance costs charged to consolidated income statement (note a)	**125**	**—**	**125**
Interest paid	**(12)**	**—**	**(12)**
	1,916	**769**	**2,685**
Interest amount payable included in amounts due to fellow subsidiaries	**(12)**	**—**	**(12)**
Balance at December 31, 2006	**1,904**	**769**	**2,673**
Less: Amount classified as current liabilities	**(24)**	**—**	**(24)**
	1,880	**769**	**2,649**

21. LONG-TERM BORROWINGS – CONTINUED

		The Group 2005	
HK$ million	Long-term borrowings	Convertible notes reserve	Total
Balance at January 1, 2005	2,516	1,160	3,676
Finance costs charged to consolidated income statement (note a)	127	—	127
Reduction in balances as a result of the Conversion (note b)	(816)	(391)	(1,207)
Interest paid	(12)	—	(12)
	1,815	769	2,584
Interest amount payable included in amounts due to fellow subsidiaries	(12)	—	(12)
Balance at December 31, 2005	1,803	769	2,572
Less: Amount classified as current liabilities	(24)	—	(24)
	1,779	769	2,548

21. LONG-TERM BORROWINGS – CONTINUED

	The Company		
	2006		
HK$ million	**Long-term borrowings**	**Convertible notes reserve**	**Total**
Balance at January 1, 2006	**1,779**	**769**	**2,548**
Novation of convertible notes (tranche B note due 2014) to an indirectly wholly-owned subsidiary (note c)	**(1,779)**	**(769)**	**(2,548)**
Balance at December 31, 2006	**—**	**—**	**—**

	The Company		
	2005		
HK$ million	Long-term borrowings	Convertible notes reserve	Total
Balance at January 1, 2005	2,516	1,160	3,676
Finance costs charged to income statement (note a)	127	—	127
Reduction in balances as a result of the Conversion (note b)	(816)	(391)	(1,207)
Interest paid	(12)	—	(12)
	1,815	769	2,584
Interest amount payable included in amounts due to fellow subsidiaries	(12)	—	(12)
Balance at December 31, 2005	1,803	769	2,572
Less: Amount classified as current liabilities	(24)	—	(24)
	1,779	769	2,548

21. LONG-TERM BORROWINGS – CONTINUED

Long-term borrowings comprise the outstanding principal amount of the convertible notes or any part that may, at the discretion of PCCW or its designated subsidiary, the holder of the notes, be converted into the ordinary shares of the Company, issued to PCCW or its designated subsidiary at any time and from time to time on or after the date of issue (but on or prior to the maturity date) at the relevant conversion price.

a. Interest expense on the convertible notes is calculated using the effective interest method by applying the effective interest rate of 6.87 per cent to the liability component.

b. On February 24, 2005, PCCW elected to convert the tranche A note due 2011 with a principal amount of HK$1,170 million into new shares of HK$0.10 each at HK$2.25 per share pursuant to the terms of the tranche A note (the "Conversion"). The Company issued 520,000,000 ordinary shares to a wholly-owned subsidiary of PCCW as a result of the Conversion and increased its issued equity by HK$52 million (note 23b(i)).

c. The tranche B note due 2014 with a principal amount of HK$2,420 million could be converted into new shares of HK$0.10 each at a conversion price of HK$3.60 per share, subject to adjustment. The tranche B note may be redeemed at 120 per cent of the outstanding principal amount if conversion does not occur. Effective from January 1, 2006, the Company novated the tranche B note to an indirectly wholly-owned subsidiary at a consideration of HK$2,128 million. The terms of the tranche B note remain unchanged after the novation that the noteholder retains the right to convert such note into 672,222,222 shares of the Company at HK$3.6 per share. The Company has granted rights to this indirectly wholly-owned subsidiary to purchase the same number of shares of the Company at HK$3.6 per share with expiry in 2014. The Company has recorded this call option at its fair value on the date of grant at HK$222 million under other reserve in equity (note 26).

