

CHINA UNICOM (HONG KONG) Ltd

Form 20-F

April 25, 2012

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## SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

### FORM 20-F

.. REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR 12(g) OF THE SECURITIES EXCHANGE ACT OF 1934

OR

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
For the fiscal year ended December 31, 2011

OR

.. TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
For the transition period from \_\_\_\_\_ to \_\_\_\_\_

OR

.. SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
Date of event requiring this shell company report \_\_\_\_\_

Commission file number 1-15028

## CHINA UNICOM (HONG KONG) LIMITED

(Exact Name of Registrant as Specified in Its Charter)

N/A

Hong Kong

(Translation of Registrant's Name Into English)

(Jurisdiction of Incorporation or Organization)

75<sup>th</sup> Floor, The Center

99 Queen's Road Central

Hong Kong

(Address of Principal Executive Offices)

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75<sup>th</sup> Floor, The Center

99 Queen's Road Central

Hong Kong

(Name, Telephone, E-mail and/or Facsimile Number and Address of Company Contact person)

Securities registered or to be registered pursuant to Section 12(b) of the Act:

<u>Title of Each Class</u>	<u>Name of Each Exchange On Which Registered</u>
Ordinary shares, par value HK\$0.10 per share	The New York Stock Exchange, Inc.*

\* Not for trading, but only in connection with the listing on The New York Stock Exchange, Inc. of American depository shares, or ADSs, each representing 10 ordinary shares.

Securities registered or to be registered pursuant to Section 12(g) of the Act:

None

(Title of class)

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act:

None

(Title of Class)

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the annual report.

As of December 31, 2011, 23,564,901,919 ordinary shares were issued and outstanding.

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934. Yes  No

Note: Checking the box above will not relieve any registrant required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 from their obligations under those Sections.

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated Filer  Accelerated Filer  Non-Accelerated Filer

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Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing.

U.S. GAAP

International Financial Reporting Standards as issued by the International Accounting Standards Board

Other

If  Other has been checked in response to the previous question, indicate by check mark which financial statement item the registrant has elected to follow.

Item 17  Item 18

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

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**Note Regarding Forward-Looking Statements**

This annual report contains certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Such forward-looking statements may include, without limitation, statements relating to (i) our plans and strategies, including those in connection with our restructuring and integration after our merger with China Netcom Group Corporation (Hong Kong) Limited, or China Netcom, mergers and acquisitions and capital expenditures; (ii) our plans for network expansion, including those in connection with the build-out of third generation mobile telecommunications, or 3G, digital cellular business and network infrastructure; (iii) our competitive position, including our ability to upgrade and expand existing networks and increase network efficiency, to improve existing services and offer new services, to develop new technological applications and to leverage our position as an integrated telecommunications operator and expand into new businesses and markets; (iv) our future business condition, including our future financial results, cash flows, financing plans and dividends; (v) the future growth of market demand of, and opportunities for, our new and existing products and services, in particular, 3G services; and (vi) future regulatory and other developments in the PRC telecommunications industry.

The words anticipate, believe, could, estimate, intend, may, seek, will and similar expressions, as they relate to us, are intended to describe certain of these forward-looking statements. We do not intend to update any of these forward-looking statements.

The forward-looking statements contained in this annual report are, by their nature, subject to significant risks and uncertainties. In addition, these forward-looking statements reflect our current views with respect to future events and are not a guarantee of our future performance. Actual results may differ materially from those expressed or implied in the forward-looking statements as a result of a number of factors, including, without limitation:

changes in the regulatory regime and policies for the PRC telecommunications industry, including without limitation changes in the regulatory policies of the Ministry of Industry and Information Technology, or the MIIT (which has assumed the regulatory functions of the former Ministry of Information Industry), the State-owned Assets Supervision and Administration Commission, or the SASAC, and other relevant government authorities of the PRC;

changes in the PRC telecommunications industry resulting from the issuance of 3G licenses by the central government of the PRC;

effects of tariff reduction and other policy initiatives from the relevant PRC government authorities;

changes in telecommunications and related technologies and applications based on such technologies;

the level of demand for telecommunications services, in particular, 3G services;

competitive forces from more liberalized markets and our ability to retain market share in the face of competition from existing telecommunications companies and potential new market entrants;

effects of competition on the demand and price of our telecommunications services;

the availability, terms and deployment of capital and the impact of regulatory and competitive developments on capital outlays;

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the result of the anti-monopoly investigation by the National Development and Reform Commission of the PRC, or the NDRC, relating to the price charged for Internet dedicated leased line access service provided by us to Internet service providers;

changes in the assumptions upon which we have prepared our projected financial information and capital expenditure plans;  
and

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changes in the political, economic, legal and social conditions in China, including the PRC Government's policies and initiatives with respect to economic development in light of the recent global economic downturn, foreign exchange policies, foreign investment activities and policies, entry by foreign companies into the PRC telecommunications market and structural changes in the PRC telecommunications industry.

Please also see D. Risk Factors under Item 3.

**Certain Definitions**

As used in this annual report, references to we, us, our, the Company, our company and Unicom are to China Unicom (Hong Kong) (formerly known as China Unicom Limited). Unless the context otherwise requires, these references include all of our subsidiaries. In respect of any time prior to our incorporation, references to we, us, our and Unicom are to the telecommunications businesses in which our predecessors were engaged and which were subsequently assumed by us. All references to Unicom Group are to China United Network Communications Group Company Limited (formerly known as China United Telecommunications Corporation), our indirect controlling shareholder. Unless the context otherwise requires, these references include all of Unicom Group's subsidiaries, including us and our subsidiaries.

All references to China Netcom are to China Netcom Group Corporation (Hong Kong) Limited, which merged with us in October 2008, and, as the context may require, its subsidiaries. References to Netcom Group mean China Network Communications Group Corporation, which merged with, and was absorbed by, Unicom Group in January 2009 and, as the context may require, its subsidiaries, other than us and our subsidiaries.

As used in this annual report:

references to China or PRC mean the People's Republic of China, excluding, for purposes of this annual report, Hong Kong, Macau and Taiwan, and references to the central government or the PRC Government mean the central government of the PRC;

references to our fixed-line northern service region mean the 10 municipalities, provinces and region where we operate fixed-line business in northern China, consisting of Beijing and Tianjin Municipalities, and Hebei, Henan, Shandong, Liaoning, Heilongjiang, Jilin, and Shanxi Provinces, and the Inner Mongolia Autonomous Region;

references to the 21 provinces in southern China mean Shanghai Municipality, Jiangsu Province, Zhejiang Province, Anhui Province, Fujian Province, Jiangxi Province, Hubei Province, Hunan Province, Guangdong Province, Guangxi Zhuang Autonomous Region, Hainan Province, Chongqing Municipality, Sichuan Province, Guizhou Province, Yunnan Province, Tibet Autonomous Region, Shaanxi Province, Gansu Province, Qinghai Province, Ningxia Hui Autonomous Region and Xinjiang Uygur Autonomous Region; we completed the acquisitions of certain telecommunications business and assets, including the fixed-line business in those 21 provinces in southern China, from Unicom Group and Netcom Group and/or their respective subsidiaries and branches in January 2009; see A. History and Development of the Company Unicom Acquisitions and Sales Acquisitions of Fixed-Line Business in 21 Provinces in Southern China and Other Assets from Parent Companies and Lease of Telecommunications Networks in 21 Provinces in Southern China under Item 4;

references to Hong Kong Stock Exchange or HKSE mean The Stock Exchange of Hong Kong Limited, and references to NYSE or New York Stock Exchange mean The New York Stock Exchange, Inc; and

references to Renminbi or RMB are to the currency of the PRC, references to U.S. dollars or US\$ are to the currency of the United States of America, references to HK dollars or HK\$ are to the currency of the Hong Kong Special Administrative Region of the PRC and references to Euro are to the currency of the eurozone (17 of the 27 member states of the European Union).



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Not Applicable.

**Item 2. Offer Statistics and Expected Timetable**

Not Applicable.

**Item 3. Key Information****A. Selected Financial Data**

The following tables present selected historical financial data of our company as of and for the years ended December 31, 2007, 2008, 2009, 2010 and 2011. Except for amounts presented in U.S. dollars, the selected historical consolidated income statement data for the years ended December 31, 2009, 2010 and 2011 and the selected historical consolidated balance sheet data as of December 31, 2010 and 2011 set forth below are derived from, should be read in conjunction with, and are qualified in their entirety by reference to, our audited consolidated financial statements, including the related notes, included elsewhere in this annual report on Form 20-F. The selected historical consolidated income statement data for the years ended December 31, 2007 and 2008 and consolidated balance sheet data as of December 31, 2007, 2008 and 2009 set forth below are derived from our internal records and management accounts that are not included in this annual report on Form 20-F. Our consolidated financial statements as of and for the years ended December 31, 2007, 2008, 2009, 2010 and 2011 have been prepared and presented in accordance with IFRS/HKFRS. The statistical information set forth in this annual report on Form 20-F relating to China is taken or derived from various publicly available government publications that have not been prepared or independently verified by us. This statistical information may not be consistent with other statistical information from other sources within or outside China.

We completed (i) the acquisition of the entire equity interest in China Unicom NewSpace Limited, or Unicom NewSpace, by China Unicom Broadband Online Limited Corporation, or Broadband Online, a wholly-owned subsidiary of China United Network Communications Corporation Limited, or CUCL, from Unicom Group, or the 2011 Acquisition, in December 2011, (ii) the acquisitions of fixed-line business in 21 provinces in southern China, the local access telephone business in Tianjin Municipality, three subsidiaries (together referred to as the Target Business ) and certain other telecommunications assets from Unicom Group and Netcom Group (which was later merged with Unicom Group in January 2009), or the 2009 Acquisition, in January 2009, (iii) a merger with China Netcom in October 2008, and (iv) the acquisition of assets and business of the Guizhou Province branch of Unicom Group, or Unicom Guizhou, from Unicom Group in December 2007, or the 2007 Acquisition. Prior to its merger with us, China Netcom completed an acquisition of the entire equity interest of Beijing Planning and Design Institute, or Design Institute, a wholly-owned subsidiary of Netcom Group, in December 2007. See A. History and Development of the Company Unicom Acquisitions and Sales 2011 Acquisition , A. History and Development of the Company Unicom Acquisitions and Sales Acquisitions of Fixed-Line Business in 21 Provinces in Southern China and Other Assets from Parent Companies and Lease of Telecommunications Networks in 21 Provinces in Southern China , A. History and Development of the Company Sale of CDMA Business, Merger with China Netcom and Related Transactions Merger with China Netcom and Related Transactions , A. History and Development of the Company Unicom Acquisitions and Sales and A. History and Development of the Company History and Corporate Development of China Netcom under Item 4, respectively. Because (i) we and Unicom NewSpace were under common control of Unicom Group both prior to and after the 2011 Acquisition, (ii) we and the Target Business were under common control of Unicom Group both prior to and after the 2009 Acquisition, (iii) we and China Netcom were under the common control of the PRC Government both prior to and after the merger, (iv) we and Unicom Guizhou were under the common control of Unicom Group both prior to and after our acquisition of Unicom Guizhou and (v) China Netcom and Design Institute were under the common control of Netcom Group (which merged with, and was absorbed by, Unicom Group in January 2009) both prior to and after China Netcom's acquisition of Design Institute, each of the acquisitions and the merger is considered as a business combination of entities and businesses under common control and has been accounted for using merger accounting in accordance with Accounting Guideline 5 Merger accounting for common control combinations , or AG 5, issued by the HKICPA in November 2005. Upon our adoption of IFRS, we adopted the accounting policy to account for business combination of entities and businesses under common control using the predecessor values method, which is consistent with HKFRS. Given that the acquired entities and businesses mentioned above in this paragraph had always been under common control during all the periods presented, the assets and liabilities thereof are stated at predecessor values and are included in the consolidated financial statements included in this annual report on Form 20-F as if these entities and their

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businesses acquired had always been part of our company during all the periods presented. As a result, the selected consolidated financial statements data as of and for the years ended December 31, 2007, 2008, 2009 and 2010 was restated to reflect the 2011 Acquisition.

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The adoption of amended IFRS/HKFRS 1 in 2011 resulted in a change in accounting policy for property, plant and equipment, which has been applied retrospectively so that the comparative data presented in the selected consolidated financial statements data as of and for the years ended December 31, 2007, 2008, 2009 and 2010 have been restated to conform to the changed policy. A detailed description is set forth in Note 2.2(d) to our consolidated financial statements included elsewhere in this annual report on Form 20-F.

We completed the disposal of our CDMA business in October 2008. See A. History and Development of the Company Sale of CDMA Business, Merger with China Netcom and Related Transactions Disposal of CDMA Business and Related Transactions under Item 4. In accordance with IFRS/HKFRS 5, Non-Current Assets Held for Sale and Discontinued Operations, we recognized the CDMA business as discontinued operations and the CDMA business was presented separately as discontinued operations in our audited consolidated statements of income and statements of cash flows for the years ended December 31, 2007 and 2008.

Prior to our merger with China Netcom, China Netcom completed the disposal of the fixed-line telecommunications and related services in its Guangdong and Shanghai branches in February 2007. See A. History and Development of the Company History and Corporate Development of China Netcom under Item 4. After considering that we reacquired the fixed-line business in Guangdong and Shanghai branches in January 2009, we did not present the fixed-line business in Guangdong and Shanghai branches as discontinued operations and derecognized the gain on disposal previously recorded in our 2007 consolidated financial statements.

	As of or for the year ended December 31					
	2007 (Restated) <sup>(1)</sup> RMB	2008 (Restated) <sup>(1)</sup> RMB	2009 (Restated) <sup>(1)</sup> RMB	2010 (Restated) <sup>(1)</sup> RMB	2011 RMB	2011 US\$ <sup>(2)</sup>
(in millions, except for per share data)						
<b>Consolidated Income Statement Data:</b>						
<b>CONTINUING OPERATIONS</b>						
<b>Revenue<sup>(3)</sup></b>						
<b>Mobile business</b>						
Service revenue	62,476	64,674	70,102	82,449	103,307	16,414
Sales of mobile telecommunications products	14	532	1,970	7,173	23,219	3,689
<b>Total mobile telecommunications revenue</b>	<b>62,490</b>	<b>65,206</b>	<b>72,072</b>	<b>89,622</b>	<b>126,526</b>	<b>20,103</b>
<b>Fixed-line business</b>						
Service revenue <sup>(3)</sup>	95,875	92,593	81,160	79,942	81,642	12,971
Sales of fixed-line telecommunications products	980	1,362	193	114	63	10
<b>Total fixed-line telecommunications revenue</b>	<b>96,855</b>	<b>93,955</b>	<b>81,353</b>	<b>80,056</b>	<b>81,705</b>	<b>12,981</b>
<b>Unallocated amounts</b>						
Service revenue <sup>(3)</sup>	648	701	601	1,692	936	149
Sales of other telecommunications products	-	5	-	-	-	-
	648	706	601	1,692	936	149
<b>Total revenue</b>	<b>159,993</b>	<b>159,867</b>	<b>154,026</b>	<b>171,370</b>	<b>209,167</b>	<b>33,233</b>
<b>Total costs, expenses and others</b>	<b>(137,088)</b>	<b>(156,444)</b>	<b>(141,870)</b>	<b>(166,786)</b>	<b>(203,569)</b>	<b>(32,344)</b>
<b>Income from continuing operations before income tax</b>	<b>22,905</b>	<b>3,423</b>	<b>12,156</b>	<b>4,584</b>	<b>5,598</b>	<b>889</b>
Income tax expenses	(6,988)	(1,664)	(2,692)	(883)	(1,371)	(217)

