

The following is the reproduction of the audited financial statements of HKTGH for the year ended 31 December 2012 together with the independent auditor's report. References to page number refer to the original page number of the audited financial statements.

INDEPENDENT AUDITOR'S REPORT
TO THE BOARD OF DIRECTORS OF HKT GROUP HOLDINGS LIMITED
(Incorporated in the Cayman Islands with limited liability)

We have audited the consolidated financial statements of HKT Group Holdings Limited (the "Company") and its subsidiaries (together, the "Group") set out on pages 3 to 100, which comprise the consolidated and the company balance sheets as at December 31, 2012, and the consolidated income statement, the consolidated statement of comprehensive income, the consolidated statement of changes in equity and the consolidated statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Directors' Responsibility for the Consolidated Financial Statements

The directors of the Company are responsible for the preparation of consolidated financial statements that give a true and fair view in accordance with Hong Kong Financial Reporting Standards issued by the Hong Kong Institute of Certified Public Accountants, and for such internal control as the directors determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit and to report our opinion solely to you, as a body, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

We conducted our audit in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

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

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

INDEPENDENT AUDITOR'S REPORT
TO THE BOARD OF DIRECTORS OF HKT GROUP HOLDINGS LIMITED
(CONTINUED)
(Incorporated in the Cayman Islands with limited liability)

Opinion

In our opinion, the consolidated financial statements give a true and fair view of the financial position of the Company and the Group as at December 31, 2012, and of the Group's financial performance and cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards.

PricewaterhouseCoopers
Certified Public Accountants

Hong Kong, March 4, 2013

HKT GROUP HOLDINGS LIMITED

CONSOLIDATED INCOME STATEMENT FOR THE YEAR ENDED DECEMBER 31, 2012

	Note	2011 HK\$ million	2012 HK\$ million
Continuing operations			
Turnover	5	18,755	21,081
Cost of sales		(7,426)	(9,027)
General and administrative expenses		(8,097)	(9,067)
Other gains, net	6	213	20
Interest income		41	25
Finance costs	8	(1,547)	(876)
Share of results of an associate		(17)	(35)
Share of results of jointly controlled companies		(3)	(44)
		<hr/>	<hr/>
Profit before income tax	7	1,919	2,077
Income tax	10	(347)	(449)
		<hr/>	<hr/>
Profit for the year from continuing operations		1,572	1,628
Discontinued operations			
Profit for the year from discontinued operations	13	42	-
		<hr/>	<hr/>
Profit for the year		<u>1,614</u>	<u>1,628</u>
Attributable to:			
Equity holders of the Company		1,564	1,578
Non-controlling interests		50	50
		<hr/>	<hr/>
Profit for the year		<u>1,614</u>	<u>1,628</u>
Attributable to:			
Equity holders of the Company arising from:			
- continuing operations		1,522	1,578
- discontinued operations		42	-
		<hr/>	<hr/>
		<u>1,564</u>	<u>1,578</u>

The notes on pages 11 to 100 form part of these consolidated financial statements.

HKT GROUP HOLDINGS LIMITED

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME FOR THE YEAR ENDED DECEMBER 31, 2012

		2011 HK\$ million	2012 HK\$ million
	Note		
Profit for the year		1,614	1,628
Other comprehensive income			
Translation exchange differences			
- exchange differences on translating foreign operations		6	98
- release of translation reserve upon distribution in specie of shares in subsidiaries	38	11	-
Available-for-sale financial assets			
- changes in fair value		24	13
Cash flow hedges			
- effective portion of changes in fair value		16	(54)
- transfer from equity to consolidated income statement		(12)	19
Other comprehensive income for the year		45	76
Total comprehensive income for the year		<u>1,659</u>	<u>1,704</u>
Attributable to:			
Equity holders of the Company arising from:			
- continuing operations		1,562	1,654
- discontinued operations		47	-
Non-controlling interests		<u>1,609</u>	<u>1,654</u>
Total comprehensive income for the year		<u>1,659</u>	<u>1,704</u>

The notes on pages 11 to 100 form part of these consolidated financial statements.

HKT GROUP HOLDINGS LIMITED

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED DECEMBER 31, 2012

		Attributable to equity holders of the Company HK\$ million	Non- controlling interests HK\$ million	Total equity HK\$ million
	Note(s)			
At January 1, 2011		22,199	162	22,361
Comprehensive income				
Profit for the year		1,564	50	1,614
Total other comprehensive income		45	-	45
Total comprehensive income for the year		1,609	50	1,659
Total contributions by and distributions to owners of the company recognized in equity				
Capital contribution from CAS Holding No. 1 Limited	28	2,005	-	2,005
Special dividend in specie of shares in subsidiaries	28, 38	(2,861)	-	(2,861)
Dividend declared and paid to non-controlling shareholders of a subsidiary		-	(35)	(35)
Total contributions by and distributions to owners of the company recognized in equity		(856)	(35)	(891)
At December 31, 2011		22,952	177	23,129

The notes on pages 11 to 100 form part of these consolidated financial statements.

HKT GROUP HOLDINGS LIMITED

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY (CONTINUED) FOR THE YEAR ENDED DECEMBER 31, 2012

		Attributable to equity holders of the Company HK\$ million	Non- controlling interests HK\$ million	Total equity HK\$ million
	Note(s)			
At January 1, 2012		22,952	177	23,129
Comprehensive income				
Profit for the year		1,578	50	1,628
Total other comprehensive income		76	-	76
Total comprehensive income for the year		1,654	50	1,704
Total contributions by and distributions to owners of the company recognized in equity				
Interim dividend declared and paid in respect of the current year	11, 28	(1,287)	-	(1,287)
Issue of an ordinary share	26	168	-	168
Increase in interests in subsidiaries	39	(2)	(3)	(5)
Dividend declared and paid to non-controlling shareholders of a subsidiary		-	(41)	(41)
Total contributions by and distributions to owners of the company recognized in equity		(1,121)	(44)	(1,165)
At December 31, 2012		<u>23,485</u>	<u>183</u>	<u>23,668</u>

The notes on pages 11 to 100 form part of these consolidated financial statements.

HKT GROUP HOLDINGS LIMITED

**CONSOLIDATED BALANCE SHEET
AS AT DECEMBER 31, 2012**

	Note	2011 HK\$ million	2012 HK\$ million
ASSETS AND LIABILITIES			
Non-current assets			
Property, plant and equipment	14	14,253	14,227
Interests in leasehold land	15	316	303
Goodwill	16	35,892	36,025
Intangible assets	17	4,872	4,573
Interest in an associate	19	95	200
Interests in jointly controlled companies	20	506	534
Available-for-sale financial assets	21	72	85
Financial assets at fair value through profit or loss	22	-	8
Derivative financial instruments	25	275	253
Deferred income tax assets	29	3	3
Other non-current assets		498	531
		<u>56,782</u>	<u>56,742</u>
Current assets			
Prepayments, deposits and other current assets		2,272	2,732
Inventories	23(a)	1,076	971
Trade receivables, net	23(b)	2,541	3,425
Amounts due from related companies		-	25
Derivative financial instruments	25	-	4
Financial assets at fair value through profit or loss	22	-	8
Income tax recoverable		68	-
Cash and cash equivalents	31(d)	1,793	2,398
		<u>7,750</u>	<u>9,563</u>
Current liabilities			
Short-term borrowings	23(c)	31	8,462
Trade payables		1,532	1,966
Accruals and other payables		2,264	2,539
Carrier licence fee liabilities	30	190	200
Amounts due to related companies	4(c)	29	135
Amounts due to fellow subsidiaries, the immediate holding company and the ultimate holding company	4(c)	8,631	8,059
Advances from customers		1,483	1,684
Current income tax liabilities		-	341
		<u>14,160</u>	<u>23,386</u>
Net current liabilities		<u>(6,410)</u>	<u>(13,823)</u>
Total assets less current liabilities		<u>50,372</u>	<u>42,919</u>

HKT GROUP HOLDINGS LIMITED**CONSOLIDATED BALANCE SHEET (CONTINUED)**
AS AT DECEMBER 31, 2012

	Note	2011 HK\$ million	2012 HK\$ million
Non-current liabilities			
Long-term borrowings	24	23,470	15,644
Deferred income tax liabilities	29	1,991	1,831
Deferred income		893	989
Carrier licence fee liabilities	30	838	736
Other long-term liabilities		51	51
		<u>27,243</u>	<u>19,251</u>
Net assets		<u>23,129</u>	<u>23,668</u>
CAPITAL AND RESERVES			
Share capital	26	4,961	4,961
Reserves	28	17,991	18,524
		<u>22,952</u>	<u>23,485</u>
Equity attributable to equity holders of the Company		<u>22,952</u>	<u>23,485</u>
Non-controlling interests		<u>177</u>	<u>183</u>
		<u>23,129</u>	<u>23,668</u>
Total equity		<u>23,129</u>	<u>23,668</u>

Approved and authorized for issue by the Board of Directors on March 4, 2013 and signed on behalf of the Board by

Alexander Anthony Arena
Director

Hui Hon Hing, Susanna
Director

The notes on pages 11 to 100 form part of these consolidated financial statements.

HKT GROUP HOLDINGS LIMITED**BALANCE SHEET
AS AT DECEMBER 31, 2012**

	Note	2011 HK\$ million	2012 HK\$ million
ASSETS AND LIABILITIES			
Non-current assets			
Investments in subsidiaries	18	17,226	17,394
		-----	-----
Current assets			
Amounts due from subsidiaries	18(a)	4,488	3,344
Amount due from the immediate holding company	4(c)	-	91
		-----	-----
		4,488	3,435
		-----	-----
Current liabilities			
Amounts due to subsidiaries	18(b)	2,484	1,429
		-----	-----
Net current assets			
		2,004	2,006
		-----	-----
Net assets			
		19,230	19,400
		=====	=====
CAPITAL AND RESERVES			
Share capital	26	4,961	4,961
Reserves	28	14,269	14,439
		-----	-----
Total equity			
		19,230	19,400
		=====	=====

Approved and authorized for issue by the Board of Directors on March 4, 2013 and signed on behalf of the Board by

Alexander Anthony Arena
Director

Hui Hon Hing, Susanna
Director

The notes on pages 11 to 100 form part of these consolidated financial statements.

HKT GROUP HOLDINGS LIMITED

CONSOLIDATED STATEMENT OF CASH FLOWS FOR THE YEAR ENDED DECEMBER 31, 2012

	Note	2011 HK\$ million	2012 HK\$ million
Net cash generated from operating activities	31(a)	7,889	6,477
Investing activities			
Proceeds from disposals of property, plant and equipment		19	6
Purchases of property, plant and equipment		(1,704)	(1,906)
Purchases of intangible assets		(1,771)	(1,719)
Net outflow of cash and cash equivalents in respect of additions upon business combinations	31(b)	-	(227)
Settlement of obligation assumed upon business combinations	31(b)	-	(121)
Purchases of available-for-sale financial assets		(223)	-
Proceeds from disposal of available-for-sale financial assets		31	-
Acquisition of an associate		(41)	-
Loans to an associate		(71)	(139)
Acquisition of jointly controlled companies		(6)	-
Loan to a jointly controlled company		(41)	(71)
Disposal of a subsidiary	31(c)	(16)	-
Consideration paid to non-controlling interests for an increase in ownership interest in subsidiaries		-	(5)
Net cash used in investing activities		(3,823)	(4,182)
Financing activities			
New borrowings raised		6,251	3,617
Interest paid		(1,362)	(735)
Repayments of borrowings		(17,972)	(3,075)
Increase/(decrease) in amount due to the immediate holding company		7,800	(195)
(Decrease)/increase in non-trade balance due to fellow subsidiaries and the ultimate holding company		(2,475)	21
Special dividend in specie of shares in subsidiaries	38	(124)	-
Interim dividend paid to shareholders of the Company	11	-	(1,287)
Dividend paid to non-controlling shareholders of a subsidiary		(35)	(41)
Net cash used in financing activities		(7,917)	(1,695)
Net (decrease)/increase in cash and cash equivalents		(3,851)	600
Exchange differences		7	5
Cash and cash equivalents			
Beginning of year		5,637	1,793
End of year	31(d)	1,793	2,398

The notes on pages 11 to 100 form part of these consolidated financial statements.

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1 General information and group reorganization

(a) General Information

HKT Group Holdings Limited (the “Company”) was incorporated in the Cayman Islands on January 18, 2008. The address of its registered office is PO Box 309, Uglund House, Grand Cayman, KY1-1104, Cayman Islands.

The Company is a direct wholly-owned subsidiary of HKT Limited (“HKT”) which is a company incorporated in the Cayman Islands with its share stapled units jointly issued with HKT Trust (the “Share Stapled Units”) listed on The Stock Exchange of Hong Kong Limited (the “Stock Exchange”), upon the completion of the group reorganization as set out in note 1(b). The directors consider PCCW Limited (“PCCW”), a company incorporated in Hong Kong with its shares listed on the Stock Exchange, to be the Company’s ultimate holding company.

The principal activities of the Company and its subsidiaries (collectively, the “Group”) are the provision of fixed core, mobile, local and international telecommunications services, Internet access services and the sale and rental of telecommunications equipment primarily in Hong Kong, and also in mainland China (the “PRC”) and elsewhere in the Asia Pacific region (the “Telecommunications Business”).

During the year, the Group was involved in the following principal activities:

Continuing operations

Provision of fixed core, mobile, local and international telecommunications services, Internet access services and the sale and rental of telecommunications equipment primarily in Hong Kong, and also in mainland China (the “PRC”) and elsewhere in the Asia Pacific region (the “Telecommunications Business”).

The Group was also involved in the following activities during the year ended December 31, 2011 and the Group’s involvement in these activities was discontinued upon completion of the Group reorganization set out in note 1(b).

Discontinued operations

- (i) Media Business includes interactive pay-TV service, Internet portal multimedia entertainment platform and the directories operations in Hong Kong and the PRC carried out by the Media Group (as defined below); and
- (ii) Solutions Business offers information and communications technologies services and solutions in Hong Kong and the PRC carried out by the Solutions Group (as defined below).

These consolidated financial statements are presented in millions of units of Hong Kong dollars (HK\$ million), unless otherwise stated. These consolidated financial statements have been approved for issue by the Board of Directors on March 4, 2013.

(b) Group reorganization

On November 29, 2011, the Telecommunications Business of PCCW was spun off and separately listed on the Stock Exchange (the “Listing”) as Share Stapled Units. In preparation for the Listing, a group reorganization was completed on or before November 29, 2011 as summarized below:

- (i) PCCW Holding Company (Beijing) Limited, an indirect wholly-owned subsidiary of the Company, transferred the entire registered capital of 電訊盈科(北京)有限公司 (unofficial name: PCCW (Beijing) Limited) to PCCW Services Limited, a wholly-owned subsidiary of PCCW at a consideration of HK\$51.8 million.

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1 General information and group reorganization (continued)

(b) Group reorganization (continued)

- (ii) The Company transferred businesses other than the Telecommunications Business to subsidiaries of PCCW through distribution of its interests in HKT Solutions Holdings Limited (“HKT Solutions”) and thereby its subsidiaries (the “Solutions Group”) and HKT Media Holdings Limited (“HKT Media”) and thereby its subsidiaries (the “Media Group”) to its immediate holding company, CAS Holding No. 1 Limited (“CAS No. 1”) by way of special dividend in specie of shares in subsidiaries;
- (iii) Certain entities and assets that constitute businesses managed by management of the Telecommunications Business were transferred from the Solutions Group to subsidiaries of the Company;
- (iv) Certain entities and assets that constitute businesses managed by management of the Solutions Group were transferred from subsidiaries of the Company to the Solutions Group;
- (v) HKT issued 4,363,361,192 ordinary shares and 4,363,361,192 preference shares, and a promissory note of approximately HK\$1,144 million to CAS No. 1, in consideration of the transfer of all the shares in the Company held by CAS No. 1, representing 100% interest in the Company, to HKT. Subsequent to the transfer, the Company became a direct wholly-owned subsidiary of HKT.

2 Basis of preparation and principal accounting policies

(a) Basis of preparation of the financial statements

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

- financial assets at fair value through profit or loss (see *note 2(k)(i)*);
- available-for-sale financial assets (see *note 2(k)(ii)*); and
- derivative financial instruments (see *note 2(m)*).

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

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

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

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

2 Basis of preparation and principal accounting policies (continued)

(b) Statement of compliance

These consolidated financial statements have been prepared in accordance with the HKFRSs, which is a collective term for all individual Hong Kong Financial Reporting Standards, Hong Kong Accounting Standards (“HKASs”) and Interpretations (“Ints”) issued by the Hong Kong Institute of Certified Public Accountants (“HKICPA”), and have been prepared under the historical cost convention except for certain financial instruments which are stated at fair values, as explained in the significant accounting policies set out below.

The following new HKFRSs are mandatory for the first time for the financial year beginning January 1, 2012, but have no material effect on the Group’s results and financial position for the current and prior accounting periods.

- HKFRS 1 (Amendment), Severe hyperinflation and removal of fixed dates for first-time adopters.
- HKFRS 7 (Amendment), Disclosures – Transfers of financial assets.
- HKAS 12 (Amendment), Deferred tax – Recovery of underlying assets.

The Group has not adopted any new or revised standard or interpretation that is not yet effective for the current accounting period, details of which are set out in note 40.

(c) Subsidiaries and non-controlling interests

Subsidiaries are entities controlled directly or indirectly 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.

The acquisition method of accounting is used to account for the acquisition of subsidiaries by the Group. The cost of an acquisition is measured as the aggregate fair value of the assets transferred, equity instruments issued and liabilities incurred or assumed at the date of exchange. Acquisition-related costs are expensed as incurred. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. On an acquisition-by-acquisition basis, the Group recognizes any non-controlling interest in the acquiree either at fair value or at the non-controlling interest’s proportionate share of the acquiree’s net assets. The excess of the consideration transferred, the amount of any non-controlling interest in the acquiree and the acquisition-date fair value of any previous equity interest in the acquiree over the fair value of the identifiable net assets acquired is recorded as goodwill (see *note 2(i)*). If this is less than the fair value of the net assets of the subsidiary acquired in the case of a bargain purchase, the difference is recognized directly in the consolidated income statement. Where businesses are acquired and fair values of the net assets of the acquired business are finalized within 12 months of the acquisition date, all fair value adjustments are recorded with effect from the date of acquisition and consequently may result in the restatement of previously reported financial results (see *note 37*).