22. PROVISIONS

	The Group		
	2006		
HK$ million	Payment to the Government (note a)	Others	Total
Balance at January 1, 2006	**6,705**	**29**	**6,734**
Additional provisions included in properties under development	**390**	**—**	**390**
Additional provisions made	**—**	**16**	**16**
Provisions settled	**(3,615)**	**(20)**	**(3,635)**
Balance at December 31, 2006	**3,480**	**25**	**3,505**
Less: Amount classified as current liabilities	**(1,889)**	**(25)**	**(1,914)**
	1,591	**—**	**1,591**

	The Group		
	2005		
HK$ million	Payment to the Government (note a)	Others	Total
Balance at January 1, 2005	6,380	31	6,411
Additional provisions included in properties under development	1,648	—	1,648
Additional provisions made	—	12	12
Provisions settled	(1,323)	(14)	(1,337)
Balance at December 31, 2005	6,705	29	6,734
Less: Amount classified as current liabilities	(5,270)	(29)	(5,299)
	1,435	—	1,435

December 31, 2006 (Amount expressed in Hong Kong dollars unless otherwise stated)

22. PROVISIONS – CONTINUED

a. Pursuant to the Cyberport Project Agreement (note 15a), the Government of the HKSAR shall be entitled to receive payments of approximately 65 per cent from the surplus cash flow 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 of the HKSAR is included in properties under development as the amount is considered as a part of the development costs for the Cyberport project. The provision is based on estimated sales proceeds of the residential portion of the project and the estimated development costs of the Cyberport project. The estimated amount to be paid to the Government of the HKSAR during the forthcoming year is classified as current liabilities.

23. ISSUED EQUITY

	The Group	
	Number of shares	**Issued equity**
		HK$ million
	(note a)	**(note a)**
Ordinary shares of HK$0.10 each at January 1, 2005	1,882,459,873	3,424
Issue of new shares for the Conversion of convertible notes tranche A (note b(i))	520,000,000	1,207
Ordinary shares of HK$0.10 each at December 31, 2005 and January 1, 2006	**2,402,459,873**	**4,631**
Reduction of share premium (note c)	—	(322)
Ordinary shares of HK$0.10 each at December 31, 2006	**2,402,459,873**	**4,309**

a. Due to the use of reverse acquisition basis of accounting (as stated in note 2(d) to the 2004 Financial Statements), the amount of issued equity, which includes share capital and share premium in the consolidated balance sheet, represents the amount of issued equity of the legal subsidiary, Ipswich Holdings Limited, at date of completion of the reverse acquisition plus equity changes attributable to the Group after the reverse acquisition. The equity structure (i.e. the number and type of shares) reflects the equity structure of the legal parent, Pacific Century Premium Developments Limited for all accounting periods presented.

23. ISSUED EQUITY – CONTINUED

b. The following is the movement in the share capital of the Company:

	The Company	
	Number of shares	**Nominal value**
		HK$ million
Authorised:		
Ordinary shares of HK$0.10 each at January 1, 2005, December 31, 2005 and December 31, 2006	**10,000,000,000**	**1,000**
Issued and fully paid:		
Ordinary shares of HK$0.10 each at January 1, 2005	**1,882,459,873**	**188**
Issue of new shares for the Conversion of convertible notes tranche A (note (i))	**520,000,000**	**52**
Ordinary shares of HK$0.10 each at December 31, 2005 and December 31, 2006	**2,402,459,873**	**240**

(i) On February 24, 2005, PCCW elected to convert the tranche A note due 2011 with a principal amount of HK$1,170 million into new shares of HK$0.10 each at HK$2.25 per share pursuant to the terms of the tranche A note (the "Conversion"). The Company issued 520,000,000 ordinary shares to a wholly-owned subsidiary of PCCW as a result of the Conversion and increased its issued equity by HK$52 million. Prior to the Conversion, PCCW held approximately 51.07 per cent of the issued shares of the Company. Immediately after the Conversion, PCCW held approximately 61.66 per cent of the enlarged issued share capital of the Company.

c. On May 16, 2006, a special resolution was passed at the Company's Annual General Meeting approving the reduction of share premium by cancelling a sum of approximately HK$322 million standing to the credit of the Company's share premium account against the accumulated losses of the Company of same amount.

24. EMPLOYEE RETIREMENT BENEFITS

a. Defined benefit retirement schemes

A number of employees of the Group are entitled to join the defined benefit retirement schemes ("DB Schemes"), operated by PCCW, which provide lump sum benefits to employees upon resignation and retirement. The DB Schemes are final salary defined benefit retirement schemes. The scheme assets are administered by independent trustees and are maintained independently.