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Income from continuing operations	15,917	1,759	9,464	3,701	4,227	672
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	As of or for the year ended December 31					
	2007 (Restated) <sup>(1)</sup> RMB	2008 (Restated) <sup>(1)</sup> RMB	2009 (Restated) <sup>(1)</sup> RMB	2010 (Restated) <sup>(1)</sup> RMB	2011 RMB	2011 US\$ <sup>(2)</sup>
(in millions, except for per share data)						
<b>DISCONTINUED OPERATIONS<sup>(4)</sup></b>						
Income from discontinued operations	656	1,438	-	-	-	-
Gain on disposal of discontinued operations	-	26,135	-	-	-	-
Sub-total for discontinued operation	656	27,573	-	-	-	-
<b>Net income</b>	<b>16,573</b>	<b>29,332</b>	<b>9,464</b>	<b>3,701</b>	<b>4,227</b>	<b>672</b>
<b>Earnings per share for income attributable to owners of the parent during the year</b>						
-Basic earnings per share <sup>(5)</sup>	0.72	1.23	0.40	0.16	0.18	0.03
-Diluted earnings per share <sup>(5)</sup>	0.71	1.23	0.40	0.16	0.18	0.03
-Basic earnings per ADS <sup>(6)</sup>	7.18	12.35	3.98	1.57	1.79	0.29
-Diluted earnings per ADS <sup>(6)</sup>	7.11	12.25	3.96	1.56	1.78	0.28
<b>Earnings per share for income from continuing operations attributable to owners of the parent during the year</b>						
-Basic earnings per share <sup>(5)</sup>	0.69	0.07	0.40	0.16	0.18	0.03
-Diluted earnings per share <sup>(5)</sup>	0.68	0.07	0.40	0.16	0.18	0.03
-Basic earnings per ADS <sup>(6)</sup>	6.90	0.74	3.98	1.57	1.79	0.29
-Diluted earnings per ADS <sup>(6)</sup>	6.83	0.73	3.96	1.56	1.78	0.28
<b>Earnings per share for income from discontinued operations attributable to owners of the parent during the year</b>						
-Basic earnings per share <sup>(5)</sup>	0.03	1.16	-	-	-	-
-Diluted earnings per share <sup>(5)</sup>	0.03	1.15	-	-	-	-
-Basic earnings per ADS <sup>(6)</sup>	0.28	11.61	-	-	-	-
-Diluted earnings per ADS <sup>(6)</sup>	0.28	11.52	-	-	-	-
-Number of shares outstanding for basic earnings per share <sup>(5)</sup>	23,075	23,751	23,767	23,562	23,564	23,564
-Number of shares outstanding for diluted earnings per share <sup>(5)</sup>	23,321	23,941	23,895	23,704	23,785	23,785
-Number of ADS outstanding for basic earnings per ADS <sup>(6)</sup>	2,308	2,375	2,377	2,356	2,356	2,356
-Number of ADS outstanding for diluted earnings per ADS <sup>(6)</sup>	2,332	2,394	2,389	2,370	2,379	2,379
<b>Consolidated Balance Sheet Data:</b>						
<b>Assets</b>						
Cash and cash equivalents and short-term bank deposits	13,582	10,652	8,891	22,870	15,410	2,448
Property, plant and equipment	307,071	315,526	350,976	365,654	381,859	60,671
Inventories and consumables	2,816	1,147	2,412	3,728	4,651	739
Prepayments and other current assets	5,181	2,876	4,253	5,115	6,127	973
Financial assets at fair value through other comprehensive income	287	95	7,977	6,214	6,951	1,104
Proceeds receivable for the disposal of the CDMA business	-	13,140	5,121	-	-	-
<b>Total assets</b>	<b>369,000</b>	<b>380,438</b>	<b>417,008</b>	<b>441,269</b>	<b>456,233</b>	<b>72,488</b>
<b>Liabilities</b>						
Accounts payable and accrued liabilities	61,376	73,933	104,096	97,666	95,252	15,134
Long-term loans due to ultimate holding company	27,213	35,652	-	-	-	-
Payables in relation to the disposal of the CDMA business	-	4,232	7	-	-	-
Short-term bank loans	11,850	10,780	63,909	36,727	32,322	5,135
Commercial papers	20,000	10,000	-	23,000	38,000	6,038
Current portion of long-term bank loans	7,413	1,216	62	58	50	8
Current portion of other obligations	3,381	3,012	2,534	2,637	2,586	411
Long-term bank loans	16,086	997	759	1,462	1,384	220

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Promissory notes	-	-	-	15,000	15,000	2,383
Convertible bonds	-	-	-	11,558	11,118	1,766
Corporate bonds	2,000	7,000	7,000	7,000	7,000	1,112
Tax payable	5,091	11,370	908	1,483	1,232	196
<b>Total liabilities</b>	<b>195,177</b>	<b>183,143</b>	<b>210,571</b>	<b>235,608</b>	<b>250,335</b>	<b>39,774</b>
<b>Shareholders equity</b>	<b>173,823</b>	<b>197,295</b>	<b>206,437</b>	<b>205,661</b>	<b>205,898</b>	<b>32,714</b>
Share capital	1,437	2,329	2,310	2,310	2,311	367

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	As of or for the year ended December 31					
	2007 (Restated) <sup>(1)</sup> RMB	2008 (Restated) <sup>(1)</sup> RMB	2009 (Restated) <sup>(1)</sup> RMB	2010 (Restated) <sup>(1)</sup> RMB	2011 RMB	2011 US\$ <sup>(2)</sup>
(in millions, except for per share data)						
<b>Other Financial Data:</b>						
<b>CONTINUING OPERATIONS</b>						
Net cash inflow from operating activities of continuing operations	68,855	57,296	57,732	66,376	66,491	10,565
Net cash outflow from investing activities of continuing operations	(54,749)	(61,030)	(85,310)	(76,619)	(82,970)	(13,183)
Net cash (outflow)/inflow from financing activities of continuing operations	(22,834)	(28,786)	30,197	19,824	8,988	1,428
<b>Net cash (outflow)/inflow from continuing operations</b>	<b>(8,728)</b>	<b>(32,520)</b>	<b>2,619</b>	<b>9,581</b>	<b>(7,491)</b>	<b>(1,190)</b>
<b>DISCONTINUED OPERATIONS<sup>(4)</sup></b>						
Net cash inflow from operating activities of discontinued operations	837	656	-	-	-	-
Net cash (outflow)/inflow from investing activities of discontinued operations <sup>(7)</sup>	(25)	29,489	(5,039)	5,121	-	-
Net cash outflow from financing activities of discontinued operations	-	-	-	-	-	-
<b>Net cash inflow/(outflow) from discontinued operations</b>	<b>812</b>	<b>30,145</b>	<b>(5,039)</b>	<b>5,121</b>	<b>-</b>	<b>-</b>
<b>Net (decrease)/increase in cash and cash equivalents</b>	<b>(7,916)</b>	<b>(2,375)</b>	<b>(2,420)</b>	<b>14,702</b>	<b>(7,491)</b>	<b>(1,190)</b>
<b>Dividend declared per share</b>	<b>0.20</b>	<b>0.20</b>	<b>0.16</b>	<b>0.08</b>	<b>0.10</b>	<b>0.02</b>

(1) The comparative financial data prior to January 1, 2011 presented herein was restated to reflect the effects of 2011 Acquisition and the change in accounting policy for property, plant and equipment upon the adoption of amended IFRS/HKFRS 1 in 2011. See Note 2.2 to our consolidated financial statements included elsewhere in this annual report on Form 20-F.

(2) The translation of RMB into U.S. dollars has been made at the rate of RMB6.2939 to US\$1.00, representing the exchange rate as set forth in the H.10 statistical release of the Federal Reserve Board on December 30, 2011. The translations are solely for the convenience of the reader.

(3) Includes fixed-line upfront connection fees for basic telephone access services that were eliminated by order of the former Ministry of Information Industry in July 2001.

(4) Results of our CDMA business have been disclosed as discontinued operations for the years ended December 31, 2007 and 2008.

(5) See Note 38 to our consolidated financial statements included elsewhere in this annual report on Form 20-F on how basic and diluted earnings per share are calculated under IFRS/HKFRS.

(6) Earnings per ADS is calculated by multiplying earnings per share by 10, which is the number of shares represented by each ADS.

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<sup>(7)</sup> See Note b of the consolidated statement of cash flows to our consolidated financial statements included elsewhere in this annual report on Form 20-F on the cash flows from discontinued operations in 2009 and 2010.

### **Exchange Rate Information**

We publish our consolidated financial statements in Renminbi. Solely for the convenience of the reader, this annual report on Form 20-F contains translations of certain Renminbi and Hong Kong dollar amounts into U.S. dollars at specific rates. Prior to January 1, 2009, the exchange rate refers to the noon buying rates in New York City for cable transfers as certified for customs purposes by the Federal Reserve Bank of New York, or the noon buying rate. For January 1, 2009 and all later dates and periods, the exchange rate refers to the exchange rate as set forth in the H.10 statistical release of the Federal Reserve Board, or the daily exchange rate. Unless otherwise indicated, conversions of Renminbi or Hong Kong dollars into U.S. dollars in this annual report are based on the exchange rate on December 30, 2011 (RMB6.2939 to US\$1.00 and HK\$7.7663 to US\$1.00). These translations should not be construed as representations that the Renminbi or Hong Kong dollar amounts could actually be converted into U.S. dollars at such rates or at all.



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The daily exchange rates were RMB6.3080 = US\$1.00 and HK\$7.7607 = US\$1.00, respectively, on April 20, 2012. The following table sets forth the high and low daily exchange rates between Renminbi and U.S. dollars and between Hong Kong dollars and U.S. dollars for each month during the previous six months:

**Exchange Rate**

	RMB per US\$1.00		HK\$ per US\$1.00	
	High	Low	High	Low
October 2011	6.3825	6.3534	7.7884	7.7634
November 2011	6.3839	6.3400	7.7957	7.7679
December 2011	6.3733	6.2939	7.7851	7.7663
January 2012	6.3330	6.2940	7.7674	7.7538
February 2012	6.3120	6.2935	7.7559	7.7532
March 2012	6.3315	6.2975	7.7678	7.7551
April 2012 (up to April 20, 2012)	6.3150	6.2975	7.7660	7.7580

The following table sets forth the average exchange rates between Renminbi and U.S. dollars and between Hong Kong dollars and U.S. dollars for each of 2007, 2008, 2009, 2010 and 2011, calculated by averaging, in the case of 2007 and 2008, the noon buying rates, or in the case of 2009 to 2011, the daily exchange rate, on the last day of each month during the relevant years.

**Average Exchange Rate**

	RMB per US\$1.00	HK\$ per US\$1.00
2007	7.5806	7.8008
2008	6.9193	7.7814
2009	6.8295	7.7513
2010	6.7603	7.7692
2011	6.4475	7.7793

**B. Capitalization and Indebtedness**

Not Applicable.

**C. Reasons for the Offer and Use of Proceeds**

Not Applicable.

**D. Risk Factors****Risks Relating to Our Business**

*We face intense competition in all our businesses from other telecommunications service providers, including China Mobile and China Telecom, which may materially adversely affect our financial condition, results of operations and growth prospects.*

The telecommunications industry in China has been rapidly evolving. Following the restructuring of the PRC telecommunications industry in 2008, we, along with China Mobile and China Telecom, have become full-service telecommunications service providers that operate both fixed-line and mobile telecommunications networks in China. See A. History and Development of the Company Restructurings of the Telecommunications Industry under Item 4. We face intense competition in each of our business lines from China Mobile and China Telecom

and expect that this competition will further intensify and may also include other telecommunications service providers in the future.

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For mobile business, China Mobile is the largest mobile operator in China, while China Telecom has become a new competitor after acquiring our CDMA business in the 2008 industry restructuring. In the emerging 3G mobile market, we face intense competition from the other two operators. For fixed-line business, we are a leading fixed-line operator in northern China, but remain relatively small in southern China, where China Telecom has a dominant market position. We also face increasing competition from competitors outside the telecommunications industry, such as cable television companies for fixed-line broadband business. Furthermore, the PRC Government is in the process of initiating new policies, in particular, the policies regarding the convergence of television broadcast, telecommunications and Internet access networks and the policies that would allow mobile subscribers to switch to the networks of another telecommunications operator with their existing numbers in certain areas in China. Although these new initiatives may present opportunities for us to attract new users, they also pose additional uncertainties to the competition in mobile business in China, and we cannot assure you that our business will not be adversely affected by such initiatives.

Intensive competition from China Mobile and China Telecom, as well as other telecommunications service providers, could lead to slower subscriber growth, lower traffic volume of our telecommunications services, continued price pressure and higher customer acquisition costs, which may materially adversely affect our financial condition, results of operations and growth prospects.

***We may continue to lose subscribers, in particular, fixed-line services subscribers, which may materially adversely affect our financial condition, results of operations and growth prospects.***

We continue to lose fixed-line services subscribers due to the trend of mobile service substitution for fixed-line services. Consistent with trends in global markets in recent years, significant traffic from our fixed-line networks has been diverted to mobile networks, including mobile networks of other mobile operators. While we have been taking various measures to retain our fixed-line subscribers, we cannot assure you that we will be successful in mitigating the adverse impact of mobile service substitution for fixed-line telephone services. Although we have experienced net increases in the total number of mobile subscribers in recent years, we may experience loss of mobile subscribers, especially GSM mobile subscribers, in the future due to intensified competition from other mobile operators and increased migration of GSM mobile subscribers to 3G networks. If we lose a significant number of fixed-line and mobile subscribers, our relevant market share may be materially and adversely affected and our costs of additional customer acquisitions and bad debts may increase, which would materially adversely affect our financial condition, results of operations and growth prospects.

***Competition from foreign-invested operators and other new entrants may further increase the competition for employees, exacerbate price competition and increase our operating expenses, thereby adversely affecting our financial condition, results of operations and growth prospects.***

As a result of China's accession to the World Trade Organization, or WTO, in December 2001 and the adoption of the Regulations on the Administration of Foreign-Invested Telecommunications Enterprises in January 2002, which implement China's commitments to the WTO, the PRC Government has agreed to gradually liberalize the various segments and regions of the telecommunications market in China to foreign investors. Currently, foreign investors are permitted to own up to 49% of joint ventures that offer basic telecommunications services without any geographic restrictions in China and up to 50% of joint ventures that offer value-added telecommunications services without any geographic restrictions in China. More foreign-invested operators may enter China's telecommunications market as a result of this liberalization. They may have greater financial, managerial and technical resources and more expertise in network management and sales and marketing than we do.

Increased competition from these and other new entrants into the Chinese telecommunications market may further increase the competition for skilled and experienced employees, exacerbate price competition and increase our customer acquisition costs and other operating expenses, and thereby adversely affect our financial condition, results of operations and growth prospects.

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***Failure to respond to technological and industry developments in a timely and effective manner or failure to continually optimize, expand and upgrade our networks and infrastructure could materially adversely affect our competitive position and hinder our growth.***

The telecommunications industry in China and elsewhere in the world has been experiencing rapid and significant changes in the diversity and sophistication of the technologies and services offered. Such changes may render our existing services or technologies inadequate or obsolete. As a result, we expect that we will need to constantly upgrade our telecommunications technologies and services to respond to such changes in order to maintain our competitiveness, which typically involves substantial time, costs and risk. We cannot assure you that we will be able to respond to technological and industry developments in a timely and cost-effective manner, or at all. Our inability to respond successfully to technological or industry developments may adversely affect our financial condition, results of operations and growth prospects. Furthermore, if the new technologies adopted by us do not perform as expected, or if we are unable to effectively deliver new services based on these technologies in a commercially viable manner, our revenue growth may decline and our competitive position may be adversely affected.

In addition, the growth of our business, particularly the mobile business, depends on whether we are able to continue to optimize the capacity, expand the coverage and improve the quality of, and upgrade our existing networks and infrastructure in a timely and effective manner. Our failure to do so could result in loss of our customers and thus materially adversely affect our competitive position and hinder our growth.

Our ability to expand and upgrade our networks and infrastructure is subject to a number of uncertainties, including our ability to achieve the following on a timely basis and on acceptable terms:

manage technology migration in an effective manner, including effectively responding to a shortage of available Internet Protocol version 4 addresses and timely developing 3GPP Long Term Evolution, or LTE, or other fourth generation mobile telecommunications technologies;

obtain adequate financing;

obtain relevant government licenses, permits and approvals;

obtain adequate network equipment and software;

retain experienced management and technical personnel;

obtain sufficient spectrum frequencies, network numbers and other telecommunications resources controlled by the PRC Government;

gain access to the sites for network construction or upgrade; and

enter into interconnection and other arrangements with other operators.

