

Statement on ruling of Takeovers Executive (“Executive”) of the Securities and Futures Commission regarding whether certain parties were acting in concert in respect of PCCW Limited

Application and ruling

1. On 2 November 2006 Mr Francis Leung (“**Mr Leung**”) applied to the Executive, through his advisers, for a ruling that for the purposes of the Takeovers Code:
 - (a) Mr Leung and Fiorlatte Limited (“**Fiorlatte**”) (a company wholly-owned by Mr Leung) were not acting in concert with Telefónica S.A. (“**Telefónica**”) or China Network Communications Group Corporation (“**CNC**”); and
 - (b) the Li Ka Shing Foundation Limited (“**HK Foundation**”) and/or the Li Ka Shing (Canada) Foundation (“**Canada Foundation**”) (together referred to as the “**Foundations**”) were not acting in concert with Telefónica or CNC,
in relation to certain proposed transactions in shares of PCCW Limited (Stock Code 0008) (“**PCCW**”).
2. The outcome of the application was important at the time it was made because, if the parties were found to be acting in concert, a number of proposed transactions (including the proposed sale of 22.65% of the issued share capital of PCCW to Mr Leung) may have resulted in the enlarged concert group holding an aggregate of 30% or more of the voting rights of PCCW and in consequence a general offer obligation would have been triggered under Rule 26.1 of the Takeovers Code. In any event on 30 November 2006 PCCW announced that the proposed sale to Mr Leung had not received the requisite shareholder approval and therefore the proposed transactions did not go ahead.
3. Following receipt of the application on 2 November 2006 the Executive raised numerous enquiries with the various parties. This statement refers to the facts which emerged as a result of these inquiries on which the Executive made its determination. The application letter of 2 November 2006 and the subsequent submissions from the parties are together referred to as the “**Application**”.
4. On 10 November 2006 the Executive ruled that, at the time of the ruling, there was insufficient evidence to conclude that Mr Leung and/or Fiorlatte and/or Mr Li Ka Shing (“**Mr KS Li**”) and/or the HK Foundation and/or the Canada Foundation on the one hand and Telefónica and/or CNC on the other were parties acting in concert as defined in the Codes on Takeovers and Mergers and Share Repurchases (“**Codes**”).
5. Section 16.3 of the Introduction to the Codes provides that ‘*Subject to confidentiality considerations, it is the policy of the Executive to publish its important rulings and interpretations of the Codes, and the reasons for them, so that its activities may be understood by the public. There may be announcements of rulings in specific cases where the rulings are considered to have general application, or statements of policy which may take the form of Practice Notes setting out in greater detail the Executive’s practice and interpretation of the Codes.*’ The ruling given in the present case is an important ruling and, accordingly, the Executive now publishes this statement.

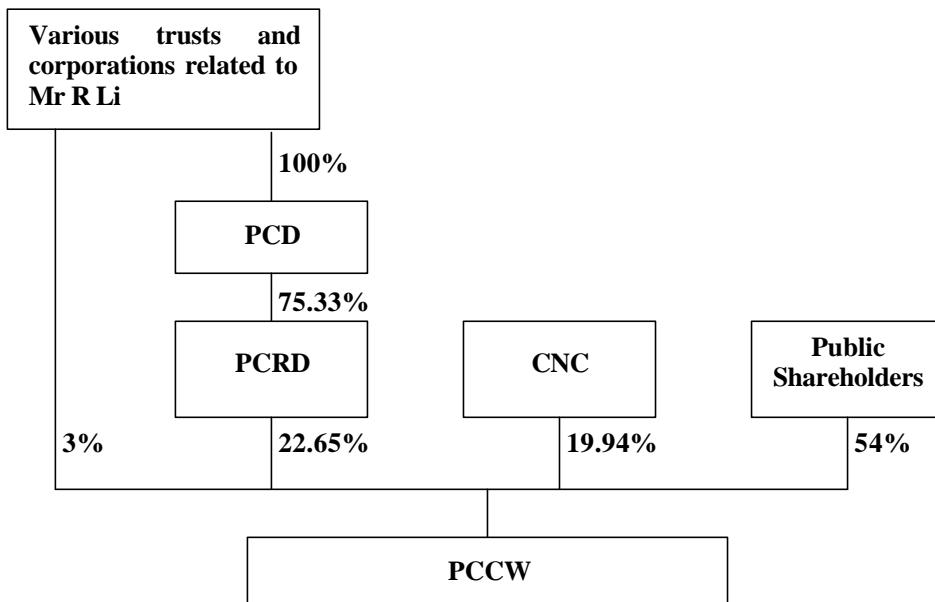
Background and facts

6. The Executive found the following facts on the basis of the evidence before it. On 10 July 2006 PCCW announced that Mr Leung had entered into an agreement with Pacific Century Regional Developments Ltd (“**PCRD**”) for Mr Leung to purchase (through his wholly-owned company, Fiorlatte) all of PCRD’s interest of 22.65% in PCCW (“**Subject Shares**”) at \$6 per share (“**Acquisition**”). PRCD is a Singapore listed company. Pacific Century Diversified Limited (“**PCD**”), a company indirectly controlled by Mr Richard Li

(“**Mr R Li**”), holds an interest in approximately 75.33% of PCRD.¹ At all relevant times Mr R Li was the Chairman and an executive director of both PCCW and PCRD. Mr KS Li is Mr R Li’s father.

