

# PACIFIC CENTURY GROUP

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*Delivery by hand*

RICHARD LI  
CHAIRMAN AND CHIEF EXECUTIVE

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Mr. K.C. Kwong  
Secretary for Information  
Technology and Broadcasting  
Government of the Hong Kong  
Special Administrative Region  
2/F., Murray Building  
Hong Kong

*K.C.*  
Dear Mr. Kwong,

## Cyber-Port

I write to follow-up our meeting of January 25 at which you presented us with the Government's "mode of implementation: possible framework" document.

It has always been our intention to cooperate with the Government in the nature of a partnership in order to bring the Cyber-Port into reality. In that spirit we have studied the Government's proposals with an open mind in the hope that we can quickly reach an acceptable way forward.

I have to say that there are so many different dimensions to balance that it is not easy to find the right formula. This is compounded by the fact that PCG has consistently maintained that we would develop the Cyber-Port for the Government on a cost plus a thin margin basis - however, given the real risks involved in the project, PCG needs to assure itself that it is not putting itself at peril in agreeing a way forward with the Government.

After considerable study we think we can move a long way towards meeting the Government's "mode of implementation: possible framework". The scheme we have in mind is outlined in the Attachment. It is more complex than the PTG proposal that we last made to Government (which we still prefer) but it is effectively what the Government has asked for and is a workable approach. I have asked PCG executives to be on standby to explain the scheme and negotiate the necessary agreements with Government.

Yours sincerely,



RICHARD LI

c.c. Miss Eva Cheng - ITBB

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PACIFIC CENTURY GROUP HOLDINGS LIMITED

Proposed scheme to implement the  
Government's "mode of implementation : possible framework"

a) Development of Cyber-Port

- Corporate structure. PCG would agree to a private joint venture on the terms outlined below. The private joint venture would be a Company (called the Cyber-Port Development and Management Corporation (CDMC)). Ordinary shares in the CDMC would be held by the Government and PCG (the proportion is discussed below) and voting rights would attach only to ordinary shares in proportion to the holding of such shares by PCG and the Government. Note that it is our requirement to have PCG as the holder of the shares (not PCC) as PCC does not have the requisite expertise, the managerial structure or business focus to be able to take on the project management role whereas PCG does. PCG as the majority shareholder in PCC can commit PCC as an anchor tenant to the Cyber-Port so the Government still maintains PCC's attachment to this project.
- Shareholding in the CDMC. In principle, PCG is prepared to accept that if any premium is to be imputed at the Pok Fu Lam site that it could only extend to the 38% of the land ear-marked for the residential development for private sale. Further, such land premium would have to recognise that the Cyber-Port design requires the creation of the right environment and a plot ratio of 3.8:1 on the residential portion versus the normally acceptable 5:1. (For discussion purposes we can designate this premium to have a value of \$ x billion). The 62% of the land earmarked for the core of the Cyber-Port must not attract any premium.

PCG would accept that the \$ x billion in land premium should be injected into the CDMC as preference shares. We believe this would be the best both practically and presentationally. Practically, it would allow the Government to have these preference shares retired against receipt of an equivalent value of assets in the Cyber-Port once constructed; presentationally, it would ensure that the Government's interests were protected in the scheme as preference shares rank higher than ordinary shares. The preference shares ought to have a maximum time period for redemption (e.g. 15 years) and could carry a coupon rate of return (which we believe should be no higher than 2% p.a.). Upon redemption of the preference shares, the Cyber-Port assets received in return by the Government would need to be leased back to the CDMC and the Government would continue to receive a return via the lease on its assets. The lease back terms would have to be

negotiated between the Government and the CDMC but the terms could not be any more favourable than the then current rental income being achieved by the CDMC.

As far as the ordinary shareholding is concerned, PCG notes the Government's desire to have a portion being broadly equivalent to the \$ x billion in land premium foregone and PCG's portion being related to the working capital required for the project. The shareholding should also take into account the project risks involved and the time-scale of the project. Total capital and interest costs will approach \$20 billion and this is a large amount for any developer to shoulder, particularly on a thin margin. In light of this PCG would suggest the shareholding ought to be 20% Government and 80% PCG. At a lower percentage to PCG, the risks versus reward issues rapidly put the project out of contemplation.

PCG notes the Government's willingness to divest its ordinary shares to other anchor tenants of the Cyber-Port. PCG has no in principle objection to this; however, PCG would prefer that the Government did not divest its shares during the construction phase of the project as the introduction of too many shareholders too early could adversely affect implementation of the project.

- Cashflow. PCG does not foresee the need for a major equity investment by the Government. The CDMC would need some initial funds to commence operations and we would suggest this could be less than \$100 million and would be contributed by PCG and the Government in proportion to their holding of ordinary shares.
- Government's role. In addition to carrying out advance earthworks and granting the land by PTG to the CDMC we believe it is necessary for the Government to commit to depressing the section of the proposed Route 7 that will run alongside the waterfront of the Cyber-Port. Unless this section of Route 7 is constructed properly the whole environment we are proposing to achieve at the Cyber-Port will be ruined and the viability of the project would be called into question.
- PCG's role : project manager, designer, marketing and managing partner of the developer (CDMC). PCC as an anchor tenant. To provide working capital for the construction phase. To actively engage other anchor tenants. To ensure that the design, quality of buildings/equipment/facilities meet the needs of tenants.

b) Role of residential property

- We agree that residential property is an integral part of the Cyber-Port design and we intend that it will be seamlessly incorporated into the design.
- There are two residential property components. The first relates to low density quality housing in the core of the Cyber-Port. This component remains essential as we outlined in our initial presentation to Government on September 2, 1998. Allocation rules would need to be developed to allow take-up of this housing by Cyber-Port tenants. The second component of housing relates to the higher density housing originally designated for commercial sale under the PTC proposal. The bulk of this housing needs to be sold or leased on the open market without any restrictions (of course, Cyber-Port tenants could acquire on this basis) in order to repay the CDMC's debts incurred in construction of the project.
- Revenue from all housing (whether by rent or lease) would be ploughed back into the CDMC. Surpluses (if any) from sale of residential property would be distributed to the shareholders in proportion to their ordinary shareholdings.

c) Cyber-Port Development and Management Corporation (CDMC)

- A private company initially held by the Government and PCG. Should there be other shareholders in time, they would be represented on the CDMC Board. Regarding day to day management of the Cyber-Port, PCG has no objection to the establishment of some form of advising board comprising Government, PCC and other anchor tenants plus representatives of smaller tenants.
- PCG would take up the management role through the CDMC and would appoint the CEO and other staff with the Government having the right of veto with respect to the CEO. It is agreed that there will need to be an agreed mechanism for selection of tenants.

# Schematic of the Proposed Arrangement

## GOVERNMENT

## PCG