If we are not able to timely and effectively overcome the uncertainties and difficulties we may encounter in expanding and upgrading our networks and infrastructure, our competitive position, financial condition, results of operations and growth prospects may be materially adversely affected.

***The successful development of our 3G business is subject to market demand, consumer acceptance, technological challenges, competition on service fees, handset subsidies and other marketing expenses, other uncertainties, expected benefits from investments in our 3G networks and technology may not be realized and our business may be adversely affected due to the competitive nature between 3G services and 2G mobile business and fixed-line broadband services in the industry.***

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We commercially launched our 3G service in October 2009 and we are still making investments in our 3G networks. As is common with undertakings of this scale and complexity, we may experience various difficulties in the development of our 3G business, including software, network, handset and other technical issues. While we generally believe we are capable of solving these issues, we cannot assure you that we will be able to do so in a timely fashion or that we will not encounter other difficulties. Moreover, we cannot assure you that:

we will be able to gain access to sufficient sites for 3G network expansion;

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there will be sufficient demand for 3G services;

our 3G services will be more popular among potential subscribers than those of our competitors;

we will not encounter unexpected technological difficulties in implementing the WCDMA technology; or

our 3G services will generate an acceptable or commercially viable rate of return.

Any failure or delay in completing and expanding our 3G networks, any increase in the associated costs (including the costs and expenses that may be incurred as a result of the changes of our marketing and sales policies, including handsets subsidies, to meet the market demand), or any problem encountered in our operations of 3G business could hinder the recovery of our significant capital investment in the 3G business, which could in turn have a material adverse effect on our financial condition, results of operations and growth prospects. For example, 3G handsets subsidy cost was RMB5.79 billion in 2011, representing an increase by 82.6% from RMB3.17 billion in 2010, primarily due to the significant increase in the number of subscribers of our 3G bundled packages, of which we subsidize the handsets, as a result of our efforts in developing 3G business. If our 3G handsets subsidy cost continues to increase without corresponding increase in the relevant service revenue, the profitability of our 3G business would reduce. Furthermore, we expect to spend approximately RMB35.5 billion, representing 35.5% of our capital expenditure in 2012, on 3G network expansion and upgrade, which may significantly increase our depreciation and amortization expenses in future periods, thereby adversely affecting our profitability.

In addition, we expect that 3G services will compete with 2G services and fixed-line broadband as an industry trend in the future. Therefore, while we continue to promote our 3G business, we cannot assure you that our 2G business and fixed-line broadband will not be adversely affected by the industry-wide competition.

***Because we rely on arrangements with other telecommunications operators, changes to the terms or availability of these arrangements may result in disruptions to our services and operations and may result in customer dissatisfaction and materially adversely affect our financial condition, results of operations and growth prospects.***

Our ability to provide telecommunications services depends upon arrangements with other telecommunications operators. In particular, interconnection is necessary to complete all calls between our subscribers and subscribers of other telecommunications operators. We, either through ourselves or through Unicom Group, have established interconnection and transmission line leasing arrangements with other telecommunications operators, including our parent company, as required to conduct our current business. Any disruption to our interconnection with the networks of those operators or other international telecommunications carriers with which we interconnect may affect our operations, service quality and customer satisfaction, thus adversely affecting our business. Furthermore, we are generally not entitled to collect indirect or consequential damages resulting from disruptions in the networks with which we are interconnected. Any disruption in existing interconnection arrangements and leased line arrangements or any significant change of their terms, as a result of natural events or accidents or for regulatory, technical, competitive or other reasons, may lead to temporary service interruptions and increased costs that can seriously jeopardize our operations and adversely affect our financial condition, results of operations and growth prospects. Difficulties in executing alternative arrangements with other operators on a timely basis and on acceptable terms, including the inability to promptly establish additional interconnection links or increase interconnection bandwidths as required, could also materially adversely affect our financial condition, results of operations and growth prospects.

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***Interruptions to our networks and operating systems or to those with which we interconnect, including those caused by natural disaster and service maintenance and upgrades, may disrupt our services and operations and may result in customer dissatisfaction and materially adversely affect our financial condition, results of operations and growth prospects.***

Our network infrastructure and the networks with which we interconnect are vulnerable to potential damages or interruptions from floods, wind, storms, fires, power loss, severed cables, acts of terrorism and similar events. The occurrence of a natural disaster or other unanticipated problems at our facilities or any other failure of our networks or systems, or the networks to which we are interconnected, may result in consequential interruptions in services across our telecommunications infrastructure. For example, in May 2008, an earthquake registering 8.0 on the Richter scale struck Sichuan Province and its neighboring areas in China. In 2010, another major earthquake registering 7.1 on the Richter scale struck Qinghai Province. Our network equipment, including our base stations, in the affected areas sustained extensive damage, leading to service stoppage and other disruptions in our operations in those areas. Any future natural disasters may, among other things, significantly disrupt our ability to adequately staff our business, and may generally disrupt our services and operations. Moreover, our networks and systems and the networks with which we interconnect also require regular maintenance and upgrades. Such maintenance and upgrades may cause service disruptions. Network or system failures, as well as high traffic volumes, may also affect the quality of our services and cause temporary service interruptions. Any such future occurrence may result in customer dissatisfaction and materially adversely affect our financial condition, results of operations and growth prospects.

***If we are unable to fund our capital expenditure and debt service requirements, our financial condition, results of operations and growth prospects will be materially adversely affected.***

We continue to have a significant level of capital expenditure and debt service requirements necessary to implement our business strategies. We plan to spend approximately RMB100 billion for capital expenditure in 2012, which would represent a 30.4% increase compared to the actual capital expenditure in 2011. This is primarily due to expected increases in investments in our 3G and fixed-line broadband network, as well as infrastructure and transmission network. To the extent these capital expenditures exceed our cash resources, we will be required to seek additional debt or equity financing. Our wholly-owned subsidiary, CUCL, completed the issue of two tranches of commercial paper for the year of 2011 in an amount of RMB15 billion and RMB8 billion at an interest rate of 5.23% and 5.78% per annum, respectively, as well as the issue of five tranches of super & short-term commercial paper for the year of 2011 in an amount of RMB8 billion, RMB8 billion, RMB4 billion, RMB4 billion and RMB15 billion at an interest rate of 3.88%, 3.88%, 5.35%, 5.35% and 4.65% per annum, respectively. We cannot assure you that we will be able to obtain future financing on a timely basis and/or on acceptable terms. Even if we obtain such financing, our financing cost may increase significantly as a result of additional financing or higher interest rate. See **Liquidity and Capital Resources** under Item 5. Our failure to do so may adversely affect our financial condition, results of operations and growth prospects. Our ability to obtain acceptable financing at any time may depend on a number of factors, including, among others:

our financial condition and results of operations;

our creditworthiness and relationship with lenders;

changes in credit policies, other government or banking policies that may affect credit markets in China;

conditions of the economy and the telecommunications industry in China;

conditions in relevant financial markets in China and elsewhere in the world; and

our ability to obtain any required government approvals for our financings.

***We may experience further declines in ARPU for our telecommunications services.***

In 2011, the ARPU for our mobile business increased by 8.2% from 2010, primarily because (i) the ARPU for our 3G business is significantly higher than that of our 2G business and (ii) the number of our 3G subscribers has increased as a percentage of the total number of our mobile

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subscribers. However, we have been experiencing declining ARPU for each of our GSM mobile services, 3G mobile services and fixed-lined business, mainly due to (i) the pricing competition with other telecommunications operators in China; (ii) downward adjustments on some of the telecommunications tariffs by the PRC Government (which may continue in the future); (iii) many new subscribers are users with lower usage of telecommunications services; and (iv) the substitution effect of mobile Internet, such as instant mobile communication applications. Our current GSM mobile services, 3G mobile services and fixed-lined services may continue to experience declining ARPU in the foreseeable future, which could have a material adverse effect on our financial condition and results of operations. Although we have been making efforts to mitigate those effects by allocating more resources to diversify our service offerings, particularly the value-added services, to encourage more usage of our services and developing our high-end customers, we cannot assure you that these efforts will be able to achieve the anticipated results.



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***Our controlling shareholder, Unicom Group, can exert influence on us and cause us to make decisions that may not always be in the best interests of us or our other shareholders and may fail to provide services and facilities that we rely on to operate our business.***

Unicom Group indirectly controlled an aggregate of 71.01% of our issued share capital as of April 20, 2012 and all of our executive directors also serve as directors or executive officers of Unicom Group. As our controlling shareholder, subject to our articles of association and applicable laws and regulations, Unicom Group is effectively able to control our management, policies and business by controlling the composition of our board of directors and, in turn, indirectly controlling the selection of our senior management, determining the timing and amount of our dividend payments, approving significant corporate transactions, including mergers and acquisitions, and approving our annual budgets. The interests of Unicom Group as our controlling shareholder may conflict with our interests or the interests of our other shareholders. As a result, Unicom Group may cause us to enter into transactions or take (or fail to take) other actions or make decisions that may not be in our or our other shareholders' best interests.

In addition, our operations depend on a number of services and facilities provided by Unicom Group. For example, following our acquisition of the fixed-line business in 21 provinces in southern China in January 2009, we began leasing fixed-line networks from Unicom Group for our fixed-line business operations in those provinces. Unicom Group also provides us with international gateway services, interconnection services, sales agency and collection services and provision of premises. See B. Related Party Transactions under Item 7 and A. History and Development of the Company under Item 4. The interests of Unicom Group as provider of these services and facilities may conflict with our interests. Failure by Unicom Group to fulfill its obligations under any of these arrangements may have a material adverse effect on our business operations. We currently have limited alternative sources of supply for these services and facilities and, as a result, may have limited ability to negotiate with Unicom Group regarding the terms for providing these services and facilities. Changes in the availability, pricing or quality of these services or facilities may have a material adverse effect on our business and profitability.

***The previous internal reorganization of Unicom Group for the A Share offering created a two-step voting mechanism that requires the approval of the minority shareholders of both our Company and China United Network Communications Limited (formerly known as China United Telecommunications Corporation Limited), or the A Share Company, for significant related party transactions between us and Unicom Group.***

In October 2002, Unicom Group completed an internal reorganization of its shareholding in our company and the initial public offering in China of its then newly established subsidiary, the A Share Company. As part of this restructuring, a portion of Unicom Group's indirect shareholding in our company was transferred to the A Share Company, whose business is limited to indirectly holding the equity interest of our company without any other direct business operations. A voting mechanism was established to allow public shareholders of the A Share Company to indirectly participate in our shareholders' meetings and a two-step voting mechanism was established for the approval of related party transactions. As a result, any significant related party transaction between us or our subsidiaries and Unicom Group or its other subsidiaries will require the separate approval of the independent minority shareholders of both our company and the A Share Company. Related party transactions approved by our independent minority shareholders nevertheless cannot proceed if they are not approved by the independent minority shareholders of the A Share Company. This adds another necessary step of approval process for those transactions. See A. History and Development of the Company Two-Step Voting Arrangements under Item 4.

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***Investor confidence and the market prices of our shares and ADSs may be materially and adversely impacted if we are or our independent registered public accounting firm is unable to conclude that our internal control over financial reporting is effective in future years as required by Section 404 of the Sarbanes-Oxley Act of 2002.***

We are a public company in the United States that is subject to the Sarbanes-Oxley Act of 2002. Pursuant to the requirements of Section 404 of the Sarbanes-Oxley Act of 2002, we include in this annual report a report of management on our internal control over financial reporting and an attestation report of our independent registered public accounting firm on the effectiveness of our internal control over financial reporting.

As of December 31, 2011, our management conducted an assessment of the effectiveness of our internal control over financial reporting and concluded that our internal control over financial reporting as of December 31, 2011 was effective. The effectiveness of our internal control over financial reporting as of December 31, 2011 has been audited by PricewaterhouseCoopers, an independent registered public accounting firm, as stated in their report appearing on page F2. However, we cannot assure you that, in the future, our management will continue to conclude that our internal control over financial reporting is effective. Even if our management concludes that our internal control over financial reporting is effective for future periods, our independent registered public accounting firm may disagree. If our independent registered public accounting firm is not satisfied with our internal control over financial reporting or the level at which our controls are documented, designed, operated, reviewed or evaluated, or if the independent registered public accounting firm interprets the relevant requirements, rules or regulations differently from us, then it may issue an adverse opinion. Any of these possible outcomes in the future could result in an adverse reaction in the financial marketplace due to a loss of investor confidence in the reliability of our consolidated financial statements, which could materially adversely affect the market prices of our shares and ADSs.

Moreover, internal control over financial reporting may not prevent or detect misstatements because of its inherent limitations, including the possibility of human error, the circumvention or overriding of controls, or fraud. Therefore, even effective internal control over financial reporting can provide only reasonable assurance with respect to the preparation and fair presentation of financial statements. If we fail to maintain the adequacy of our internal control over financial reporting, including through a failure to implement required new or improved controls, or if we experience difficulties in their implementation, our business and operating results could be harmed, we could fail to meet our reporting obligations and there could be a material adverse effect on the market prices of our shares and ADSs.

***Our outstanding convertible bonds may dilute the ownership interest of existing shareholders and may adversely affect the market price of our ordinary shares.***

On October 18, 2010, Billion Express Investments Limited, a wholly-owned subsidiary of our company, completed the issue of the 2015 Convertible Bonds, which are exchangeable into ordinary shares of our company. Pursuant to the subscription agreement with respect to the 2015 Convertible Bonds, the holders of the 2015 Convertible Bonds may, beginning on November 28, 2010, elect to convert its bonds into our ordinary shares at an initial conversion price of HK\$15.85 per share, subject to certain adjustments. As of April 20, 2012, none of the 2015 Convertible Bonds has been converted into our ordinary shares. Assuming a full conversion of the 2015 Convertible Bonds at the initial conversion price of HK\$15.85 per share, the bonds would be convertible into 899,979,487 ordinary shares, representing approximately 3.68% of our enlarged issued and outstanding share capital as of April 20, 2012.

The conversion of the 2015 Convertible Bonds, if converted in full or in part, would dilute the ownership interest of our existing shareholders and our earnings per share, and could adversely affect the market price of our shares. Even if the 2015 Convertible Bonds are not converted, their existence may encourage the short selling of our ordinary shares by the holders of the 2015 Convertible Bonds as well as other market participants, depressing the price of our ordinary shares.

***The NDRC is conducting an anti-monopoly investigation relating to the price charged for Internet dedicated leased line access service provided by us to Internet service providers. The outcome of this investigation may subject us to a fine, and harm our reputation, which could adversely affect the prices of our shares and ADSs.***

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The NDRC is conducting an anti-monopoly investigation relating to the price charged for Internet dedicated leased line access service provided by us to Internet service providers. In response to the NDRC's investigation, we (i) provided the NDRC with pricing, volume, turnover and other information relevant to our Internet access bandwidth leasing business with Internet service providers for the year 2010, (ii) conducted a comprehensive self-inspection of our operations, and (iii) submitted to the NDRC a proposal for enhancement initiatives and an application for suspension of the NDRC's investigation. Through our comprehensive self-inspection of our operations, we have identified room for improvement in pricing management and relatively wide pricing variation, in respect of our business relating to the Internet dedicated leased line access service provided by us to the Internet service providers. In addition, the quality of interconnection between us and other backbone network operators also requires further improvement. As of the date of this annual report, the NDRC has not informed us of any results or conclusions of the investigation. If the outcome of the NDRC's investigation is not in our favor, we may be subject to a fine, and if we become the target of any negative publicity, our reputation would be harmed, which may have a material adverse effect on the prices of our shares and ADSs.