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

2 Basis of preparation and principal accounting policies (continued)

(c) Subsidiaries and non-controlling interests (continued)

Non-controlling interests represent the portion of the net assets of subsidiaries attributable to interests that are not owned by the Group, whether directly or indirectly through subsidiaries, and in respect of which the Group has not agreed any additional terms with the holders of those interests which would result in the Group as a whole having a contractual obligation in respect of those interests that meets the definition of a financial liability. Non-controlling interests are presented within equity in the consolidated balance sheet and consolidated statement of changes in equity, separately from equity attributable to the equity holders of the Company. Non-controlling interests in the results of the Group are presented on the face of the consolidated income statement as an allocation of the total profit or loss for the year between non-controlling interests and the equity holders of the Company.

The Group treats transactions with non-controlling interests that do not result in a loss of control as transactions with equity owners of the Group. For purchases from non-controlling interests, the difference between any consideration paid and the relevant share acquired of the carrying value of net assets of the subsidiary is recorded in equity. Gains or losses on disposals of equity interests to non-controlling interests are also recorded in equity.

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

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

Adjustments have been made to the financial statements of subsidiaries when necessary to align their accounting policies to ensure consistency with the policies adopted by the Group.

(d) Associates

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

Interest in an associate is accounted for in the consolidated financial statements under the equity method and is initially recorded at cost. The Group's interest in an associate includes goodwill identified on acquisition, net of any accumulated impairment loss and adjusted thereafter for the post-acquisition change in the Group's share of the associates' net assets. The consolidated income statement includes the Group's share of post-acquisition, post-tax results of the associate and any impairment losses for the year. The consolidated statement of comprehensive income includes the Group's share of the post-acquisition post-tax items of the associate's other comprehensive income.

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

2 Basis of preparation and principal accounting policies (continued)

(d) Associates (continued)

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

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

If the ownership interest in an associate is reduced but significant influence is retained, only a proportionate share of the amounts previously recognized in other comprehensive income are reclassified to profit or loss where appropriate.

The results of the associate are accounted for by the Group on the basis of dividends received and receivable.

Adjustments have been made to the financial statements of the associate when necessary to align its accounting policies to ensure consistency with the policies adopted by the Group.

(e) Jointly controlled companies

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

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

Investments in jointly controlled companies are accounted for in the consolidated financial statements under the equity method and are initially recorded at cost. The Group's investment in jointly controlled companies includes goodwill identified on acquisition, net of any accumulated impairment loss and adjusted thereafter for the post-acquisition change in the Group's share of the jointly controlled companies' net assets. The consolidated income statement includes the Group's share of post-acquisition, post-tax results of the jointly controlled companies and any impairment losses for the year. The consolidated statement of comprehensive income include the Group's share of the post-acquisition, post-tax items of the jointly controlled companies' other comprehensive income.

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

2 Basis of preparation and principal accounting policies (continued)

(e) Jointly controlled companies (continued)

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

Unrealized profits and losses resulting from transactions between the Group and their jointly controlled companies are eliminated to the extent of the Group's interest in the jointly controlled companies, except where unrealized losses provide evidence of an impairment of the asset transferred, in which case they are recognized immediately in the consolidated income statement.

Adjustments have been made to the financial statements of jointly controlled entities when necessary to align their accounting policies to ensure consistency with the policies adopted by the Group.

(f) Gaining or losing control or significant influence

When the Group ceases to have control or significant influence, any retained interest in the entity is re-measured to its fair value, with the change in carrying amount recognized in investor profit or loss. The fair value is the initial carrying amount for the purposes of subsequently accounting for the retained interest as joint venture, associates or financial asset. In addition, any amounts previously recognized in other comprehensive income in respect of that entity are accounted for as if the Group had disposed of the related assets or liabilities. This may mean that amounts previously recognized in other comprehensive income are reclassified to profit or loss.

(g) Property, plant and equipment

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

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

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

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

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

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

2 Basis of preparation and principal accounting policies (continued)

(g) Property, plant and equipment (continued)

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

Buildings	Over the shorter of the unexpired term of land lease and the estimated useful lives
Exchange equipment	5 to 12 years
Transmission plant	5 to 30 years
Other plant and equipment	Over the shorter of 1 to 17 years and the term of lease

The assets' useful lives and residual values, if any, are reviewed, and adjusted if appropriate, at each balance sheet date.

(h) Leased assets

An arrangement, comprising a transaction or a series of transactions, is or contains a lease if the Group determines that the arrangement conveys a right to use a specific asset or assets for an agreed period of time in return for a payment or a series of payments. Such a determination is made based on an evaluation of the substance of the arrangement and is regardless of whether the arrangement takes the legal form of a lease.

(i) Classification of assets leased to the Group

Leases which do not transfer substantially all the risks and rewards of ownership to the Group are classified as operating leases.

(ii) Assets leased out under operating leases

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

(iii) Operating lease charges

Where the Group has the use of assets held under operating leases, payments made under the leases are charged to the consolidated income statement in equal instalments over the accounting periods covered by the lease term. Lease incentives received are recognized in the consolidated income statement as an integral part of the aggregate net lease payments made. Contingent rentals are charged to the consolidated income statement in the accounting period in which they are incurred.

The cost of acquiring land held under an operating lease is stated in the consolidated balance sheet as "Interests in leasehold land" and is amortized to the consolidated income statement on a straight-line basis over the period of the lease term.

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

2 Basis of preparation and principal accounting policies (continued)

(i) Goodwill

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

Goodwill is stated in the consolidated balance sheet at cost less accumulated impairment losses. Goodwill is allocated to cash-generating units ("CGUs") and is tested annually for impairment (see *note 2(l)(ii)*). In respect of the associate and jointly controlled companies, the carrying amount of goodwill is included in the carrying amount of the interests in an associate and jointly controlled companies respectively.

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

(j) Intangible assets (other than goodwill)

(i) Customer acquisition costs

Costs incurred to acquire contractual relationships with customers are capitalized if it is probable that future economic benefits will flow from the customers to the Group and such costs can be measured reliably. Capitalized customer acquisition costs are amortized on a straight-line basis over the minimum enforceable contractual periods. By the end of the minimum enforceable contractual period, fully amortized customer acquisition costs will be written off.

In the event that a customer terminates the contract prior to the end of the minimum enforceable contractual period, the unamortized customer acquisition cost will be written off immediately in the consolidated income statement.

(ii) Carrier licences

The carrier licences to establish and maintain the telecommunication network and to provide telecommunication services are recorded as intangible assets. Upon the issuance of the licence, the cost thereof, which is the discounted value of the minimum annual fees payable over the period of the licence and directly attributable costs of preparing the asset for its intended use, is recorded together with the related obligations. Where the Group has the right to return a licence and expect to do so, the asset and the related obligation recorded reflect the expected period that the licence will be held. Amortization is provided on a straight-line basis over the estimated useful life of the licence, commencing from the date of launch of the relevant telecommunication services.

The difference between the discounted value and the total of the minimum annual fee payments represents the effective cost of financing. Such finance cost will be charged to the consolidated income statement in the period in which it is incurred using the effective interest method.

Variable annual payments on top of the minimum annual payments, if any, are recognized in the consolidated income statement as incurred.

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

2 Basis of preparation and principal accounting policies (continued)

(j) Intangible assets (other than goodwill) (continued)

(iii) Software

Costs incurred to acquire, develop or enhance scientific or technical knowledge, design and implementation of new process or systems, licences, intellectual property, market knowledge and trademarks are capitalized as “intangible assets” if it is identifiable and the entity has power to obtain future economic benefits flowing from the underlying resource.

Development costs that are directly attributable to the design and testing of the identifiable software are capitalized as intangible assets if the following criteria are met:

- it is technically feasible to complete the software so that it will be available for use;
- adequate technical, financial and other resources are available to complete the development and to use the software;
- the costs attributable to acquisition, development and enhancement of the software can be reliably measured; and
- the Group has power to obtain future economic benefits flowing from the underlying source.

Development costs that do not meet the above criteria are expensed in the consolidated income statement as incurred.

Capitalized software costs are amortized on a straight-line basis over the estimated useful life of 7 years.

(iv) Other intangible assets

Other intangible assets that are acquired by the Group are stated in the consolidated balance sheet at cost less accumulated amortization (where the estimated useful life is finite) and impairment losses (see *note 2(l)(ii)*). Expenditures on internally generated goodwill and brands are recognized as expenses in the period in which they are incurred.

Amortization of intangible assets with finite useful lives is charged to the consolidated income statement on a straight-line basis over their estimated useful lives. The following intangible assets with finite useful lives are amortized from the date they are available for use and their estimated useful lives are as follows:

Trademarks	20 years
Customer base	1 to 10 years
Programme costs	Over the terms of the contract period

The assets' useful lives and their amortization method are reviewed annually.

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

2 Basis of preparation and principal accounting policies (continued)

(k) Investments in equity securities

The Group classifies its investments in equity securities, other than interests in subsidiaries and interests in an associate and jointly controlled companies, as (i) financial assets at fair value through profit or loss, or (ii) available-for-sale financial assets.

Investments in equity securities are initially recognized at fair value plus transaction costs, except as indicated otherwise below. The fair value of quoted investments is based on current bid price. The investments are subsequently accounted for based on their classification as set out below:

(i) Financial assets at fair value through profit or loss

This category comprises financial assets designated as fair value through profit or loss at inception.

Financial assets at fair value through profit or loss are classified as current assets, if they are either held for trading or are expected to be realized within 12 months from the balance sheet date. Any attributable transaction costs are recognized in the income statement as incurred.

At each balance sheet date, the fair value is re-measured based on their current bid prices in an active market, with any unrealized holding gains or losses arising from the changes in fair value being recognized in 'other (losses)/gains, net' in the consolidated income statement in the period in which they arise. The net gain or loss recognized in the income statement does not include any interest earned or dividends on the financial assets as these are recognized in accordance with the policies set out in notes 2(u)(v) and 2(u)(vii) respectively.

(ii) Available-for-sale financial assets

Available-for-sale financial assets are non-derivative financial assets that are either designated in this category or not classified as financial assets at fair value through profit and loss, held-to-maturity investments and loans and receivables. They are included in non-current assets unless the Group intends to dispose of the investment within 12 months from the balance sheet date.

At each balance sheet date, the fair value of available-for-sale financial assets is re-measured, with any unrealized holding gains or losses arising from the changes in fair value being recognized in other comprehensive income and accumulated separately in the available-for-sale financial assets reserve under equity, except for impairment losses (see note 2(l)(i)) and, in the case of monetary items, foreign exchange gains and losses which are recognized directly in the consolidated income statement. Dividend income from these investments is recognized in the consolidated income statement in accordance with the policy set out in note 2(u)(vii). When the investments are derecognized or impaired (see note 2(l)(i)), the cumulative gain or loss previously recognized directly in the equity is recognized in the consolidated income statement.

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

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

2 Basis of preparation and principal accounting policies (continued)

(1) Impairment of assets

(i) Impairment of investments in equity securities and other receivables

Investments in equity securities (other than investments in subsidiaries and interests in an associate and jointly controlled companies: see *note 2(l)(ii)*) and other current and non-current receivables that are stated at cost or amortized cost or are classified as available-for-sale financial assets are reviewed at each balance sheet date to determine whether there is objective evidence of impairment. Objective evidence of impairment includes observable data that comes to the attention of the Group about one or more of the following loss events:

- significant financial difficulty of the debtor;
- a breach of contract, such as a default or delinquency in interest or principal payments;
- it becoming probable that the debtor will enter bankruptcy or other financial reorganization; or
- observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of financial assets.

If any such evidence exists, any impairment loss is determined and recognized as follows:

- For trade and other current receivables and other financial assets carried at amortized cost, the impairment loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition of these assets), where the effect of discounting is material. This assessment is made collectively where financial assets carried at amortized cost share similar risk characteristics, such as similar past due status, and have not been individually assessed as impaired. Future cash flows for financial assets which are assessed for impairment collectively are based on historical loss experience for assets with credit risk characteristics similar to the collective group.

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

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

Impairment losses recognized in the consolidated income statement in respect of equity instruments classified as available-for-sale financial assets are not reversed through the consolidated income statement. Any subsequent increase in the fair value of such assets is recognized in other comprehensive income and accumulated separately in the available-for-sale financial assets reserve under equity.

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

2 Basis of preparation and principal accounting policies (continued)

(1) Impairment of assets (continued)

(i) Impairment of investments in equity securities and other receivables (continued)

Impairment losses are written off against the corresponding assets directly, except for impairment losses recognized in respect of trade receivables, whose recovery are considered doubtful but not remote. In this case, the impairment loss for doubtful debts is recorded using an allowance account. When the Group is satisfied that recovery is remote, the amount considered irrecoverable is written off against receivables directly and any amounts held in the allowance account relating to that debt are reversed. Subsequent recoveries of amounts previously charged to the allowance account are reversed against the allowance account. Other changes in the allowance account and subsequent recoveries of amounts previously written off directly are recognized in the consolidated income statement.

(ii) Impairment of other assets

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

- property, plant and equipment;
- interests in leasehold land;
- goodwill and other intangible assets;
- interests in an associate and jointly controlled companies; and
- investments in subsidiaries (at Company level).

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

– Calculation of recoverable amount

The recoverable amount of an asset is the greater of its fair value less cost to sell and value in use. Fair value less cost 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. Where an asset does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the smallest group of assets that generates cash inflows independently (i.e. a CGU).

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

2 Basis of preparation and principal accounting policies (continued)

(l) Impairment of assets (continued)

(ii) Impairment of other assets (continued)

– Recognition of impairment losses

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

– Reversals of impairment losses

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

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

(m) Derivative financial instruments

Derivative financial instruments are initially recognized at fair value on the date a derivative contract is entered into and are subsequently remeasured at their fair value at each balance sheet date. The gain or loss on remeasurement to fair value is recognized immediately in the consolidated income statement, except where the derivatives are designated and qualify for hedge accounting, in which case recognition of any resultant gain or loss depends on the nature of the item being hedged (see *note 2(n)*).

The full fair value of a hedging derivative is classified as non-current asset or liability when the remaining hedged item has a maturity of more than 12 months, and as a current asset or liability when the remaining maturity of the hedged item is less than 12 months. Trading derivatives are classified as current assets or liabilities.

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

2 Basis of preparation and principal accounting policies (continued)

(n) Hedging

(i) Fair value hedge

Where a derivative financial instrument is designated as a hedge of the fair value of a recognized asset or liability or an unrecognized firm commitment (or an identified portion of such asset, liability or firm commitment), changes in the fair value of the derivative are recorded in the consolidated income statement within “Finance costs, net”, together with any changes in fair value of the hedged asset or liability that are attributable to the hedged risk.

When a hedging instrument expires or is sold, terminated or exercised, or no longer meets the criteria for hedge accounting; or the Group revokes designation of the hedge relationship, the cumulative adjustment to the carrying amount of a hedged item for which the effective interest method is used is amortized to the consolidated income statement over the residual period to maturity.

(ii) Cash flow hedge

Where a derivative financial instrument is designated as a hedge of the variability in cash flows of a recognized asset or liability, or a highly probable forecast transaction or the foreign currency risk of a committed future transaction, the effective portion of changes in the fair value of the derivative is recognized in other comprehensive income and accumulated separately in the hedging reserve under equity. The ineffective portion of any gain or loss is recognized immediately in the consolidated income statement.

If a hedge of a forecast transaction subsequently results in the recognition of a non-financial asset or non-financial liability, the associated cumulative gain or loss is removed from equity and included in the initial cost or other carrying amount of the non-financial asset or liability.

If a hedge of a forecast transaction subsequently results in the recognition of a financial asset or a financial liability, the associated cumulative gain or loss is removed from equity and recognized in the consolidated income statement in the same period or periods during which the asset acquired or liability assumed affects the consolidated income statement (such as when the interest income or expense is recognized).

For cash flow hedges, other than those covered by the preceding two policy statements, the associated cumulative gain or loss is removed from equity and recognized in the consolidated income statement in the same period or periods during which the hedged forecast transaction affects the consolidated income statement.

When a hedging instrument expires or is sold, terminated or exercised, or no longer meets the criteria for hedge accounting; or the Group revokes designation of the hedge relationship but the hedged forecast transaction is still expected to occur, the associated cumulative gain or loss at that point remains in equity and is recognized in accordance with the above policy when the transaction occurs. If the hedged transaction is no longer expected to occur, the cumulative unrealized gain or loss recognized in equity is recognized immediately in the consolidated income statement.

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

2 Basis of preparation and principal accounting policies (continued)

(o) Inventories

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

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

Work-in-progress is stated at the lower of cost, which comprises labor, materials and overheads where appropriate, and the net realizable value.

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

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

(p) Trade and other receivables

Trade and other receivables are initially recognized at fair value and thereafter stated at amortized cost using the effective interest method, less allowance for impairment of doubtful debts (see *note 2(l)(i)*).

(q) Cash and cash equivalents

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

(r) Trade and other payables

Trade and other payables are initially recognized at fair value and subsequently stated at amortized cost using the effective interest method.

(s) Borrowings

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

Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the end of the reporting period.

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

2 Basis of preparation and principal accounting policies (continued)

(t) Provisions and contingent liabilities

Provisions are recognized when (i) the Group has a present legal or constructive obligation arising as a result of a past event; (ii) it is probable that an outflow of economic benefits will be required to settle the obligation; and (iii) a reliable estimate can be made of the amount of the obligation. Where the time value of money is material, provisions are stated at the present value of the expenditure expected to settle the obligation. The increase in provision due to the passage of time is recognized as interest expense.

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

(u) Revenue recognition

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

(i) Telecommunications and other services

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

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

Up-front fees received for installation of equipment and activation of customer service are deferred and recognized over the estimated customer relationship period.

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

(ii) Sales of goods

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

(iii) Rental income from operating leases

Rental income receivable under operating leases is recognized in the consolidated income statement in equal installments over the periods covered by the lease term. Lease incentives granted are recognized in the consolidated income statement as an integral part of the aggregate net lease payments receivable. Contingent rentals are recognized as income in the accounting period in which they are earned.

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

2 Basis of preparation and principal accounting policies (continued)

(u) Revenue recognition (continued)

(iv) Contract revenue

Revenue from a fixed price contract is recognized using the percentage of completion method, measured by reference to the percentage of contract costs incurred to date to estimated total contract costs for the contract.