7. The Acquisition agreement was subject to, amongst other things, the approval of PCRD’s shareholders in a general meeting which was scheduled to take place on 30 November 2006.

Shareholdings in PCCW at time of Application



8. CNC is a state-owned enterprise in the PRC. CNC acquired its 19.94% interest in PCCW through a subscription of new shares in January 2005 (“**Subscription**”).²
9. Telefónica is an international telecoms company headquartered in Spain. At the time of the Application, Telefónica held a 5% interest in China Netcom Group Corporation (Hong Kong) Limited (“**CNCHK**”, a Hong Kong listed company) and had a seat on its board. CNC holds an interest of 75% in CNCHK. Telefónica formed a strategic alliance with CNCHK in July 2005 as a result of its investment in CNCHK.
10. Mr Leung was formerly a managing director of Citigroup Global Markets Asia (“**Citigroup**”) and held the title of Chairman (Asia). Mr Leung intended to invite third parties to join him in his investment in PCCW via a private equity fund. However Mr Leung was not able to implement such arrangements as a number of potential investors indicated that they were looking for greater liquidity than could be provided by a private equity fund. Mr Leung then considered breaking the Subject Shares into smaller blocks.

¹ In addition to the Subject Shares, at the time of the Application, Mr R Li was interested in approximately 3% of the issued share capital of PCCW held through trusts and corporations other than PCRD.

² On 20 January 2005 PCCW and CNC announced that the Executive had ruled that it did not consider CNC to be acting in concert with PCCW substantial shareholders (i.e. PCRD and companies controlled by Mr R Li and his related trusts) as a result of the Subscription.

11. On 2 November 2006 Mr Leung submitted the request for a ruling to the Executive referred to in paragraph 1 above. He also informed the Executive that upon completion of the Acquisition he proposed to on-sell the Subject Shares as follows (“**On-Sales**”):

- 10% (of the issued share capital of PCCW) to HK Foundation³ at \$6 per share;
- 2% (of the issued share capital of PCCW) to the Canada Foundation⁴ at \$6 per share; and
- 8% (of the issued share capital of PCCW) to Telefónica at \$6 per share (subject to the price adjustment described in the Note below).

Note: Under the price adjustment mechanism (which applied only to Telefónica’s acquisition) if the market price of PCCW’s shares on any day over a period of 40 consecutive days, ending on the date which was 10 months after the “First Payment Date”,⁵ was less than HK\$7.20, then Fiorlatte would pay to Telefónica HK\$0.60 for each share acquired by Telefónica. This meant that, if the price adjustment mechanism was triggered, Telefónica would effectively buy the PCCW shares at HK\$5.40 per share.

12. Upon completion of the Acquisition and the On-Sales, Mr Leung intended to retain an interest in the Subject Shares of 2.65% of the issued share capital in PCCW through Fiorlatte. It was proposed that Mr KS Li would provide funds to Mr Leung to finance part of the consideration for this acquisition. The On-Sales were expected to complete contemporaneously with or immediately after the completion of the Acquisition.
13. On 8 November 2006 CNC reached agreements with Telefónica to set up a joint venture vehicle in which to hold their combined interests in PCCW (“**SPV**”) following completion of the On-Sales. The SPV would then have held an aggregate interest of 27.94% (i.e. CNC’s 19.94% and Telefónica’s 8%) in PCCW.

Discussion of application of the Codes

14. The issue before the Executive was whether for the purposes of the Takeovers Code:
 - (a) Mr Leung and Fiorlatte were acting in concert with Telefónica or CNC; and
 - (b) the Foundations were acting in concert with Telefónica or CNC.

Relevant provisions of the Codes

15. **Definition of “acting in concert”** - Under the Codes the term “*acting in concert*” is defined as:

“Persons acting in concert comprise persons who, pursuant to an agreement or understanding (whether formal or informal), actively co-operate to obtain or consolidate “control” ... of a company through the acquisition by any of them of voting rights of the company.”

16. The definition of acting in concert also sets out nine classes of person who are presumed to be acting in concert with others in the same class unless the contrary is established. The

³ HK Foundation is a company incorporated in Hong Kong with liability limited by guarantee and is a charitable organisation registered under section 88 of the Inland Revenue Ordinance since 1980. It was founded by Mr KS Li who is one of its directors and members. None of the directors and members of HK Foundation may benefit from any of the assets and income of HK Foundation which may only be directed towards charitable objects and causes.