### **Risks Relating to the Telecommunications Industry in China**

***Government regulation of the telecommunications industry in China may affect our ability to respond to market conditions or competition, and may have a material adverse effect on our financial condition, results of operations and growth prospects.***

As a telecommunications operator in China, we are subject to regulation by, and under the supervision of, the MIIT, which is the primary regulator of the telecommunications industry in China. The MIIT is responsible for formulating policies and regulations for the telecommunications industry, granting telecommunications licenses, allocating frequency spectrum and numbers, formulating interconnection and settlement arrangements between telecommunications operators, and enforcing industry regulations. Other PRC Governmental authorities also regulate tariff policies, capital investment and foreign investment in the telecommunications industry. See B. Business Overview Regulatory and Related Matters under Item 4. The regulatory framework within which we operate may constrain our ability to implement our business strategies and limit our ability to respond to market conditions or to changes in our cost structure. Moreover, we operate our businesses pursuant to approvals granted by the State Council of the PRC, or the State Council, and under licenses granted by the MIIT. If these approvals or licenses were revoked or suspended, our business and operations would be materially adversely affected. In addition, we are subject to various regulatory requirements as to service quality, pricing and other actions, and failure to comply with such requirements may subject us to mandatory penalties or other punitive measures, any of which could have a material adverse effect on our financial condition, results of operations and growth prospects.

***Regulatory or policy changes relating to the PRC telecommunications industry or any future industry restructuring may materially adversely affect our financial condition, results of operations and growth prospects.***

The PRC Government continues to regulate many aspects of the telecommunications industry in China. Potential changes in regulations and policies and their implementation could lead to significant changes in the overall industry environment and may have a material adverse effect on our financial condition, results of operations and growth prospects. As part of the comprehensive plan to restructure the telecommunications industry in China, the PRC Government has been adjusting and improving its regulatory oversight of the telecommunications industry, including further deregulating telecommunications tariffs.

The MIIT, under the direction of the State Council, is currently preparing a telecommunications law to provide a uniform regulatory framework for the telecommunications industry in China. As of the date of this annual report, the proposed nature and scope of the telecommunications law have not yet been officially announced by the PRC Government. The telecommunications law and other new telecommunications regulations or rules, or future changes thereto, such as enforcement of existing regulations and policies, may materially adversely affect our financial condition, results of operations and growth prospects.

Issues may also arise regarding the interpretation and enforcement of China's WTO commitments regarding telecommunications services. Any future regulatory changes, such as those relating to the issuance of additional telecommunications licenses, tariff setting, interconnection and settlement arrangements, changes in technical and service standards, universal service obligations and spectrum and number allocations, may have a material adverse effect on our business and operations.

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The PRC telecommunications industry has been extensively restructured in recent years and may be subject to further restructuring. Such further industry restructuring may materially affect the operations of all telecommunications operators in China, including us. Accordingly, we cannot predict the scope and effect of any further restructuring on our financial condition, results of operations and growth prospects.

*New regulations, regulatory changes or changes in enforcement policies relating to tariffs and other aspects of telecommunications services may materially adversely affect our competitiveness, business and financial condition, results of operations and growth prospects.*

Tariffs are the prices we charge our customers for our telecommunications services. We are subject to extensive government regulations on tariffs, especially those relating to our basic telecommunications services, such as mobile services, local and long distance fixed-line telephone services, managed data services, leased line services and interconnection agreements. In recent years, we have experienced significant downward adjustments on tariffs of telecommunications services as well as regulatory restrictions that have significant impacts on our tariff setting. For example: (i) in February 2008, the MIIT and the NDRC lowered the regulatory tariff cap for roaming services; and (ii) in 2009, the MIIT and the NDRC required us and other PRC telecommunications operators to offer certain fixed-line local telephone plans that are subject to a tariff cap. These changes adversely affected our revenue.

We cannot predict with accuracy the timing, likelihood or magnitude of tariff adjustments by the PRC Government or the extent or potential impact on our business of future tariff adjustments. If the PRC Government substantially lowers the tariffs for our services, our business and our financial condition, results of operations and growth prospects may be adversely affected. In particular, monthly fees on fixed-line services have recently drawn attention from customers and the PRC Government. Revenue from some of our customers has decreased as a result of discounts on monthly fees that we offered through bundled service packages. Our revenue will be adversely affected if the PRC Government abolishes such monthly fees. In addition, the PRC Government is in the process of initiating detailed policies following the industry restructuring in 2008, including those that allow mobile subscribers to switch to the networks of another telecommunications operator with their existing numbers and those relating to the convergence of telecommunications, Internet and television broadcast networks. Since November 2010, a growing number of cities in China have carried out trials on the switch of telecommunications operator networks with existing numbers. The potential new regulatory policies and regulations may materially adversely affect our financial condition, results of operations and growth prospects.

*The PRC Government may require us, along with other telecommunications service providers in China, to provide universal services with specified obligations, and we may not be compensated adequately for providing such services.*

Under the Telecommunications Regulations promulgated by the State Council, telecommunications service providers in China are required to fulfill universal service obligations in accordance with relevant regulations to be promulgated by the PRC Government authorities, and the MIIT has the authority to delineate the scope of universal service obligations. The MIIT, together with government finance and pricing authorities, is also responsible for formulating administrative rules relating to the establishment of a universal service fund and compensation schemes for universal services. These rules have not yet been promulgated, and there are currently no specific regulatory requirements relating to the provision of universal services in China.

While specific universal services obligations are not yet clear, we believe that such services may include mandatory provision of basic telecommunications services in less economically developed areas in China and mandatory contribution by telecommunications service providers to a universal service fund. In addition, as part of the transitional measures prior to the formalization of a universal service obligation framework, the MIIT has required major telecommunications service providers in China, including Unicom Group, to participate in a project to provide telephone services in thousands of remote villages in China. See B. Business Overview Regulatory and Related Matters Universal Services under Item 4.

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We cannot predict whether the PRC Government will specifically require us to undertake universal service obligations in the future. To the extent we are required to do so, it is currently uncertain whether we will be adequately or timely compensated by the PRC Government or by the universal service fund. We cannot assure you that we will be able to realize an adequate return on investments for expanding networks to, and providing telecommunications services in, less economically developed areas due to potentially higher capital expenditure requirements, lower usage by customers and lack of flexibility in setting our tariffs. We also cannot predict whether we will be required to make a contribution to the universal service fund. Any of these events may adversely affect our financial condition and results of operations.

*Actual or perceived health risks associated with the use of mobile devices could impair our ability to retain and attract customers of our mobile services, reduce mobile service usage or result in litigation.*

Concerns have been expressed in some countries that the electromagnetic signals emitted by wireless telephone handsets and base stations may pose health risks at exposure levels below existing guideline levels, and interfere with the operation of electronic equipment. In addition, mobile operators have been subject to lawsuits alleging various health consequences as a result of mobile handset usage or proximity to base stations or seeking protective or remedial measures. While we are not aware that such health risks have been substantiated, there can be no assurance that the actual, or perceived, risks associated with the transmission of electromagnetic signals will not impair our ability to retain customers and attract new customers, reduce mobile service usage or result in litigation.

### **Risks Relating to Doing Business in China**

*Our operations may be materially adversely affected by changes in China's economic, political and social conditions.*

Substantially all of our business operations are conducted in China and substantially all of our revenue is derived from our operations in China. Accordingly, our business, financial condition, results of operations and prospects are affected to a significant degree by economic, political and social conditions in China. The PRC economy differs from the economies of most developed countries in many respects, including with respect to the extent of government involvement, level of development, growth rate, and control of foreign exchange and allocation of resources. While the PRC economy has experienced significant growth in the past three decades, growth has been uneven across different regions and among various economic sectors. The PRC Government has implemented various measures to encourage economic development and guide the allocation of resources. Some of these measures benefit the overall PRC economy, but may also have a negative effect on us. For example, our financial condition and results of operations may be materially adversely affected by government control over capital investments.

In addition, the PRC Government has implemented various measures since 2011 to rein in economic growth and control inflation, such as tightening bank lending policies and cooling down the housing market. In particular, the PRC Government in March 2012 reduced its 2012 annual GDP growth target to 7.5% from 8%. If China's economic growth slows down, our subscribers' usage of our services may decrease and we may experience increased difficulties in retaining existing subscribers or acquiring new subscribers, which could materially and adversely affect our business, as well as our financial condition and results of operations.

*If the PRC Government revises the current regulations that allow a foreign-invested enterprise to pay foreign exchange in current account transactions, our operating subsidiary's ability to satisfy its foreign exchange obligations and to pay dividends to us in foreign currencies may be restricted.*

The ability of our major operating subsidiary, CUCL, to satisfy its foreign exchange obligations and to pay dividends to us depends on existing and future foreign exchange regulations in China. The Renminbi is currently convertible by foreign-invested enterprises in China to settle transactions under the current account, which include trade and service related foreign exchange transactions and payments of dividends. The Renminbi currently cannot be freely converted without regulatory approval for transactions under the capital account, which includes outbound foreign investment and payments on foreign loans. CUCL, which holds substantially all of our assets and through which we conduct substantially all of our business, is a foreign-invested enterprise in China. However, there is no assurance that in the future the relevant PRC government authorities will not impose any limitation on the ability of foreign-invested enterprises to purchase foreign exchange to satisfy their foreign exchange obligations or to pay dividends. In that event, CUCL's ability to satisfy its foreign exchange obligations and to pay dividends to us in foreign currencies may be restricted and the interests of our shareholders may, in turn, be affected.

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***Fluctuations in the value of the Renminbi could adversely affect the prices of our shares and ADSs as well as our profitability.***

Substantially all of our revenue and costs and expenses are denominated in Renminbi, while a portion of our borrowings, equipment purchases and other capital expenditures are denominated in foreign currencies. On July 21, 2005, the PRC Government changed its decade-old policy to permit Renminbi to fluctuate within a narrow and managed band against a basket of certain foreign currencies determined by the People's Bank of China, or the PBOC. On May 19, 2007, the PBOC announced a policy to further expand the maximum daily floating range of RMB trading prices against the U.S. dollar in the inter-bank spot foreign exchange market. With the increased floating range of the Renminbi's value against foreign currencies, the Renminbi may appreciate or depreciate significantly in value against the U.S. dollar or other foreign currencies in the long term, depending on the fluctuation of the basket of currencies against which it is currently valued, or it may be permitted to enter into a full float. Increased fluctuations of the Renminbi could adversely affect the value in foreign currency terms of cash flow generated from our operations or any dividends payable on our shares and ADSs, and therefore the price of our shares and ADSs. Any future Renminbi devaluations could also increase our equipment importation costs or lead to significant fluctuations in the exposure of our foreign-currency-denominated liabilities, thereby adversely affecting our profitability.

***Uncertainties in the PRC legal system could limit the legal protections available to us and to foreign investors and materially adversely affect our financial condition, results of operations and growth prospects.***

Our wholly-owned operating subsidiary, CUCL, is organized under the laws of PRC and is generally subject to laws and regulations applicable to foreign-invested enterprises in China. The Chinese legal system is a civil law system based on written statutes. Unlike common law systems, it is a system in which decided legal cases may be cited for reference but have limited precedential value. Since 1979, the PRC Government has promulgated laws and regulations dealing with economic matters such as foreign investment, corporate organization and governance, commerce, property, taxation and trade. However, because these laws and regulations are relatively new, and because of the relatively limited volume of published cases and their non-binding nature, interpretation and/or enforcement of these laws and regulations involves uncertainties, which may limit the remedies available to you as an investor and to us in the event of any claims or disputes with third parties. In addition, any litigation in China may be protracted and result in costs and diversion of resources and management attention. Therefore, the protection provided by the PRC legal system may not be the same as the legal protection available to investors in the United States or elsewhere. Furthermore, various uncertainties involved in the rulemaking, interpretation and enforcement process of the laws, regulations and rules in China that are related to our business operations, in particular, those in respect of telecommunications and enterprise income tax, may also materially and adversely affect our financial condition, results of operations and growth prospects.

***Since we are a Hong Kong company, you will not have certain investor rights as our shareholder, such as the right to bring legal action against other shareholders on behalf of the company.***

We were incorporated in Hong Kong. The Hong Kong Companies Ordinance does not provide for any right for our shareholders, including our significant shareholders, to bring legal action against any other shareholder on our behalf to enforce any claim against such party or parties if we fail to enforce such claim ourselves.

***You may experience difficulties in effecting service of legal process and enforcing judgments against us and our management.***

Most of our current operations are conducted in China and most of our assets are located in China. In addition, five out of eleven of our current directors and all of our current executive officers reside within China, and substantially all of the assets of these persons are located within China. As a result, it may not be possible to effect service of process within the United States or elsewhere outside China upon these directors or executive officers, including with respect to matters arising under U.S. federal securities laws or applicable state securities laws. Moreover, our PRC counsel has advised us that China does not have treaties with the United States or many other countries providing for the reciprocal recognition and enforcement of court judgments. Our Hong Kong counsel has also advised us that Hong Kong has no arrangement for the reciprocal enforcement of judgments with the United States. As a result, recognition and enforcement in China of judgments of a court of the United States or any other jurisdiction, including judgments against us or our directors, executive officers, underwriters or experts, may be difficult or impossible.

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*Natural disasters and health hazards in China may severely disrupt our business and operations and may severely restrict the level of economic activities in affected areas which in turn may have a material adverse effect on our financial condition and results of operations.*

In 2008, we experienced severe sleet and snowstorms in southern China and a devastating earthquake in Sichuan province. Those natural disasters resulted in significant and extensive damage to our base stations and network equipment. Moreover, certain countries and regions, including China, have encountered incidents of the H5N1 strain of bird flu, or avian flu, as well as severe acute respiratory syndrome, or SARS, over the past several years and, more recently in 2009, the outbreak of influenza A (H1N1). In 2010, another major earthquake registering 7.1 on the Richter scale struck Qinghai Province. We are also unable to predict the effect, if any, that any other future natural disasters and health hazards may have on our business. Any future natural disasters and health hazards may, among other things, significantly disrupt our ability to adequately staff our business, and may generally disrupt our operations. Furthermore, natural disasters and health hazards may severely restrict the level of economic activities in affected areas, which may in turn materially adversely affect our business and prospects. As a result, any natural disasters or health hazards in China may have a material adverse effect on our financial condition and results of operations.

### **Risk Relating to our ADSs**

*Holders of our ADSs will not have the same voting rights as the holders of our shares and may not receive voting materials in time to be able to exercise their right to vote.*

Except as described in this annual report and in the deposit agreement, holders of our ADSs will not be able to exercise voting rights attaching to the shares represented by our ADSs on an individual basis. Holders of our ADSs will receive proxy materials with respect to matters to be voted on at a meeting of shareholders through the depositary and may only exercise voting rights by appointing the depositary or its nominee as their representative to exercise the voting rights attaching to the shares represented by the ADSs. Consequently, if the materials to be forwarded to holders of ADSs by the depositary are delayed or if the depositary sets deadlines by which holders of ADSs must give their instructions regarding how to vote that fall too soon after mailing of the proxy materials, the holders of our ADSs may not receive voting materials in time to instruct the depositary to vote. Thus, it is possible that such holders, or persons who hold their ADSs through brokers, dealers or other third parties, may not have the opportunity to exercise a right to vote.

## **Item 4. Information on the Company**

### **A. History and Development of the Company**

We were incorporated under the laws of Hong Kong on February 8, 2000 under the Companies Ordinance as a company limited by shares under the name China Unicom Limited. In connection with the telecommunications industry restructuring initiated by the MIIT, the NDRC and the Ministry of Finance of the PRC in 2008 as discussed below, we merged with China Netcom and changed our name to China Unicom (Hong Kong) Limited with effect from October 15, 2008. Following our merger with China Netcom, we became an operator providing a full range of telecommunications services, including mobile and fixed-line services, in China.

Our registered office and principal executive offices are located at 75th Floor, The Center, 99 Queen's Road Central, Hong Kong (telephone number: 852-2126-2018).

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**Restructurings of the Telecommunications Industry**

Since 1993, the PRC Government has implemented a number of measures to restructure and introduce competition in the telecommunications industry. Prior to July 1994, China Telecom was the sole provider of telecommunications services in China. In July 1994, Unicom Group was established in accordance with the State Council's approval to introduce orderly competition in the telecommunications industry. Since then, the PRC Government has approved Jitong Network Communications Company Limited, or Jitong, and China Netcom Corporation Ltd., or CNCL, to provide Internet protocol, or IP, telephony, Internet and data services. It has also approved China Tietong to provide most telecommunications services other than mobile services.