When the outcome of a construction contract cannot be estimated reliably, revenue is recognized only to the extent that it is probable the contract costs incurred will be recoverable.

(v) Interest income

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

(vi) Commission income

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

(vii) Dividend income

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

(v) Borrowing costs

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

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

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

(w) Income tax

- (i)** Income tax for the year comprises current income tax and movements in deferred income tax assets and liabilities. Current income tax and movements in deferred income tax assets and liabilities are recognized in the consolidated income statement except to the extent that they relate to items recognized in other comprehensive income or directly in equity, in which case the relevant amounts are recognized in other comprehensive income or directly in equity, respectively.

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

2 Basis of preparation and principal accounting policies (continued)

(w) Income tax (continued)

- (ii) Current income 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 income tax payable in respect of previous year.
- (iii) Deferred income tax assets and liabilities arise from deductible and taxable temporary differences respectively, being the differences between the carrying amounts of assets and liabilities for financial reporting purposes and the tax bases. Deferred income tax assets also arise from unused tax losses and unused tax credits.

All deferred income tax liabilities, and all deferred income tax assets to the extent that it is probable that future taxable profits will be available against which the asset can be utilized, are recognized. Future taxable profits that may support the recognition of deferred income tax assets arising from deductible temporary differences include those that will arise from the reversal of existing taxable temporary differences, provided those differences relate to the same taxation authority and the same taxable entity, and are expected to reverse either in the same period as the expected reversal of the deductible temporary difference or in periods into which a tax loss arising from the deferred income tax asset can be carried back or forward. The same criteria are adopted when determining whether existing taxable temporary differences support the recognition of deferred income tax assets arising from unused tax losses and credits, that is, those differences are taken into account if they relate to the same taxation authority and the same taxable entity, and are expected to reverse in a period, or periods, in which the tax loss or credit can be utilized.

The amount of deferred income tax recognized is measured based on the expected manner of realization or settlement of the carrying amount of the assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date and are expected to apply when the related deferred income tax asset is realized and the deferred income tax liability is settled. Deferred income tax assets and liabilities are not discounted.

The carrying amount of a deferred income tax asset is reviewed at each balance sheet date and is reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow the related tax benefit to be utilized. Any such reduction is reversed to the extent that it becomes probable that sufficient taxable profits will be available.

- (iv) Current income tax balances and deferred income tax balances, and movements therein, are presented separately from each other and are not offset. Current income tax assets are offset against current income tax liabilities, and deferred income tax assets against deferred income tax liabilities, if the Group has the legally enforceable right to set off current income tax assets against current income tax liabilities and the following additional conditions are met:
 - in the case of current income tax assets and liabilities, the Group intends either to settle on a net basis, or to realize the asset and settle the liability simultaneously; or
 - in the case of deferred income tax assets and liabilities, if they relate to income taxes levied by the same taxation authority on either:
 - the same taxable entity; or
 - different taxable entities, which, in each future period in which significant amounts of deferred income tax liabilities or assets are expected to be settled or recovered, intend to realize the current income tax assets and settle the current income tax liabilities on a net basis or realize and settle simultaneously.

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

2 Basis of preparation and principal accounting policies (continued)

(x) Employee benefits

(i) Short-term employee benefits

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

(ii) Retirement benefits

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

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

(iii) Share-based payments

PCCW, HKT Trust and HKT operate share option schemes where employees of the Group (and including directors) are granted options to acquire shares of PCCW and Share Stapled Units at specified exercise prices, and accounted for as equity-settled share-based payments. The fair value of the employee services received in exchange for the grant of the options is recognized as staff costs in the consolidated income statement with a corresponding increase in capital contribution from shareholders in respect of employee share-based compensation under equity. The fair value of the options granted is measured at grant date using the trinomial option pricing model, taking into account the terms and conditions upon which the options were granted, and spread over the respective vesting period during which the employees become unconditionally entitled to the options. During the vesting period, the number of share options that is expected to vest is reviewed. Any adjustment to the cumulative fair value recognized in prior years is charged or credited in the consolidated income statement for the year of the review, unless the original staff costs qualify for recognition as an asset, with a corresponding adjustment to the capital contribution from shareholders in respect of employee share-based compensation under equity. On vesting date, the amount recognized as staff costs is adjusted to reflect the actual number of share options that vest (with a corresponding adjustment to the capital contribution from shareholders in respect of employee share-based compensation under equity). The equity amount is recognized in the capital contribution from shareholders in respect of employee share-based compensation under equity until the share options lapse.

The board of directors of PCCW and the directors of HKT Management Limited (the trustee-manager of HKT Trust) and HKT may also grant shares of PCCW and Share Stapled Units, respectively, to employees of the participating subsidiaries of PCCW, HKT and HKT Trust at nil consideration under their share award schemes, under which the awarded shares are either newly issued at par value (the "PCCW Subscription Scheme" and the "HKT Share Stapled Units Subscription Scheme") or are purchased from the open market (the "PCCW Purchase Scheme" and the "HKT Share Stapled Units Purchase Scheme").

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

2 Basis of preparation and principal accounting policies (continued)

(x) Employee benefits (continued)

(iii) Share-based payments (continued)

For the PCCW Subscription Scheme and the HKT Share Stapled Units Subscription Scheme, it is accounted for as equity-settled share-based payment. The fair values of the awarded PCCW shares and Share Stapled Units are measured by the quoted market prices of PCCW shares and Share Stapled Units at grant date. The fair values of the employee services received in exchange for the grant of PCCW shares and Share Stapled Units are recognized as staff costs in the consolidated income statement over the respective vesting period with a corresponding increase in the capital contribution from shareholders in respect of employee share-based compensation under equity.

For the PCCW Purchase Scheme and the HKT Share Stapled Units Purchase Scheme, it is accounted for as cash-settled share-based payment. The fair values of the awarded PCCW shares and Share Stapled Units represent the quoted market prices of PCCW shares and Share Stapled Units purchased from the open market and are recognized as financial assets at fair value through profit and loss, and subsequently measured at fair value. The fair values of the employee services received in exchange for the grant of PCCW shares and Share Stapled Units are recognized as staff costs in the consolidated income statement over the respective vesting period with a corresponding obligation being recognized.

Shares of PCCW granted to employees of the Group by the principal shareholder of PCCW are accounted for in accordance with the same policy for the awarded shares under the share award schemes of PCCW as described above. The fair value of the PCCW shares granted by the principal shareholder is measured by the quoted market price of the PCCW shares at grant date and is charged to the consolidated income statement over the respective vesting period, with a corresponding increase in the capital contribution from shareholder in respect of employee share-based compensation under equity.

(iv) Termination benefits

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

(y) Translation of foreign currencies

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). The consolidated financial statements are presented in Hong Kong dollars (HK\$), which is the Group's functional and the Group's presentation currency.

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

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

2 Basis of preparation and principal accounting policies (continued)

(y) Translation of foreign currencies (continued)

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

The results of foreign operations are translated into Hong Kong dollars at the exchange rates approximating the foreign exchange rates ruling at the dates of transactions. Balance sheet items of foreign operations, including goodwill arising on consolidation of foreign operations, are translated into Hong Kong dollars at the foreign exchange rates ruling at the balance sheet date. The resulting exchange differences are recognized in other comprehensive income and accumulated separately in the currency translation reserve under equity.

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

(z) Related parties

For the purposes of the consolidated financial statements, a party is considered to be related to the Group if:

- (i) the party has the ability, directly or indirectly through one or more intermediaries, to control the Group or exercise significant influence over the Group in making financial and operating policy decisions, or has joint control over the Group;
- (ii) the Group and the party are subject to common control;
- (iii) the party is an associate of the Group or a joint venture in which the Group is a venturer;
- (iv) the party is a member of key management personnel of the Group or the Group's parent, or a close family member of such an individual, or is an entity under the control, joint control or significant influence of such individuals;
- (v) the party is a close family member of a party referred to in (i) above or is an entity under the control, joint control or significant influence of such individuals; or
- (vi) the party is a post-employment benefit plan which is for the benefit of employees of the Group or of any entity that is a related party of the Group.

Close family members of an individual are those family members who may be expected to influence, or be influenced by, that individual in their dealings with the entity.

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

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.

Key sources of estimation uncertainty

The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. Notes 16 and 33 contain information about the assumptions and the risk factors relating to goodwill impairment and financial instruments. Other key sources of estimation uncertainty are discussed below:

(i) Recognition and fair value of identifiable intangible assets through business combination

The Group applies the acquisition method of accounting to account for acquisitions of businesses. The cost of an acquisition is measured as the aggregate of the fair values at the date of exchange of the assets given, liabilities incurred, equity instruments issued, and costs directly attributable to the acquisition. Identifiable assets, liabilities and contingent liabilities acquired or assumed are measured separately at their fair values as of the acquisition date. The excess of the cost of the acquisition over the fair value of the identifiable net assets acquired is recorded as goodwill.

The determination and allocation of fair values to the identifiable assets acquired and liabilities assumed is based on various assumptions and valuation methodologies requiring considerable management judgement. The most significant variables in these valuations are discount rates, terminal values, the number of years on which the cash flow projections are based, as well as the assumptions and estimates used to determine the cash inflows and outflows. Management determines discount rates to be used based on the risk inherent in the related activity's current business model and industry comparisons. Terminal values are based on the expected life of products and forecasted life cycle and forecasted cash flows over that period. Although the assumptions applied in the determination are reasonable based on information available at the date of acquisition, actual results may differ from the forecasted amounts and the difference could be material.

Upon an acquisition of a business it is necessary to attribute fair values to any intangible assets acquired (provided they meet the criteria to be recognized). The fair values of these intangible assets are dependent on estimates of attributable future revenue, margin, cash flow, useful lives and discount rate used.

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

3 Critical accounting estimates and judgements (continued)

(ii) Impairment of assets (other than investments in equity securities and other receivables)

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

- property, plant and equipment;
- interests in leasehold land;
- intangible assets;
- interests in an associate and jointly controlled companies;
- goodwill; and
- investments in subsidiaries (at Company level).

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

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

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

(iii) Revenue recognition

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

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

3 Critical accounting estimates and judgements (continued)

(iii) Revenue recognition (continued)

The Group offers certain arrangements whereby a customer can purchase telecommunications equipment together with a fixed period of telecommunications service arrangement. When such multiple-element arrangements exist, the amount recognized as revenue upon the sale of the telecommunications equipment is the fair value of the equipment in relation to the fair value of the arrangement taken as a whole. The revenue relating to the service element, which represents the fair value of the servicing arrangement in relation to the fair value of the arrangement taken as a whole, is recognized over the service period. The fair values of each element are determined based on the current market price of each of the elements when sold separately.

Where the Group is unable to determine the fair value of each of the elements in an arrangement, it uses the residual value method. Under this method, the Group determines the fair value of the delivered element by deducting the fair value of the undelivered element from the total contract consideration.

To the extent that there is a discount on the arrangement, such discount is allocated between the elements of the contract in such a manner as to reflect the fair value of the elements.

(iv) Deferred income tax

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

(v) Current income tax

The Group makes a provision for current income tax based on estimated taxable income for the year. The estimated income tax liabilities are primarily computed based on the tax computations as prepared by the Group. Nevertheless, from time to time, there are cases of disagreements with the tax authorities of Hong Kong and elsewhere on the tax treatment of items included in the tax computations and certain non-routine transactions. If the Group considers it probable that these disputes or judgements will result in different tax positions, the most likely amounts of the outcome will be estimated and adjustments to the income tax expense and income tax liabilities will be made accordingly.

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

The Group has significant property, plant and equipment and intangible assets (other than goodwill). The Group is required to estimate the useful lives of property, plant and equipment and intangible assets (other than goodwill) in order to ascertain the amount of depreciation and amortization charges for each reporting period.

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

3 Critical accounting estimates and judgements (continued)

- (vi) Useful lives of property, plant and equipment and intangible assets (other than goodwill) (continued)

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

- (vii) Recognition of intangible asset – carrier licences

In order to measure the intangible assets, HKAS 39 “Financial Instruments: Recognition and Measurement” is applied for recognition of the minimum annual fee and royalty payments as they constitute contractual obligations to deliver cash and, hence, should be considered as financial liabilities. To establish the fair value of the minimum annual fee and royalty payments for the right of use of the carrier licences, the discount rate used is an indicative incremental borrowing rate estimated by the Group. Had a different discount rate been used to determine the fair value, the Group's result of operations and financial position could be materially different.

4 Related party transactions

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

	Note(s)	The Group	
		2011 HK\$ million	2012 HK\$ million
Telecommunications service fees and systems integration charges received or receivable from a substantial shareholder of PCCW	(a)	234	141
Telecommunications service fees paid or payable to a substantial shareholder of PCCW	(a)	254	126
Telecommunications service fees received or receivable from a related party	(a)	43	70
Telecommunications service fees, outsourcing fees and rental charges paid or payable to a related party	(a)	292	315
Telecommunications service fees, IT and logistics charge, management fee and other costs recharge received or receivable from fellow subsidiaries	(a)	599	627
Rental and facilities management charges paid or payable to fellow subsidiaries	(a)	12	130
Telecommunication service fees, outsourcing fees and rental charges paid or payable to fellow subsidiaries	(a)	189	869
Cost recharge paid or payable to fellow subsidiaries	(a)	188	618
Interest paid/payable to the immediate holding company	(a) & (c)	4	46

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

4 Related party transactions (continued)

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

- (b) Key management compensation

	The Group	
	2011	2012
	HK\$ million	HK\$ million
Salaries, other short-term employee benefits and post-employment benefits	22	44

The salaries, other short-term employee benefits and post-employment benefits of approximately HK\$41,530,000 and HK\$2,080,000 (2011: HK\$21,434,000 and HK\$440,000) respectively cover the compensation for three key management for the full year (2011: one key management for the full year and two key management for the period from November 29, 2011 to December 31, 2011.)

- (c) Balances with the immediate holding company, the ultimate holding company, related companies and fellow subsidiaries

The balances included in the amounts due to the immediate holding company and fellow subsidiaries are unsecured, non-interest bearing and have no fixed repayment terms, except for the loans payable to the immediate holding company of HK\$7,437 million as at December 31, 2012 (2011: HK\$7,800 million) which bears interest of Hong Kong Interbank Offered Rate (“HIBOR”) plus 0.3% per annum and repayable within one year.

The balance with the ultimate holding company as at December 31, 2011 was unsecured, non-interest bearing and had no fixed repayment terms.

The balances included in the amounts due to related companies are unsecured, non-interest bearing and have no fixed repayment terms as at December 31, 2011 and 2012.

- (d) During the year ended December 31, 2011, in addition to the above, the Group, Telstra Corporation Limited (“Telstra”) and a related company completed certain transactions which resulted in the transfer of the majority of the related company’s assets, business platforms and operations to the Group and Telstra. The Group received assets and businesses from the related company valued at approximately HK\$644 million. The consideration was settled in part by a credit note received from the related company in the sum of approximately HK\$491 million and in part by offsetting against the inter-company balance between the Group and PCCW. As a result, the Group recorded credits to revenue, cost of sales, operating expenses, and an increase in amounts due to the ultimate holding company and fellow subsidiaries in the amounts of approximately HK\$339 million, HK\$97 million, HK\$29 million, and HK\$179 million, respectively.

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

5 Turnover

	The Group	
	2011	2012
	HK\$ million	HK\$ million
Telecommunications and other service revenue	19,823	18,439
Amounts received and receivable in respect of goods sold	2,253	2,610
Amounts received and receivable from the rental of investment properties	25	32
	<u>22,101</u>	<u>21,081</u>
Represented by:		
- continuing operations	18,755	21,081
- discontinued operations	3,346	-
	<u>22,101</u>	<u>21,081</u>

6 Other gains, net

	The Group	
	2011	2012
	HK\$ million	HK\$ million
Net realized gain on disposal of a subsidiary (note 31(c))	186	-
Net gain on cash flow hedging instruments transferred from equity	1	19
Impairment loss on interest in a jointly controlled company	(16)	-
Others	(1)	1
	<u>170</u>	<u>20</u>
Represented by:		
- continuing operations	213	20
- discontinued operations	(43)	-
	<u>170</u>	<u>20</u>

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

7 Profit before income tax

Profit before income tax is stated after charging and crediting the following:

(a) Staff costs

	The Group	
	2011	2012
	HK\$ million	HK\$ million
Salaries, bonuses and other benefits	1,800	1,416
Share-based compensation	-	9
Retirement costs for staff under defined contribution retirement schemes	220	198
	<u>2,020</u>	<u>1,623</u>

(b) Other items

	The Group	
	2011	2012
	HK\$ million	HK\$ million
Crediting:		
Gross rental income	25	32
Gain on disposal of property, plant and equipment, net	5	-
Charging:		
Impairment loss for doubtful debts	160	138
Provision for inventory obsolescence	7	5
Depreciation of property, plant and equipment	2,432	2,229
Operating costs of property, plant and equipment, net	447	532
Amortization of land lease premium	14	13
Amortization of intangible assets	2,182	2,446
Cost of inventories sold	2,269	2,547
Cost of sales, excluding inventories sold	7,259	6,480
Exchange losses, net	19	(26)
Cash flow hedges: transferred from equity	(11)	37
Auditor's remuneration	10	7
Operating lease rental		
- equipment	16	54
- other assets (including property rentals)	543	744

Particulars of profit before income tax of discontinued operations for the year ended 31 December 2011 are set out in note 13.

HKT GROUP HOLDINGS LIMITED**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****8 Finance costs**

	The Group	
	2011 HK\$ million	2012 HK\$ million
Interest paid/payable for:		
Overdrafts and bank borrowings wholly repayable within 5 years	458	265
Other borrowings wholly repayable within 5 years	1,026	525
Notional accretion on carrier licence fee liabilities	74	68
Other borrowing costs	15	52
Cash flow hedges: transferred from equity	1	1
Fair value gains on derivative financial instruments on fair value hedges	(198)	(38)
Fair value adjustment of borrowings attributable to interest rate risk	202	42
	<hr/>	<hr/>
	1,578	915
Interest capitalized in property, plant and equipment	(31)	(39)
	<hr/>	<hr/>
	1,547	876
	<hr/>	<hr/>

The capitalization rate used to determine the amount of interest eligible for capitalization for the year ranged from 4.54% to 4.70% for the year ended December 31, 2012 (2011: 4.43% to 6.22%).

Finance costs of discontinued operations for the year ended 31 December 2011 was nil.