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.

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 retirement schemes operated by PCCW for future services, with their benefits prior to that date remained unchanged) were transferred to defined contribution retirement schemes operated by PCCW ("Transfer of past DB benefits") effective November 1, 2005. The transfer value of each member was calculated to be the leaving service benefits as at October 31, 2005, plus enhancement, if any. Enhancement is 50 per cent of the increase in vested benefit based on vesting service up to January 31, 2006. After the Transfer of past DB benefits, the DB Schemes no longer have defined benefit obligation attributed to the active members. This Transfer of past DB benefits was considered as a curtailment and settlement event under HKAS 19 "Employee Benefits". In 2005, the Group injected approximately HK$1 million to the DB Schemes to make up part of the funding deficit as at October 31, 2005.

b. Defined contribution retirement scheme

Employees of the Group are also entitled to join the defined contribution retirement schemes operated by PCCW, 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 retirement 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 per cent 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.

25. EQUITY COMPENSATION BENEFITS

Share option scheme

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

Under the 2005 Scheme, the board of directors of the Company 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 2005 Scheme. The exercise price of the options under the 2005 Scheme is determined by the board of directors of the Company in its absolute discretion but in any event shall not be less than the highest of (i) the closing price of the shares of the Company 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 the Company 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 the Company 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 Scheme and any other share option schemes of the Company must not exceed 30 per cent of the shares in issue from time to time. In addition, the maximum number of shares in respect of which options may be granted under the 2005 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 the Company) exceed 10 per cent of the issued share capital of the Company on May 23, 2005 (or some other date if renewal of this limit is approved by shareholders).

December 31, 2006 (Amount expressed in Hong Kong dollars unless otherwise stated)

25. EQUITY COMPENSATION BENEFITS – CONTINUED

Share option scheme – Continued

Details of share options granted by the Company pursuant to the 2003 share option scheme and the share options outstanding at December 31, 2006, are as follows:

(i) Movements in share options

	Number of options	
	2006	2005
Balance at January 1, and December 31, (note (ii))	**10,000,000**	10,000,000
Options vested at December 31,	**10,000,000**	10,000,000

(ii) Details of share options outstanding as at December 31,

			2006		2005	
Date of grant	Exercise period	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
			2	**10,000,000**	2	10,000,000

During the years ended December 31, 2006 and December 31, 2005, no share options were granted under the 2005 Scheme or 2003 share option scheme. All of the share options granted related to 2003 share option scheme remained unexpired and unexercised as at December 31, 2006.

25. EQUITY COMPENSATION BENEFITS – CONTINUED

Share option scheme – Continued

(iii) Movements in the number of share options outstanding and their related weighted average exercise prices are as follows:

	2006		2005	
	Average exercise price in HK$ per share	**Number of options**	Average exercise price in HK$ per share	Number of options
Balance at January 1, and December 31,	**2.375**	**10,000,000**	2.375	10,000,000

All the share options outstanding at the end of the year will expire on December 19, 2014.

The total fair value of the share options granted in December 2004 under 2003 share option scheme determined using the trinomial option pricing model was HK$12.9 million using share price of HK$2.325, exercise price of HK$2.375, risk-free interest rate of 3.95 per cent, volatility of 0.50 with expected life for 10 years and no expected dividend per share. As the share options were vested before January 1, 2005, no expenses were charged to the current and prior years' consolidated income statements as allowed by the transitional provision of HKFRS 2 "Share-based Payment".

26. RESERVES

	The Company							
	2006							
HK$ million	Share premium	Capital redemption reserve	Convertible notes reserve	Other reserve	Contributed surplus	Employee share-based compensation reserve	(Deficit)/ Retained earnings	Total
Balance at January 1, 2006	4,193	1	769	—	189	15	(322)	4,845
Profit for the year	—	—	—	—	—	—	373	373
Total recognised income for 2006	—	—	—	—	—	—	373	373
Share premium reduction (note 23c)	(322)	—	—	—	—	—	322	—
Novation of convertible notes (tranche B note due 2014) to an indirectly wholly-owned subsidiary	—	—	(769)	547	—	—	—	(222)
Call option issued to an indirectly wholly-owned subsidiary in relation to novation of convertible notes (tranche B note due 2014) (note 21c)	—	—	—	222	—	—	—	222
Value of employee services under employee share option scheme	—	—	—	—	—	2	—	2
2005 final dividend paid	—	—	—	—	(132)	—	—	(132)
2006 interim dividend paid	—	—	—	—	(36)	—	—	(36)
Balance at December 31, 2006	3,871	1	—	769	21	17	373	5,052