⁴ Canada Foundation is a company incorporated in Canada as a private foundation registered with the Minister of National Revenue as a Registered Charity within the meaning of the Income Tax Act (Canada) since July 2005. This charitable foundation was founded by Mr KS Li who is neither a director nor a member. None of the directors and members may benefit from any of the assets and income of the Canada Foundation which may only be directed towards charitable objects and causes.

⁵ The Acquisition agreement between Mr Leung and PCRD provided for the consideration to be paid to PCRD in several stages. The “First Payment Date” was due to fall on the tenth business day after satisfaction or waiver of the conditions to the agreement.

full text of the definition of “*acting in concert*” and the nine presumptions is set out in **Appendix 1** to this statement.

Concert party issues

17. **“Leung/ KS Li group”** – Class (9) of the definition of acting in concert presumes the following persons to be acting in concert:

“a person, other than an authorised institution within the meaning of the Banking Ordinance (Cap. 155) lending money in the ordinary course of business, providing finance or financial assistance (directly or indirectly) to any person (or a person acting in concert with such a person) in connection with an acquisition of voting rights (including any direct or indirect refinancing of the funding of the acquisition).
18. The Executive noted that Mr KS Li had provided a bridging loan of \$500 million to Mr Leung/Fiorlatte for the payment of an escrow deposit payment relating to the Acquisition.⁶ It was also proposed that Mr KS Li would provide finance to Mr Leung to finance part of the consideration for Mr Leung’s acquisition (through Fiorlatte) of 2.65% of PCCW. It follows that Mr Leung and Mr KS Li were presumed to be acting in concert under class 9 of the definition of acting in concert in respect of PCCW. Mr Leung and Mr KS Li accepted that, in the context of PCCW, they might be deemed to be acting in concert under the Takeovers Code. Mr KS Li is also presumed to be acting in concert with his “*close relatives*” and “*related trusts*” under class (8) of the definition of acting in concert. Mr KS Li is therefore presumed to be acting in concert with the Foundations and with his son, Mr R Li.
19. **“CNC/Telefónica group”** – CNC and Telefónica accepted that they were parties acting in concert in respect of PCCW. The Executive agreed with this view in light of the information before it including the various arrangements between CNC and Telefónica concerning PCCW (as referred to in paragraph 13 above).
20. **Two concert groups** – The Executive therefore proceeded with its analysis on the basis that the following parties were persons acting in concert in respect of PCCW:
 - (a) Mr Leung, Mr KS Li, Mr R Li⁷ and the Foundations on the one hand; and
 - (b) CNC and Telefónica on the other.
21. Given the composition of the two concert groups the Executive went on to consider whether any member of the Leung/KS Li group on the one hand and any member of the CNC/Telefónica group on the other were parties acting in concert in connection with PCCW.
22. The Executive carefully considered the submissions before it which included the parties’ responses to its enquiries. Each submission was signed by the applicant and contained a statement certifying the truth, accuracy and completeness of statements contained therein as required by section 8.3 of the Introduction to the Codes. The parties (Mr Leung, CNC, Telefónica, Mr KS Li and the Foundations) also provided the Executive with a number of signed confirmations. Finally, the Executive had also been provided with an amount of information on a confidential basis most notably relating to the commercial rationale for various decisions to invest in PCCW. The Executive took account of this information in reaching its decision.
23. Mr Leung confirmed to the Executive that he (and Fiorlatte) on the one hand and Telefónica and CNC on the other did not fall within any of the nine presumptions of acting in concert. The Executive accepted this assertion on the basis of the evidence

⁶ See PCCW’s announcement dated 20 September 2006.

⁷ As Mr R Li was presumed to be acting in concert with Mr KS Li the Executive included Mr R Li in the Leung/KS Li concert group for the purpose of its analysis.

before it and went on to consider whether, as a matter of fact, the relevant persons were acting in concert in relation to PCCW.

