Corporate Governance

Throughout the year of 2006, the Code Provisions in the Code of Corporate Governance Practices contained in Appendix 14 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited ("Listing Rules") and the disclosure requirements contained in Appendix 23 of the Listing Rules are not applicable to CITIC 1616 as the Company was only listed on the Main Board of The Stock Exchange of Hong Kong Limited ("Stock Exchange") in April, 2007.

Connected Transactions

The Group has entered into the following continuing connected transactions, each of which constitutes a non-exempt continuing connected transaction under Chapter 14A of the Listing Rules:

1. CPC Services Agreement

General terms

CITIC Pacific Communications Limited ("CPC") is the holding company of the communication arm of CITIC Pacific Limited ("CITIC Pacific"). Its subsidiaries (including CPCNet Hong Kong Ltd. (100%-owned) and CPCNet Macau Limited (85%-owned) together with CPC, the "**CPC Group**") and CITIC Guoan Co., Ltd. ("CITIC Guoan") (50%-owned) may require services from the Group.

Under the CPC Services Agreement dated 21 March 2007 between the Company and CPC ("CPC Services Agreement"), the services to be provided by the Group to CPC Group include provision of private leased circuits, conveyance of telecoms traffic, equipment co-location and other available services which the Group offers to its customers.

Relevant members of the Group and relevant members of CPC Group have entered into, and may from time to time and as necessary enter into, separate implementation agreements for specific transaction or series of transactions contemplated under the CPC Services Agreement. Each implementation agreement has and will set out details of the service, price, duration and other relevant details, which reflect the particulars of the services required and the market conditions at the material time. As the implementation agreements are simply further elaborations on the provision of services contemplated by the CPC Services Agreement, they do not constitute new categories of connected transactions and the Group and CPC Group agreed to perform these implementation agreements subject to the terms of the CPC Services Agreement (including the annual caps).

Term

The term of the CPC Services Agreement is for three years commencing as from 1 January 2007 and ending on 31 December 2009.

Reason for the transaction

The CPC Services Agreement allows the Group to enhance its customer base by securing a sophisticated user in the Group's services.

Pricing principles and annual caps

The amount of fees payable by CPC Group in respect of services provided by the Group for the three years ended 31 December 2004, 2005 and 2006 were approximately HK$1.7 million, HK$2.3 million and HK$2.3 million, respectively.

The terms and conditions on which such services are to be provided by the Group under the CPC Services Agreement should be no less favourable to the Group than those offered from independent third parties. The price which the Group may receive from CPC Group for the relevant services shall be fair and reasonable with reference to market price and in any event shall be subject to an annual cap of HK$2.5 million for each of the three years ending 31 December 2009.

The above annual caps, being the expected maximum annual transaction amount, have been determined on the basis of estimated volume of services required by CPC Group with reference to historical transaction value with CPC Group and the potential growth in demand generally in the market for such services with reference to market price.

2. Tenancy Agreements

General terms

Goldon Investment Limited ("Goldon") is a company in which CITIC Pacific has a 40% interest and therefore an associate of CITIC Pacific, and the owner of CITIC Tower in Hong Kong. Under the two Tenancy Agreements, both dated 22 December 2006 between the Company and Goldon ("Tenancy Agreements"), Goldon agreed to lease (with the right of exclusive possession) to the Company the premises located at 8th Floor and portion of 9th Floor, CITIC Tower, 1 Tim Mei Avenue, Central, Hong Kong (with a floor area of approximately 29,038 sq.ft.). There is one tenancy agreement for each floor.

The premises are used by the Group as office premises and to house its telecoms equipments and facilities.

Term

The term of the Tenancy Agreements is for three years commencing from 16 November 2006 and ending on 15 November 2009.

Reason for the transaction

The Group has been operating in CITIC Tower in the past, and in view of administrative convenience will continue to do so provided the rentals are comparable to the market rates and are fair and reasonable.

Pricing principles and annual caps

The aggregate rentals and building management fees paid by the Group to Goldon for its premises in CITIC Tower, Hong Kong in the three years ended 31 December 2004, 2005 and 2006 were approximately HK$11.1 million, HK$11.2 million and HK$12.0 million, respectively. The rents were comparatively low during the three years ended 31 December 2006 as a result of the effect of severe acute respiratory syndrome in Hong Kong.

