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February 23, 2007

Honorable Chan Kam-lam, SBS, JP
Chairman
Panel on Financial Affairs
Legislative Council
Hong Kong Special Administrative Region of the People's Republic of China
Legislative Council Building
8 Jackson Road
Central, Hong Kong

Dear Honorable Mr Chan,

Re: Octopus EPS Add-Value Transactions Incident and Measures Being Taken to Rectify the Situation

Thank you for inviting Octopus Cards Limited ('OCL') to present our thoughts on the subject issue and to discuss this matter with you and the members of your Panel on March 2, 2007. We welcome the opportunity to share background on the matter of the failed Octopus EPS add-value transactions and the actions that are being taken to identify the cause of this problem and to do whatever is required to make certain that these problems are not repeated. This is a matter of the highest priority to our Board of Directors, our management, and our employees.

The success of the Octopus card system has been based on the fact that we have not only made life more convenient for the people of Hong Kong and visitors to our city, but we have also earned the full confidence and trust of the millions of people who have used our system since we were launched in 1997. This trust and confidence is a responsibility we take very seriously and our corporate goal is to "make everyday life easier" for our customers.

We are aware that the recent incidents associated with the failed Octopus EPS add-value transactions raise certain questions about the operation of the technology associated with those transactions and this is something we have been working with EPS and others to address but, in the meantime, we have suspended that system and no further problems have taken place.

I want to assure the millions of our card holders that the Octopus system remains unaffected and they can continue to use it with the full confidence that has made us an integral part of daily life in Hong Kong.

As you may be aware, there are some 14.7 million Octopus cards in circulation. We currently have approximately 10 million daily average transactions totaling approximately HK\$80 million in value. On any given day, there are approximately 570,000 add-value transactions with some 500,000 of those transactions carried out using cash and some 60,000 done using our automatic add-value service (AAVS). An average 8,900 of the daily add-value transactions are done through the 324 Octopus EPS add-value machines located at MTR and KCR stations, car parks, and shopping malls throughout Hong Kong. Octopus EPS add-value transactions represent an average of 1.5% of total daily add-value transactions and their HK\$2.1 million in value equates to approximately 2.9% of the total value of daily add-value transactions.

We are providing this background information to demonstrate that, while we are working hard to address the source of the problem linked to the Octopus EPS add-value system, the rest of the Octopus system is operating as it was designed to do and we have full confidence in its integrity.

When we first became aware of the customer complaint regarding the failed transactions at the MTR station at Diamond Hill, we commenced investigation with EPS and then asked MTR and KCR to suspend the Octopus EPS service on all add-value machines in their stations (effective by 10.30pm February 3, 2007). We confined the suspension to these machines because the Octopus EPS add-value machines at car parks and shopping malls operate using a different network and hardware equipment and we believed, at the time, that the problems were caused by an EPS system upgrade that took effect on December 5, 2006 and that upgrade was only done to the system serving the machines in the MTR and KCR stations.

At the same time, we sought to identify the technological aspects of this problem, working with EPS, we also carried out a review of the estimated 500,000 Octopus EPS add-value transactions that had taken place during the period between December 5, 2006 and February 3, 2007. As we announced on February 9, 2007, we subsequently identified 571 cases where EPS accounts were charged and no Octopus card was credited. In each of these cases, no reversal message was received by the EPS host even though the transaction failed after the customer's bank account had been debited. Since the type of error quoted by the complainant had not been reported prior to the system upgrade this was the basis of our decision to focus on transactions taking place from the time of the upgrade.

We then took immediate steps to identify the source of this problem and to also determine how many of our customers were affected. The investigation of the technical aspects of the problem involves multiple parties, including our firm, EPSCO, MTR, KCR, the modem and network provider and the EPS terminal suppliers. While we viewed the system upgrade of the EPS system as the cause of the problem, at this time the investigation continues. As we have informed the Hong Kong Monetary Authority (HKMA), identifying the cause of this problem and prescribing solutions

will be important elements of the scope of work of the international management consultant that will be appointed very soon by OCL, with the approval of the HKMA, to carry out an independent review on the operation of the add-value services through EPS as well as OCL's operational risk control environment.

As we committed on February 9, 2007, refunds to all 571 affected customers were completed by February 14, 2007.

As was stated in the HKMA press release of February 16, 2007, the specific problem related to the absence of a reversal message back to the EPS host was believed to have begun with the system upgrade of the communication network that links the EPS host to the add-value machines. We are aware, however, that there have been some other instances in the past where failed Octopus EPS add-value transactions have occurred, and where refunds have not been claimed by customers for some of those failed transactions. While the magnitude of the problem is limited, determining the number of transactions, the customers affected, and the technical reasons associated with these earlier failed add-value transactions is something to which we have assigned the highest priority and it will be the key item in the scope of work of the international management consultant.

It is important to note that OCL has always had an open and responsive policy regarding customer refunds – a policy emphasizing a commitment to respond promptly and professionally to any request for refund. This policy has been purposely reactive given the fact that about 90% of our customers are anonymous. However, we will ask the international management consultant to assist in refining our policies to support the refund process, to examine actions we could take operationally and technically, and to make recommendations to rectify the issues so as to avoid similar problems in the future.

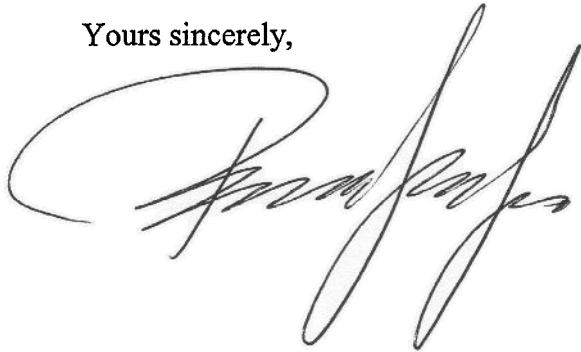
As soon as we have this information we will provide full disclosure to the public and we will act according to the recommendations of the independent review, under the guidance of the Independent Advisor, Professor Andrew Chan Chi-fai, who has been appointed by the HKMA.

After discussion with the HKMA, it was determined that since failed Octopus EPS add-value transactions may not have been confined to the Octopus EPS add-value system serving the MTR and KCR stations, it would be prudent to extend the suspension of the system to all Octopus EPS add-value machines while an investigation is carried out. That suspension was fully implemented on February 17, 2007 and we are committed to not resuming that service until the investigation to be carried out by the international management consultant has been completed and we are certain that the Octopus EPS add-value system is free of any of the technical issues that caused these problems.

As you may be aware, on February 23, 2007 we published advertisements and informed the media of the availability of alternative methods of adding value to Octopus cards for those customers affected by the Octopus EPS add-value suspension. This was done to keep our customers informed and to promote the other convenient options available to add value to their cards.

Mr. Chairman, I look forward to providing more details regarding this matter and responding to any questions you or members of your Panel may have when we meet on March 2, 2007. I can assure you that we are committed to addressing this matter as quickly and as appropriately as possible. As I said earlier, we fully recognize the responsibility we have to the millions of Hong Kong people and visitors who use our system each and every day.

Yours sincerely,

A handwritten signature in black ink, appearing to be 'Paul Tang', written in a cursive style.