9 Directors' emoluments

The salaries and other short-term employee benefits and post-employment benefits of approximately HK\$41,530,000 and HK\$2,080,000 (2011: HK\$21,430,000 and HK\$440,000) respectively cover the compensation for three directors for the full year (2011: one director for the full year and two directors for the period from November 29, 2011 to December 31, 2011).

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

10 Income tax expense

(a) Income tax expense in the consolidated income statement represents:

	The Group	
	2011 HK\$ million	2012 HK\$ million
Hong Kong profits tax		
- provision for current year	387	573
- overprovision for prior year	-	(3)
Overseas tax		
- provision for current year	44	41
Movement of deferred income tax (note 29(a))	(95)	(162)
	<u>336</u>	<u>449</u>
Represented by:		
- continuing operations	347	449
- discontinued operations	(11)	-
	<u>336</u>	<u>449</u>

Hong Kong profits tax has been provided at the rate of 16.5% (2011: 16.5%) on the estimated assessable profits for the year.

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

(b) Reconciliation between income tax expense and accounting profit at applicable tax rate:

	The Group	
	2011 HK\$ million	2012 HK\$ million
Profit before income tax	<u>1,950</u>	<u>2,077</u>
Notional tax on profit before income tax, calculated at applicable tax rate	322	343
Income not subject to tax	(12)	(1)
Expenses not deductible for tax purposes	15	3
Tax losses not recognized	25	74
Utilization of previously unrecognized tax losses	(61)	(21)
Loss not deductible for jointly controlled companies	3	13
Overprovision in respect of prior year	-	(3)
Current tax provision of overseas operations	44	41
Income tax expense	<u>336</u>	<u>449</u>

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

11 Dividends

	The Company	
	2011 HK\$ million	2012 HK\$ million
Special dividend in specie of shares in subsidiaries	3,192	-
Interim dividend declared and paid in respect of the current year	-	1,287
	<u>3,192</u>	<u>1,287</u>
Final dividend proposed after the balance sheet date	-	1,385

Pursuant to the written resolutions of all the directors of the Company on November 8, 2011, a non-cash special dividend in specie of shares in HKT Media and HKT Solutions was approved, declared and paid to CAS No. 1, the sole shareholder of the Company, on the date of the resolutions. Two ordinary shares in HKT Media and two ordinary shares in HKT Solutions in an aggregate amount of HK\$3,192 million, representing the carrying cost of HK\$2,619 million and HK\$573 million of HKT Media and HKT Solutions, respectively on the date of resolutions, were distributed by the Company.

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

12 Profit attributable to equity holders of the Company

Profit of approximately HK\$1,289 million (2011: HK\$573 million) attributable to equity holders of the Company was dealt with in the financial statements of the Company.

13 Discontinued operations

In 2011, pursuant to the reorganization as detailed in note 1(b) to the financial statements, the Group discontinued its businesses carried out by the Media Group and the Solutions Group by way of a special dividend in specie of shares (note 1(b)(ii)). These transactions were completed on November 8, 2011 (the "Transactions").

The results of discontinued operations for the period from January 1, 2011 to the date of completion of the Transactions, which have been included in the consolidated income statement and consolidated statement of comprehensive income, were as follows:

	Note	2011 HK\$ million
Turnover	5	3,346
Cost of sales		(2,102)
General and administrative expenses		(1,170)
Other gains, net	6	(43)
		<u>31</u>
Profit before income tax		31
Income tax credit	10	11
		<u>42</u>
Profit for the year		<u>42</u>

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

13 Discontinued operations (continued)

The net cash flows incurred by the discontinued operations are as follows:

	2011 HK\$ million
Operating activities	630
Investing activities	(688)
Financing activities	-
Net cash outflow	<u>(58)</u>

14 Property, plant and equipment

	The Group 2011					
	Buildings HK\$ million	Exchange equipment HK\$ million	Transmission plant HK\$ million	Other plant and equipment HK\$ million	Projects under construction HK\$ million	Total HK\$ million
Cost						
Beginning of year	1,110	20,276	18,413	11,784	468	52,051
Additions	-	274	340	335	786	1,735
Acquisition of assets from a related company	-	-	629	-	-	629
Transfers	-	(32)	79	84	(368)	(237)
Disposals	-	(1,346)	(63)	(265)	-	(1,674)
Disposal on special dividend in specie of shares in subsidiaries (note 38)	(33)	(181)	(97)	(2,461)	(246)	(3,018)
Exchange differences	-	-	(20)	(5)	-	(25)
End of year	<u>1,077</u>	<u>18,991</u>	<u>19,281</u>	<u>9,472</u>	<u>640</u>	<u>49,461</u>
Accumulated depreciation and impairment						
Beginning of year	517	16,191	11,401	9,004	-	37,113
Charge for the year	22	970	823	617	-	2,432
Transfers	-	(208)	-	-	-	(208)
Disposals	-	(1,342)	(54)	(261)	-	(1,657)
Disposal on special dividend in specie of shares in subsidiaries (note 38)	(8)	(88)	(7)	(2,339)	-	(2,442)
Exchange differences	-	-	(14)	(16)	-	(30)
End of year	<u>531</u>	<u>15,523</u>	<u>12,149</u>	<u>7,005</u>	<u>-</u>	<u>35,208</u>
Net book value						
End of year	<u>546</u>	<u>3,468</u>	<u>7,132</u>	<u>2,467</u>	<u>640</u>	<u>14,253</u>
Beginning of year	<u>593</u>	<u>4,085</u>	<u>7,012</u>	<u>2,780</u>	<u>468</u>	<u>14,938</u>

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

14 Property, plant and equipment (continued)

	The Group					
	2012					
	Buildings HK\$ million	Exchange equipment HK\$ million	Transmission plant HK\$ million	Other plant and equipment HK\$ million	Projects under construction HK\$ million	Total HK\$ million
Cost						
Beginning of year	1,077	18,991	19,281	9,472	640	49,461
Additions	-	232	174	260	1,279	1,945
Additions upon business combinations (note 37)	-	41	121	16	-	178
Transfers	-	220	118	87	(425)	-
Transfer to inventory	-	(49)	-	-	-	(49)
Disposals	-	(542)	(11)	(101)	-	(654)
Exchange differences	-	57	81	4	-	142
End of year	1,077	18,950	19,764	9,738	1,494	51,023
Accumulated depreciation and impairment						
Beginning of year	531	15,523	12,149	7,005	-	35,208
Charge for the year	20	922	835	452	-	2,229
Transfers	-	-	-	-	-	-
Transfer to inventory	-	(49)	-	-	-	(49)
Disposals	-	(541)	(11)	(96)	-	(648)
Exchange differences	-	52	6	(2)	-	56
End of year	551	15,907	12,979	7,359	-	36,796
Net book value						
End of year	526	3,043	6,785	2,379	1,494	14,227
Beginning of year	546	3,468	7,132	2,467	640	14,253

Certain property, plant and equipment with an aggregate carrying value of approximately HK\$23 million were pledged as security for bank borrowings of the Group as at December 31, 2011. No property, plant and equipment were pledged as at December 31, 2012.

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

	The Group	
	2011 HK\$ million	2012 HK\$ million
Held in Hong Kong		
On long-term lease (over 50 years)	39	37
On medium-term lease (10-50 years)	507	489
	546	526

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

15 Interests in leasehold land

	The Group	
	2011 HK\$ million	2012 HK\$ million
Cost		
Beginning of year	570	536
Disposal on special dividend in specie of shares in subsidiaries (note 38)	(34)	-
End of year	536	536
Accumulated amortization		
Beginning of year	209	220
Charge for the year	14	13
Disposal on special dividend in specie of shares in subsidiaries (note 38)	(3)	-
End of year	220	233
Net book value		
End of year	316	303
Beginning of year	361	316

The carrying amount of interests in leasehold land of the Group is analyzed as follows:

	The Group	
	2011 HK\$ million	2012 HK\$ million
Held in Hong Kong		
On long-term lease (over 50 years)	31	29
On medium-term lease (10-50 years)	285	274
	316	303

16 Goodwill

	The Group	
	2011 HK\$ million	2012 HK\$ million
Cost		
Beginning of year	37,098	35,892
Addition upon business combination (note 37)	-	129
Disposal on special dividend in specie of shares in subsidiaries (note 38)	(1,206)	-
Exchange differences	-	4
End of year	35,892	36,025

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

16 Goodwill (continued)

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

	The Group	
	2011 HK\$ million	2012 HK\$ million
Telecommunications Services		
- HKT	30,830	30,830
- Mobile	3,356	3,356
- Global	997	1,126
Others	709	713
Total	35,892	36,025

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

Key assumptions used for value-in-use calculations:

	2011			2012		
	Gross margin	Terminal growth rate	Discount rate	Gross margin	Terminal growth rate	Discount rate
Telecommunications Services						
- HKT	72%	1%	9%	70%	1%	8%
- Mobile	60%	2%	15%	61%	2%	14%
- Global	22%	3%	11%	15%	3%	10%

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

There was no evidence of impairment arising from review on goodwill as at October 31, 2012.

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

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17 Intangible assets

	The Group					
	2011					
	Trademarks HK\$ million	Carrier licences HK\$ million	Customer acquisition costs HK\$ million	Customer base HK\$ million	Others HK\$ million	Total HK\$ million
Cost						
Beginning of year	865	1,395	1,644	5,606	12	9,522
Additions	-	38	1,630	-	-	1,668
Write-off	-	-	(821)	(471)	-	(1,292)
Disposal on special dividend in specie of shares in subsidiaries (note 38)	(406)	-	(479)	(95)	-	(980)
End of year	459	1,433	1,974	5,040	12	8,918
Accumulated amortization						
Beginning of year	94	248	842	2,274	10	3,468
Charge for the year (note (a))	40	153	1,148	840	1	2,182
Write-off	-	-	(821)	(471)	-	(1,292)
Disposal on special dividend in specie of shares in subsidiaries (note 38)	(61)	-	(200)	(52)	-	(313)
Exchange differences	-	-	-	-	1	1
End of year	73	401	969	2,591	12	4,046
Net book value						
End of year	386	1,032	1,005	2,449	-	4,872
Beginning of year	771	1,147	802	3,332	2	6,054

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

17 Intangible assets (continued)

	The Group						
	2012						
	Trademarks	Carrier	Customer	Customer	Software	Others	Total
	HK\$ million	licences	acquisition	base			
		HK\$ million	costs	HK\$ million	HK\$ million	HK\$ million	
			HK\$ million				
Cost							
Beginning of year	459	1,433	1,974	5,040	-	12	8,918
Additions	-	68	1,490	-	342	128	2,028
Write-off	-	-	(848)	-	-	(140)	(988)
Addition upon business combinations (note 37)	71	-	-	47	-	-	118
Exchange differences	-	-	1	-	-	-	1
End of year	530	1,501	2,617	5,087	342	-	10,077
Accumulated amortization							
Beginning of year	73	401	969	2,591	-	12	4,046
Charge for the year (note (a))	23	203	1,250	819	23	128	2,446
Write-off	-	-	(848)	-	-	(140)	(988)
End of year	96	604	1,371	3,410	23	-	5,504
Net book value							
End of year	434	897	1,246	1,677	319	-	4,573
Beginning of year	386	1,032	1,005	2,449	-	-	4,872

- (a) The amortization charge for the year is included in “General and administrative expenses” in the consolidated income statement.

18 Investments in subsidiaries

	The Company	
	2011 HK\$ million	2012 HK\$ million
Unlisted shares, at cost	17,226	17,394

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

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18 Investments in subsidiaries (continued)

(a) Amounts due from subsidiaries

	The Company	
	2011 HK\$ million	2012 HK\$ million
Amounts due from subsidiaries	4,488	3,344

(b) Amounts due to subsidiaries

	The Company	
	2011 HK\$ million	2012 HK\$ million
Amounts due to subsidiaries	2,484	1,429

Balances with subsidiaries are unsecured, non-interest bearing and repayable on demand.

During the year ended December 31, 2011, the Company acquired and disposed of certain subsidiaries pursuant to the group reorganization. Further details are as set out in note 1(b).

As at December 31, 2012, 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	Interest held by the Company	
				Directly	Indirectly
Hong Kong Telecommunications (HKT) Limited ("HKTL")	Hong Kong	Provision of telecommunications services	HK\$2,488,200,001	-	100%
HKT Services Limited	Hong Kong	Provision of management services to group companies	HK\$1	-	100%
PCCW Mobile HK Limited	Hong Kong	Provision of mobile services to its customers, which is procured from HKTL, and the sale of mobile phones and accessories	HK\$100 ordinary shares and HK\$1,254,000,000 non-voting deferred shares	-	100%
PCCW Teleservices (Hong Kong) Limited	Hong Kong	Provision of customer relationship management and customer contact management solutions and services	HK\$12	-	100%
PCCW Teleservices Operations (Hong Kong) Limited	Hong Kong	Provision of customer relationship management and customer contact management solutions and services	HK\$2	-	100%

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

18 Investments in subsidiaries (continued)

<u>Company name</u>	<u>Place of incorporation/ operations</u>	<u>Principal activities</u>	<u>Nominal value of issued capital/ registered capital</u>	<u>Interest held by the Company</u>	
				<u>Directly</u>	<u>Indirectly</u>
PCCW Customer Management Technology and Services (Guangzhou) Limited ^{1,2}	The PRC	Customer service and consultancy	HK\$53,803,000 ⁵	-	100%
PCCW (Macau), Limitada	Macau	Selling customer premises equipment and related solutions, conducting systems integration projects and providing outsourced call center services	MOP2,000,000	-	75%
PCCW Teleservices (US), Inc.	Nebraska, U.S.	Telemarketing and direct marketing services	US\$1,169	-	100%
PCCW Global (HK) Limited	Hong Kong	Provision of satellite-based and network-based telecommunications services	HK\$10	-	100%
PCCW Global B.V.	Netherlands/ France	Investment holding and provision of telecommunications and related services	EUR18,000	-	100%
PCCW Global Limited	Hong Kong/ Dubai Technology and Media Free Zone	Provision of network-based telecommunications services	HK\$3	-	100%
PCCW Global, Inc.	Delaware, U.S.	Supply of broadband internet access solutions and web services	US\$18.01	-	100%
PCCW Global (Singapore) Pte. Ltd. (In Member's Voluntary Liquidation)	Singapore	Telecommunication solutions related services	S\$172,124,441.71	-	100%
HKT Global (Singapore) Pte. Ltd.	Singapore	Provision of telecommunications solutions related services	S\$60,956,485.64	-	100%
Gateway Global Communications Limited (formerly known as PCCW Global (UK) Limited)	United Kingdom	Provision of network-based telecommunications services to customers, and the provision of sales and marketing services to related companies	GBP1	-	100%
Unihub China Information Technology Company Limited ^{3,4}	The PRC	Selling of hardware and software and information system consulting services	RMB200,000,000	-	38.2%

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

Notes:

1. Represents a wholly foreign owned enterprise.
2. Unofficial company name.
3. Represents a sino-foreign equity joint venture.
4. This company is consolidated by the Group as the Group owns more than one half of the voting rights of this company.
5. The change of registered capital from HK\$53,803,000 to HK\$93,240,000 has been approved by the PRC authority in February 2013.

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NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

19 Interest in an associate

	The Group	
	2011	2012
	HK\$ million	HK\$ million
Share of net assets of an associate	24	-
Loans to an associate, net	71	200
	<u>95</u>	<u>200</u>
Investments at cost, unlisted shares	41	41

The loans due from an associate comprised two unsecured loans with fixed terms of repayment of approximately HK\$31 million (2011: HK\$43 million) repayable in 1 to 2 years bears interest at a fixed rate of 5% (2011: 5%) per annum and approximately HK\$43 million (2011: HK\$28 million) repayable in 1 year bears interest at a fixed rate of 5% (2011: 6.5%) per annum, certain secured loans with fixed terms of repayment of approximately HK\$12 million (2011: nil) repayable in 1 year bears interest at a fixed rate of 6.5% per annum and approximately HK\$124 million (2011: nil) repayable in 1 year bears interest at a fixed rate of 6% per annum.

As at December 31, 2012, particulars of the principal associate of the Group are as follows:

<u>Company name</u>	<u>Place of incorporation</u>	<u>Principal activities</u>	<u>Nominal value of issued capital/ registered capital</u>	<u>Interest held by the Company</u>	
				<u>Directly</u>	<u>Indirectly</u>
東莞捷通達電訊有限公司 (Dongguan Jietongda Telecommunications Company Limited#)	The PRC	Provision of support service for mobile service subscription, sales of mobile phones and accessories	RMB40,000,000	-	35%

Unofficial company name

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

	2011	2012
	HK\$ million	HK\$ million
Total assets	176	213
Total liabilities	(174)	(309)
Turnover	82	405
Loss after income tax	(47)	(99)

During the year ended December 31, 2012, the Group did not have any unrecognized share of losses of an associate (2011: nil). As at December 31, 2012, the accumulated share of loss of the associate unrecognized by the Group was nil (2011: nil).

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NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

20 Interests in jointly controlled companies

	The Group	
	2011 HK\$ million	2012 HK\$ million
Share of net assets of jointly controlled companies	221	178
Loan to a jointly controlled company (note (a))	301	372
	<hr/>	<hr/>
	522	550
Provision for impairment	(16)	(16)
	<hr/>	<hr/>
	506	534
	<hr/>	<hr/>
Investments at cost, unlisted shares	287	287
	<hr/>	<hr/>

- (a) The loan to a jointly controlled company bears interests at HIBOR plus 3% per annum (2011: HIBOR plus 3% per annum). The loan is unsecured and has no fixed terms of repayment.
- (b) As at December 31, 2012, particulars of the principal jointly controlled companies of the Group are as follows:

Company name	Place of incorporation	Principal activities	Nominal value of issued capital/ registered capital	Interest held by the Company	
				Directly	Indirectly
China Netcom Broadband Corporation Limited	The PRC	Internet access services business, information services business and resale of broadband resources, etc.	RMB644,518,697	-	50%
Genius Brand Limited	Hong Kong	Provision of mobile telecommunications services in Hong Kong	HK\$10,000	-	50%

HKT GROUP HOLDINGS LIMITED**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****20 Interests in jointly controlled companies (continued)**

Summarized unaudited financial information of the Group's interests in jointly controlled companies is as follows:

	2011 HK\$ million	2012 HK\$ million
Non-current assets	727	738
Current assets	229	177
Total assets	956	915
Non-current liabilities	(346)	(422)
Current liabilities	(298)	(236)
Total liabilities	(644)	(658)
Net assets	312	257
Non-controlling interests of a jointly controlled company	(107)	(95)
Equity attributable to equity holders of the Group	205	162
Turnover	291	368
Expenses	(275)	(347)
Profit before income tax	16	21
Income tax	(6)	(6)
Profit after income tax	10	15
Profit for the year attributable to the non-controlling interests of a jointly controlled company	(13)	(12)
(Loss)/profit for the year attributable to equity holders of the Group	(3)	3

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21 Available-for-sale financial assets

	The Group	
	2011 HK\$ million	2012 HK\$ million
Beginning of year	48	72
Additions	223	-
Disposal	(31)	-
Disposal on special dividend in specie of shares in subsidiaries (note 38)	(192)	-
Net gains transferred to equity (note 28)	24	13
End of year	<u>72</u>	<u>85</u>
Market value of listed equity securities - overseas	<u>72</u>	<u>85</u>

As at December 31, 2012, the Group's equity securities were reviewed for impairment by management. Consequently, there was no provision for impairment (2011: nil) recognized in the consolidated income statement for the year ended December 31, 2012. The Group does not hold any collateral over these securities.