24. The Executive reminded itself of the three elements of acting in concert. There must be (i) an agreement or understanding (whether formal or informal), (ii) to actively co-operate to obtain or consolidate control, (iii) through the acquisition of voting rights of the company.
25. The proposed Acquisition and On-Sales (were they to proceed) provided clear evidence of acquisitions of voting rights by members of both the Leung/KS Li group and the CNC/Telefónica group. The question for the Executive to determine therefore was whether such acquisitions were to be made in pursuance of any agreement or understanding, between members of the Leung/KS Li group on the one hand and members of the CNC/Telefónica group on the other, actively to co-operate to obtain or consolidate control of PCCW.
26. Evidence of contact between parties and the nature of that contact is always a relevant factor in determining whether a concert party exists or has been formed. During his employment at Citigroup, Mr Leung advised CNCHK on investment banking activities.⁸ This provided clear and undisputed evidence of a pre-existing business relationship between Mr Leung and CNCHK (and CNC as its parent). However whilst this was a factor to be taken into account in establishing whether a concert party relationship existed it was not in itself determinative. The Executive therefore explored whether there were any other factors from which it could reasonably be inferred that the CNC/Telefónica group was acting in concert with the Leung/KS Li group. In view of the evidence before it the Executive concluded that there was insufficient evidence to draw such a conclusion. In reaching this view the Executive paid particular regard to the factors considered below.
 - (a) Although Mr Leung had met with CNC on a couple of occasions in July and August 2006 there was no evidence to suggest that those meetings involved any discussion or the entering into of any understanding or agreement to cooperate actively to obtain control of PCCW. The Executive did not believe it to be particularly unusual or unreasonable for a potential incoming substantial shareholder to wish to meet with an incumbent substantial shareholder and vice versa. In all the circumstances of this matter and in the absence of evidence to the contrary the Executive did not consider the mere fact that the meetings had taken place to provide sufficient grounds to infer a concert party relationship. The Executive noted this view was consistent with the rationale of Note 7 to Rule 26.1 which clarifies that it is natural for a vendor of part of a controlling holding to select a purchaser whose ideas, as regards the way the company is to be directed, are reasonably compatible with his own. The Executive also paid due regard to the representations and confirmations by Mr Leung and CNC regarding the absence of discussions or any agreement or understanding (whether formal or informal) between them.
 - (b) As regards Mr Leung and Telefónica the Executive accepted on the evidence that Mr Leung and Telefónica did not have any past or present business or other relationship other than during the negotiations in respect of the On-Sales and in that regard the only relationship between them was as a potential purchaser and vendor respectively.
 - (c) The Executive carefully reviewed the evidence relating to Mr KS Li and the Foundations and concluded that there was no evidence to suggest that any

⁸ It follows that at that time Citigroup would have been presumed to be acting in concert with CNCHK by virtue of class (5) of the definition of acting in concert. Class (5) presumes the following persons to be acting in concert “*a financial adviser ... with its client in respect of the shareholdings of the adviser and persons controlling, controlled or under the same control as the adviser ...*”. However it is important to note that the class (5) presumption does not apply to individual employees of a financial adviser and therefore the advisory role played by Mr Leung did not result in him being presumed to be acting in concert with CNCHK or CNC.

arrangement or understanding (whether formal or informal) existed between them and any member of the CNC/Telefónica group.

27. The Executive also paid significant regard to the representations and signed confirmations provided by the relevant parties including:
 - (a) Confirmations regarding the nature of the discussions between the relevant parties and the absence of any relevant agreement or understanding (whether formal or informal) concerning the acquisition or consolidation of control of PCCW.
 - (b) Confirmations of the absence of any relevant discussions, agreements or understandings between any of the relevant parties in relation to appointments to the board of PCCW.
 - (c) Confirmations that CNC was independent from and had no relationship with Mr KS Li (except in respect of usual business arrangements concerning connectivity between networks of CNC (and its subsidiaries) and telecom companies associated with Mr KS Li). It was also confirmed that none of such arrangements would create any presumption of acting in concert between CNC and Mr KS Li and/or companies associated with him under the Codes nor were they material in considering whether CNC was acting in concert with Mr KS Li.
 - (d) Confirmations that Telefónica had no past or present business or other relationship with any of the relevant parties other than during negotiation of the proposed On-Sales and in this regard, only in the capacity as a potential purchaser of PCCW shares from Mr Leung/Fiorlatte.
 - (e) Confirmations that Telefónica had no past or present business or any other relationship with Mr Leung before the initial meeting arranged by CNC.
 28. The Executive also paid considerable attention to the terms of the public announcements that CNC and Mr Leung agreed to issue.⁹ CNC proposed to issue an announcement confirming amongst other things that:
 - (a) CNC was not acting in concert with any person (apart from Telefónica) in respect of its shareholding in PCCW;
 - (b) CNC had not, in regard to such shareholding, entered into any agreement or arrangement with any of Mr Leung, the HK Foundation, the Canada Foundation and their representatives, Mr KS Li and Mr R Li (apart from the previously disclosed shareholders agreements dated 19 January 2005 which did not render them parties acting in concert); and
 - (c) CNC and persons acting in concert with it did not have control (within the meaning of the Takeovers Code) over PCCW, and CNC did not intend to control the board of PCCW and would not seek to do so in future unless CNC gained control of PCCW in accordance with the Takeovers Code.
 29. Mr Leung proposed to issue an announcement providing an up-date of the progress of the Acquisition and On-Sales and setting out details of the Executive's ruling.
 30. The Executive noted the possible implications under the Takeovers Code and the Securities and Futures Ordinance of issuing announcements which contained false or misleading information.
- Application of Note 7 to Rule 26.1 (vendor of part only of a shareholding)*
31. Sometimes a purchaser wishes to acquire close to but less than 30% of voting rights of a company thereby avoiding an obligation to make a general offer under Rule 26. This may