According to the Tenancy Agreements, the aggregate rentals and building management fee to be paid by the Company for each of the three years ending 31 December 2009 will not exceed HK$24 million. The increase is mainly due to the increase in rental pursuant to the revised rental agreement entered into at the end of 2006. The property valuer has confirmed that such rental charge is in line with the market rent.

The independent valuer, Knight Frank Petty Limited, has reviewed the Tenancy Agreements and confirmed that the rentals reflect the prevailing market rates.

3. Payment to HKIX Co

General terms

HKIX Hong Kong Ltd. ("HKIX Co") owns and operates Hong Kong Internet Exchange ("HKIX"), which is a layer-two settlement-free multi-lateral exchange point providing mainly interconnection amongst Internet access providers in Hong Kong. It owns 25% of Asia Pacific Internet Exchange Limited ("APIX"), which is a 75%-owned subsidiary of the Company, and provides a secondary site to HKIX on a non-profit basis. As HKIX Co is a substantial shareholder of the Company's subsidiary (i.e. APIX), HKIX Co and its subsidiaries are connected persons of the Company.

Pursuant to the Shareholders' Agreement entered into between HKIX Co, CITIC Data 1616 Limited, The Chinese University of Hong Kong Foundation Limited and the Company on 18 August 2004 ("the HKIX2 Shareholders' Agreement"), APIX will provide various financial and operational support to HKIX Co which includes an annual payment of HK$1,000,000 to a wholly-owned subsidiary of HKIX Co. As a partner in the Hong Kong Internet Exchange 2 ("HKIX2") project, the Company's tangible contributions are provisions of financial support and the location to host HKIX2 free of charge. HKIX Co remains the operator of HKIX. The Group has not entered into similar agreement before and APIX is the only joint venture of the Group.

Term

Under the HKIX2 Shareholders' Agreement, the annual payment shall be for an initial period of 6 years until 17 August 2010 (which, subject to annual review by APIX, may be renewed on a yearly basis for no more than four years). The term and the annual payment were agreed as part of the overall arrangement concerning the governance and operation of APIX. Indeed, the term of six years (with an option to renew for no more than four years) (instead of a 3-year term) is appropriate for contracts of a similar nature, i.e. shareholders' agreement which relates to the continuous governance and operations of a company on a continuous basis. Shareholders' agreement usually does not have a fixed term and terminates according to the commercial agreement of the shareholders (e.g. a particular party ceasing to be a shareholder or a fixed term). As the HKIX2 Shareholders' Agreement relates to an unique service in internet services, namely, a mirror site to the HKIX, there is no comparable joint venture in Hong Kong which can produce a reference to determine the standard/normal term of this type of joint venture agreements. The parties have considered that the term of 6 years (with an option to renew for no more than 4 years) is a reasonable period to build up the cooperation and the term was arrived at based on the arm's-length negotiation between the parties, taking into account the operation and the development of such internet exchange centre in order to provide a productive outcome.

Reason for the transaction

The HKIX2 Shareholders' Agreement allows APIX to provide support for HKIX Co's future expansion and the right to provide a secondary site to HKIX on a non-profit basis. The benefit is the prestige of involving in the provision of HKIX2, the mirror site of a crucial internet exchange point in Hong Kong, and is intangible. As HKIX is unique and crucial in maintaining the internet connection and provide community services to the Hong Kong public at large, the Company sees the entering into of the HKIX2 Shareholders' Agreement as a good opportunity whereby it can participate and provide community services to the public.

Pricing principles and annual caps

As a term of the joint venture in APIX, the annual payment to a wholly-owned subsidiary of HKIX Co by APIX shall not be more than HK$1 million a year in the form of financial support to HKIX Co.

4. Application for waiver for non-exempt continuing connected transactions

The Directors (including the independent non-executive Directors), having reviewed the relevant information (including the historical figures, the underlying agreements, the trend and the growth in demand generally in the market for the services rendered to CPC and the confirmations from the property valuer) provided by the Company relating to the continuing connected transactions set out in the sub-paragraphs headed "Reason for the transaction" and "Pricing principles and annual caps" under each of the transactions above, consider that the CPC Services Agreement, the Tenancy Agreements, and the annual payment to a wholly-owned subsidiary of HKIX Co have been entered into in the ordinary and usual course of business of the Group, on normal commercial terms, and the proposed terms and the proposed annual caps are fair and reasonable and in the interest of the shareholders of the Company as a whole. Under the Listing Rules, such transactions will constitute non-exempt continuing connected transactions of the Company and will be subject to the disclosure and/or independent shareholders' approval requirements provided for in the Listing Rules.