No available-for-sale financial assets were pledged as security for bank borrowings of the Group as at December 31, 2011 and 2012.

22 Financial assets at fair value through profit or loss

	The Group	
	2011 HK\$ million	2012 HK\$ million
Market value of listed securities	-	16
Less: Securities held for employee share award to be vested within one year classified as current assets	-	8
Non-current portion	<u>-</u>	<u>8</u>

Financial assets at fair value through profit or loss represent shares of PCCW and Share Stapled Units acquired under the PCCW Purchase Scheme and the HKT Share Stapled Units Purchase Scheme, respectively. Please refer to notes 27(b)(iv) and 27(b)(iii) for details of the share award schemes of PCCW and Share Stapled Units award schemes of HKT, respectively.

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23 Current assets and liabilities

(a) Inventories

	The Group	
	2011	2012
	HK\$ million	HK\$ million
Work-in-progress	521	445
Finished goods	412	394
Consumable inventories	143	132
	<u>1,076</u>	<u>971</u>

(b) Trade receivables, net

	The Group	
	2011	2012
	HK\$ million	HK\$ million
Trade receivables	2,651	3,550
Less: Impairment loss for doubtful debts (note (i))	(110)	(125)
Trade receivables, net	<u>2,541</u>	<u>3,425</u>

(i) Impairment loss for doubtful debts

The movement in the provision for doubtful debts during the year, including both specific and collective loss components, is as follows:

	The Group	
	2011	2012
	HK\$ million	HK\$ million
Beginning of year	199	110
Impairment loss recognized	160	138
Uncollectible amounts written off	(198)	(123)
Disposal on special dividend in specie of shares in subsidiaries (note 38)	(51)	-
End of year	<u>110</u>	<u>125</u>

As at December 31, 2012, the Group's trade receivables of HK\$125 million (2011: HK\$110 million) were individually determined to be impaired. The individually impaired receivables related to customers that were in financial difficulties and management assessed that only a portion of the receivables are expected to be recovered. Consequently, specific provision for doubtful debts of HK\$88 million (2011: HK\$160 million) was recognized. The Group does not hold any collateral over these balances.

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NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

23 Current assets and liabilities (continued)

(b) Trade receivables, net (continued)

(ii) Trade receivables that are not impaired

The aging of trade receivables that are neither individually nor collectively considered to be impaired is as follows:

	The Group	
	2011 HK\$ million	2012 HK\$ million
Neither past due nor impaired	1,323	1,297
o - 30 days past due	363	714
31 - 60 days past due	181	270
61 - 90 days past due	96	227
Over 90 days past due	578	917
Past due but not impaired	1,218	2,128
	<u>2,541</u>	<u>3,425</u>

Trade receivables that were neither past due nor impaired relate to a wide range of customers for whom there was no recent history of default.

Trade receivables that were past due but not impaired relate to customers that have a good track record with the Group or a sound credit quality. Based on past experience and regular credit risk assessment performed on all significant outstanding trade receivables, management believes that no provision for impairment is necessary in respect of these balances as there has not been a significant change in credit quality and the balances are still considered fully recoverable.

As at December 31, 2011 certain trade receivables with an aggregate carrying value of approximately HK\$37 million were pledged as security for certain bank borrowings of the Group. Please refer to note 36 for details of the Group's bank loan facilities. No trade receivables were pledged as at December 31, 2012.

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23 Current assets and liabilities (continued)

(c) Short-term borrowings

	The Group	
	2011 HK\$ million	2012 HK\$ million
US\$500 million 6% guaranteed notes due 2013	-	3,873
Bank borrowings	31	4,589
	<u>31</u>	<u>8,462</u>
Secured	<u>31</u>	<u>-</u>
Unsecured	<u>-</u>	<u>8,462</u>

(i) US\$500 million 6% guaranteed notes due 2013 (the “Notes due 2013”)

In July 2003, PCCW-HKT Capital No.2 Limited, an indirect wholly-owned subsidiary of the Company, issued US\$500 million 6% guaranteed notes due 2013 which are listed on the Luxembourg Stock Exchange. The Notes due 2013 are irrevocably and unconditionally guaranteed by PCCW-HKT Telephone Limited (“HKTC”), HKTL and the Company will rank pari passu with all other outstanding unsecured and unsubordinated obligations of HKTC, HKTL and the Company.

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NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

24 Long-term borrowings

	The Group	
	2011 HK\$ million	2012 HK\$ million
Repayable within a period		
- over one year, but not exceeding two years	8,123	2,292
- over two years, but not exceeding five years	15,347	13,352
- over five years	-	-
	<u>23,470</u>	<u>15,644</u>
Representing:		
US\$500 million 6% guaranteed notes due 2013 (note (a))	3,881	-
US\$500 million 5.25% guaranteed notes due 2015 (note (b))	3,867	3,861
US\$500 million 4.25% guaranteed notes due 2016 (note (c))	3,979	4,016
Bank borrowings	11,743	7,767
	<u>23,470</u>	<u>15,644</u>
Secured	<u>2</u>	<u>-</u>
Unsecured	<u>23,468</u>	<u>15,644</u>

- (a) US\$500 million 6% guaranteed notes due 2013 (the “Notes due 2013”)

The Notes due 2013 were classified as short-term borrowing as at 31 December 2012. Please refer to note 23(c)(i) for details.

- (b) US\$500 million 5.25% guaranteed notes due 2015 (the “Notes due 2015”)

In July 2005, PCCW-HKT Capital No.3 Limited, an indirect wholly-owned subsidiary of the Company, issued US\$500 million 5.25% guaranteed notes due 2015 which are listed on the Singapore Exchange Securities Trading Limited. The Notes due 2015 were irrevocably and unconditionally guaranteed by HKTC, HKTL and the Company and will rank pari passu with all other outstanding unsecured and unsubordinated obligations of HKTC, HKTL and the Company.

- (c) US\$500 million 4.25% guaranteed notes due 2016 (the “Notes due 2016”)

In August 2010, PCCW-HKT Capital No.4 Limited, an indirect wholly-owned subsidiary of the Company, issued US\$500 million 4.25% guaranteed notes due 2016 which are listed on the Singapore Exchange Securities Trading Limited. The Notes due 2016 are irrevocably and unconditionally guaranteed by HKTL and the Company and will rank pari passu with all other outstanding unsecured and unsubordinated obligations of HKTL and the Company.

Please refer to note 36 for details of the Group’s bank loan facilities.

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25 Derivative financial instruments

	The Group	
	2011	2012
	HK\$ million	HK\$ million
Non-current assets		
Fixed-to-fixed cross currency swap contracts - cash flow hedges (note (a))	114	65
Fixed-to-floating cross currency swap contracts - cash hedges (note (b))	31	22
Fixed-to-floating cross currency swap contracts - fair value hedges (note (b))	130	166
	<u>275</u>	<u>253</u>
Current assets		
Fixed-to-fixed cross currency swap contracts - cash flow hedges (note (a))	-	4
	<u>-</u>	<u>4</u>

As at December 31, 2012, the Group had outstanding cross currency swap contracts with notional contract amounts of US\$1,500 million (approximately HK\$11,627 million) (2011: US\$1,500 million (approximately HK\$11,664 million)), at various rates, to manage the Group's exposure to foreign currency fluctuations and interest rate risk.

The full fair value of a hedging derivative is classified as non-current asset or liability when the remaining hedged item is more than 12 months, and as a current asset or liability when the remaining maturity of the hedged item is less than 12 months.

- a. All of the fixed-to-fixed cross currency swap contracts outstanding as at December 31, 2012 with notional contract amounts of US\$1,000 million (approximately HK\$7,751 million) (2011: US\$1,000 million (approximately HK\$7,776 million)) was designated as cash flow hedges of the foreign exchange rate risk in the Group foreign currency denominated borrowings. Maturity of these swaps matches with the maturity of the underlying borrowings and has fixed the USD/HKD exchange rate at 7.7790 to 7.8014 as at December 31, 2012 (2011: 7.7790 to 7.8014) for the notional amounts (see note 33(c)(i)). Gains and losses recognized in the hedging reserve under equity on these cross currency swap contracts will be continuously released to the consolidated income statements until the repayment of the borrowings.
- b. The Group have entered into fixed-to-floating cross currency swap contracts outstanding as at December 31, 2012 with notional contract amounts of US\$500 million (approximately HK\$3,876 million) (2011: US\$500 million (approximately HK\$3,888 million)). Maturity of these swaps matches with the maturity of the underlying fixed rate borrowings and has fixed the USD/HKD exchange rate at 7.7708 to 7.7711 as at December 31, 2012 (2011: 7.7708 to 7.7711) for the notional amounts (see note 33(c)(i)). The swaps also pre-determined the interest rates at HIBOR plus 2.24% (see note 33(c)(ii)).

These swap contracts were designated as (i) cash flow hedges of the foreign exchange rate risk in the Group's foreign currency denominated borrowings and (ii) fair value hedges of the interest rate risk in the Group's borrowings at fixed interest rates.

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26 Share capital

	2011		2012	
	Number of shares	Nominal value HK\$ million	Number of shares	Nominal Value HK\$ million
Authorized:				
Ordinary shares of US\$1 each				
Beginning and end of year	<u>650,000,000</u>	<u>5,070</u>	<u>650,000,000</u>	<u>5,070</u>
Issued and fully paid:				
Ordinary shares of US\$1 each				
Beginning of year	636,000,001	4,961	636,000,002	4,961
Issue of one ordinary share (note (a))	<u>1</u>	<u>-</u>	<u>1</u>	<u>-</u>
End of year	<u>636,000,002</u>	<u>4,961</u>	<u>636,000,003</u>	<u>4,961</u>

- (a) During the year ended December 31, 2011, all intercompany balances between the Company and its subsidiaries, and their fellow subsidiaries and its holding companies, including the Solutions Group and the Media Group, and PCCW, were assigned or novated with a net balance between CAS No. 1 and the Company. The net amount owing from the Company to CAS No. 1 was approximately HK\$2,005 million and the Company issued one new ordinary share to CAS No. 1 to capitalize the net intercompany balance owing from the Company to CAS No. 1.

During the year ended December 31, 2012, the Company issued one ordinary share of US\$1 to the shareholders of the Company at a premium of US\$21,505,573 (approximately HK\$168 million).

27 Employee benefits

- (a) Employee retirement benefits - Defined contribution retirement schemes

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

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

Under the MPF scheme, the employer and its employees are each required to make contributions to the scheme at 5% of the employees' relevant income, subject to a cap of monthly relevant income of HK\$20,000 which was revised upward to HK\$25,000 with effect from June 1, 2012. Contributions to the scheme vest immediately upon the completion of the service in the relevant service period.

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NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

27 Employee benefits (continued)

(b) Equity compensation benefits

i. 1994 and 2004 PCCW Share option schemes

PCCW has a share option scheme (the “1994 PCCW Scheme”) which was adopted in September 1994 to be valid for a period of ten years commencing on September 20, 1994. The 1994 PCCW Scheme was amended in May 2002 such that the board of directors of PCCW (the “PCCW Board”) may, at its discretion, invite employees of PCCW and its subsidiaries, including directors of PCCW, and other eligible persons, to take up options to subscribe for shares of PCCW. The vesting period and exercise period of the options are determined by the PCCW Board but in any case no options can be exercised later than 10 years from the date of grant. Each option gives the holder the right to subscribe for one share.

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

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NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

27 Employee benefits (continued)

(b) Equity compensation benefits (continued)

(i) 1994 and 2004 PCCW share option schemes (continued)

(1) Movements in the number of share options outstanding and their related weighted average exercise prices

	2011		2012	
	Weighted average exercise price HK\$	Number of options	Weighted average exercise price HK\$	Number of Options
Beginning of year	6.14	36,078,483	4.82	22,614,335
Net reduction due to transfer of employees to fellow subsidiaries (note (3))	5.44	(350,035)	4.35	(3,411,000)
Cancelled/lapsed (note (4))	8.44	(13,114,113)	6.1577	(5,862,000)
End of year (note (2))	4.82	22,614,335	4.35	13,341,335
Exercisable at end of year		22,614,335		13,341,335

(2) Terms of unexpired and unexercised share options at the balance sheet date

Date of grant	Vesting period	Exercise period	Exercise price HK\$	Number of options	
				2011	2012
August 1, 2002	August 1, 2003 to August 1, 2005	August 1, 2003 to July 31, 2012	8.0600	200,000	-
November 13, 2002	November 13, 2003 to November 13, 2005	November 13, 2003 to November 12, 2012	6.1500	5,440,000	-
July 25, 2003	July 25, 2004 to July 25, 2006	July 25, 2004 to July 23, 2013	4.3500	16,967,335	13,341,335
September 16, 2003	September 16, 2004 to September 16, 2006	September 16, 2004 to September 14, 2013	4.9000	7,000	-
				22,614,335	13,341,335

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

27 Employee benefits (continued)

(b) Equity compensation benefits (continued)

(i) 1994 and 2004 PCCW share option schemes (continued)

(2) Terms of unexpired and unexercised share options at the balance sheet date (continued)

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

Range of exercise prices		2011		2012	
		Weighted average remaining contractual life (years)	Number of options	Weighted average remaining contractual life (years)	Number of Options
HK\$	4.01 to 5.04	1.56	16,974,335	1.56	13,341,335
	5.05 to 7.54	0.87	5,440,000	0.87	-
	7.55 to 11.29	0.58	200,000	0.58	-
			<u>22,614,335</u>		<u>13,341,335</u>

(3) Details of share options transferred out from the Group with employees transferred to fellow subsidiaries of the Company during the year:

Date of grant	Vesting period	Exercise period	Exercise price HK\$	Number of options	
				2011	2012
April 11, 2002	April 11, 2003 to April 11, 2007	April 11, 2003 to April 11, 2012	7.9150	(86,700)	-
November 13, 2002	November 13, 2003 to November 13, 2005	November 13, 2003 to November 12, 2012	6.1500	(40,000)	-
July 25, 2003	July 25, 2004 to July 25, 2006	July 25, 2004 to July 23, 2013	4.3500	(223,335)	(3,411,000)
				<u>(350,035)</u>	<u>(3,411,000)</u>

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

27 Employee benefits (continued)

(b) Equity compensation benefits (continued)

(i) 1994 and 2004 PCCW share option schemes (continued)

(4) Details of share options cancelled or lapsed during the year:

Exercise period	Exercise price HK\$	Number of options	
		2011	2012
January 22, 2001 to January 22, 2011	16.8400	4,089,813	-
February 8, 2002 to February 8, 2011	18.76	86,700	-
May 26, 2001 to April 17, 2011	10.3000	78,240	-
July 16, 2002 to July 16, 2011	9.1600	167,360	-
August 1, 2003 to July 31, 2012	8.0600	-	200,000
November 13, 2003 to November 12, 2012	6.1500	-	5,440,000
July 25, 2004 to July 23, 2013	4.3500	8,692,000	215,000
September 16, 2003 to September 14, 2013	4.9000	-	7,000
		<u>13,114,113</u>	<u>5,862,000</u>

(5) There were no share options granted during the year (2011: nil).

(6) There were no share options exercised during the year (2011: nil).

(ii) 2011-2021 Share Stapled Units Option Scheme of the HKT Trust and HKT

On November 7, 2011 (the “Adoption Date”), the HKT Trust and HKT conditionally adopted a Share Stapled Units option scheme (“HKT 2011-2021 Option Scheme”) which has become effective upon Listing, to enable the HKT Trust and HKT, acting jointly by mutual agreement between them, to grant options to (a) any full-time or part-time employees of the HKT and/or any of its subsidiaries; (b) any director (including executive, non-executive and independent non-executive director) of HKT and/or any of its subsidiaries; and (c) any consultant or adviser (whether professional or otherwise and whether on an employment or contractual or honorary basis or otherwise and whether paid or unpaid), distributor, contractor, supplier, service provider, agent, customer and business partner of HKT and/or any of its subsidiaries (“Eligible Participants”) as incentives or rewards for their contribution to the growth of the HKT Group and to provide the HKT Group with a more flexible means to reward, remunerate, compensate and/or provide benefits to the Eligible Participants.

No Share Stapled Units option has been granted under the HKT 2011-2021 Option Scheme since the Adoption Date. Accordingly, there were no outstanding options under the HKT 2011-2021 Option Scheme as at December 31, 2011 and 2012 and no options were granted to or exercised by any directors of the Company, employees of the Group, or other participants, nor cancelled or lapsed during the year ended December 31, 2011 and 2012.

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

27 Employee benefits (continued)

(b) Equity compensation benefits (continued)

(iii) Share Stapled Units award schemes of HKT

On October 11, 2011, HKT conditionally adopted two award schemes pursuant to which awards of Share Stapled Units may be made, namely the HKT Share Stapled Units Purchase Scheme and the HKT Share Stapled Units Subscription Scheme (collectively the “HKT Share Stapled Units Award Schemes”).

In the case of the HKT Share Stapled Units Subscription Scheme:

The same group of potential eligible participants as referred to above except for any directors of HKT or its subsidiaries and/or any other connected persons of HKT.