⁹ On 12 November 2006 Mr Leung and CNC issued the announcements as proposed. Copies of the announcements are attached at **Appendix 2**.

involve the vendor selling part only of his holding to the purchaser and retaining the remaining shares. In these circumstances the Executive will be concerned to see whether the arrangements between the purchaser and vendor effectively allow the purchaser to exercise a significant degree of control over the retained voting rights in which case a general offer would normally be required. Note 7 to Rule 26.1 sets out a number of factors that the Executive will take into account in reaching a decision in this respect. These factors include the following (the full text of Note 7 is set out in **Appendix 1** to this statement):

- (a) any other transactions between the purchaser and the vendor, and between the purchaser and other members of the group acting in concert with the vendor;
 - (b) whether the vendor is an “*insider*” – if the vendor is not an “*insider*” there is less likelihood of the purchaser acquiring a significant degree of control over the retained voting rights;
 - (c) the price paid by the purchaser for the voting rights – if a very high price is paid this would tend to suggest that control over the entire holding was being secured;
 - (d) whether the parties negotiate options over the retained voting rights; and
 - (e) if the retained voting rights represent a significant part of the company’s capital (or a significant sum of money in absolute terms) a correspondingly greater element of independence may be presumed.
32. Upon completion of the On-Sales the Leung/KS Li group would have held in aggregate 18.35% (including Mr R Li’s 3% shareholding) whilst the CNC/Telefónica group would have held 27.94% through the SPV. In view of the closeness of this holding to the 30% trigger level under Rule 26.1 of the Takeovers Code and the fact that Mr Leung/Fiorlatte were proposing to retain some of the Subject Shares, the Executive was also concerned as to whether there were any arrangements between Mr Leung/Fiorlatte (as vendor) and Telefónica (as purchaser) that effectively allowed the CNC/Telefónica group to exercise a significant degree of control over the retained shares. If this had been the case the Executive would have aggregated the holdings of the Leung/KS Li group with those of the CNC/Telefónica group which would have exceeded 30% (had the Acquisition and On-Sales have proceeded) thereby triggering a general offer obligation under Rule 26.1 of the Takeovers Code.

33. Given these concerns, the Executive considered each of the factors set out in Note 7 to Rule 26.1 to determine whether there were any arrangements which enabled any member of the CNC/Telefónica group to exercise any control over the retained interests of the Leung/KS Li group. On the basis of the evidence before it, including the factors set out in Note 7 considered below, the Executive reached the conclusion that there was insufficient evidence to suggest that CNC or Telefónica had entered into any understanding or arrangement to exercise control over Mr Leung/Fiorlatte’s retained voting rights.

Were there any other transactions between the Leung/KS Li group and the CNC/Telefónica group?

34. The Executive noted the parties’ representations that the only transactions or arrangements between the two groups related solely to the proposed On-Sale to Telefónica and the confirmations that there were no other agreements or arrangements, whether formal or informal, between Mr Leung (and companies controlled by him) and any member of either the CNC group or the Telefónica group. The Executive also took account of the following representations:

- (a) that neither Mr KS Li nor any company controlled by him was or had been involved in the discussions between Mr Leung and Telefónica in connection with the On-Sales;

- (b) that neither Mr KS Li nor any company controlled by him was or had been involved with the discussions between CNC and Telefónica in connection with their strategic alliance and related arrangements;
- (c) that there were no agreements or arrangements, whether formal or informal, between Mr KS Li (and companies controlled by him) and any member of the CNC group or any member of the Telefónica group in connection with the acquisition, holding or voting of PCCW shares; and
- (d) similar representations by each of the HK Foundation and the Canada Foundation.

(a) Was the vendor an “insider”?

35. The Executive next enquired into whether Mr Leung was an insider with respect to PCCW. In the current context an “*insider*” refers to a director of PCCW or a member of its management team. If Mr Leung had been an “*insider*” Note 7 suggests that there would have been a greater likelihood of a significant degree of control over his retained shares. The Executive noted the representations that Mr Leung was proposing to on-sell shares that, at that time, he did not own.

(b) Was a very high price being paid for the voting rights?

36. If a “*very high price*” is paid to a vendor of part only of his shareholding it implies that there may be other agreements or understandings relating to the retained shares. Where a high price is paid to an “*insider*” or vendor of part only of his shareholding it implies that a control premium is being paid in respect of the retained shares. Members of the Leung/KS Li group were proposing to pay \$6 per share for the Subject Shares. Telefónica was proposing to pay \$6 per share or \$5.40 if the price adjustment mechanism had been triggered. In 2005 CNC had paid \$5.90 per share for its acquisition of 19.94% of new shares in PCCW. PCCW shares closed at \$5.50 per share and \$5.02 per share respectively on 7 July 2006 and 10 November 2006. In view of the price proposed to be paid by Mr Leung (\$6 per share) and the size of the shareholding to be sold (it is not unusual for large blocks of shares to attract a premium), the Executive did not consider the price to be paid by Telefónica to Mr Leung to be a “*very high price*” that would tend to suggest that control over his remaining shareholding was being secured. Indeed with regards to the proposed prices for the On-Sales to Telefónica it appeared that Mr Leung would at best break even or at worst suffer a loss.

