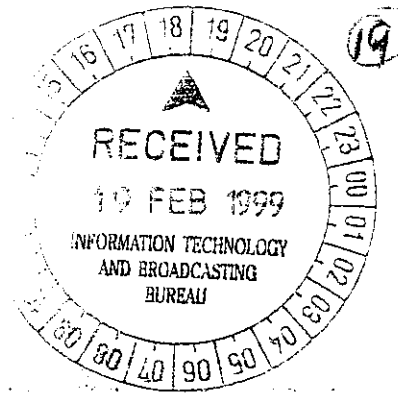


19th February 1999

Miss Eva Cheng
Deputy Secretary
Information Technology and Broadcasting Bureau
1/F Murray Building
Garden Road
Hong Kong



Dear Eva,

We appreciate the efforts you have been making pursue the issues we raised in our letter of 15th February. We also appreciate the meeting we held on Wednesday – despite its intrusion on your Chinese New Year holiday.

That meeting was particularly useful as it clarified several points, for example, that;

- the Government recognizes the “efficiency dividend” from mobilizing PCG to realize the Cyber-Port project. This would translate into a much shorter project completion time, lower cost, more relevant design and a better quality project. Thus PCG would bring substantial value to the project that needs to be factored into any structuring of commercial arrangements between PCG and the Government.
- the Government is insistent on PCG bearing the project risk – particularly on cost overrun, including capital cost and investment cost overrun. Although the risks are substantial, we have always maintained that PCG would be prepared to bear such risks as long as the overall commercial arrangements are satisfactory. We confirm our commitment to accept such risks on this basis.
- the land premium issue is a substantial one. We accept land premium needs to be calculated on the residential portion of the Cyber-Port slated for commercial marketing to accrue sales revenue. We find the Government’s estimate of \$5.5 billion excessive compared to our estimate of \$4 billion. Moreover, the cost of associated investment in infrastructure (currently estimated at HK\$548 million) should be borne by the Government and should not be added to the land premium. We need to finalize this quickly as it factors into both the financial arrangements and the project risk profile very significantly. Regarding the land premium on the Cyber-Port proper, we have consistently argued against the setting of any land premium on this infrastructure project. Indeed, the land premium of \$1.5 billion proposed by the Government would raise directly the level of Cyber-Port rentals – an effect completely at odds with the Cyber-Port’s entire objective of attracting high-value add information technology companies to Hong Kong with competitive

rents. We provided several arguments against applying land premium to the Cyber-Port proper and we cautioned against adopting other mechanisms (e.g. reducing land premiums across the site as a whole). We trust the Government will revisit this issue and resolve it as a matter of priority within the next few days.

- PCG is required to make a capital commitment to the project but this does not need to be in the form of cash equity – particularly as too much cash injection would be idle for excessive periods of time. PCG would not accept a cash equity arrangement nor a performance bond. However, capital commitment would be acceptable to PCG on one condition – that PCG had flexibility to decide how we meet that commitment.
- the concept of relative equity between the Government and PCG is problematic. We realize your desire is to peg the equity shares to the relative land premium forgone by the Government and the capital commitment made by PCG. This is complicated by the fact that the land premium is not yet settled and the amount of land premium directly affects both the capital commitment and the project risk. We suggested that there were other ways in which the commercial arrangements might be structured – for example, the concept of a profit sharing scheme modelled after MTRC station developments.
- subsequent to the meeting, you suggested to Richard by phone that a Cyber-Port Management Fund could be setup to maintain and upgrade the facility and environment of the Cyber-Port on an on-going basis. The funding could be in the tune of US\$1.8 million contributed by both sides every three years starting from the third anniversary of the completion of the Cyber-Port. We would be prepared to consider this proposal.

Regarding the process to resolve these issues, we agreed that we need to settle them before Wednesday next week. We should find time to discuss on Monday, 22nd February through to Wednesday 24th February aiming at producing a Heads of Agreement Document. We are willing to commit PCG's resources to this endeavor because we believe that the Cyber-Port is intrinsically the right thing to do for Hong Kong. We think our meeting last Wednesday was a helpful step forward.

Yours sincerely,

Gus.
Chui Kam