26. RESERVES – CONTINUED

	The Company							
	2005							
HK$ million	Share premium	Capital redemption reserve	Convertible notes reserve	Other reserve	Contributed surplus	Employee share-based compensation reserve	Deficit	Total
Balance at January 1, 2005	3,038	1	1,160	—	393	10	(197)	4,405
Loss for the year	—	—	—	—	—	—	(125)	(125)
Total recognised loss for 2005	—	—	—	—	—	—	(125)	(125)
Issue of ordinary shares upon conversion of convertible notes	1,155	—	(391)	—	—	—	—	764
Value of employee services under employee share option scheme	—	—	—	—	—	5	—	5
2004 final dividend paid	—	—	—	—	(168)	—	—	(168)
2005 interim dividend paid	—	—	—	—	(36)	—	—	(36)
Balance at December 31, 2005	4,193	1	769	—	189	15	(322)	4,845

27. EMPLOYEE SHARE-BASED COMPENSATION RESERVE

	The Group	
HK$ million	**2006**	2005
At January 1,	**15**	10
Employee share option benefits	**2**	5
At December 31,	**17**	15

The share options are granted to the directors and employees of the Group to subscribe for shares in PCCW or the Company in accordance with the terms and conditions of the share option scheme (note 2(v)(iii)).

28. DEFERRED TAXATION

a. The components of deferred tax liabilities recognised in the consolidated balance sheet and the movements during the year are as follows:

	The Group				
	2006				
HK$ million	Accelerated tax depreciation	Revaluation of properties	Tax losses	Others	Total
At January 1, 2006	196	146	(11)	(12)	319
Charged/(Credited) to consolidated income statement (note 10)	33	(3)	11	3	44
Exchange differences	7	5	—	—	12
At December 31, 2006	236	148	—	(9)	375

28. DEFERRED TAXATION – CONTINUED

a. The components of deferred tax liabilities recognised in the consolidated balance sheet and the movements during the year are as follows: – Continued

	The Group				
	2005				
HK$ million	Accelerated tax depreciation	Revaluation of properties	Tax losses	Others	Total
At January 1, 2005	186	65	—	9	260
Charged/(Credited) to consolidated income statement (note 10)	48	3	(11)	(21)	19
Reclassification of deferred tax assets previously provided	(41)	75	—	—	34
Exchange differences	3	3	—	—	6
At December 31, 2005	196	146	(11)	(12)	319

	The Group	
HK$ million	**2006**	2005
Deferred tax liabilities recognised in the consolidated balance sheet	**389**	344
Less: Amount netted off against deferred tax assets recognised in the consolidated balance sheet	**(14)**	(25)
Balance at December 31,	**375**	319

28. DEFERRED TAXATION – CONTINUED

b. Deferred tax assets are recognised for tax losses carried forward to the extent that realisation of the related tax benefit through utilisation against future taxable profits is probable. Movements in deferred tax assets during the year is as follows:

	The Group	
HK$ million	**2006**	2005
Balance at January 1,	**2**	2
Charged to consolidated income statement (note 10)	**(1)**	—
Balance at December 31,	**1**	2

c. The Group has unutilised estimated tax losses of HK$136 million as at December 31, 2006 (2005: HK$71 million) to be carried forward for deduction against future taxable profits. The tax losses are mainly relating to Hong Kong companies which can be carried forward indefinitely.

29. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT

a. Reconciliation of profit before taxation to net cash (outflow)/inflow from operating activities

	The Group	
HK$ million	**2006**	2005
Profit before taxation	**1,160**	710
Adjustment for:		
Interest income	**(376)**	(222)
Finance costs	**130**	127
Gain on disposal of an investment property	**—**	(8)
Depreciation	**15**	11
Amortisation of leasehold land	**5**	—
Foreign exchange loss	**2**	—
Provision for impairment loss	**25**	6
Provision for doubtful debts	**—**	7
Value of employee services under employee share option scheme	**2**	5
Provision for rental guarantee	**—**	41
Surplus on revaluation of investment properties	**(2)**	(16)
Operating profit before changes in working capital	**961**	661

29. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT – CONTINUED

a. Reconciliation of profit before taxation to net cash (outflow)/inflow from operating activities – Continued

	The Group	
HK$ million	**2006**	2005
Decrease/(Increase) in operating assets:		
- properties under development/held for sale	**4,044**	(838)
- interest in leasehold land	**(260)**	—
- other non-current receivables	**(7)**	—
- accounts receivable	**(199)**	(147)
- prepayments, deposits and other current assets	**32**	(16)
- sales proceeds held in stakeholders' accounts	**821**	125
- restricted cash	**506**	(428)
- amounts due from fellow subsidiaries	**5**	2
- amounts due from related companies	**(3)**	5
Increase/(Decrease) in operating liabilities:		
- accounts payable, accruals, other payables and deferred income	**(491)**	129
- provisions	**(3,229)**	323
- deposits received on sales of properties	**(724)**	822
- gross amounts due to customers for contract work	**(4)**	6
- amount due to ultimate holding company	**(1,985)**	(727)
- amounts due to fellow subsidiaries	**(7)**	2
- other long-term liabilities	**(19)**	(46)
Cash Used In Operations	**(559)**	(127)
Interest paid	**(24)**	(28)
Interest received	**389**	198
Tax paid		
- Hong Kong profits tax paid	**(241)**	(2)
- mainland China income tax paid	**—**	(1)
Net Cash (Outflow)/Inflow from Operating Activities	**(435)**	40

29. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT – CONTINUED

b. Analysis of cash and cash equivalents

	The Group	
HK$ million	**2006**	2005
Cash and bank balances	**3,444**	4,686
Less: Short-term deposits	**(173)**	(655)
Less: Restricted cash	**(826)**	(1,332)
Cash and cash equivalents at December 31,	**2,445**	2,699

30. COMMITMENTS

a. Capital

	The Group	
HK$ million	**2006**	2005
Authorised and contracted for	**1,739**	2,120
Authorised but not contracted for	**659**	772
	2,398	2,892

30. COMMITMENTS – CONTINUED

a. Capital – Continued

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

	The Group	
HK$ million	**2006**	2005
Property development for Cyberport project (note (i))	**2,181**	2,735
Property development for other projects	**171**	141
Investment properties	**37**	—
Acquisition of property, plant and equipment	**2**	14
Others	**7**	2
	2,398	2,892

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

30. COMMITMENTS – CONTINUED

b. Operating leases

(i) As at December 31, 2006, the total future minimum lease payments under non-cancellable operating leases were payable as follows:

Land and buildings (as lessee)

	The Group	
HK$ million	**2006**	2005
Within 1 year	**7**	6
After 1 year but within 5 years	**12**	2
	19	8

The leases typically run for an initial period of one to five years. None of these leases include contingent rentals.

Equipment (as lessee)

	The Group	
HK$ million	**2006**	2005
Within 1 year	**2**	7
After 1 year but within 5 years	**—**	1
	2	8

The leases typically run for an initial period of one to five years. None of these leases include contingent rentals.

30. COMMITMENTS – CONTINUED

b. Operating leases – Continued

(ii) The Group leases out properties under operating leases. The leases typically run for an initial period of one to ten years. Two of the leases include contingent rental with reference to the turnover of the lessees' operations. As at December 31, 2006, the total future minimum lease receipts under non-cancellable operating leases were receivable as follows:

Land and buildings (as lessor)

	The Group	
HK$ million	**2006**	2005
Within 1 year	**178**	196
After 1 year but within 5 years	**281**	332
After 5 years	**1**	45
	460	573

31. CONTINGENT LIABILITIES

The contingent liabilities of the Group not provided for in the financial statements are set out as follows:

	The Group	
HK$ million	**2006**	2005
Performance guarantee	**1**	1

31. CONTINGENT LIABILITIES – CONTINUED

a. Under the Property Sales and Purchase Agreement (note 13), on completion of the disposal of the PCCW Tower, there is a rental guarantee pursuant to which Partner Link 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 up to February 7, 2010. 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. The Group had also made a provision of approximately HK$41 million in relation to the rental guarantee over the remaining term of the guarantee period in 2005. These amounts have been included in "Other loss" in the consolidated income statement in 2005. The Group has updated the assessment on the rental guarantee as at December 31, 2006 and considered no further provision for rental guarantee is required.