(c) Are there any options over the retained voting rights?

37. The parties confirmed that none of Mr Leung, the Foundations, CNC or Telefónica had options or similar rights or arrangements (whether formal or informal) in respect of any shares held by any of the parties (save for the arrangements between CNC and Telefónica discussed above).

(d) Selection by Mr Leung of a purchaser with reasonably compatible ideas

38. Mr Leung informed the Executive that he considered Telefónica, as a major multinational communications group, to be a solid strategic investor in PCCW. The Executive also noted that on completion of the On-Sales it was intended that, through the SPV, CNC would nominate one further representative (in addition to the then existing two non-executive directors and one executive director on the PCCW board nominated by CNC) while Telefónica would nominate two representatives to the board of PCCW. At the time of the Application there were 16 directors on the PCCW board, comprising nine non-executive directors of which six were independent non-executive directors. In this regard Note 7 to Rule 26.1 states that it would be natural for a vendor of part of a controlling holding to select a purchaser whose ideas as regards the way the company is to be directed are reasonably compatible with his own. It is also natural that a purchaser of a

substantial holding in a company should press for board representation and perhaps make the vendor's support for this a condition of purchase. Accordingly, these factors, divorced from other evidence of a significant degree of control over the retained voting rights, would not lead the Executive to conclude that a general offer should be made.

Ruling

39. On the basis of the above, on 10 November 2006, the Executive issued the ruling referred to in paragraph 4 above. The ruling also clarified that the Executive considered Mr Leung, Mr KS Li and the Foundations to be acting in concert in respect of PCCW and confirmed that the Executive would continue to monitor developments in the case. The Executive requested to be advised immediately if there was any material change to the information or representations made so that it could decide on whether its ruling remained valid.

17 May 2007

DEFINITIONS

Acquisition of voting rights: Acquisition of voting rights includes the exercise of control or direction over voting rights other than by way of a revocable proxy given for no or nominal consideration for the purpose of one meeting of shareholders only.

Acting in concert: Persons acting in concert comprise persons who, pursuant to an agreement or understanding (whether formal or informal), actively co-operate to obtain or consolidate “control” (as defined below) of a company through the acquisition by any of them of voting rights of the company.

Without prejudice to the general application of this definition, persons falling within each of the following classes will be presumed to be acting in concert with others in the same class unless the contrary is established:-

- (1) a company, its parent, its subsidiaries, its fellow subsidiaries, associated companies of any of the foregoing, and companies of which such companies are associated companies;
- (2) a company with any directors (together with their close relatives, related trusts and companies controlled[#] by any of the directors, their close relatives or related trusts) of it or of its parent;
- (3) a company with any of its pension funds, provident funds and employee share schemes;

Note: Class (3) does not apply to an employee benefit trust. The Executive will apply Note 20 to Rule 26.1 to determine whether the directors and shareholders of a company are acting in concert with the trustees of an employee benefit trust of the same company.

- (4) a fund manager (including an exempt fund manager) with any investment company, mutual fund, unit trust or other person, whose investments such fund manager manages on a discretionary basis, in respect of the relevant investment accounts;
- (5) a financial or other professional adviser (including a stockbroker)* with its client in respect of the shareholdings of the adviser and persons controlling[#], controlled by or under the same control as the adviser (except in the capacity of an exempt principal trader);
- (6) directors of a company (together with their close relatives, related trusts and companies controlled[#] by such directors, their close relatives and related trusts) which is subject to an offer or where the directors have reason to believe a bona fide offer for their company may be imminent;
- (7) partners;

- (8) an individual (including any person who is accustomed to act in accordance with the instructions of the individual) with his close relatives, related trusts and companies controlled[#] by him, his close relatives or related trusts; and
- (9) a person, other than an authorised institution within the meaning of the Banking Ordinance (Cap. 155) lending money in the ordinary course of business, providing finance or financial assistance (directly or indirectly) to any person (or a person acting in concert with such a person) in connection with an acquisition of voting rights (including any direct or indirect refinancing of the funding of the acquisition).

TAKEOVERS CODE

Note 7 to Rule 26.1:

7. *Vendor of part only of a shareholding*

Shareholders sometimes wish to sell part only of their holdings or a purchaser may be prepared to acquire part only of a holding. This arises particularly where an acquirer wishes to acquire under 30%, thereby avoiding an obligation under this Rule 26 to make a general offer. The Executive will be concerned to see whether in such circumstances the arrangements between the purchaser and vendor effectively allow the purchaser to exercise a significant degree of control over the retained voting rights, in which case a general offer would normally be required. These concerns will also apply when the purchaser is already a member of a group acting in concert with the vendor, or when the purchaser joins such a group.