In 1999, the State Council approved a plan to restructure the former China Telecom along four business lines: fixed-line, mobile, paging and satellite communications. As a result of the restructuring, China Telecom retained the fixed-line, data and Internet businesses, while China Mobile assumed the mobile business previously operated by China Telecom. In 2002, the PRC Government further separated China Telecom into two companies, with the southern company retaining the name of China Telecom and assets and businesses in 21 provinces in southern China and the northern company retaining assets and businesses in 10 provinces in northern China and merging with CNCL and Jitong to form China Netcom. As a result of the PRC Government's efforts to introduce competition in the telecommunications industry, there are currently more than one service providers in most of the sectors within the telecommunications industry.

On May 24, 2008, the MIIT, the NDRC and the Ministry of Finance issued a joint announcement relating to the further reform of the PRC telecommunications industry. According to the joint announcement, the principal objectives of such further reform included, among others: (i) supporting the formation of three telecommunications services providers of comparable scale and standing, each with nationwide network resources, full-service capabilities and competitive strength, in order to help optimize the allocation of telecommunications resources and foster market competition; (ii) promoting homegrown innovation by telecommunications services providers; and (iii) enhancing the service capabilities and quality of, and the regulatory framework governing, the telecommunications industry. To achieve these objectives, the three ministries encouraged the following restructuring transactions: (a) the acquisition by China Telecom of the CDMA network (including both assets and subscriber base) then owned by Unicom Group along with us; (b) the merger between China Unicom and China Netcom; (c) the transfer of the basic telecommunications services business operated by China Satellite into China Telecom; and (d) the consolidation of China Tietong into China Mobile. The detailed implementation plans relating to these restructuring transactions were subsequently formulated by the relevant parties and, as a result, China Mobile, China Telecom and we became the current three major telecommunications operators in China, each providing a full range of telecommunications services nationwide.

**Sale of CDMA Business, Merger with China Netcom and Related Transactions**

***Disposal of CDMA Business and Related Transactions***

Pursuant to the 2008 telecommunications industry restructuring announcement, on June 2, 2008, we, CUCL and China Telecom entered into a CDMA business disposal framework agreement, under which CUCL agreed to sell, and China Telecom agreed to purchase, the CDMA business of CUCL, including (i) the entire CDMA business, which is owned and operated by CUCL, together with the assets of CUCL that are relevant to the CDMA operations and the rights and liabilities of CUCL relating to its CDMA subscribers; (ii) the entire equity interest in China Unicom (Macau) Company Limited, our wholly-owned subsidiary; and (iii) all of the 99.5% equity interest in Unicom Huasheng Telecommunications Technology Company Limited, a limited liability company incorporated under the laws of the PRC, held by CUCL.

On July 27, 2008, we, CUCL and China Telecom further entered into a CDMA business disposal agreement which set out the detailed terms and conditions of the CDMA business disposal. The consideration for the CDMA business disposal was RMB43.8 billion in cash, payable in three installments. While the consideration was subject to a price adjustment mechanism based on the CDMA service revenue generated by us for the six months ended June 30, 2007 and June 30, 2008, as agreed with China Telecom, there was no subsequent adjustment to the consideration as a result of the price adjustment mechanism.



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On July 27, 2008, in connection with the CDMA business disposal, CUCL agreed (i) to waive its right to exercise its option to purchase the CDMA network from Unicom New Horizon Mobile Telecommunications Company Limited, or Unicom New Horizon, a wholly-owned subsidiary of Unicom Group, and (ii) to terminate the CDMA lease pursuant to which CUCL leased capacity on the CDMA network from Unicom New Horizon, in each case with effect upon the completion of the CDMA business disposal.

At our shareholders' meeting held on September 16, 2008, our shareholders approved the CDMA business disposal and our independent shareholders approved the waiver by CUCL of the option to purchase the CDMA network and the termination of the CDMA lease. As all of the conditions of the CDMA business disposal as specified in the CDMA business disposal agreement had been satisfied or deemed to have been satisfied, the CDMA business disposal was completed on October 1, 2008. On that date, China Telecom became the legal owner of the CDMA business and all the rights, interests, obligations and liabilities in relation to the CDMA business have been borne by China Telecom with effect from October 1, 2008. We recognized in our statements of income for the year ended December 31, 2008 a gain on disposal of the CDMA business of approximately RMB26.1 billion, net of corresponding income tax of approximately RMB9.0 billion. For further details, see *Operating Results - Year Ended December 31, 2008 Compared to Year Ended December 31, 2007 - Income from Discontinued Operations* under Item 5.

In connection with the CDMA business disposal, we had been notified by Unicom Group that on June 2, 2008 and July 27, 2008, Unicom Group, Unicom New Horizon and China Telecom entered into a CDMA network framework agreement and a CDMA network disposal agreement, respectively, which set out the terms and conditions, under which Unicom Group and Unicom New Horizon agreed to sell, and China Telecom agreed to purchase, the CDMA network at a consideration of RMB66.2 billion. The disposal of the CDMA network was completed concurrently with our CDMA business disposal, on October 1, 2008.

### ***Merger with China Netcom and Related Transactions***

#### ***Merger with China Netcom***

On October 15, 2008, following the approval of the merger by our shareholders and the shareholders of China Netcom at shareholders' meetings held on September 16, 2008 and September 17, 2008, respectively, and the satisfaction of all other conditions, the merger between China Unicom and China Netcom by way of a scheme of arrangement of China Netcom under Section 166 of the Hong Kong Companies Ordinance became effective. Upon the merger becoming effective, all ordinary shares of China Netcom outstanding at 5:00 p.m., Hong Kong time, on October 14, 2008 and all outstanding options to acquire China Netcom shares granted under the share option scheme of China Netcom were cancelled and new China Netcom shares were issued to us. As a result, China Netcom became our wholly-owned subsidiary and the listings of China Netcom's ordinary shares and ADSs on the HKSE and the NYSE, respectively, were withdrawn.

In connection with our merger with China Netcom, each holder of China Netcom shares was entitled to receive 1.508 of our new ordinary shares for every cancelled China Netcom share and each holder of Netcom ADSs was entitled to receive 3.016 of our new ADSs for every cancelled China Netcom ADS. A total of 10,102,389,377 of our new ordinary shares (including ordinary shares underlying our newly issued ADSs) were issued to China Netcom's shareholders as consideration for the cancellation of the China Netcom shares held by China Netcom shareholders.

Furthermore, we adopted a special purpose share option scheme, pursuant to which we have granted new Unicom options to the holders of China Netcom options in consideration for the cancellation of their outstanding Netcom options (whether vested or not). The number of Unicom options granted and the exercise price of such options were determined in accordance with a formula which ensures that the value of the Unicom options received by a holder of Netcom options is equivalent to the value determined by deducting the exercise price of the relevant Netcom option from the value of HK\$27.87 per Netcom share. See *E. Share Ownership - Stock Incentive Schemes - Special Purpose Share Option Scheme* under Item 6 for further details.

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As a result of our merger with China Netcom, we have become an operator providing a full range of telecommunications services, including mobile voice and value-added, fixed-line voice and value-added, fixed-line broadband, data communications and other telecommunications services, to our customers through our two business segments comprised of mobile services and fixed-line services. Following the merger, we have taken measures to combine the respective experience and technologies of Unicom and China Netcom and develop business strategies, taking into account current market developments, to promote business innovation and competitiveness and to improve operating and financial performance. By combining the resources and business strengths of Unicom and China Netcom in different areas, we seek to become a world-class provider of telecommunications services, in particular in fixed-line broadband communications and information services, establish competitive advantages in our technologies, products and services and provide professional and multi-tiered information services to satisfy the changing and diverse needs of the telecommunications market in China.

### *Change of Company Name*

Upon our merger with China Netcom becoming effective on October 15, 2008, our name changed from China Unicom Limited to China Unicom (Hong Kong) Limited. Our stock trading code on the HKSE and our ticker symbol on the NYSE remain unchanged.

### *Related Transactions*

As part of our integration with China Netcom, our wholly-owned subsidiary, CUCL, merged with China Netcom (Group) Company Limited, or CNC China, a wholly-owned subsidiary of China Netcom, in January 2009, and upon that merger becoming effective, CUCL assumed all the rights and obligations of CNC China, and all the assets, liabilities and business of CNC China were vested in CUCL. In addition, in January 2009, Unicom Group, our parent company, merged with and absorbed Netcom Group, the parent company of China Netcom. Upon completion of the merger between Unicom Group and Netcom Group, Unicom Group assumed all the rights and obligations of Netcom Group, and all the assets, liabilities and business of Netcom Group have vested in Unicom Group.

## **History and Corporate Development of China Netcom**

China Netcom was incorporated in Hong Kong on October 22, 1999, under the Hong Kong Companies Ordinance as a company limited by shares under the name Target Strong Limited. The company changed its name to China Netcom (Hong Kong) Corporation Limited on December 9, 1999, to China Netcom Corporation (Hong Kong) Limited on August 4, 2000, and to China Netcom Group Corporation (Hong Kong) Limited on July 23, 2004 (the last name change in anticipation of its IPO in 2004).

China Netcom's principal operating subsidiary, CNC China, which merged with, and was absorbed by, CUCL in January 2009, was incorporated as a PRC limited liability company in August 1999 by its four founders and shareholders, the Academy of Sciences, INC-SARFT, CRTC and Shanghai Alliance, as a facilities-based telecommunications operator in China. China Netcom was established in October 1999 to facilitate investments by foreign investors, including CNC Fund, L.P., in CNC China. Shortly thereafter, the four founders, using their respective equity interests in CNC China as capital contributions, established China Netcom (Holdings) Company Limited, or China Netcom Holdings, which in turn contributed its entire interests in CNC China through CNC BVI to China Netcom. China Netcom, through China Netcom Corporation International Limited, established Asia Netcom in 2002. Asia Netcom remained inactive until it acquired substantially all the assets, including cash, and most of the subsidiaries, of the former Asia Global Crossing Ltd. by the end of 2003.

China Netcom successfully completed its IPO in November 2004 with the listing of its ordinary shares on the HKSE and ADSs, each representing 20 of its ordinary shares, on the NYSE.

In October 2005, China Netcom acquired from CNC BVI the entire equity interests of China Netcom Group New Horizon Communications Corporation (BVI) Limited, or CNC New Horizon BVI, which merged into CNC China in November 2006. As a result of the merger, China Netcom acquired the fixed-line telecommunications assets and related liabilities in Heilongjiang Province, Jilin Province, the Inner Mongolia Autonomous Region and Shanxi Province. In August 2006, China Netcom sold the entire equity interest in Asia Netcom, which then provided international telecommunications services in the Asia-Pacific region, to Connect Holdings Limited. In February 2007, China Netcom sold its telecommunications assets, liabilities and business operations in Guangdong Province and Shanghai Municipality to Netcom Group. In December 2007, China Netcom's wholly-owned subsidiary, China Netcom Group System Integration Limited Corporation, or China Netcom System Integration, acquired the entire equity interest in Design Institute from China Netcom Group Beijing Communications Corporation, a wholly-owned subsidiary of Netcom Group, in order to develop two of its key information and communication technologies, or ICT, services.

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### **Our Parent Company and Our Initial Public Offering**

Our ultimate controlling shareholder is Unicom Group, a company incorporated under the laws of the PRC and majority-owned by the PRC Government. Unicom Group was established in accordance with the State Council's approval to introduce orderly competition in the telecommunications industry in 1994.

Unicom Group transferred certain of its telecommunications assets, rights and liabilities to CUCL (which became our wholly-owned subsidiary in China) in April 2000 in preparation for our IPO. In June 2000, we successfully completed our IPO. Our ordinary shares are listed on the HKSE and our ADSs, each representing ten of our ordinary shares, are listed on the NYSE.

### **Unicom Acquisitions and Sales**

In December 2002 and December 2003, respectively, we completed our acquisitions from Unicom Group of 100% of the equity interests in Unicom New Century and Unicom New World, both of which held mobile telecommunications operations (including GSM assets and business and CDMA business) in various provinces and autonomous regions in China. Subsequent to the completion of those acquisitions, Unicom New Century and Unicom New World merged into CUCL in July 2004 and September 2005, respectively.

In March 2003, we completed the sale to Unicom Group of the entire equity interest of Guoxin Paging Corporation Ltd., which at the time of transfer was engaged in paging business.

In September 2004, we acquired from Unicom Group of 100% of the equity interest in China Unicom International Limited, or Unicom International, a limited liability company established in Hong Kong and engaged in voice wholesale business, telephone cards business, line leasing services, managed bandwidth services and mobile virtual network services. In September 2009, the name of China Unicom International Limited was changed to China Unicom (Hong Kong) Operations Limited. Unicom International's wholly-owned U.S. subsidiary, China Unicom USA Corporation, is engaged in the wholesale business of voice traffic between the United States and PRC. In August 2009, the name of China Unicom USA Corporation changed into China Unicom (Americas) Operations Limited upon the completion of its merger with China Netcom (USA) Operations Limited, a subsidiary of China Netcom.

In October 2004, we established China Unicom (Macau) Company Limited, or Unicom Macau, in Macau, which then provided CDMA mobile services to local CDMA users in Macau. In connection with the disposal of our CDMA business in October 2008, we sold the entire equity interest in Unicom Macau to China Telecom along with our other CDMA business and certain related assets.

In July 2005, CUCL and Unicom Xingye Science and Technology Trade Co., Ltd., or Unicom Xingye, a subsidiary of Unicom Group, incorporated Unicom Huasheng. Unicom Huasheng was principally engaged in the sales of CDMA handsets and telecommunications equipment and the provision of technical services for us. In connection with the disposal of our CDMA business in October 2008, CUCL sold all of the 99.5% equity interest it held in Unicom Huasheng to China Telecom.

In December 2007, we completed the acquisition from Unicom Group of the mobile telecommunications operations (including GSM assets and business and CDMA business) of its Guizhou Province branch. As a result of the acquisitions of Unicom New Century, Unicom New World and Unicom Guizhou, we extended our GSM and CDMA mobile businesses to all provinces, autonomous regions and municipalities across China.

On August 19, 2008, CUCL established a wholly-owned subsidiary, Unicom Huakai Telecommunications Company Limited, or Unicom Huakai, as a limited liability company under the laws of the PRC. Unicom Huakai is principally engaged in the sales of handsets and telecommunications equipment and the provision of technical services. The paid-in capital of Unicom Huakai is RMB500 million. On December 26, 2008, the name of Unicom Huakai was changed to Unicom Vsens Telecommunications Company Limited.

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***Acquisitions of Fixed-Line Business in 21 Provinces in Southern China and Other Assets from Parent Companies and Lease of Telecommunications Networks in 21 Provinces in Southern China***

Following the approval by our independent shareholders and the shareholders of the A Share Company and upon the satisfaction of all other conditions, in January 2009, we completed our acquisitions, through CUCL, of certain telecommunications business and assets from Unicom Group and Netcom Group (which merged with, and was absorbed by, Unicom Group in January 2009), including:

the fixed-line business across 21 provinces in southern China operated by Unicom Group and Netcom Group and/or their respective subsidiaries and branches (but not the underlying fixed assets) and the local access telephone business in Tianjin Municipality operated by Unicom Group and related fixed assets (other than land and buildings) necessary for the operation of such local access telephone business and/or respective subsidiaries and branches;

the backbone transmission assets in 10 provinces in northern China owned by Netcom Group and/or its subsidiaries;

100% of the equity interest in Unicom Xingye, a limited liability company incorporated under the laws of the PRC and a wholly-owned subsidiary of Unicom Group;

100% of the equity interest in China Information Technology Designing & Consulting Institute Company Limited, or CITC, a limited liability company incorporated under the laws of the PRC and a wholly-owned subsidiary of Unicom Group; and

100% of the equity interest in New Guoxin Telecom Corporation of China Unicom, or New Guoxin, a limited liability company incorporated under the laws of the PRC and a wholly-owned subsidiary of Unicom Group.

The total consideration for the above acquisitions is approximately RMB4.43 billion, payable in cash. Following the completion of these acquisitions, the coverage of our fixed-line services expanded to all 31 provinces, autonomous regions and municipalities across China. We believe that these acquisitions will help integrate and optimize our business and resources and enhance our overall competitive position.