The Company has, pursuant to Rule 14A.42(3) of the Listing Rules, applied to the Stock Exchange for a waiver from strict compliance from the following upon the Listing:

(1) the announcement requirements under Rule 14A.34 of the Listing Rules, for the CPC Services Agreement and the payment to HKIX Co; and

(2) the announcement requirements and independent shareholders' approval requirements under Rules 14A.34 and 14A.35 of the Listing Rules, respectively, for Tenancy Agreements.

The Stock Exchange has granted a wavier from strict compliance with the applicable requirements under the Listing Rules as mentioned above and the Company should comply with the annual review requirements and the reporting requirements under Rules 14A.37 to 14A.41 and Rules 14A.45 to 14A.46 of the Listing Rules, subject to the respective annual caps for each of the continuing connected transactions set out above.

Management Contract

The Company will share certain administrative services, namely, company secretarial services and internal audit services, with CITIC Pacific, being a substantial shareholder of the Company. This arrangement may be terminated if CITIC Pacific's shareholding in the Company shall fall below 30% or by either party by giving a six month's notice in writing to the other. The charges payable by the Company under the administrative services agreement dated 21 March 2007 will be calculated based on cost of the services which are identifiable and allocated on a fair and equitable basis. Mr. Lee Chung Hing had indirect interests in the management agreement as he is a director of CITIC Pacific.

Independent Non-Executive Directors

The Company has, upon the appointment of the independent non-executive directors, received from each of them a confirmation of their independence pursuant to the new independence guidelines under the Listing Rules and that the Company considers such directors to be independent.

Directors' Interest in Securities

As at 31 December 2006, none of the directors of the Company had nor were they taken to or deemed to have, under Part XV of the Securities and Futures Ordinance ("SFO"), any interests or short positions in the shares, underlying shares or debentures of the Company or its associated corporations or any interests which are required to be entered into the register under section 352 of the SFO or any interests which are required to be notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Companies in the Listing Rules as the Company was only listed in April, 2007.

Disclosure under Rule 8.10(2) of the Listing Rules

Dr. Li Bin, a director and the Chief Operating Officer of the Company, has declared to the Company that his wife, Gu Jie ("**Ms. Gu**"), is a director of GTI (HK) Limited ("**GTI (HK)**"). GTI (HK) was incorporated in June 2005 in Hong Kong to engage in logistic system development and other telecoms services which include IDD connections mainly targeting calling-card vendors.

GTI (HK) is an extension of the business of Galaxy Telesys Inc ("**Galaxy**"), which was incorporated in the US by Ms. Gu's parents in 2001 to engage in US-based data communication, voice communication and network design. Both GTI (HK) and Galaxy are beneficially owned as to 100% by the parents of Ms. Gu. They employed less than 15 employees in total and with around 30 customers only. Galaxy and GTI (HK) are family-run business with technological settings which allow them to handle voice-only traffic with limited capacity.

The business of Galaxy and GTI (HK) does not compete with that of the Company, nor would it create any conflict of interest against the Company. Galaxy and GTI (HK) provide IDD connections mainly to calling-card vendors (as opposed to telecoms operators to which the Company focuses), are of such small scale and target a different market segment in the IDD market which the Company had not considered to enter into.

Ms. Gu became a director in August 2006 when Mr. Gu (the father of Ms. Gu) resigned as a director of GTI (HK) for health reasons. Ms. Gu is not involved in the business of Galaxy. Currently, she does not have any beneficial interest in both Galaxy and GTI (HK). Dr. Li Bin is not involved, nor does he have any beneficial interest, in the business of Galaxy and GTI (HK). The business of Galaxy and GTI (HK) were developed independently of Dr. Li Bin and prior to his joining the Company in 2006. They were also operated independently of the Company. Other than a transaction in 2006 pursuant to which GTI (HK) acquired IDD capacity from the Company for less than HK$100,000, the Directors are not aware of any transactions between the Company, and Galaxy and/or GTI (HK) during the three years ended 31 December 2006.