The Executive will also take into account any other transactions between the purchaser and the vendor, and between the purchaser and other members of the group acting in concert with the vendor. This could include, for example, the aggregation of transfers of voting rights to the purchaser over a period of time, or arrangements which have an effect similar to transfer, such as the underwriting by a purchaser of a rights issue which the vendor has agreed not to take up, or a placing of shares with the purchaser.

A judgement on whether such a significant degree of control exists will obviously depend on the circumstances of each individual case, but, by way of guidance, the Executive would regard the following points as having some significance:-

- (a) *there would be less likelihood of a significant degree of control over the retained voting rights if the vendor was not an “insider”;*
- (b) *the payment of a very high price for the voting rights would tend to suggest that control over the entire holding was being secured;*
- (c) *if the parties negotiate options over the retained voting rights it may be more difficult for them to satisfy the Executive that a significant degree of control is absent. On the other hand, where the retained voting rights are in themselves a significant part of the company’s capital (or even in certain circumstances represent a significant sum of money in absolute terms) a correspondingly greater element of independence may be presumed; and*

(d) *it would be natural for a vendor of part of a controlling holding to select a purchaser whose ideas as regards the way the company is to be directed are reasonably compatible with his own. It is also natural that a purchaser of a substantial holding in a company should press for board representation and perhaps make the vendor's support for this a condition of purchase. Accordingly, these factors, divorced from any other evidence of a significant degree of control over the retained voting rights, would not lead the Executive to conclude that a general offer should be made.*

This announcement is made under the Hong Kong Codes on Takeovers and Mergers and Share Repurchases.



**CHINA NETWORK COMMUNICATIONS GROUP CORPORATION
中國網絡通信集團公司**

Announcement

China Network Communications Group Corporation ("CNC") announces that it has reached an agreement on 12 November 2006 with Telefónica Internacional S.A.U. ("Telefónica") that upon Telefónica acquiring 8% of the issued share capital of PCCW Limited ("PCCW"), CNC and Telefónica will transfer all of their respective interests in PCCW into a special purpose vehicle (the "SPV") which will hold an approximately 27.94% stake in PCCW and become the single largest shareholder of PCCW.

CNC, Telefónica and PCCW have signed a non-binding memorandum of understanding to develop a strategic alliance in relation to certain areas of business in the telecommunications and media sectors including, among others, IPTV and international wholesale services, in order to achieve synergy of the competitive advantages of the three groups of companies.

CNC is not acting in concert (within the meaning of the Hong Kong Codes on Takeovers and Mergers and Share Repurchases (the "Codes")) with any person (apart from Telefónica) in regard to its shareholding in PCCW. It has not, in regard to such shareholding, entered into any agreement or arrangement with any of Mr. Francis P. T. Leung, Li Ka-shing Foundation Limited and its representatives, Li Ka Shing (Canada) Foundation and its representatives, Mr. Li Ka Shing (or any company controlled by him) whether personally or through his agents or representatives, and Mr. Richard Li (apart from the shareholders' agreements entered into between CNC and three companies associated with Mr. Richard Li on 19 January 2005, the entering into of which was previously disclosed to the public and which shareholders' agreements do not render CNC be regarded as acting in concert with the parties to the agreements or any of the aforementioned persons).

Notwithstanding the establishment of the SPV as a shareholder of PCCW, CNC and persons acting in concert with it do not have control (within the meaning of the Codes) over PCCW, and CNC does not intend to control the board of PCCW and will not seek to do so in the future unless CNC gains control of PCCW by observing all applicable regulatory requirements under the Codes.

For and on behalf of
China Network Communications Group Corporation
ZHANG Chunjiang
(Legal Representative and General Manager)

Beijing, 12 November 2006

The Legal Representative and General Manager of CNC accepts full responsibility for the accuracy of information contained in this announcement and confirms, having made all reasonable inquiries, that to the best of his knowledge, opinions expressed in this announcement have been arrived at after due and careful consideration and there are no other facts not contained in this announcement, the omission of which would make any statement in this announcement misleading.

ANNOUNCEMENT

As previously announced, Mr Francis P.T Leung (“Mr Leung”) through his wholly owned company, Fiorlatte Limited (“Fiorlatte”), entered into an agreement (“Fiorlatte-PCRD Agreement”) on 9 July 2006 with Pacific Century Regional Developments Ltd. (“PCRD”), pursuant to which Fiorlatte agreed to acquire PCRD’s entire stake in PCCW Limited (“PCCW”), which amounts to approximately 22.65% of the existing issued share capital of PCCW. The purchase price was HK\$6.00 per share.