In addition, in order to operate the fixed-line business in the 21 provinces in southern China, on December 16, 2008, CUCL entered into a network lease agreement, or the initial network lease agreement, with Unicom Group, Netcom Group and Unicom New Horizon, a wholly-owned subsidiary of Unicom Group, to lease on an exclusive basis the telecommunications networks in those provinces, which are held by Unicom New Horizon and are necessary for the operation of the fixed-line business in southern China. The initial network lease agreement became effective in January 2009 upon the completion of our acquisitions of the fixed-line business in southern China and was for an initial term of two years effective from January 2009. On October 29, 2010, CUCL entered into a network leasing agreement or, the 2011-2012 network lease agreement, with Unicom New Horizon, which became effective on January 1, 2011. The 2011-2012 network lease agreement is for an initial term of two years effective from January 1, 2011 and is renewable at the option of CUCL with at least two months' prior notice on the same terms and conditions, except for the future lease fee which will remain subject to further negotiations between the parties. The annual lease fee payable by CUCL under the 2011-2012 network lease agreement for the years ending December 31, 2011 and 2012 is RMB2.4 billion and RMB2.6 billion, respectively. In connection with the 2011-2012 network lease agreement, Unicom New Horizon also granted CUCL an option, but not an obligation, to purchase the telecommunications networks leased in southern China. The purchase option may be exercised, at the discretion of CUCL, at any time during the term of the lease. No premium has been paid or will be payable by CUCL for such purchase option. In the event that CUCL elects to exercise this purchase option, the parties will discuss and negotiate the purchase price with reference to the appraised value of the telecommunications networks in southern China, which is to be determined in accordance with applicable laws of Hong Kong and the PRC, after taking into account the prevailing market conditions and other factors. Under the 2011-2012 network lease agreement, CUCL is responsible for the ongoing cost and expenses incurred in respect of the maintenance and management which may arise from the use of the leased telecommunications networks in southern China.

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### ***2011 Acquisition***

In December 2011, we completed our acquisitions through Broadband Online, a wholly-owned subsidiary of CUCL, of the entire equity interest in Unicom NewSpace from Unicom Group for a total cash consideration of RMB158 million. Unicom NewSpace primarily engages in mobile value-added business in China.

### **Mutual Investment with Telefónica, S.A.**

On September 6, 2009, we entered into a share subscription agreement with Telefónica, S.A., or Telefónica, one of our shareholders, to strengthen our cooperation. Pursuant to this agreement, we and Telefónica agreed to make a mutual investment in the amount of the equivalent of US\$1 billion in each other through acquisitions of shares in the other party. On October 21, 2009, we and Telefónica completed such mutual investments which were implemented by way of the subscription by Telefónica of 693,912,264 new ordinary shares in the capital of our company at a price of HK\$11.17 each and the contribution by Telefónica of 40,730,735 treasury shares in the capital of Telefónica at a price of Euro17.24 each to us. In addition, on September 6, 2009, we entered into a strategic alliance agreement with Telefónica, pursuant to which Telefónica and we agreed to establish a strategic alliance to strengthen the business of each party by cooperation based on our respective networks, business model and experience.

On January 23, 2011, we entered into the Agreement to Enhance the Strategic Alliance with Telefónica. Pursuant to this agreement, we acquired from Telefónica 21,827,499 ordinary shares in the capital of Telefónica for aggregate purchase price of Euro374,559,882.84 on January 25, 2011, and Telefónica, through its wholly-owned subsidiary, Telefónica International, acquired 282,063,000 ordinary shares in the capital of our company for aggregate consideration of approximately US\$500,000,000 in several transactions executed in the period between January 25, 2011 and September 7, 2011. In addition, Chang Xiaobing, our Chairman and Chief Executive Officer, as our designated representative, was appointed in May 2011 as a director on the board of directors of Telefónica.

### **Share Repurchase from SK Telecom**

On September 25, 2009, we received a conditional irrevocable offer from SK Telecom Co., Ltd. for sale, and we repurchased from SK Telecom by way of an off-market share repurchase of 899,745,075 shares, which comprised all of our shares previously owned by SK Telecom. The consideration for this share repurchase was approximately HK\$9.99 billion, HK\$11.105 for each share repurchased, and was paid in cash. The share repurchase was completed on November 5, 2009 and the 899,745,075 repurchased shares were subsequently cancelled by our company.

### **Our Relationship with Unicom Group**

Unicom Group holds the licenses required for our telecommunications businesses and we derive our rights to operate our businesses from our status as a subsidiary of Unicom Group. Unicom Group undertook to hold and maintain all licenses received from the MIIT in connection with our businesses solely for our benefit during the term of such licenses and at no cost to us. In addition, Unicom Group undertook to take all actions necessary to obtain and maintain for our benefit such governmental licenses or approvals as we shall require to continue to operate our businesses. Unicom Group also agreed not to engage in any business which competes with our businesses other than the then-existing competing businesses of Unicom Group and to grant us a right of first refusal in relation to any government authorization, license or permit, or other business opportunity to develop any new telecommunications technology, product or service. Finally, Unicom Group also gave us an undertaking not to seek an overseas listing for any of its businesses or the businesses of its subsidiaries in which we are engaged or may engage in the future, except through us.

In connection with the restructuring of Unicom Group and the acquisitions of Unicom New Century, Unicom New World and Unicom International, we entered into a number of agreements with Unicom Group pursuant to the two-step process described in **A. Development and History of the Company** **Two-Step Voting Arrangements** below. These agreements expired on December 31, 2010. On October 29, 2010, CUCL and Unicom Group entered into a new comprehensive services agreement, or the 2010 comprehensive services agreement, to provide certain services and facilities to each other for a term of three years commencing on January 1, 2011 and expiring on December 31, 2013. See **B. Related Party Transactions** under Item 7 for a detailed description of our agreements with Unicom Group.

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Set forth below is our shareholding structure and significant subsidiaries as of April 20, 2012.

### **Two-Step Voting Arrangements**

As a result of a series of internal restructurings of Unicom Group's shareholding in us following our IPO, Unicom BVI became our direct controlling shareholder, which in turn is directly controlled by the A Share Company and indirectly controlled by the Unicom Group. The A Share Company's business is limited to indirectly holding the equity interest in Unicom without any other direct business operations. The A Share Company was listed on the Shanghai Stock Exchange in 2002. In order to allow public shareholders of the A Share Company to indirectly participate in our shareholders' meeting, a voting mechanism was designed in accordance with the articles of association of Unicom BVI and the A Share Company. Under this voting mechanism, before Unicom BVI votes on certain proposals at our shareholders' meeting, the A Share Company must first convene a shareholders' meeting to consider the same proposals in order to direct Unicom BVI to vote the shares in our company indirectly held by the A Share Company through Unicom BVI. Unicom Group can similarly direct the voting in respect of its direct equity interest in Unicom BVI.

The voting mechanism described above, however, will not apply to the approval process for any related party transaction between us or our subsidiaries and Unicom Group or its subsidiaries, on which Unicom BVI will not be permitted to vote under the Rules Governing the Listing of Securities on HKSE, or the HKSE Listing Rules. Those related party transactions would require the separate approvals of the public shareholders of each of our company and the A Share Company. We and the A Share Company therefore created the two-step voting arrangements, pursuant to which each related party transaction between us or our subsidiaries and Unicom Group or its subsidiaries will consist of an initial agreement and a further agreement. The initial agreement would be entered into by Unicom Group or its subsidiaries (excluding the A Share Company and its subsidiaries) on the one hand and the A Share Company or Unicom BVI on the other hand. The initial agreement would contain the following terms:

the closing of the initial agreement would be subject to (i) the successful transfer of all rights and obligations of the A Share Company or Unicom BVI under the initial agreement to us or our subsidiaries, and (ii) the approval of the further agreement by our independent shareholders; and

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Unicom Group or its subsidiaries (excluding the A Share Company and its subsidiaries) would agree and acknowledge that all rights and obligations under the initial agreement can be transferred to us or our subsidiaries without any further consent requirements.

The initial agreement will constitute a related party transaction of the A Share Company and, if certain thresholds are met, will require the approval of the public or independent shareholders of the A Share Company under the rules of the Shanghai Stock Exchange. The further agreement would be entered into by the A Share Company or Unicom BVI, on the one hand, and us or our subsidiaries, on the other hand, and will provide for the transfer of all rights and obligations of the A Share Company or Unicom BVI under the initial agreement to us or our subsidiaries. The further agreement will constitute a related party transaction of our company and, if certain thresholds are met, will require the approval of our public or independent shareholders under the HKSE Listing Rules. We expect, to the extent the nature of a particular related party transaction allows, the two-step voting arrangements to apply as described above. However, when we or our subsidiaries are the providers, rather than recipients, of certain services, the two-step voting arrangements will need to be adjusted so that the process as described above is effectively reversed, such that the initial agreement is entered into by us or our subsidiaries rather than Unicom Group or its subsidiaries (excluding the A Share Company and its subsidiaries) with the A Share Company or Unicom BVI. Accordingly, Unicom Group or its subsidiaries (excluding the A Share Company and its subsidiaries), rather than us or our subsidiaries, will be a party to the further agreement. The arrangements (including the conditions) will apply correspondingly. This two-step structure will be applied in all related party transactions between us or our subsidiaries and Unicom Group or its subsidiaries and will effectively require the separate approvals of the public or independent shareholders of each of Unicom and the A Share Company for such related party transactions.

**Capital Expenditures and Divestitures**

See *Liquidity and Capital Resources* *Capital Expenditures* under Item 5 for information concerning our principal capital expenditures for the previous two years and those planned for 2012. We currently do not have any significant divestiture in progress.

***B. Business Overview***

**General**

We are an integrated telecommunications operator in China providing mobile voice and value-added, fixed-line voice and value-added, fixed-line broadband, data communications and other telecommunications services to our customers through our two business segments – mobile services and fixed-line services. Following our acquisition of fixed-line business in 21 provinces in southern China from our parent companies in January 2009, we have extended the coverage of all of our services nationwide. We, China Mobile and China Telecom are the three major telecommunications operators in China. See *A. History and Development of the Company* *Restructurings of the Telecommunications Industry*.

In 2011, 3G business became the largest driver of our revenue growth. The total number of our 3G subscribers increased significantly from 14.06 million as of December 31, 2010 to 40.02 million as of December 31, 2011, and service revenue from our 3G business increased significantly from RMB11.60 billion 2010 to RMB32.74 billion in 2011. As a percentage of our total service revenue from mobile business, service revenue from 3G business increased from 14.1% in 2010 to 31.7% in 2011. In addition, our fixed-line broadband business continued to grow rapidly. Service revenue from fixed-line broadband business increased by 18.1% compared with 2010, accounting for 43.2% of total service revenue from the fixed-line business (excluding fixed-line upfront connection fees of RMB192 million and RMB15 million in 2010 and 2011, respectively).

**Table of Contents****Mobile Business**

Our mobile business consists of GSM and 3G mobile business. Our mobile business revenue, subscribers and usage maintained growth in 2011, primarily driven by the growth of our 3G mobile business. As of December 31, 2011, we had a total of 199.7 million mobile subscribers, representing a 19.3% increase from 167.43 million as of December 31, 2010. Revenue from our mobile business was RMB126.53 billion in 2011, of which, service revenue of our mobile business increased by 25.3% from RMB82.45 billion in 2010 to RMB103.31 billion in 2011, accounted for 50.3% and 55.6% of our total service revenue in 2010 and 2011, respectively (excluding fixed-line upfront connection fees of RMB192 million and RMB15 million in 2010 and 2011, respectively).

The following table sets forth selected historical information for our mobile operations and our subscriber base for the periods indicated.

	As of or for		
	the year ended December 31,		
	2009 <sup>(1)</sup>	2010 <sup>(1)</sup>	2011 <sup>(1)</sup>
Number of subscribers (in thousands)	147,587	167,426	199,660
Estimated market share in our service areas <sup>(2)</sup>	19.8%	19.5%	20.2%
Average minutes of usage per subscriber per month (MOU) <sup>(3)</sup>	253.1	280.5	303.8
Average revenue per subscriber per month (ARPU) (in RMB) <sup>(4)</sup>	41.6	43.7	47.3

(1) Including our 3G business which we launched on a trial basis in May 2009 and began operating on a commercial basis in October 2009.

(2) Market share in a given area is determined by dividing the number of our mobile subscribers in the area by the total number of mobile subscribers in the area.  
*Source: MIIT.*

(3) MOU is calculated by dividing the total minutes of usage during the period by the average number of our mobile business subscribers during the period, and dividing the result by the number of months in the relevant period.

(4) ARPU is calculated by dividing the sum of revenue of mobile business during the relevant period by the average number of our mobile business subscribers during the period, and dividing the result by the number of months in the period.

Our total number of mobile subscribers increased by 19.3% from 167.43 million as of December 31, 2010 to 199.7 million as of December 31, 2011, which was mainly due to the increase in our 3G subscribers. The MOU of our mobile business increased from 280.5 minutes in 2010 to 303.8 minutes in 2011, which was mainly because the subscribers of our 3G business, which has significantly higher MOU than our GSM business, has increased as a percentage of the total number of our mobile subscribers. The overall ARPU of our mobile business increased by 8.2% from RMB43.7 in 2010 to RMB47.3 in 2011 despite the ARPU of each of our GSM and 3G businesses continued to decrease in 2011 compared to 2010. This was mainly due to the continuing change of revenue mix between our GSM business and 3G business. 3G business has a significantly higher ARPU than GSM business. As the service revenue from 3G business increased significantly as a percentage of total service revenue from the mobile business from 14.1% in 2010 to 31.7% in 2011, the overall ARPU of our mobile business increased.

**3G Mobile Business**

In January 2009, our parent company, Unicom Group, received a 3G license to operate a 3G business based on the WCDMA technology nationwide in China and, with the approval of the MIIT, authorized our major wholly-owned subsidiary, CUCL, to operate this business. We launched our 3G operations on a trial basis in 55 cities in China under the brand **WO** in May 2009 and began commercial 3G operations in 285 cities in China on October 1, 2009. Our 3G mobile business primarily consists of 3G voice business and 3G non-voice business. Our 3G voice business enables our subscribers to make and receive phone calls with a mobile handset at any point within the coverage area of our mobile telecommunications networks. Our 3G non-voice services primarily include wireless Internet, mobile TV, mobile reading, **WO App Store**, **WO**



Friend and other wireless information services.

*Subscriber.* Our total number of 3G subscribers increased significantly from 14.06 million as of December 31, 2010 to 40.02 million as of December 31, 2011 (which includes 3.80 million wireless data card subscribers). The increase was primarily due to our active sales and marketing efforts, including expanding our sales channels, improving our sales and marketing strategies, diversifying our 3G tariff plans and product offerings, and adjusting and optimizing our subsidy policies for 3G handsets.

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*MOU and ARPU.* With respect to our 3G mobile business, MOU decreased by 2.7% from 653.2 minutes in 2010 to 635.3 minutes in 2011 and ARPU decreased by 11.3% from RMB124.0 in 2010 to RMB110.0 in 2011. The decrease in our MOU and ARPU is mainly attributed to (i) our business strategy to lower the thresholds of the 3G tariff plans and increase the number of our subscribers, which resulted in an increased proportion of new subscribers who are users with lower usage of telecommunications services, and (ii) the intensified competition among the telecommunications operators in China.

*3G Voice Business.* The total 3G voice usage increased from 55.47 billion minutes in 2010 to 169.5 billion minutes in 2011, primarily as a result of the increase in our 3G subscribers.

*3G Non-Voice Business.* The average data usage per subscriber per month with respect to our 3G mobile business increased from 178M in 2010 to 267.2M in 2011, which was largely due to the popularity of smartphones, our innovation efforts in developing new applications, our promotion of subscribers' data usage and our promotional activities for data and information services. As of December 31, 2011, we had 3.50 million registered subscribers of *WO App Store* and 1.20 million registered subscribers of *WO Friend* (an instant communication tool).