b. In relation to the novation of the convertible notes (tranche B note due 2014) by the Company to an indirectly wholly-owned subsidiary, effective from January 1, 2006, the Company has provided a guarantee to the noteholder in respect of the performance of the subsidiary's obligation under the convertible notes (tranche B note due 2014) including the due and punctual payment of all sums under the convertible notes and the issuances of 672,222,222 shares of the Company at HK$3.6 per share upon conversion of the convertible notes by the noteholder (note 21c). Such guarantee has no impact to the Group's consolidated financial statements.

32. BANKING FACILITY

An indirectly wholly-owned subsidiary of the Company had been granted a banking facility amounting to approximately HK$20 million from a bank for the purpose of providing guarantee to the Government of the HKSAR. Such facility is to be secured by a bank deposit placed by the subsidiary from time to time to secure the amount of guarantee issued by the bank. No guarantee was issued by the bank under this banking facility as at December 31, 2006 and December 31, 2005.

33. MATERIAL RELATED PARTY TRANSACTIONS

The Group is controlled by PCCW which owns 61.66 per cent of the Company's shares. The remaining 38.34 per cent of the shares are widely held.

The following transactions were carried out with related parties:

a. During the year, the Group had the following significant transactions with related companies:

	The Group	
HK$ million	**2006**	2005
Sales of services:		
- Fellow subsidiaries		
Facility management services	**45**	47
Office leases rental	**11**	14
- Related companies		
Facility management services	**24**	23
Office leases rental	**2**	—
Other services	**2**	—
Purchases of services:		
- Fellow subsidiaries		
Corporate services	**5**	10
Office sub-leases	**8**	10
Information technology and other logistic services	**14**	27

The above 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.

During the year, a fellow subsidiary of the Company paid approximately HK$7 million (2005: HK$1 million) to the Group for sharing the costs incurred for certain addition and alteration works conducted at a property development site where the fellow subsidiary is a tenant.

The related party transactions in respect of items above also constitute connected transactions or continuing connected transactions as defined in Chapter 14A of the Stock Exchange's listing rules.

33. MATERIAL RELATED PARTY TRANSACTIONS – CONTINUED

b. Details of key management compensation

HK$ million	The Group 2006	2005
Salaries and other short-term employee benefits	**17**	17
Bonuses	**11**	16
Directors' fee	**1**	1
Post-employment benefits	**1**	1
	30	35
Share-based compensation accounting adjustment (note (i))	**1**	4
	31	39

(i) Share-based compensation accounting adjustment involves calculation of the fair value of share options granted to certain directors under PCCW's share option scheme using trinomial option pricing model. The figures shown in the above table do not represent realisable gains which are affected by a combination of a number of factors, including, performance of PCCW's share price, vesting period and timing of exercise.

(ii) The remuneration of executive directors employed by PCCW, the ultimate holding company of the Group, is borne by PCCW except a bonus was paid to Hubert Chak by the Company in 2005.

c. Year-end balances arising from sales/purchases of services and loan interest

HK$ million	The Group 2006	2005
Receivables from related parties:		
- Fellow subsidiaries	**5**	10
- Related companies	**5**	2
	10	12
Payables to related parties:		
- Fellow subsidiaries	**17**	24

33. MATERIAL RELATED PARTY TRANSACTIONS – CONTINUED

d. Loans from/amounts due to related parties

(i) The movements of the amount due to ultimate holding company of HK$1,195 million as at December 31, 2006 (2005: HK$3,180 million) are as follows:

	The Group	
HK$ million	**2006**	2005
Loans from/amount due to ultimate holding company:		
Balance at January 1,	**3,180**	7,528
Repayment of amount due to ultimate holding company	**(1,985)**	(727)
Conversion of convertible notes (tranche A note due 2011)	—	(1,170)
Interest expenses	—	24
Interest amount payable included in current liabilities	—	(12)
Interest paid	—	(12)
Provision for redemption premium	—	48
Convertible notes (tranche B note due 2014) assigned to a fellow subsidiary (note (ii)(a))	—	(2,499)
Balance at December 31,	**1,195**	3,180

The balance due to ultimate holding company as at December 31, 2006 is interest free and is recorded under the current liabilities in the consolidated balance sheet.