Mr. Yuen Kee Tong, executive Director, will under an agreement with CITIC Pacific spend some of his time on the business of CITIC Pacific but has ceased to act as director of all subsidiaries or associated companies of CITIC Pacific. CITIC Pacific will pay Mr. Yuen for his such services separately. Mr. Yuen's role in CITIC Pacific and its subsidiaries (excluding the Group) ("Retained Group") after the listing of the Company will facilitate the continued operation and oversight of the remaining non-core telecoms businesses of CITIC Pacific. Mr. Yuen's continued involvement will be on a non-executive and part-time basis and CITIC Pacific will not engage more than 5% of his time than the time he would spent with the Group.

Mr. Lee Chung Hing, non-executive Director, is the Vice-Chairman of CITIC Guoan. Mr. Kwok Man Leung, a non-executive Director, is a director of CITIC Guoan. CITIC Guoan's primary business is its 41.63% interest in CITIC Guoan Information Industry Co. Ltd. ("Guoan Information"), a Shenzhen Stock Exchange listed company. Guoan Information operates cable television networks in 18 cities and one province in China. Guoan Information also has interests in systems integration, software development, hotel management, salt lake consolidated resources development and property development.

Guoan Information's system integration services and Companhia de Telecomunicacoes de Macau S.A.R.L.'s international hubbing services, leased circuits, data centre and co-location services are the only areas of the Retained Group's telecoms business which may compete with the Company's business.

Directors (except the independent non-executive Directors), have undertaken in favour of the Company to the effect that, save for those interests as disclosed or interest in any company which a Director together with any of his associates own less than 5%, at any time during which he is a Director, he will not engage, and will procure its associates not to engage, on its own account or with each other or in conjunction with or on behalf of any person, firm or company, carry on or be engaged in, concerned with or interested in, directly or indirectly, whether as a shareholder (other than being a director or a shareholder of the Group or its associated companies), partner, agent or otherwise, in the provisions of telecoms hub based service globally, or in any other business that may compete, directly or indirectly, with such business.

Disclosure Requirements under Appendix 16 of the Listing Rules

As required under Appendix 16 of the Listing Rules, additional financial information was extracted from the prospectus of the Group, which has been reviewed by KPMG. Details are as follows:

1. Basic and diluted earnings per share

	2006	**2005**
From continuing and discontinued operations *(HK cents)*	11.9	5.8
From continuing operations *(HK cents)*	10.7	5.6
From discontinued operations *(HK cents)*	1.2	0.2

(a) From continuing and discontinued operations

The basic earnings per share for the current and prior year is calculated based on the profit attributable to the equity holders of the Company during the year and the 1,692,000,000 ordinary shares pursuant to the sub-division of share capital of the Company in connection with the changes to the Company's capital structure on 16 March 2007 ("Reorganisation"), as if the shares were outstanding throughout the entire year; and immediately before the share offering.

(b) From continuing operations

The basic earnings per share from continuing operations for the current and prior year is calculated based on the profit from continuing operations attributable to the equity holders of the Company during the year and the 1,692,000,000 ordinary shares pursuant to the sub-division of share capital of the Company in connection with the Reorganisation, as if the shares were outstanding throughout the entire year; and immediately before the share offering.

(c) *From discontinued operations*

The basic earnings per share from discontinued operations for the current and prior year is calculated based on the profit from discontinued operations attributable to the equity holders of the Company during the year and the 1,692,000,000 ordinary shares pursuant to the sub-division of share capital of the Company in connection with the Reorganisation, as if the shares were outstanding throughout the entire year; and immediately before the share offering.

(d) *Diluted earnings per share*

There were no diluted potential ordinary shares during the year and, therefore, diluted earnings per share are the same as basic earnings per share for the current and prior year.

2. Directors' Remuneration

Details of directors' remuneration are as follows:

Year ended 31 December 2005

	Fees	**Basic salaries, allowances and other benefits**	**Contributions to defined contribution retirement plan**	**Discretionary bonus**	**Total**
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Executive director					
Mr Peter Chan Kwong Choi	—	272	—	—	272
Non-executive directors					
Mr Lee Chung Hing	—	—	—	—	—
Ms Frances Yung Ming Fong	—	—	—	—	—
Mr Kwok Man Leung	—	—	—	—	—
Total	—	272	—	—	272

Year ended 31 December 2006

	Fees	Basic salaries, allowances and other benefits	Contributions to defined contribution retirement plan	Discretionary bonus	Total
	HK$'000	*HK$'000*	*HK$'000*	*HK$'000*	*HK$'000*
Executive director					
Mr Peter Chan Kwong Choi	—	211	1	3,000	3,212
Non-executive directors					
Mr Lee Chung Hing	—	—	—	—	—
Ms Frances Yung Ming Fong	—	—	—	—	—
Mr Kwok Man Leung	—	—	—	—	—
Total	—	211	1	3,000	3,212

A number of the Company's directors were granted share options of CITIC Pacific, its ultimate holding company. Details of the share options plan are set out in note 22 included in the Financial Statements.