The HKT Share Stapled Units Award Schemes are administered by the board of directors of HKT (“HKT Board”) and an independent trustee (the “Trustee”), as trustee appointed to hold the relevant Share Stapled Units until such time as the Share Stapled Units vest in the selected participants. Under both schemes, following the making of an award to eligible participants, the relevant share stapled units are held by the Trustee for that eligible participant and then vest over a period of time provided that the eligible participant remains an employee of the Group at the relevant time and satisfies any other conditions specified at the time the award is made, notwithstanding that the relevant committee of the HKT Board shall be at liberty to waive such condition.

Awards may be made by the HKT Board or any committee, sub-committee or person duly delegated, such as the remuneration committee and, in the case of Share Stapled Units that are not vested or transferred as originally intended, the Trustee may hold such units and income deriving therefrom for the purpose of any eligible participants, having taken into consideration the recommendations of the HKT Board.

No awards have been made or agreed to be made, under the HKT Share Stapled Units Subscription Scheme for the years ended December 31, 2011 and 2012.

The HKT Share Stapled Units Award Schemes are on similar terms and were conditionally adopted by HKT which became effective upon Listing as a potential means to incentivize and reward the eligible participants as follows:

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NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

27 Employee benefits (continued)

(b) Equity compensation benefits (continued)

(iii) Share Stapled Units award schemes of HKT (continued)

In the case of the HKT Share Stapled Units Purchase Scheme:

- (1) any full-time or part-time employees of HKT and/or any of its subsidiaries;
- (2) any director (including executive, non-executive and independent non-executive director) of HKT and/or any of its subsidiaries.

A summary of movements in the Share Stapled Units held by the Group under the HKT Share Stapled Units Purchase Scheme in respect of eligible employees of the Group during the year is as follows:

	The Group	
	Number of Share Stapled Units 2011	2012
Beginning of year	-	-
Purchase from the market by the trustee at average market price of HK\$6.07 per Share Stapled Unit	-	1,158,000
End of year	-	1,158,000

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NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

27 Employee benefits (continued)

(b) Equity compensation benefits (continued)

(iii) Share Stapled Units award schemes of HKT (continued)

Details of Share Stapled Units awarded to eligible employees of the Group pursuant to the HKT Share Stapled Units Purchase Scheme during the year and the unvested Share Stapled Units held by the Group are as follows:

(1) Movements in the number of unvested Share Stapled Units and their related weighted average fair value at their measurement dates

	The Group			
	2011		2012	
	Weighted average fair value at date of award HK\$	Number of Share Stapled Units	Weighted average fair value at date of award HK\$	Number of Share Stapled Units
Beginning of year	-	-	-	-
Awarded (<i>note (3)</i>)	-	-	5.98	1,145,831
Forfeited (<i>note (4)</i>)	-	-	5.98	(5,566)
End of year (<i>note (2)</i>)		-		1,140,265

The average fair value of Share Stapled Units awarded to eligible employees of the Group during the year at the measurement date is HK\$5.98 per Share Stapled Unit, which is measured by the quoted market price of the Share Stapled Units at the respective award dates.

(2) Terms of unvested Share Stapled Units held by the Group at balance sheet date

Date of award	Vesting period	Fair value at date of award HK\$	The Group	
			Number of Share Stapled Units	
			2011	2012
April 11, 2012	April 11, 2012 to April 11, 2013	5.98	-	534,748
April 11, 2012	April 11, 2013 to April 11, 2014	5.98	-	605,517
			-	1,140,265

The unvested Share Stapled Units held by the Group at December 31, 2012 had a weighted average remaining vesting period of 0.81 years (2011: Nil).

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NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

27 Employee benefits (continued)

(b) Equity compensation benefits (continued)

(iii) Share Stapled Units award schemes of HKT (continued)

(3) Details of Share Stapled Units awarded to eligible employees of the Group during the year

Date of award	Vesting period	Fair value at date of award HK\$	The Group	
			Number of Share Stapled Units	
			2011	2012
April 11, 2012	April 11, 2012 to April 11, 2013	5.98	-	537,532
April 11, 2012	April 11, 2013 to April 11, 2014	5.98	-	608,299
				<u>1,145,831</u>

(4) Details of Share Stapled Units forfeited by eligible employees of the Group during the year

Date of award	Vesting period	Fair value at date of award HK\$	The Group	
			Number of Share Stapled Units	
			2011	2012
April 11, 2012	April 11, 2012 to April 11, 2013	5.98	-	2,784
April 11, 2012	April 11, 2013 to April 11, 2014	5.98	-	2,782
				<u>5,566</u>

The fair value of the Share Stapled Units awarded to eligible employees of the Group during the year at the measurement dates is measured by the quoted market price of the Share Stapled Units at the respective award dates.

During the year, share-based compensation expenses of HK\$5 million is recognized for the HKT Share Stapled Units Award Schemes in the consolidated income statement and a corresponding HK\$5 million is recognized as an obligation in liabilities.

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

27 Employee benefits (continued)

(b) Equity compensation benefits (continued)

iv. Share award schemes of PCCW

In 2002, PCCW established two employee share incentive award schemes under which awards of shares may be granted to employees of participating subsidiaries. The directors of PCCW were not eligible to participate in either scheme. On June 10, 2002, PCCW approved the establishment of the PCCW Purchase Scheme under which selected employees are awarded shares purchased in the market. On November 12, 2002, PCCW approved the establishment of the PCCW Subscription Scheme under which selected employees are awarded newly issued shares. The purpose of both the PCCW Purchase Scheme and the PCCW Subscription Scheme is to recognize the contributions of certain employees of PCCW and its subsidiaries ("PCCW Group"), to retain them for the continued operation and development of the PCCW Group. Under both schemes, following the making of an award to an employee, the relevant shares are held on trust for that employee and then vest over a period of time provided that the employee remains an employee of the PCCW Group at the relevant time and satisfies any other conditions specified at the time the award is made, notwithstanding that the relevant Committee of the board of directors of PCCW shall be at liberty to waive such condition. In May 2006, the PCCW Purchase Scheme was altered such that the directors of PCCW are also eligible to participate in this scheme. The maximum aggregate number of shares that can be awarded under the two schemes is limited to 1% of the issued share capital of PCCW (excluding shares that have already been transferred to employees on vesting).

Pursuant to the relevant scheme rules of the PCCW Purchase Scheme and the PCCW Subscription Scheme, both schemes expired on November 15, 2012. The expiry of the scheme rules would not effect the shares which were previously awarded prior to expiry date. Each of the participating subsidiaries of PCCW is in the process of adopting a new set of scheme rules in respect of the PCCW Purchase Scheme and the PCCW Subscription Scheme so as to continue to participate in both Schemes for a further 10 years and to accommodate the granting of the Share Stapled Units in the future in addition or as alternative to the shares of PCCW.

No awards have been made or agreed to be made, under the PCCW Subscription Scheme for the years ended December 31, 2011 and 2012.

A summary of movements in PCCW shares held by the Group under the PCCW Purchase Scheme in respect of eligible employees of the Group during the year is as follows:

	Number of PCCW shares	
	2011	2012
Beginning of year	-	-
Purchase from the market by the trustee at average market price of HK\$2.87 per PCCW share	-	2,236,000
End of year	-	2,236,000

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

27 Employee benefits (continued)

(b) Equity compensation benefits (continued)

iv. Share award schemes of PCCW (continued)

Details of PCCW shares awarded to eligible employees of the Group pursuant to the PCCW Purchase Scheme during the year and the unvested PCCW shares held by the Group are as follows:

(1) Movements in the number of unvested PCCW shares held by the Group and their related weighted average fair value at their measurement dates

	The Group			
	2011		2012	
	Weighted average fair value at date of award HK\$	Number of PCCW shares	Weighted average fair value at date of award HK\$	Number of PCCW shares
Beginning of year	-	-	-	-
Awarded (<i>note (3)</i>)	-	-	2.80	2,215,122
Forfeited (<i>note (4)</i>)	-	-	2.80	(10,187)
End of year (<i>note (2)</i>)		-		2,204,935

The average fair value of PCCW shares awarded to eligible employees of the Group during the year at the measurement date is HK\$2.80 per PCCW share, which is measured by the quoted market price of PCCW shares at the respective award dates.

(2) Terms of unvested PCCW shares held by the Group at balance sheet date

Date of award	Vesting period	Fair value at date of award HK\$	The Group	
			Number of PCCW shares	
			2011	2012
April 11, 2012	April 11, 2012 to April 11, 2013	2.80	-	1,026,370
April 11, 2012	April 11, 2013 to April 11, 2014	2.80	-	1,178,565
			-	2,204,935

The unvested PCCW shares held by the Group at December 31, 2012 had a weighted average remaining vesting period of 0.81 years (2011: Nil).

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

27 Employee benefits (Continued)

(b) Equity compensation benefits (Continued)

iv. Share award schemes of PCCW (Continued)

(3) Details of PCCW shares awarded to eligible employees of the Group during the year

Date of award	Vesting period	Fair value at date of award HK\$	The Group	
			Number of PCCW shares 2011	2012
April 11, 2012	April 11, 2012 to April 11, 2013	2.80	-	1,031,464
April 11, 2012	April 11, 2013 to April 11, 2014	2.80	-	1,183,658
			<hr/>	<hr/>
			-	2,215,122
			<hr/>	<hr/>

(4) Details of PCCW shares forfeited by eligible employees of the Group during the year

Date of award	Vesting period	Fair value at date of award HK\$	The Group	
			Number of PCCW shares 2011	2012
April 11, 2012	April 11, 2012 to April 11, 2013	2.80	-	5,094
April 11, 2012	April 11, 2013 to April 11, 2014	2.80	-	5,093
			<hr/>	<hr/>
			-	10,187
			<hr/>	<hr/>

The fair value of the PCCW shares awarded to eligible employees of the Group during the year at the measurement dates is measured by the quoted market price of the PCCW shares at the respective award dates.

During the year, share-based compensation expenses of HK\$4 million is recognized in the consolidated income statement and HK\$4 million is recognized as an obligation in liabilities.

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

28 Reserves

	The Group								
	Share premium	Capital contribution reserve	Currency translation reserve	Merger reserve	Hedging reserve	Available- for-sale financial assets reserve	Other reserve	Retained profits	Total
	HK\$ million	HK\$ million	HK\$ million	HK\$ million	HK\$ million	HK\$ million	HK\$ million	HK\$ million	HK\$ Million
At January 1, 2011	14,884	28	350	(695)	208	41	(31)	2,453	17,238
Total comprehensive income for the year									
Profit for the year	-	-	-	-	-	-	-	1,564	1,564
Other comprehensive income									
Translation exchange differences									
- exchange differences on translating foreign operations	-	-	6	-	-	-	-	-	6
- release of translation reserve upon distribution in specie of shares in subsidiaries	-	-	11	-	-	-	-	-	11
Available-for-sale financial assets									
- changes in fair value	-	-	-	-	-	24	-	-	24
Cash flow hedges									
- effective portion of changes in fair value	-	-	-	-	16	-	-	-	16
- transfer from equity to consolidated income statement	-	-	-	-	(12)	-	-	-	(12)
	-	-	17	-	4	24	-	1,564	1,609
Capital contribution (note 26(a))	2,005	-	-	-	-	-	-	-	2,005
Special dividend in specie of shares in subsidiaries (notes 11 and 38)	(3,192)	-	-	-	-	-	-	331	(2,861)
At December 31, 2011	13,697	28	367	(695)	212	65	(31)	4,348	17,991

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

28 Reserves (continued)

	The Group								
	2012								
	Share premium HK\$ million	Capital contribution reserve HK\$ million	Currency translation reserve HK\$ million	Merger reserve HK\$ million	Hedging reserve HK\$ million	Available- for-sale financial assets reserve HK\$ million	Other reserve HK\$ million	Retained profits HK\$ million	Total HK\$ Million
At January 1, 2012	13,697	28	367	(695)	212	65	(31)	4,348	17,991
Total comprehensive income for the year									
Profit for the year	-	-	-	-	-	-	-	1,578	1,578
Other comprehensive income									
Translation exchange differences									
- exchange differences on translating foreign operations	-	-	98	-	-	-	-	-	98
Available-for-sale financial assets									
- changes in fair value	-	-	-	-	-	13	-	-	13
Cash flow hedges									
- effective portion of changes in fair value	-	-	-	-	(54)	-	-	-	(54)
- transfer from equity to consolidated income statement	-	-	-	-	19	-	-	-	19
	-	-	98	-	(35)	13	-	1,578	1,654
Issue of an ordinary share (note 26(a))	168	-	-	-	-	-	-	-	168
Interim dividend paid in respect of the current year (note 11)	-	-	-	-	-	-	-	(1,287)	(1,287)
Increase in interests in subsidiaries (note 39)	-	-	-	-	-	-	-	(2)	(2)
At December 31, 2012	13,865	28	465	(695)	177	78	(31)	4,637	18,524

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

28 Reserves (continued)

	The Company		
	Share premium HK\$ million	2011 Retained profits HK\$ million	Total HK\$ million
At January 1, 2011	14,884	(1)	14,883
Profit for the year	-	573	573
Special dividend in specie of shares in subsidiaries (note 11)	(3,192)	-	(3,192)
Capital contribution (note 26(a))	2,005	-	2,005
	<u>13,697</u>	<u>572</u>	<u>14,269</u>
At December 31, 2011	<u>13,697</u>	<u>572</u>	<u>14,269</u>

	The Company		
	Share premium HK\$ million	2012 Retained profits HK\$ million	Total HK\$ million
At January 1, 2012	13,697	572	14,269
Profit for the year	-	1,289	1,289
Interim dividend paid in respect of current year (note 11)	-	(1,287)	(1,287)
Issue of an ordinary share (note 26(a))	168	-	168
	<u>13,865</u>	<u>574</u>	<u>14,439</u>
At December 31, 2012	<u>13,865</u>	<u>574</u>	<u>14,439</u>

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

29 Deferred income tax

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

	The Group				
	2011				
	Accelerated tax depreciation and amortization HK\$ million	Valuation of leasehold land and properties HK\$ million	Tax losses HK\$ million	Others HK\$ million	Total HK\$ million
Beginning of year	2,260	6	(102)	(4)	2,160
(Credited)/charged to the consolidated income statement (note 10(a))	(197)	-	102	-	(95)
Transfer on special dividend in specie of shares in subsidiaries (note 38)	(72)	(6)	-	1	(77)
End of year	<u>1,991</u>	<u>-</u>	<u>-</u>	<u>(3)</u>	<u>1,988</u>

	The Group				
	2012				
	Accelerated tax depreciation and amortization HK\$ million	Valuation of leasehold land and properties HK\$ million	Tax losses HK\$ million	Others HK\$ million	Total HK\$ million
Beginning of year	1,991	-	-	(3)	1,988
(Credited)/charged to the consolidated income statement (note 10(a))	(164)	-	2	-	(162)
Additions upon business combinations (note 37)	-	-	-	2	2
End of year	<u>1,827</u>	<u>-</u>	<u>2</u>	<u>(1)</u>	<u>1,828</u>

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

29 Deferred income tax (continued)

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

	The Group	
	2011 HK\$ million	2012 HK\$ million
Deferred income tax assets recognized in the consolidated balance sheet (note (b))	(3)	(3)
Net deferred income tax liabilities recognized in the consolidated balance sheet	1,991	1,831
	<u>1,988</u>	<u>1,828</u>

- (b) During the year ended December 31, 2012, previously unrecognized tax losses of HK\$128 million (2011: HK\$102 million) have been reversed and utilized against current year taxable profits. The Group has unutilized estimated tax losses for which no deferred income tax assets have been recognized of HK\$8,659 million as at December 31, 2012 (2011: HK\$8,979 million) to carry forward for deduction against future taxable income. Estimated tax losses of HK\$13 million as at December 31, 2012 (2011: HK\$ 40 million) will expire within 1 to 5 years. HK\$13 million tax losses as at December 31, 2012 will expire after 5 years (2011: nil). The remaining portion of the tax losses, mainly relating to Hong Kong companies, can be carried forward indefinitely.