33. MATERIAL RELATED PARTY TRANSACTIONS – CONTINUED

d. Loans from/amounts due to related parties – Continued

(ii) The movements of the loan from a fellow subsidiary of HK$2,548 million as at December 31, 2006 (2005: HK$2,499 million) are as follows:

	The Group	
HK$ million	**2006**	2005
Loan from a fellow subsidiary:		
Balance at January 1,	**2,499**	—
Interest expenses	**24**	—
Interest amount payable included in amounts due to fellow subsidiaries	**(12)**	—
Interest paid	**(12)**	—
Provision for redemption premium	**49**	—
Convertible notes (tranche B note due 2014) assigned from ultimate holding company (note a)	**—**	2,499
Balance at December 31,	**2,548**	2,499

a. The convertible notes (tranche B note due 2014) with face value of HK$2,420 million together with the provision for redemption premium of HK$79 million was assigned, as directed by PCCW, to a wholly-owned subsidiary of PCCW in 2005.

34. FINANCIAL RISK MANAGEMENT

The Group's investment policy is to prudently invest all surplus funds managed by the Group in a manner which will satisfy liquidity requirements, safeguard financial assets and manage risks while optimising return on investments.

The Group's activities expose it to a variety of financial risks: market risk (including foreign exchange risk and equity price risk), credit risk, liquidity risk, fair value interest rate risk and cash flow interest rate risk. The Group's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Group's performance.

Risk management is carried out by a central treasury department ("Group Treasury") under policies approved by the Board. Group Treasury identifies, evaluates and hedges financial risks in close co-operation with the Group's business units. The Board provides principle policies for overall risk management, as well as written policies covering specific areas, such as foreign exchange risk, interest-rate risk, credit risk, use of derivative financial instruments and non-derivative financial instruments, and investing excess liquidity.

a. Market risk

(i) Foreign exchange risk

The Group operates mainly in mainland China and Hong Kong and is exposed to foreign exchange risk arising from Renminbi currency exposures, primarily with respect to the HK dollar. Foreign exchange risk arises from future commercial transactions, recognised assets and liabilities and net investments in foreign operations. The risk management policy is to have the liquid assets mainly denominated in HK dollars, US dollars and Renminbi. As US dollar is pegged to HK dollar, the Group does not expect any significant movements in the US dollar/HK dollar exchange rate. The Group ensures that the net exposure is kept to an acceptable level by buying or selling foreign currencies at spot rates where necessary to address short-term imbalances.

The Group has operations in mainland China where the net assets are exposed to foreign currency translation risk. The Group's currency exposure with respect to these operations is mainly from Renminbi and HK dollar.

(ii) Equity and commodity price risk

The Group is not exposed to equity and commodity price risk.

34. FINANCIAL RISK MANAGEMENT – CONTINUED

b. Credit risk

The Group is exposed to credit risk, which is the risk that a counterparty will be unable to pay outstanding amounts in full when due. The Group has policies in place to ensure that the pre-sale of the properties and the sale of completed properties are both binding and enforceable. For the property investment and other business segments, the Group obtained rental deposits from the tenants while for other business, the customers are mainly fellow subsidiaries and related parties which the credit risk is relatively low. For the property pre-sale, there is a certain degree of concentrations of credit risk but the Group, through the binding and enforceable pre-sale contracts, manages the concentrated credit risk.

c. Liquidity risk

Due to the dynamic nature of the Group's underlying businesses, prudent liquidity risk management implies maintaining sufficient cash and cash equivalents to meet operational needs and possible investment opportunities.

d. Fair value and cash flow interest rate risks

Fair value interest rate risk is the risk that the value of a financial instrument will fluctuate because of changes in market interest rates. Cash flow interest rate risk is the risk that future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Group is not exposed to cash flow interest rate risk since the Group's long-term borrowings are fixed rate borrowings, which, however, will expose the Group to fair value interest-rate risk. The Group's policy is to maintain stable cash flows by entering into fixed interest rate borrowings.