Mr Leung would like to announce that Fiorlatte has now reached binding agreements with Telefónica Internacional S.A.U (“Telefónica”) and separately with each of Li Ka Shing Foundation Limited (“HK Foundation”) and Li Ka Shing (Canada) Foundation (“Canadian Foundation”) so that:

- Telefónica will acquire and hold PCCW shares representing 8% of PCCW’s issued share capital;
- HK Foundation will acquire and hold PCCW shares representing 10% of PCCW’s issued share capital; and
- Canadian Foundation will acquire and hold PCCW shares representing 2% of PCCW’s issued share capital (collectively the “Transactions”).

Mr Leung will acquire and will continue to hold the remaining 2.65% interest. Mr Leung expects to finance this acquisition through a combination of his own resources, bank financing and a loan from Mr Li Ka Shing. Mr Leung currently holds PCCW shares amounting to approximately 0.7% of PCCW’s issued share capital, directly and through wholly owned companies, including Fiorlatte. Upon completion of the Fiorlatte-PCRD Agreement and the Transactions, he will hold an aggregate interest of 3.35% in PCCW’s issued share capital.

The agreements were entered into on 12 November 2006. The PCCW shares are being acquired at HK\$6.00 per share. In the case of the transaction with Telefónica, however, the price per share is subject to a downward adjustment of HK\$0.60 depending on the performance of PCCW’s share price for a certain period within 10 months after payment has been made by Telefónica.

Completion of each of the Transactions between Fiorlatte and each of Telefónica, HK Foundation and Canadian Foundation is conditional upon certain conditions, including the approval by the shareholders of PCRD of the transaction with Fiorlatte, the lapse or withdrawal of a scheme of arrangement currently proposed by PCRD to its shareholders, and the obtaining of all necessary regulatory consents or waivers, including from the Broadcasting Authority of Hong Kong.

The Takeovers Executive (“Executive”) of the Securities and Futures Commission of Hong Kong has ruled that Mr Leung, Mr Li Ka Shing, HK Foundation and Canadian Foundation are presumed to be acting in concert under The Codes on Takeovers and Mergers and Share Repurchases (“Code”) in respect of PCCW. The Executive has also ruled that there is not sufficient evidence to conclude that Mr Leung, Mr Li Ka Shing, HK Foundation and

Canadian Foundation (on the one hand) and Telefónica and China Network Communications Group Corporation (“CNC”) (on the other hand) are acting in concert in respect of PCCW within the meaning of the Code. Accordingly, there is not sufficient evidence that the Transactions give rise to any one or more of Mr Leung, Mr Li Ka Shing, HK Foundation, Canadian Foundation, Telefónica and CNC having to make a mandatory offer for any part or all of the issued share capital of PCCW.

In reaching this view the Executive has carefully considered the representations made to the Executive and in particular:

- the various confirmations therein to the effect that there is no agreement or understanding, whether formal or informal, between Mr Leung (and companies controlled by him) and/or Fiorlatte and/or Mr Li Ka Shing (and companies controlled by him) whether personally or through his agents or representatives and/or the Foundations (on the one hand) with any member of the CNC group and/or any member of the Telefónica group (on the other hand) in connection with the acquisition, holding or voting of PCCW Shares and/or in relation to the representation of CNC and/or Telefónica on the board of PCCW; and
- CNC’s indication that it will issue an announcement that (i) it is not acting in concert with any person (apart from Telefónica) in respect of its shareholding in PCCW; (ii) CNC has not entered into any agreement or arrangement with any of Mr Leung, HK Foundation, Canada Foundation and their representatives, Mr Li Ka Shing (or any company controlled by him) whether personally or through his agents or representatives and Mr Richard Li (apart from the previously disclosed shareholders agreements dated 19 January 2005 which do not render them parties acting in concert); and (iii) CNC and persons acting in concert with it do not have control (within the meaning of the Code) over PCCW, and that CNC does not intend to control the board of PCCW and will not seek to do so in future unless CNC gains control of PCCW in accordance with the Code.

The Transactions will terminate automatically if the Fiorlatte-PCRD Agreement terminates because its conditions are not satisfied by the long-stop date under the Fiorlatte-PCRD Agreement, which is 30 November 2006 or such later date and time as may be agreed in writing between PCRD and Fiorlatte.

The long-stop date for the closing of the Transactions will be 5 January 2007.

As provided in the Fiorlatte-PCRD Agreement, Fiorlatte has the right to accelerate completion of the acquisition of the PCCW shares under that agreement to a date that is on or after 20 December 2006.

FRANCIS P.T. LEUNG
12 November 2006

Mr Leung, in his own capacity and as the sole director of Fiorlatte Limited, accepts full responsibility for the accuracy of information contained in this announcement and confirms, having made all reasonable inquiries, that to the best of his knowledge, opinions expressed in this announcement have been arrived at after due and careful consideration and there are no other facts not contained in this announcement, the omission of which would make any statement in this announcement misleading.

Please also refer to the published version of this announcement in The Standard.