30 Carrier licence fee liabilities

As at December 31, 2012, the Group had carrier licence fee liabilities repayable as follows:

	The Group					
	2011			2012		
	Present value of the minimum annual fees HK\$ million	Interest expense relating to future periods HK\$ million	Total minimum annual fees HK\$ million	Present value of the minimum annual fees HK\$ million	Interest expense relating to future periods HK\$ million	Total minimum annual fees HK\$ million
Repayable within a period						
- not exceeding one year	190	9	199	200	9	209
- over one year, but not exceeding two years	149	22	171	159	23	182
- over two years, but not exceeding five years	429	144	573	345	97	442
- over five years	260	140	400	232	118	350
	<u>1,028</u>	<u>315</u>	<u>1,343</u>	<u>936</u>	<u>247</u>	<u>1,183</u>
Less: Amounts repayable within one year included under current liabilities	(190)	(9)	(199)	(200)	(9)	(209)
	<u>838</u>	<u>306</u>	<u>1,144</u>	<u>736</u>	<u>238</u>	<u>974</u>

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

31 Notes to the consolidated statement of cash flows

(a) Reconciliation of profit before income tax to net cash generated from operating activities

	The Group	
	2011 HK\$ million	2012 HK\$ million
Profit before income tax	1,950	2,077
Adjustments for:		
Provision for inventory obsolescence	7	5
Net gain on cash flow hedging instruments transferred from equity	(1)	(19)
Interest income	(41)	(25)
Interest expense	1,316	777
Finance charges	226	94
Cash flow hedges: transferred from equity	1	1
Fair value gains on derivative financial instruments on fair value hedges	(198)	(38)
Fair value adjustment of borrowings attributable to interest rate risk	202	42
Depreciation of property, plant and equipment	2,432	2,229
Gain on disposals of property, plant and equipment	(5)	-
Impairment loss for doubtful debts	160	138
Amortization of intangible assets	2,182	2,446
Amortization of land lease premium	14	13
Share of results of an associate	17	35
Share of results of jointly controlled companies	3	44
Impairment loss on interest in a joint controlled company	16	-
Assets and business received from a related company	(491)	-
Net realized gain on disposal of a subsidiary	(186)	-
Fair value gain on financial assets at fair value through profit or loss	-	(3)
Share-based payment	-	9
Increase in financial assets at fair value through profit or loss for equity compensation scheme	-	(13)
(Increase)/decrease in operating assets		
- inventories	(208)	100
- trade receivables	(601)	(143)
- prepayments, deposits and other current assets	(404)	(377)
- other non-current assets	(50)	(33)
Increase/(decrease) in operating liabilities		
- trade payables, accruals and other payables	264	(324)
- other long-term liabilities	11	(3)
- advances from customers	(79)	193
- amounts due to related companies	(29)	99
- amounts due to fellow subsidiaries, the immediate holding company and the ultimate holding company	1,309	(746)
- deferred income (non-current)	165	95
Cash generated from operations	7,982	6,673
Interest received	41	7
Income tax paid, net of tax refund		
- Hong Kong profits tax paid	(92)	(172)
- Overseas profits tax paid	(42)	(31)
Net cash generated from operating activities	7,889	6,477

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

31 Notes to the consolidated statement of cash flows(continued)

(b) Additions upon business combinations in 2012

	<u>The Group</u> 2012 HK\$ million
Purchases consideration	268
Estimated fair value of net assets/(liabilities) acquired (note 37 (a)):	
Property, plant and equipment	178
Intangible assets	118
Trade receivables, prepayments, deposits and other current assets	927
Cash and cash equivalents	41
Trade payables, accruals, other payables and advances from customers	(1,001)
Current income tax liabilities	(1)
Deferred tax liabilities	(2)
	260
Obligation assumed upon acquisition (note 37 (a))	121
Goodwill on acquisition (note 16)	129
Satisfied by:	
Cash (note 37 (a))	268

Analysis of the net outflow of cash and cash equivalents in respect of the additions upon business combinations:

	<u>The Group</u> 2012 HK\$ million
Purchase consideration settled in cash	(268)
Cash and cash equivalents of subsidiaries acquired	41
	(227)
Settlement of obligation assumed upon acquisition	(121)

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

31 Notes to the consolidated statement of cash flows (continued)

(c) Disposal of a subsidiary in 2011

The Group
2011
HK\$ million

Net liabilities disposed of:

Property, plant and equipment	1
Inventories	45
Trade receivables	135
Prepayments, deposits and other current assets	87
Cash and cash equivalents	16
Trade payables	(91)
Accruals and other payables	(55)
Current income tax liabilities	(2)
Amount due to fellow subsidiaries	(221)
Advances from customers	(30)
	<hr/>
	(115)
Cumulative exchange differences in respect of the net liabilities of the subsidiary	(19)
Net realized gain on disposal of a subsidiary (note 6)	186
	<hr/>
Total consideration receivable from a fellow subsidiary	52
	<hr/>

Analysis of the net outflow of cash and cash equivalents in respect of the disposal of a subsidiary:

The Group
2011
HK\$ million

Cash and cash equivalents disposed of	16
	<hr/>
Net cash outflow in respect of the disposal of a subsidiary	16
	<hr/>

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

31 Notes to the consolidated statement of cash flows (continued)

(d) Analysis of cash and cash equivalents

	The Group	
	2011 HK\$ million	2012 HK\$ million
Cash and bank balances	1,794	2,398
Bank overdrafts	(1)	-
Cash and cash equivalents	<u>1,793</u>	<u>2,398</u>

(e) Major non-cash transactions

During the year ended December 31, 2011, PCCW, Telstra and a related company completed certain transactions which resulted in the transfer by PCCW and Telstra the majority of the related company's assets, business platforms and operations to the Group. Please refer to note 4(d) for details.

As part of the group reorganization, all inter-company balances between the Group, the ultimate holding company and the Group's fellow subsidiaries, including the Solutions Group and the Media Group, assigned or novated with a net balance between the Company and CAS No. 1. The net amount owing from the Company to CAS No. 1 was capitalized by way of the Company issuing one ordinary share to CAS No. 1 (see note 26(a)).

During the year ended December 31, 2011, certain interests in subsidiaries have been distributed to CAS No. 1 by way of a special dividend in specie. Further details of the distribution are set out in notes 11 and 38.

During the year ended December 31, 2012, the Group acquired certain software and content from fellow subsidiaries amounting to approximately HK\$470 million, which was settled through offsetting with corresponding amounts due from fellow subsidiaries for cash received on behalf.

During the year ended December 31, 2012, the Company issued one ordinary share of US\$1 to the shareholders of the Company at a premium of US\$21,505,573 (approximately HK\$168 million) which was settled through offsetting with corresponding amount due to the immediate holding company.

32 Capital management

The Group's primary objectives when managing capital are to safeguard the Group's ability to continue as a going concern, so that it can continue to provide returns for shareholders, and benefits for other stakeholders, to support the Group's stability and growth; and to earn a margin commensurate with the level of business and market risks in the Group's operation.

The Group monitors capital by reviewing the level of capital that is at the disposal of the Group ("Adjusted Capital"), taking into consideration the future capital requirements of the Group, prevailing and projected profitability, projected operating cash flows, projected capital expenditures and projected strategic investment opportunities. Adjusted Capital comprises all components of equity, other than currency translation reserve, merger reserve, hedging reserve relating to cash flow hedges, available-for-sale financial assets reserve and other reserve.

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

32 Capital management (continued)

The Adjusted Capital as at December 31, 2012 was as follows:

	The Group	
	2011	2012
	HK\$ million	HK\$ million
Equity attributable to equity holders of the Company	22,952	23,485
Excluding:		
Currency translation reserve	(367)	(465)
Merger reserve	695	695
Hedging reserve	(212)	(177)
Available-for-sale financial assets reserve	(65)	(78)
Other reserve	31	31
Adjusted Capital	<u>23,034</u>	<u>23,491</u>

Neither the Company nor any of its subsidiaries is subject to externally imposed capital requirements, except for the debt covenant requirement of the loan agreements with external parties and the minimum capital requirement of a subsidiary regulated by Bermuda Monetary Authority.

33 Financial instruments

The tables below analyze financial instruments by category:

	The Group			
	2011			
	Loans and receivables HK\$ million	Derivatives used for hedging HK\$ million	Available- for-sale financial assets HK\$ million	Total HK\$ million
Non-current assets				
Available-for-sale financial assets	-	-	72	72
Derivative financial instruments	-	275	-	275
Other non-current assets	24	-	-	24
	<u>24</u>	<u>275</u>	<u>72</u>	<u>371</u>
Current assets				
Prepayments, deposits and other current assets (excluding prepayments)	1,987	-	-	1,987
Trade receivables, net	2,541	-	-	2,541
Cash and cash equivalents	1,793	-	-	1,793
	<u>6,321</u>	<u>-</u>	<u>-</u>	<u>6,321</u>
Total	<u>6,345</u>	<u>275</u>	<u>72</u>	<u>6,692</u>

HKT GROUP HOLDINGS LIMITED**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS****33 Financial instruments (continued)**

The tables below analyze financial instruments by category (continued):

	<u>The Group</u>	
	2011	
	Other financial liabilities at amortized cost HK\$ million	Total HK\$ million
Current liabilities		
Short-term borrowings	31	31
Trade payables	1,532	1,532
Accruals and other payables	2,264	2,264
Carrier licence fee liabilities	190	190
Amounts due to related companies	29	29
Amounts due to fellow subsidiaries, the immediate holding company and the ultimate holding company	8,631	8,631
	<u>12,677</u>	<u>12,677</u>
Non-current liabilities		
Long-term borrowings	23,470	23,470
Carrier licence fee liabilities	838	838
Other long-term liabilities	51	51
	<u>24,359</u>	<u>24,359</u>
Total	<u><u>37,036</u></u>	<u><u>37,036</u></u>

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

33 Financial instruments (continued)

The tables below analyze financial instruments by category (continued):

	The Group				
	2012				
	Loans and receivables HK\$ million	Asset at fair value through profit or loss HK\$ million	Derivatives used for hedging HK\$ million	Available- for-sale financial assets HK\$ million	Total HK\$ million
Non-current assets					
Available-for-sale financial assets	-	-	-	85	85
Financial assets at fair value through profit or loss	-	8	-	-	8
Derivative financial instruments	-	-	253	-	253
Other non-current assets	28	-	-	-	28
	<u>28</u>	<u>8</u>	<u>253</u>	<u>85</u>	<u>374</u>
	-----	-----	-----	-----	-----
Current assets					
Prepayments, deposits and other current assets (excluding prepayments)	2,374	-	-	-	2,374
Trade receivables, net	3,425	-	-	-	3,425
Amounts due from related companies	25	-	-	-	25
Derivative financial instrument	-	-	4	-	4
Financial assets at fair value through profit or loss	-	8	-	-	8
Cash and cash equivalents	2,398	-	-	-	2,398
	<u>8,222</u>	<u>8</u>	<u>4</u>	<u>-</u>	<u>8,234</u>
	-----	-----	-----	-----	-----
Total	8,250	16	257	85	8,608

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

33 Financial instruments (continued)

The tables below analyze financial instruments by category (continued):

	The Group 2012	
	Other financial liabilities at amortized cost HK\$ million	Total HK\$ million
Current liabilities		
Short-term borrowings	8,462	8,462
Trade payables	1,966	1,966
Accruals and other payables	2,539	2,539
Carrier licence fee liabilities	200	200
Amounts due to related companies	135	135
Amounts due to fellow subsidiaries and the immediate holding company	8,059	8,059
	<u>21,361</u>	<u>21,361</u>
Non-current liabilities		
Long-term borrowings	15,644	15,644
Carrier licence fee liabilities	736	736
Other long-term liabilities	51	51
	<u>16,431</u>	<u>16,431</u>
Total	<u>37,792</u>	<u>37,792</u>

	The Company	
	Loans and receivables	
	2011 HK\$ million	2012 HK\$ million
Current assets		
Amount due from the immediate holding company	-	91
Amounts due from subsidiaries	4,488	3,344
Total	<u>4,488</u>	<u>3,435</u>

	The Company	
	Other financial liabilities at amortized cost	
	2011 HK\$ million	2012 HK\$ million
Current liabilities		
Amounts due to subsidiaries	2,484	1,429
Total	<u>2,484</u>	<u>1,429</u>

Exposures to credit, liquidity, and market (including foreign currency, interest rate) risks arise in the normal course of the Group's business. The Group is also exposed to equity price risk arising from its equity investments in other entities. Exposures to these risks are controlled by the Group's financial management policies and practices described below.

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

33 Financial instruments (continued)

(a) Credit risk

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

Trade receivables have a normal credit period ranging up to 30 days from the date of invoice unless there is a separate mutual agreement on extension of the credit period. The Group maintains a well-defined credit policy and individual credit evaluations are performed on all customers requiring credit over a certain amount. These evaluations focus on the customer's past history of making payments when due and current ability to pay, and take into account information specific to the customer as well as pertaining to the economic environment in which the customer operates. Debtors who have overdue payable are requested to settle all outstanding balances before any further credit is granted. Normally, the Group does not obtain collateral from customers.

As at December 31, 2011 and 2012, the Group did not have a significant exposure to any individual debtors or counterparties.

Further quantitative disclosures in respect of the Group's exposure to credit risk arising from trade receivables are set out in note 23(b).

Other receivables are continuously monitored by assessing the credit quality of the counterparty, taking into account its financial position, past experience and other factors. Where necessary, impairment loss is made for estimated irrecoverable amounts. As at December 31, 2011 and 2012, other receivables were fully performing.

Investments, derivative financial instruments, interest receivable and cash transactions are executed with financial institutions or investment counterparties with sound credit ratings and the Group does not expect any significant counterparty risk. Moreover, credit limits are set for individual counterparties and periodic reviews are conducted to ensure that the limits are strictly followed.

The maximum exposure to credit risk is represented by the carrying amount of each financial asset, including derivative financial instruments, in the consolidated balance sheet. Except for the guarantees given by the Group as disclosed in note 35, the Group does not provide any other guarantees which would expose the Group to credit risk.

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

33 Financial instruments (continued)

(b) Liquidity risk

The Group's policy is to regularly monitor current and expected liquidity requirements and its compliance with debt covenants, to ensure that it maintains sufficient reserves of cash and adequate committed lines of funding from major financial institutions to meet its liquidity requirements in the short and longer term. Management believes there is no significant liquidity risk as the Group has sufficient committed facilities to fund its operations and debt servicing requirements.

The Group is subject to certain corporate guarantee obligations to guarantee performance of its subsidiaries and fellow subsidiaries in the normal course of business. Please refer to note 35(a) for details.

The following table details the remaining contractual maturities at the balance sheet date of the Group's non-derivative financial liabilities and derivative financial liabilities, which are based on contractual undiscounted cash flows (including interest payments computed using contractual rates or, if floating, based on rates current at the balance sheet date) and the earliest date the Group and the Company can be required to pay:

	The Group					Carrying Amount HK\$ million
	2011				Total contractual undiscounted cash outflow HK\$ million	
	Within 1 year or on demand HK\$ million	More than 1 year but within 2 years HK\$ million	More than 2 years but within 5 years HK\$ million	More than 5 years HK\$ million		
Current liabilities						
Short-term borrowings	(32)	-	-	-	(32)	(31)
Trade payables	(1,532)	-	-	-	(1,532)	(1,532)
Accruals and other payables	(2,264)	-	-	-	(2,264)	(2,264)
Carrier licence fee liabilities	(199)	-	-	-	(199)	(190)
Amounts due to related companies	(29)	-	-	-	(29)	(29)
Amounts due to fellow subsidiaries, the immediate holding company and the ultimate holding company	(8,631)	-	-	-	(8,631)	(8,631)
	<u>(12,687)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(12,687)</u>	<u>(12,677)</u>
Non-current liabilities						
Long-term borrowings	(686)	(8,750)	(16,011)	-	(25,447)	(23,470)
Carrier licence fee liabilities	-	(171)	(573)	(400)	(1,144)	(838)
Other long-term liabilities	(1)	(1)	(24)	(48)	(74)	(51)
	<u>(687)</u>	<u>(8,922)</u>	<u>(16,608)</u>	<u>(448)</u>	<u>(26,665)</u>	<u>(24,359)</u>
Total	<u><u>(13,374)</u></u>	<u><u>(8,922)</u></u>	<u><u>(16,608)</u></u>	<u><u>(448)</u></u>	<u><u>(39,352)</u></u>	<u><u>(37,036)</u></u>

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

33 Financial instruments (continued)

(b) Liquidity risk (continued)

	The Group					
	2012					
	Within 1 year or on demand HK\$ million	More than 1 year but within 2 years HK\$ million	More than 2 years but within 5 years HK\$ million	More than 5 years HK\$ million	Total contractual undiscounted cash outflow HK\$ million	Carrying Amount HK\$ million
Current liabilities						
Short-term borrowings	(8,676)	-	-	-	(8,676)	(8,462)
Trade payables	(1,966)	-	-	-	(1,966)	(1,966)
Accruals and other payables	(2,539)	-	-	-	(2,539)	(2,539)
Carrier licence fee liabilities	(209)	-	-	-	(209)	(200)
Amounts due to related companies	(135)	-	-	-	(135)	(135)
Amounts due to fellow subsidiaries and the immediate holding company	(8,059)	-	-	-	(8,059)	(8,059)
	<u>(21,584)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(21,584)</u>	<u>(21,361)</u>
Non-current liabilities						
Long-term borrowings	(411)	(2,717)	(13,606)	-	(16,734)	(15,644)
Carrier licence fee liabilities	-	(182)	(442)	(350)	(974)	(736)
Other long-term liabilities	(3)	(26)	(3)	(53)	(85)	(51)
	<u>(414)</u>	<u>(2,925)</u>	<u>(14,051)</u>	<u>(403)</u>	<u>(17,793)</u>	<u>(16,431)</u>
Total	<u>(21,998)</u>	<u>(2,925)</u>	<u>(14,051)</u>	<u>(403)</u>	<u>(39,377)</u>	<u>(37,792)</u>

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

33 Financial instruments (continued)

(b) Liquidity risk (continued)

The Company					
2011					
Within 1 year or on demand HK\$ million	More than 1 year but within 2 years HK\$ million	More than 2 years but within 5 years HK\$ million	More than 5 years HK\$ million	Total contractual undiscounted cash outflow HK\$ million	Carrying Amount HK\$ million
Current liabilities					
Amount due to a subsidiary	(2,484)	-	-	-	(2,484)
The Company					
2012					
Within 1 year or on demand HK\$ million	More than 1 year but within 2 years HK\$ million	More than 2 years but within 5 years HK\$ million	More than 5 years HK\$ million	Total contractual undiscounted cash outflow HK\$ million	Carrying Amount HK\$ million
Current liabilities					
Amounts due to subsidiaries	(1,429)	-	-	-	(1,429)

(c) Market risk

Market risk composed of foreign currency, interest rate and equity price exposure deriving from the Group's operation, investment and funding activities. As a matter of policy, the Group enters into cross currency swap contracts and other financial instruments to manage its exposure to market risk directly related to its operations and financing. The Group does not undertake any speculative trading activities in connection with these financial instruments or enter into or acquire market risk sensitive instruments for trading purposes.

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

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

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

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

33 Financial instruments (continued)

(c) Market risk (continued)

(i) Foreign currency risk

The Group operates internationally and is exposed to foreign exchange risk arising from various currency exposures. Foreign exchange risk arises when the Group's recognized assets and liabilities are denominated in a currency that is not the entity's functional currency.

The Group's borrowings are mainly denominated in either Hong Kong dollars or United States dollars. As at December 31, 2012, majority of the Group's short-term and long-term borrowings denominated in United States dollars were swapped into Hong Kong dollars by cross currency swap contracts. Given this, management does not expect that there will be any significant currency risk associated with the Group's borrowings. Certain portion of the cross currency swap contracts outstanding as at December 31, 2012 with an aggregate notional contract amount of US\$1,500 million (approximately HK\$11,627 million) (2011: US\$1,500 million (approximately HK\$11,664 million)) were designated as cash flow hedges against foreign exchange rate risk.

In respect of trade receivables and payables held in currencies other than the functional currency of the operations to which they relate, 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 following table details the Group's exposure at the balance sheet date to currency risk arising from significant recognized financial assets or liabilities denominated in foreign currencies.