### ***GSM Mobile Business***

Our GSM mobile business primarily consists of GSM voice business and non-voice business. Our GSM voice business enables our subscribers to make and receive phone calls with a mobile handset at any point within the coverage area of our mobile telecommunications networks and includes local calls, domestic long distance calls, international long distance calls, intra-provincial roaming, inter-provincial roaming and international roaming. Our GSM non-voice services include mobile Internet, SMS, *Cool Ringtone* (a personalized ring-back tone service) and other wireless information services.

*Subscriber.* Our total number of GSM mobile subscribers increased by 4.1% from 153.37 million as of December 31, 2010 to 159.64 million as of December 31, 2011. We believe that this growth was attributable to a number of factors, including, among others, (i) the continued growth of the Chinese mobile telecommunications market, driven by domestic economic growth and reduction in the cost of mobile handsets and services, and (ii) our sales and marketing efforts in retaining existing subscribers and expanding our subscriber base, including through service bundling.

*MOU and ARPU.* With respect to our GSM mobile business, MOU decreased by 2.3% from 262.9 minutes in 2010 to 256.9 minutes in 2011, and ARPU decreased by 5.3% from RMB39.5 in 2010 to RMB37.4 in 2011. The decrease in our MOU and ARPU was primarily attributable to the fact that a significant portion of our new users consists of users from rural areas, many of whom tend to have less usage of telecommunications services and to be more cost-sensitive than users from urban areas, and the decrease in our ARPU was also as a result of our decreased effective tariffs, which were caused mainly by the intensified competition among the telecommunications operators in China and downward adjustments on tariffs by the PRC Government.

*GSM Voice Business.* The total voice usage of our GSM mobile services increased by 2.9% from 471.00 billion minutes in 2010 to 484.76 billion minutes in 2011, which was primarily due to the increase in our GSM mobile subscribers and the migration of certain mid- and high-end GSM subscribers to 3G network.

*GSM Non-Voice Business.* Our GSM mobile Internet subscribers increased by 14.0% from 55.81 million as of December 31, 2010 to 63.60 million as of December 31, 2011, representing an increase in the penetration rate from 36.4% to 39.8%. The total number of our subscribers to *Cool Ringtone* service decreased by 12.5% from 67.26 million as of December 31, 2010 to 58.84 million as of December 31, 2011, representing a decrease in the penetration rate from 43.9% to 36.9%. A total of 74.84 billion SMSs were transmitted by our GSM mobile subscribers in 2011, representing a decrease of 4.4% compared to 2010.

### ***Fixed-Line Business***

We are a leading fixed-line broadband and communications operator in northern China. Following our merger with China Netcom in October 2008, which previously provided mainly fixed-line services in 10 provinces in northern China, and our acquisition of the fixed-line business in 21 provinces in southern China from our parent companies in January 2009, we offer a wide range of fixed-line services nationwide in China, including (i) fixed-line broadband services and data communications services, (ii) fixed-line voice services, include local and long distance fixed-line voice services and value-added services and (iii) other services.

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In 2011, we achieved continued growth in fixed-line broadband and data communications business, which was primary due to the upgrade of our fixed-line broadband network that increases access speed and the development of content and application services. However, the trend of mobile services substitution of fixed-line voice services had a continuing negative impact on our fixed-line voice business. Excluding fixed-line upfront connection fees of RMB192 million and RMB15 million in 2010 and 2011, respectively, our revenue from fixed-line business was RMB81.69 billion in 2011, of which service revenue from our fixed-line business increased by 2.4% from RMB79.75 billion in 2010 to RMB81.63 billion in 2011, accounted for 48.7% and 43.9% of our total service revenue in 2010 and 2011, respectively.

**Fixed-Line Broadband Services and Data Communications Services***Fixed-Line Broadband Services*

Fixed-line broadband services are one of our emphases as part of our strategy to focus on high growth services. The growth in fixed-line broadband business has been driven by the increasing affordability and rising use of personal computers and other Internet access devices, gradual recognition by businesses of the importance of information and the proliferation of content and applications, such as online games and video-on-demand. We are a leading provider of fixed-line broadband services in our fixed-line northern service region and we seek to maintain this leading position by capitalizing on our extensive fixed-line network, large customer base, experienced sales force, established brand and strategy of multi-service bundling.

In 2011, we further upgraded our broadband network and improved access speed. As of December 31, 2011, our fixed-line broadband subscribers increased by 17.8% to 55.65 million, of which subscribers with 2M-and-above bandwidth accounted for 91.8% of all fixed-line broadband subscribers, representing an increase of 5 percentage points from the end of 2010, and subscribers with 4M-and-above bandwidth accounted for 41.3% of all fixed-line broadband subscribers, representing an increase of 11.7 percentage points from the end of 2010. We also continued implementing our marketing strategy to offer integrated broadband services with increased-speed and enhanced customer service. The total number of our subscribers of broadband content and applications reached 20.25 million, accounting for 36.4% of all fixed-line broadband subscribers. Our broadband ARPU decreased by 1.2% from RMB57.1 in 2010 to RMB56.4 in 2011, primarily due to intensified competition from other PRC telecommunications operators.

The following table sets forth the information of our fixed-line broadband subscribers as of the dates indicated:

	2009	As of December 31, 2010	2011
Number of fixed-line broadband subscribers (in thousands)	38,550	47,224	55,651

*Data Communications Services*

We are a leading provider of data communications services in our fixed-line northern service region. We offer managed data products, such as those based on digital data networks, or DDN, frame relay, asynchronous transfer mode, or ATM, and Internet protocol-virtual private network, or IP-VPN. We also offer leased line products, including domestic and international leased circuits. Our customers for these services include government entities, large financial institutions and other domestic and multinational businesses, Internet service providers and other telecommunications operators. As of the end of 2011, we have established business cooperation relationships with more than 170 overseas operators and multinational corporate customers to provide various international data communications products and services, such as international voice and data services. In 2011, we continued to offer full-scale data communications services to international operators and domestic and international corporate customers. We have also improved our capabilities to offer cross-border data communications and integrated information services.

**Table of Contents****Fixed-Line Voice Business**

Our fixed-line voice services consist of local voice, domestic long distance, international long distance, value-added, interconnection and PHS services. As domestic mobile operators launched service packages at competitive prices, mobile roaming tariffs were lowered, and the migration of voice usage from fixed-line to mobile continued. In 2011, leveraging on our company's full-service advantage, we enhanced market development in areas of customer premises network, or CPN, and rural markets, as well as strengthened the marketing of integrated services. For example, we actively promoted bundled products and services marketed under the brand *WO Family*. As of December 31, 2011, the number of our *WO Family* subscribers increased by 7.98 million to 8.38 million, which resulted in an increase of 2.2% in the number of our residential, business and public telephone fixed-line voice subscribers from December 31, 2010.

As of December 31, 2011, the number of our fixed-line subscribers (including PHS subscribers) decreased by 3.9% to 92.85 million from 96.64 million as of December 31, 2010. The decrease was primarily due to a decrease in the number of our PHS subscribers. The following table sets forth the information of our fixed-line subscribers as of the dates indicated:

	2009	As of December 31, 2010		2011
		(in thousands)		
<b>Number of fixed-line subscribers<sup>(1)</sup></b>				
Residential	61,733	59,681		59,363
Business	14,238	15,494		17,723
PHS	18,742	13,423		7,787
Public telephones	8,109	8,037		7,968
Total	102,822	96,635		92,851

(1) Fixed-line subscribers consist of all local access lines in service as well as PHS subscribers. We calculate PHS subscribers based on the number of active telephone numbers for our PHS services. In cases where a PHS subscriber uses the same telephone number as an access line in service, the designation as a PHS subscriber or access line in service depends on which service is first activated. We increase our total number of fixed-line subscribers as soon as practicable after activation of the service. We remove a fixed-line subscriber from the total number of fixed-line subscribers as soon as practicable after the fixed-line subscriber deactivates the service voluntarily or three months after the date on which the fixed-line subscriber's bill becomes overdue.

The PRC Government issued a policy in January 2009 requiring the current wireless access systems operating on the spectrum used by PHS services to be cleared and removed from such spectrum within three years. As a result, the number of our PHS subscribers significantly decreased over the past few years.

**Local Voice Services**

As a result of mobile substitution, our fixed-line local voice traffic has continued to decrease in recent years. As fixed-line broadband business further develops, our Internet dial-up usage has also continued to decrease. The following table sets forth information regarding usage of our local voice services for the periods indicated:

	For the Year Ended December 31,		
	2009	2010	2011
<b>Usage of local calls (pulse in millions)<sup>(1)</sup></b>			
Total usage	188,116	156,724	125,944

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	<b>For the Year Ended December 31,</b>		
	<b>2009</b>	<b>2010</b>	<b>2011</b>
Internet dial-up usage	2,577	1,162	668
Total usage excluding Internet dial-up usage	185,539	155,562	125,275

(1) Pulses are the billing units for calculating local telephone usage fees.

*Long Distance Voice Services*

We offer traditional long distance services and VoIP long distance services. In recent years, due to the general decline of our fixed-line business and competition from software applications that allow users to make long distance calls over the Internet, our long distance business has been adversely affected.

The following table shows the total minutes of domestic long distance calls carried through our long distance networks for the periods indicated:

	<b>For the Year Ended December 31,</b>		
	<b>2009</b>	<b>2010</b>	<b>2011</b>
<b>Total minutes of domestic long distance calls (minutes in millions)<sup>(1)</sup></b>			
Traditional	21,261	17,349	14,033
VoIP	11,698	8,879	7,036
Total	32,959	26,228	21,069

(1) Includes calls originated by prepaid phone cards users and VoIP subscribers that are carried over our long distance networks.

The following table sets forth certain information related to the usage of our international long distance services for the periods indicated:

	<b>For the Year Ended December 31,</b>		
	<b>2009</b>	<b>2010</b>	<b>2011</b>
<b>International long distance outbound call minutes (minutes in millions)<sup>(1)(2)</sup></b>			
Traditional	221	269	214
VoIP	403	290	270
Total	624	559	484

(1) Includes calls originated by prepaid phone cards users and VoIP subscribers that are carried over our international long distance networks.

(2) Includes long distance outbound calls made to Hong Kong, Macau and Taiwan.

*Fixed-Line Value-Added Services*

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In addition to fixed-line telephone voice services, we offer a wide range of value-added services on our fixed-line networks. Our value-added services generate additional usage on our networks and increase our average revenue per fixed-line subscriber. Our major fixed-line value-added services include Personalized Ring and caller identification services. Personalized Ring services enable our fixed-line subscribers to personalize the ring-back tone for incoming calls. As the number of our fixed-line subscribers continued to decrease in the past few years, the number of customers using our fixed-line value added services also decreased correspondingly. As of December 31, 2011, the number of our Personalized Ring subscribers reached 21.09 million, representing a decrease of approximately 11.4% from the end of 2010. The penetration rate of caller identification services amounted to 67.52%, decreasing by 2.56 percentage point over that of 2010.

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### **Interconnection and Roaming Arrangements**

#### ***Interconnection***

Interconnection refers to the arrangements that permit the connection of our telecommunications networks with other networks. Our mobile and fixed-line networks interconnect with Unicom Group's networks. Under current arrangements, settlement between Unicom Group and us is based on an internal settlement standard that takes into account either the internal costs of the relevant networks or the government standard applicable between third-party operators, whichever is the more favorable to us.

We earn interconnection fees for terminating or transiting calls that originate from other domestic telecommunications operators' networks and pay interconnection fees to other operators for calls originating from our networks that are terminated on their networks. We earn and pay such fees in respect of mobile calls, local and domestic and international long distance calls and Internet services. We are required to pay the interconnection fees regardless of our ability or inability to collect the tariff from our subscribers. Interconnection charges are accrued on a monthly basis based on the actual call volume and applicable tariff rates.

All interconnection and settlement arrangements among domestic telecommunications operators in China are governed by the Telecommunications Regulations and the rules on interconnection arrangements and settlement promulgated by the MIIT. Some of the agreements pursuant to which we interconnect with other domestic operators were entered into by Unicom Group. We have entered into an agreement with Unicom Group pursuant to which we have agreed with Unicom Group that the costs and benefits arising under these agreements, as they relate to our operations, will be incurred to our account.

For additional information about our domestic and international interconnection arrangements, see **B. Business Overview** **Regulatory and Related Matters** under Item 4 and **B. Related Party Transactions** under Item 7.

#### ***Roaming***

We provide roaming services, which allow our subscribers to access our mobile services while they are physically outside of their registered service area or in the coverage areas of other mobile networks in other countries and regions with which we have roaming arrangements. As of March 31, 2012, we had roaming arrangements for (i) GSM international voice and SMS services with 552 operators in 246 countries and regions, (ii) GPRS international inbound data services with 456 operators in 196 countries and regions and for international GPRS outbound data services with 408 operators in 180 countries and regions, and (iii) 3G services with 293 WCDMA operators in 112 countries and regions.

A mobile subscriber using roaming services is charged at our roaming usage rate for both incoming and outgoing calls, plus applicable long distance tariffs. With respect to international roaming, we settle roaming charges with international operators in accordance with roaming agreements between Unicom Group and each of the international operators. See **B. Related Party Transactions** **Our Roaming Arrangements** under Item 7 for further information regarding prior roaming arrangements between Unicom Group and us.

#### **Networks**

We operate an advanced network system to support our integrated operations. The backbone of the system is a nationwide fiber optic transmission network, which serves as the common platform for our mobile, fixed-line telephone, broadband and data services. We generally utilize a centralized network planning and equipment selection process, which ensures uniform nationwide design and network compatibility. After our merger with China Netcom in October 2008, we have actively integrated our network resources to improve our network quality and capacity.

#### ***Mobile Networks***

Our mobile network generally consists of:

cell sites, which are physical locations, each equipped with a base station that houses transmitters, receivers and other equipment used to communicate through radio channels with subscribers' mobile handsets within the range of a cell;





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base station controllers, which connect to, and control, the base stations;

mobile switching centers, which control the base station controllers and the routing of telephone calls; and

a transmission network, which links the mobile switching centers, base station controllers, base stations and the public switched telephone network.

We have deployed GSM and WCDMA mobile networks. Our GSM mobile network mainly operates at 900 MHz. We have also deployed GSM technology that operates at 1800 MHz in major metropolitan areas to supplement the capacity of our existing mobile network. We use 2x6 MHz of spectrum in the 900 frequency band and 2x20 MHz of spectrum in the 1800 frequency band for our GSM network in most of our service areas. We use 2x15 MHz of spectrum in the 2100 frequency band for our WCDMA mobile network.

As of December 31, 2011, we had approximately 374,790 GSM base stations, representing an increase by 13.9% from December 31, 2010. The call-completion rate of our GSM service was 97.12% at the end of 2011 and the call-drop rate decreased to 0.25% at the end of 2011 from 0.32% at the beginning of 2011. We also completed the GPRS network upgrade and significantly improved the configuration of static packet data channels.

We have devoted significant resources in developing our 3G networks and have established one of the biggest WCDMA networks in the world. As of December 31, 2011, we had approximately 238,818 3G base stations, representing an increase of 30.6% from December 31, 2010. As of December 31, 2011, our 3G network coverage reached cities at county level and above throughout China as well as villages and towns in eastern and central developed areas of China. In addition, in 2011, we completed the upgrade of 3G networks to HSPA+ (i.e., evolved high-speed packet access) in 56 major cities in China.

### ***Fixed-Line Networks***

We operate fixed-line networks which provide extensive coverage in China. These networks are technologically advanced and conducive to the introduction of the next generation fixed-line network and 3G technologies. These networks support a wide range of end-to-end fixed-line telecommunications services and enable customized products to be delivered to meet a variety of telecommunications needs in real-time.

Our fixed-line networks consist of fixed-line telephone networks, broadband Internet and data networks, transmission networks, value-added service platforms, IT support systems and related infrastructures. Our transmission networks consist primarily of fiber-optic based networks, which cover our major service regions, supplemented by satellite transmission and digital microwave links.