The discretionary bonus of the Group was determined and approved by the Board with reference to the performance of the Group and the respective directors.

During the years ended 31 December 2005 and 2006, no emoluments were paid by the Company to any of the directors as an inducement to join or upon joining the Company or as compensation for loss of office and none of the directors has waived or agreed to waive any emoluments.

3. Individuals with highest emoluments

The five highest paid individuals of the Group for the year include one director (2005: Nil).

An analysis of the five individuals with the highest emoluments in the Group during the year is as follows:

	2006	2005
	HK$'000	*HK$'000*
Directors	3,212	—
Employees	8,277	8,089
	11,489	8,089

The aggregate emoluments in respect of the five highest paid individuals are as follows:

	2006	2005
	HK$'000	*HK$'000*
Salaries and other emoluments	6,920	7,963
Discretionary bonuses	4,525	—
Retirement scheme contributions	44	126
	11,489	8,089

The emoluments of the individuals with the highest emoluments are within the following bands:

	2006	2005
	Number of individual	*Number of individual*
HK$		
1,000,001 — 1,500,000	—	3
1,500,001 — 2,000,000	2	1
2,000,001 — 2,500,000	2	1
3,000,001 — 3,500,000	1	—

During the years ended 31 December 2005 and 2006, no emoluments were paid by the Company to any of the five highest paid individuals as an inducement to join or upon joining the Company as or as compensation for loss of office.

4. Distributability of reserves

The aggregate amount of the reserves available for distribution to equity holders of the Company are as follows:

	The Company	
	2006	2005
	HK$'000	*HK$'000*
Available for distribution to equity holders of the Company	95,995	118,155

5. Segment reporting

As all of the Group's total turnover and profits were derived from telecommunications operations, accordingly no separate business segment analysis is presented for the Group. Further, the Group's business participates primarily in only one geographical location classified by the location of assets, i.e. Hong Kong, accordingly, no segmental analysis is provided.

Contracts of Significance with Controlling Shareholder

The Company or certain of its subsidiary companies and CITIC Pacific, the controlling shareholder of the Company or certain of its subsidiary companies had entered into the following contracts of significance:–

(a) CPC Services Agreement (as defined above); and

(b) Tenancy Agreements (as defined above).

Save as mentioned in the paragraph headed "Management Contract", there is no other contract of significance for the provision of services to the Company or any of its subsidiary companies by the controlling shareholder or any of its subsidiary companies.

Major Customers and Suppliers

The percentage of sales and purchases with the Group's customers and suppliers are as follows:

Sales	**2006**	**2005**
The largest customer	30.6%	35.3%
Five largest customers combined	47.7%	51.5%

Purchases	**2006**	**2005**
The largest supplier	10.3%	13.6%
Five largest suppliers combined	31.1%	33.8%

Share Capital

On 2 August 2006, the Company repurchased the 2,000,000 Non-Voting Deferred Shares of HK$1.00 each of the Company for a total consideration of HK$40.00 and the Non-voting Deferred Shares were then cancelled.

Save as disclosed, the Company has not redeemed any of its shares during the year ended 31 December 2006. Neither the Company nor any of its subsidiary companies has purchased or sold any of the Company's shares during the year ended 31 December 2006.

Service Contracts

As at 31 December 2006, there were no service contracts which were not determinable by the employer within one year without payment of compensation (other than statutory compensation) between any company in the Group and any director re-elected at the 2007 Annual General Meeting.

Auditors

In October, 2005, PricewaterhouseCoopers had resigned as auditors of the Company and KPMG was appointed as auditors of the Company in his stead.

Sufficiency of Public Float

Based on information that is publicly available to the Company and within the knowledge of the directors as at the date of despatching the annual report, the Directors confirm that the Company has maintained the amount of public float as required under the Listing Rules.