	The Group			
	2011		2012	
	United States Dollars HK\$ million	Chinese Renminbi HK\$ million	United States Dollars HK\$ million	Chinese Renminbi HK\$ million
Trade receivables	709	167	768	206
Amounts due from related companies	-	-	-	11
Cash and cash equivalents	316	353	282	211
Trade payables	(617)	(46)	(618)	(40)
Amounts due to related companies	(39)	-	(286)	-
Short-term borrowings	(31)	-	(3,873)	-
Long-term borrowings	(11,729)	-	(7,877)	-
Gross exposure arising from recognized financial (liabilities)/assets	(11,391)	474	(11,604)	388
Net financial liabilities denominated in respective group entities' functional currencies	(63)	(485)	(158)	(390)
Notional amounts of cross currency swap contracts designated as cash flow hedges	11,664	-	11,627	-
Overall net exposure	210	(11)	(135)	(2)

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

33 Financial instruments (continued)

(c) Market risk (continued)

(i) Foreign currency risk (continued)

As at December 31, 2012, if Hong Kong dollar had weakened/strengthened by 1% against the United States dollar, with all other variables held constant as at December 31, 2012, the profit after tax of the Group for the year ended December 31, 2012 would have decreased/increased by approximately HK\$(1.13) million (2011: HK\$1.75 million), mainly as a result of foreign exchange gains/losses on translation of United States dollar denominated recognized assets and liabilities which are not hedged by hedging instruments. Meanwhile, the hedging reserve as at December 31, 2012 would have increased/decreased by approximately HK\$116 million (2011: HK\$117 million) mainly as a result of foreign exchange gains/losses on the short-term and long-term borrowings being hedged by cross currency swap contracts.

As at December 31, 2012, if Hong Kong dollar had weakened/strengthened by 5% against the Chinese Renminbi, with all other variables held constant as at December 31, 2012, there would be no material impact on the Group's profit after tax for the year ended December 31, 2012.

The sensitivity analysis has been determined assuming that the change in foreign exchange rates had occurred at the balance sheet dates and had been applied to the Group's exposure to currency risk for recognized assets and liabilities in existence at the dates, and that all other variables, in particular interest rates, remain constant.

The stated changes represent management's assessment of reasonably possible changes in foreign exchange rates over the periods until the next annual balance sheet date. In this respect, it is assumed that the pegged rate between the Hong Kong dollar and the United States dollar would be materially unaffected by any change in the movement in value of the United States dollar against other currencies. The analysis is performed on the same basis for the years ended December 31, 2011 and 2012.

(ii) Interest rate risk

As the Group has no significant interest-bearing assets, the Group's income and operating cash flows are substantially independent of changes in market interest rates.

The Group's interest rate risk arises primarily from short-term and long-term borrowings. Borrowings at variable rates and fixed rates expose the Group to cash flow interest rate risk and fair value interest rate risk respectively. In addition, from time to time, the Group draws under long-term revolving credit and term facilities which are denominated in Hong Kong dollars and pays interest at floating rate.

The Group has entered into fixed-to-floating cross currency swap contracts to hedge the fair value interest rate risk arising from its fixed rate long-term borrowings.

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

33 Financial instruments (continued)

(c) Market risk (continued)

(ii) Interest rate risk (continued)

The following table details the interest rate profile of the Group's borrowings at the balance sheet date, after taking into account the effect of cross currency swap contracts designated as cash flow and fair value hedging instruments.

	The Group			
	2011		2012	
	Effective interest rate	HK\$ million	Effective interest rate	HK\$ million
Net fixed rate borrowings:	%		%	
Short-term borrowings with cash flow hedging instruments	-	-	6.13	3,873
Long-term borrowings with cash flow hedging instruments	5.77	7,748	5.42	3,861
		<u>7,748</u>		<u>7,734</u>
Variable rate borrowings:				
Bank borrowings	1.44	11,774	1.61	12,356
Long-term borrowings with fair value hedging instruments	4.46	3,979	4.46	4,016
		<u>15,753</u>		<u>16,372</u>
Total borrowings		<u>23,501</u>		<u>24,106</u>

At December 31, 2012, if interest rates on Hong Kong dollar denominated borrowings had been increased/decreased by 10 basis points, with all other variables held constant, the Group's profit after tax for the year would have been decreased/increased by approximately HK\$12 million (2011: HK\$11 million), mainly as a result of higher/lower interest expense on floating rate borrowings.

The sensitivity analysis above has been determined assuming that the change in interest rate had occurred at the balance sheet date and had been applied to the exposure to interest rate risk for the Group's floating rate borrowings in existence at that date. The 10 basis points increase or decrease represents management's assessment of a reasonably possible change in interest rates over the period until the next annual balance sheet date. The analysis is performed on the same basis for the years ended December 31, 2011 and 2012.

(iii) Equity price risk

The Group is exposed to equity price changes arising from equity investments classified as available-for-sale financial assets (note 21). The investments are listed on a recognized stock exchange. To manage its equity price risk, the portfolio is diversified in accordance with the limits set by the Group. Given the insignificant portfolio of listed equity securities held by the Group, management believes that the Group's equity price risk is minimal.

HKT GROUP HOLDINGS LIMITED

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

33 Financial instruments (continued)

(d) Fair values

All financial instruments are carried at amounts not materially different from their fair values as at December 31, 2012 except as follows, with fair value calculated by quoted prices:

	The Group			
	2011		2012	
	Carrying amount HK\$ million	Fair value HK\$ million	Carrying amount HK\$ million	Fair value HK\$ million
Short-term borrowings	(31)	(31)	(8,462)	(8,557)
Long-term borrowings	<u>(23,470)</u>	<u>(24,618)</u>	<u>(15,644)</u>	<u>(16,090)</u>

(e) Estimation of fair values

The table below analyses financial instruments carried at fair value, by valuation method. The different levels have been defined as follows:

- Quoted prices (unadjusted) in active markets for identical assets or liabilities (level 1).
- Inputs other than quoted prices that are observable either directly (that is, as prices) or indirectly (that is, derived from prices) (level 2).
- Inputs for asset and liability that are not based on observable market data (level 3).

The following table presents the Group's assets and liabilities that are measured at fair value:

	The Group			
	2011			Total HK\$ million
	Level 1 HK\$ million	Level 2 HK\$ million	Level 3 HK\$ million	
Assets				
Available-for-sale financial assets				
- Listed equity securities	72	-	-	72
Derivative financial instruments	-	275	-	275
Total assets	<u>72</u>	<u>275</u>	<u>-</u>	<u>347</u>

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33 Financial instruments (continued)

(e) Estimation of fair values (continued)

	The Group			
	Level 1	Level 2	Level 3	Total
	HK\$ million	HK\$ million	HK\$ million	HK\$ million
Assets				
Available-for-sale financial assets	85	-	-	85
- Listed equity securities				
Financial assets at fair value through profit or loss	16	-	-	16
Derivative financial instruments (non-current)	-	257	-	257
Total assets	101	257	-	358

The fair value of financial instruments traded in active markets is based on quoted market prices at the balance sheet date. The quoted market price used for financial assets held by the Group included in level 1 is the current bid price. Instruments included in level 1 comprise available-for-sale financial assets listed on the Alternative Investment Market operated by London Stock Exchange plc.

The fair value of financial instruments that are not traded in an active market is determined by using valuation techniques and making assumptions that are based on market conditions existing at the end of each reporting period. Instruments included in level 2 comprise cross currency swap contracts. In measuring the swap transactions, the fair value is the net present value of the estimated future cash flows discounted at the market quoted swap rates.

34 Commitments

(a) Capital

	The Group	
	2011	2012
	HK\$ million	HK\$ million
Authorized and contracted for	982	926
Authorized but not contracted for	887	739
	1,869	1,665

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

	The Group	
	2011	2012
	HK\$ million	HK\$ million
Investments	52	62
Acquisition of property, plant and equipment	1,817	1,603
	1,869	1,665

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34 Commitments (continued)

(b) Operating leases

As at December 31, 2012, the total future minimum lease payments under non-cancellable operating leases are payable as follows:

Land and buildings

	The Group	
	2011	2012
	HK\$ million	HK\$ million
Within 1 year	522	597
After 1 year but within 5 years	609	915
After 5 years	-	11
	<u>1,131</u>	<u>1,523</u>

Network capacity and equipment

	The Group	
	2011	2012
	HK\$ million	HK\$ million
Within 1 year	342	967
After 1 year but within 5 years	300	600
After 5 years	155	305
	<u>797</u>	<u>1,872</u>

Majority of the leases typically run for a period of 1 to 12 years (2011: 1 to 12 years). None of the leases include contingent rentals.

(c) Others

As at December 31, 2012, the Group has other outstanding commitments as follows:

	The Group	
	2011	2012
	HK\$ million	HK\$ million
Operating expenditure commitments	237	235
	<u>237</u>	<u>235</u>

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35 Contingent liabilities

	The Group		The Company	
	2011 HK\$ million	2012 HK\$ million	2011 HK\$ million	2012 HK\$ million
Performance guarantees (note (a))	240	280	785	695
Others	3	63	1	62
	<u>243</u>	<u>343</u>	<u>786</u>	<u>757</u>

(a) Performance guarantees

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

(b) Financial guarantees issued

As at December 31, 2012, the Company has given unconditional and irrevocable guarantees in respect of notes issued by the following subsidiaries of the Company, as to payments of principal and interests in favour of the holders of the notes.

<u>Name of issuer</u>	<u>Year of expiry</u>	<u>Outstanding principal of guaranteed notes at December 31, 2011</u>	<u>Outstanding principal of guaranteed notes at December 31, 2012</u>
PCCW-HKT Capital No.2 Limited	2013	US\$500 million	US\$500 million
PCCW-HKT Capital No.3 Limited	2015	US\$500 million	US\$500 million
PCCW-HKT Capital No.4 Limited	2016	US\$500 million	US\$500 million

The Company has not recognized any obligation in respect of these guarantees as their fair values cannot be reliably measured. The directors consider that the fair value of such guarantees is not significant and has no material impact to the Company's results and financial position.

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36 Bank loan facilities

Aggregate bank loan facilities as at December 31, 2012 were HK\$23,182 million (2011: HK\$20,444 million) of which the unused facilities amounted to HK\$10,758 million (2011: HK\$8,559 million). The Group has obtained new facilities of HK\$6,740 million maturing in 2017 and 2018.

A summary of major borrowings is set out in notes 23(c) and 24.

Security pledged for certain banking facilities includes:

	The Group	
	2011 HK\$ million	2012 HK\$ million
Property, plant and equipment	23	-
Trade receivables	37	-
Bank deposit	2	-
	<u>62</u>	<u>-</u>

37 Business combinations

(a) Business combinations for the year ended December 31, 2012

On August 31, 2012 the Group acquired 100% per cent of the share capital of Gateway Communications (UK) Limited, Gateway Communications S.A., Gateway Communications S.A.S., Gateway Communications Mozambique Limitada, Gateway Communications (Proprietary) Limited, and certain assets and liabilities of Gateway Communications Africa (UK) Limited (the "Gateway Group"), companies incorporated in United Kingdom, Belgium, France, Mozambique, South Africa, and United Kingdom, respectively. The purpose of the acquisition is to expand the Group's international voice and data services. The acquirees' business covers the provision of international voice services and data services. The Group made a payment for acquisition totaling HK\$268 million in cash.

- (i) Details of net assets acquired and goodwill in respect of acquisitions of the Gateway Group at the acquisition date were as follows:

	2012 HK\$ million
Purchase consideration settled in cash	268
Less: Estimated fair value of net assets acquired	(260)
Obligation assumed upon acquisition	121
	<u>129</u>
Goodwill on business combinations (<i>note 16</i>)	<u>129</u>

The goodwill is attributable to future profit generated from the provision of international voice services and data services.

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37 Business combinations (continued)

(a) Business combinations for the year ended December 31, 2012 (continued)

- (i) Details of net assets acquired and goodwill in respect of acquisitions of the Gateway Group at the acquisition date were as follows: (continued)

The Group is required to recognize the acquirees' identifiable assets, liabilities and contingent liabilities that satisfy the recognition criteria at their fair values at the acquisition date. As of the date of these consolidated financial statements, the purchase price allocation process is ongoing and has yet to be finalized. In the preparation of these consolidated financial statements, the Group has used the estimated fair values of the acquired assets and liabilities with the excess of the cost of acquisition over these estimated fair values being recorded as goodwill. This allocation of the purchase price allocation to the acquired assets and liabilities is provisional and will be adjusted in the Group's 2013 consolidated financial statements when the purchase price allocation is finalized. Had the purchase price allocation been completed, the fair values of the assets and liabilities acquired and the amount of goodwill to be recorded could be materially different from the amounts recognized. The values of assets and liabilities acquired and the resulting goodwill will be adjusted retrospectively upon the completion of the purchase price allocation in 2013.

The provisional amounts of the assets and liabilities of the Gateway Group at the acquisition date were as follows:

	Estimated Fair Value HK\$ million	Carrying Amount HK\$ million
Property, plant and equipment	178	178
Intangible assets	118	-
Trade receivables, prepayments, deposits and other current assets	927	927
Cash and cash equivalents	41	41
Trade payables, accruals, other payables and advances from customers	(1,001)	(1,001)
Current income tax liabilities	(1)	(1)
Deferred income tax liabilities	(2)	(2)
Net assets acquired	<u>260</u>	<u>142</u>
Obligation assumed upon acquisition	<u>121</u>	<u>121</u>
		Net cash outflow HK\$ million
Purchase consideration settled in cash		(268)
Cash and cash equivalents of Gateway Group acquired		<u>41</u>
		(227)
Settlement of obligation assumed upon acquisition		<u>(121)</u>

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37 Business combinations (continued)

(a) Business combinations for the year ended December 31, 2012 (continued)

(ii) Acquisition-related costs

Acquisition-related costs of HK\$12 million are included in the consolidated income statement for the year ended December 31, 2012.

(iii) Revenue and profit contribution

The business of Gateway Group has been integrated into the business of the Group since the acquisition date. Accordingly, it is not practical to quantify the individual contribution of the Gateway Group to the revenue and profit of the Group during the year ended December 31, 2012 on a reasonable basis.

(b) Business combinations for the year ended December 31, 2011

There was no business combination transaction occurred for the year ended December 31, 2011.

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38 Special dividend in specie of shares in subsidiaries

During the year ended December 31, 2011, pursuant to the reorganization as detailed in note 1(b)(ii) to the financial statements, the Group transferred Media Business and Solutions Business managed by the Media Group and the Solutions Group respectively by way of a special dividend in specie of the shares in HKT Media and HKT Solutions to CAS No. 1.

The net assets of the Media Group and the Solutions Group distributed by way of a special dividend in specie of the shares in HKT Media and HKT Solutions were as follows:

	HK\$ million
Non-current assets	
Property, plant and equipment	576
Investment properties	12
Interests in leasehold land	31
Goodwill	1,206
Intangible assets	667
Interest in a jointly controlled company	9
Available-for-sale financial assets	192
Current assets	
Prepayment, deposits and other current assets	1,021
Inventories	48
Trade receivables, net	278
Cash and cash equivalent	124
Current liabilities	
Trade payables	(66)
Accruals and other payables	(537)
Amounts due to fellow subsidiaries and the ultimate holding company	(441)
Advances from customers	(174)
Current income tax liabilities	(2)
Non-current liabilities	
Deferred income tax liabilities	(77)
Other long-term liabilities	(17)
Net assets transferred	2,850
Cumulative exchange differences in respect of the net assets of the subsidiaries reclassified from equity to retained profits on distribution by way of special dividend in specie of shares in subsidiaries	11
Special dividend in specie of shares in subsidiaries at carrying costs (note 28)	2,861
Net cash outflow arising on special dividend in specie of shares in subsidiaries	
Cash and cash equivalent	124

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39 Transactions with non-controlling interests

During the year, the Group acquired 30% and 15% of the issued shares of two subsidiaries of IP BPO Holdings Pte. Ltd., PCCW Teleservices (Philippines) Inc. and PCCW Teleservices (US) Inc. respectively, for an aggregate purchase consideration of approximately HK\$5 million. The aggregate carrying amount of the non-controlling interests in PCCW Teleservices (Philippines) Inc. and PCCW Teleservices (US) Inc. on the dates of acquisition was approximately HK\$3 million. The Group recognized a decrease in equity attributable to the equity holders of the Company of approximately HK\$2 million.

	The Group	
	2011	2012
	HK\$ million	HK\$ million
Consideration paid to non-controlling interests for an increase in ownership interest in a subsidiary	-	5
Less: Carrying amount of non-controlling interests acquired	-	(3)
	<u> </u>	<u> </u>
Excess of consideration paid in the transactions with non-controlling interests recognized within equity	-	2
	<u> </u>	<u> </u>

40 Possible impact of amendments, new or revised standards and interpretations issued but not yet effective for the annual accounting period ended December 31, 2012

Up to the date of approval of these financial statements, the HKICPA has issued the following amendments, new or revised standards and interpretations which are not yet effective for the accounting period ended December 31, 2012 and which have not been adopted in these financial statements:

		Effective for accounting periods beginning on or after
HKFRS 1 (Amendment)	First-time Adoption of Hong Kong Financial Reporting Standards	July 1, 2011
HKAS 1 (Revised) (Amendment)	Presentation of Financial Statements	July 1, 2012
HKFRS 7 (Amendment)	Financial Instruments: Disclosure - Offsetting Financial Assets and Financial Liabilities	January 1, 2013
HKFRS 10	Consolidated Financial Statements	January 1, 2013
HKFRS 11	Joint Arrangements	January 1, 2013
HKFRS 12	Disclosure of Interests in Other Entities	January 1, 2013
HKFRS 13	Fair Value Measurement	January 1, 2013
HKAS 19 (2011)	Employee Benefits	January 1, 2013

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40 Possible impact of amendments, new or revised standards and interpretations issued but not yet effective for the annual accounting period ended December 31, 2012 (continued)

Up to the date of approval of these financial statements, the HKICPA has issued the following amendments, new or revised standards and interpretations which are not yet effective for the accounting period ended December 31, 2012 and which have not been adopted in these financial statements:

		Effective for accounting periods beginning on or after
HKAS 27 (2011)	Separate Financial Statements	January 1, 2013
HKAS 28 (2011)	Investments in Associates and Joint Ventures	January 1, 2013
HK(IFRIC) - Int 20	Stripping Costs in the Production Phase of a Surface Mine	January 1, 2013
HKAS 32 (Amendment)	Offsetting Financial Assets and Financial Liabilities	January 1, 2014
HKFRS 7 (Amendment)	Financial Instruments: Disclosure - Mandatory Effective Date and Transaction Disclosures	January 1, 2015
HKFRS 9	Financial Instruments	January 1, 2015
HKFRS 9 (Amendment)	Financial Instruments: Mandatory Effective Date and Transition Disclosures	January 1, 2015

Apart from the above, a number of improvements and minor amendments to HKFRSs have also been issued by the HKICPA but they are not yet effective for the year ended December 31, 2012 and have not been adopted in these financial statements.

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