We have integrated our resources to optimize and improve the transport capabilities of our IP networks and improved our long-distance soft-switch network capability. In addition, we have fully implemented the upgrade of broadband connection speed and our broadband network capacity was substantially enhanced. By the end of 2011, the number of fixed-line broadband access ports was 85.92 million, up by 30.5% from the end of 2010, of which the number of access ports with FTTH/B accounted for 45% of total broadband access ports. Our international Internet outbound bandwidth reached 467G, our submarine cable capacity reached 2,036G, and our international cross-continental cable capacity reached 2,468G.

### **Marketing, Sales and Distribution**

Our marketing strategy is to establish our image as a full-service telecommunications service provider and utilize our comprehensive services platform and nationwide sales and distribution network. We implement our marketing and sales strategies under a single unified brand WO and distribute our services through a variety of distribution channels, consisting of (i) self-owned channels, including proprietary sales outlets and direct sales forces targeting retail and corporate customers, (ii) social channels, including cooperative sales outlets, exclusive sales outlets and agency sales outlets, and (iii) electronic distribution channels, including self-owned and third-party channels online e-stores. In recent years, we have continued developing our self-owned sales channels and strategically expanding our social channels. In particular, for our 3G services, in addition to the full use of our self-owned channels, we have also focused on using high-quality social channels, such as large brand name electronics retail chains and electronics outlets in China, to achieve better sales results. Further, we continued promoting our nationwide e-sales system, which has effectively supplemented our traditional sales channels and improve our service quality.



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### **Customer Service**

We provide customer services through our nationwide sales outlets, hotline number 10010, VIP hotline number 10018, online sales outlets, SMSs, Wireless Application Protocol, or WAP, official micro blog and other channels. Our customer services typically include inquiries, service initiation and termination, sales and response to customer complaints and suggestions. Since 2009, we have provided 3G-dedicated customer service and have established over 300 WO brand stores to enhance our customers' experience. In recent years, we continued to improve our customer service quality and created 3G Customer Service Centers + VIP Customer Managers, a 3G-dedicated customer service model for our 3G subscribers.

### **Information Systems**

We have established comprehensive information systems in each province, autonomous region and municipality to support our business and management. For business support, we have established core systems composed of a customer relationship management system, a comprehensive billing and accounting system, a comprehensive settlement system and an operation analysis system to support services and marketing of our mobile and fixed-line businesses. For our management support, we have focused on developing a human resources management system and a financial management system to enhance the efficiency of our control and management over our resources. In 2011, we further promoted the establishment of integrated systems, such as an integrated business support system for corporate group customers, integrated channels management system and integrated account settlement system. We also started to build an electronic sales management system featuring full services and an integrated data analysis system. Meanwhile, we focused on establishing a comprehensive enterprise resource planning system to optimize our resource allocations and enhance our operational efficiency.

### **Research and Development**

We focus on technology innovation in coordination with our various business departments in order to provide technical support to the development of our various businesses. Our research and development activities are focused primarily on 3G technologies and their further development, next generation Internet technologies and businesses, operational planning and development of value-added services. In addition, part of our research and development requirements is fulfilled by our parent company, Unicom Group, in return for a service fee. See B. Related Party Transactions under Item 7 below. With respect to research and development for our broadband business, we mainly rely on Unicom Group's National Laboratory of Next Generation Network in Broadband Application, which is China's first national level engineering laboratory in the information and telecommunications industry, focusing on the research of next generation Internet IPv6, Triple-Play and 3G operating and supporting systems. We also participate in the national research project on LTE and closely follow the development of LTE technologies and standards. We have applied for a number of patents and software copyrights in China.

### **Competition**

As a result of the telecommunications industry restructuring in 2008, the Chinese telecommunications market now has three key providers of basic telecommunications service—China Telecom, China Mobile and us—in addition to thousands of value-added service providers. We compete with China Mobile and China Telecom in virtually all aspects of our business, including mobile services, fixed-line voice services, broadband services and data communications services. We believe that the telecommunications industry restructuring in 2008 has provided an opportunity for us to integrate our various resources with those of China Netcom to create business synergies for the post-merger Unicom. However, we also believe that the restructuring may cause the competition in the telecommunications industry in China to be more intensified and complex in the future. In particular, as 3G business in China has experienced rapid growth since 2009 and has become a main growth driver for us and our major competitors, the competition in 3G business has intensified in recent years. We are also expected to face intensive competition in the next generation telecommunications business when the relevant technologies become mature and commercialized. See D. Risk Factors—Risks Relating to Our Business. We face intense competition in all our businesses from other telecommunications service providers, including China Mobile and China Telecom, which may materially adversely affect our financial condition, results of operations and growth prospects. under Item 3.

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### **Strategic Alliances with Telefónica**

On January 30, 2009, we entered into a strategic alliance framework agreement with Telefónica. Pursuant to the framework agreement, Telefónica and we agreed to share business experience and strengthen cooperation in the areas of mobile communications, broadband applications, international business, marketing and sales and telecommunications services to corporate clients. On September 6, 2009, we entered into a strategic alliance agreement with Telefónica, pursuant to which Telefónica and we agreed to establish a strategic alliance to strengthen the business of each party by cooperation based on our respective networks, business models and experience. On October 21, 2009, we and Telefónica completed a mutual investment in the amount of the equivalent of US\$1 billion in each other, which was implemented by way of the subscription by Telefónica of 693,912,264 new shares in our Company and the contribution by Telefónica of 40,730,735 treasury shares in the capital of Telefónica to us.

On January 23, 2011, we entered into the Agreement to Enhance the Strategic Alliance with Telefónica. Pursuant to this agreement, we acquired from Telefónica 21,827,499 ordinary shares in the capital of Telefónica for aggregate purchase price of Euro374,559,882.84 on January 25, 2011, and Telefónica, through its wholly-owned subsidiary, Telefónica International, acquired 282,063,000 ordinary shares in the capital of our company for aggregate consideration of approximately US\$500,000,000 in several transactions executed in the period between January 25, 2011 and September 7, 2011. In addition, Chang Xiaobing, our Chairman and Chief Executive Officer, as our designated representative, was appointed in May 2011 as a director on the board of directors of Telefónica.

### **Trademarks**

We conduct our businesses under the Unicom name and logo. Unicom Group is the registered proprietor in China of the Unicom trademark in English and the trademark bearing the Unicom logo. Unicom Group is also the registered proprietor of the trademark of the word Unicom in Chinese ( ). Unicom Group has granted us the right to use these trademarks on a royalty-free basis with periodic renewals, and licensed us any trademark that it registers in China in the future which incorporates the word Unicom.

### **Regulatory and Related Matters**

The telecommunications industry in China is subject to a high degree of government regulation. The primary regulatory authority of the Chinese telecommunications industry is the MIIT, established in 2008 as a new ministry under the PRC State Council and the successor of the former Ministry of Information Industry. The NDRC, the Ministry of Commerce and other governmental authorities also maintain regulatory responsibilities over certain aspects of the Chinese telecommunications industry.

The MIIT, under the supervision of the State Council, is responsible for, among other things:

formulating and enforcing industry policies and regulations, as well as technical standards;

granting telecommunications service licenses;

supervising the operations and quality of services of telecommunications service providers;

allocating and administering telecommunications resources such as spectrum and number resources;

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together with other relevant regulatory authorities, formulating tariff standards for telecommunications services;

formulating interconnection and settlement policies between telecommunications networks; and

maintaining fair and orderly market competition among service providers.

The MIIT has established a Telecommunications Administration in each province, autonomous region and municipality, which is mainly responsible for overseeing the implementation of the MIIT's policies and regulations and exercising regulatory authority delegated by the MIIT within that province, autonomous region or municipality.

The NDRC, together with the MIIT, sets government fixed tariffs and government guidance tariffs for certain telecommunications services. See *Tariff Setting and Price Controls* below.

The MIIT is in the process of drafting a telecommunications law that, once adopted by the National People's Congress of the PRC, will become the basic telecommunications statute and provide the principal legal framework for telecommunications regulations in China. It is currently uncertain when the law will be adopted and become effective. See *D. Risk Factors - Risks Relating to the Telecommunications Industry in China*. Regulatory or policy changes relating to the PRC telecommunications industry or any future industry restructuring may materially adversely affect our financial condition, results of operations and growth prospects. - under Item 3.

### ***Telecommunications Regulations***

On September 25, 2000, the PRC State Council promulgated the Telecommunications Regulations of the People's Republic of China, which came into effect on the same date. All telecommunications activities and related activities within China are subject to the Telecommunications Regulations.

According to the PRC Government, its administration and regulation of the Chinese telecommunications industry is based on the principles of the separation of governmental regulation from enterprise management, the elimination of monopolistic behavior, the encouragement of competition and the promotion of the development of the Chinese telecommunications industry, while also taking into account the principles of openness, equality and fairness. The Telecommunications Regulations regulate all major aspects of the telecommunications industry, including licensing, interconnection, tariffs, resources, services, security, facility construction and access to networks.

### ***Licensing***

The PRC Government licenses telecommunications businesses in accordance with their classification. Telecommunications businesses are currently classified into two broad categories of basic services and value-added services. An appendix to the Telecommunications Regulations divides each of the two categories into further sub-categories. On March 21, 2003, the former Ministry of Information Industry amended the categorization in this appendix and the amendments took effect on April 1, 2003. According to the amended appendix:

basic telecommunications services are classified into Category I basic telecommunications services and Category II basic telecommunications services. Category I basic telecommunications services include fixed-line telecommunications services (including fixed-line local, domestic long distance, international long distance and IP telephone services and services related to maintaining international telecommunications facilities), mobile telecommunications services (including 900/1800MHz GSM 2G, 800MHz CDMA 2G and 3G digital cellular mobile telecommunications services), Category I satellite telecommunications services (including satellite mobile telecommunications and international satellite private-line services) and Category I data communications services (including Internet data transmission, international data telecommunications, public telegraph and telex services). Category II basic telecommunications services include trunking telecommunications services (including analogue trunking telecommunications and digital trunking telecommunications services), wireless paging services, Category II satellite telecommunications services (including lease and sales of satellite transponders and very-small-aperture-terminal, or VSAT, telecommunications services), Category II data telecommunications services (including fixed-line domestic and wireless data transmission services), network access services (including wireless network access services and network services from customer premises), services related to maintaining domestic telecommunications facilities and network hosting services.



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value-added telecommunications services are classified into Category I value-added telecommunications services and Category II value-added telecommunications services. Category I value-added telecommunications services include on-line data processing and interchange, domestic multi-party telecommunications, IP-VPN and Internet data center, or IDC, services. Category II value-added telecommunications services include store-and-forward, call center, Internet access and information services.

On March 1, 2009, the MIIT promulgated the Measures on the Administration of Telecommunications Business Licenses, which took effect on April 10, 2009 and superseded the previous measures promulgated by the former Ministry of Information Industry on December 26, 2001.

The measures govern the application for, approval of and regulation of telecommunications business licenses in China. The operation of any basic telecommunications business is subject to the MIIT's approval and grant of License for Operation of Basic Telecommunications Businesses. The operation of any value-added business in two or more provinces, autonomous regions or municipalities is subject to the MIIT's approval and grant of License for Inter-Provincial Operation of Value-Added Telecommunications Businesses. The operation of value-added businesses within a single province, autonomous region or municipality is subject to the approval of the telecommunications authority of the relevant province, autonomous region or municipality and the grant of the License for Operation of Value-Added Telecommunications Businesses. The measures, among other things, lowered the minimum amount of registered capital required for an applicant to enter the basic telecommunications business in China.

After the PRC's accession to the WTO, on December 11, 2001, the PRC State Council promulgated the Administrative Regulations on Telecommunications Companies with Foreign Investments, which took effect on January 1, 2002, and were amended on September 10, 2008, to implement China's commitments to the WTO. Those commitments include the gradual reduction of restrictions on foreign ownership in telecommunications enterprises in China and the step-by-step opening up of the Chinese telecommunications market to foreign enterprises. In recent years, China gradually lifted restrictions for foreign investors in telecommunications enterprises in China and fulfilled its commitment to open up the Chinese telecommunications market. However, the following restrictions on investments in mobile, value-added telecommunications and fixed-line businesses remain:

for fixed-line services, there is no longer any geographic restriction and foreign ownership may be no more than 49%;

for mobile voice and data services, there is no longer any geographic restriction and foreign ownership may be no more than 49%; and

for value-added telecommunications services, there is no longer any geographic restriction and foreign ownership may be no more than 50%.

***Spectrum and Network Number Resources***

The MIIT is responsible for the management of the wireless radio frequency spectrum and the allocation of frequencies within the spectrum. The frequency assigned to a telecommunications operator may not be leased or transferred without the MIIT's approval. Standard fees for usage of the frequencies assigned to cellular telecommunications are charged to telecommunications operators: (i) for the nationwide GSM network frequency, an annual rate of RMB17 million per MHz is charged for the 900MHz band and an annual rate of RMB15 million per MHz is charged for the 1800 MHz band; (ii) for the nationwide WCDMA network frequency, a standard fee at an annual rate of RMB3.75 million per MHz in 2011, RMB7.5 million per MHz in 2012, RMB11.25 million MHz in 2013 and RMB15 million per MHz in 2014 and onwards will be charged for the 2100 MHz band; (iii) for the Femtocell experimental frequency, an annual rate of 20% of RMB15 million per MHz will be charged for the 2100 MHz band from 2011; and (iv) for any local telecommunications network frequency, an annual rate of RMB1.7 million per MHz is charged for each province for the 900 MHz band, an annual rate of RMB1.5 million per MHz is charged for each province for the 1800 MHz band and an annual rate of RMB1.5 million will be charged for each province for the 2100 MHz band.

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The MIIT is also responsible for the administration of China's telecommunications network number resources. The telecommunications network number resources are owned by the State, which shall charge fees for the use of such resources. Application for the use of number resources by any telecommunications operator is subject to the approval of the MIIT or the relevant provincial telecommunications authority and the payment of certain usage fees. The measures also provide for the procedures for the application, usage and record keeping for the telecommunications operators' use of number resources.

***Tariff Setting and Price Controls***

The levels and categories of our current tariffs are subject to regulation by various government authorities, including the MIIT, the NDRC, and, at the local level, the relevant provincial Telecommunications Administration Bureaus and price regulatory authorities. Under the Telecommunications Regulations, telecommunications tariffs are categorized into State-fixed tariffs, State-guidance tariffs and market-based tariffs.

The monthly fee and local usage fee for mobile services are regulated as State-fixed tariffs. Leased line and data services (other than ATM service) are charged at State-guidance tariffs, which are determined jointly by the MIIT and the NDRC. Pursuant to the Notice on Adjustment to Tariff Management for Local Fixed-Line Telephone Services issued by the MIIT in 2009, the monthly fee and usage fee for local fixed-line telephone services (including PHS) as well as the long-term leasing fees for circuits leasing are subject to certain tariff ceiling. Domestic long distance services, international long distance services and Hong Kong, Macau and Taiwan long distance services are also currently subject to tariff ceiling.

The Notice on Implementation of Market-Based Tariffs for Certain Telecommunications Services, promulgated jointly by the former Ministry of Information Industry and the NDRC in 2002, specifies the telecommunications businesses to which market-based tariffs are applicable, including VoIP, Internet access services, and certain value-added services provided over fixed-line telephone networks, such as telephone information, caller identification and voice mail. Market-based tariffs shall be applicable to those telecommunications services for which effective competition exists in the market. The tariffs of such telecommunications services are determined at the sole discretion of the operators, and will be implemented after filing with the MIIT or provincial Telecommunications Administration Bureaus, as applicable. There is uncertainty regarding how the MIIT determines the existence of effective competition, as the MIIT has not publicly disclosed the criteria it uses for determining whether a certain type of service should be subject to market-based tariffs. Under the Telecommunications Regulations, cost is the primary basis for tariff setting, but the tariff levels also take into account social and economic development, the development of the telecommunications industry and the purchasing power of the customers. The MIIT has not provided a timetable for tariff deregulation or indicated that operators will eventually be permitted to freely set all tariffs. We expect that increased flexibility in setting certain tariffs will allow us to better respond to changes in market demand and competitive conditions.

The PRC Government retains the ultimate authority to adopt changes to tariffs. However, the Telecommunications Regulations require the government to hold public hearings before setting or changing important State-tariff rates, which are attended by telecommunications operators, consumers and others. Operators are required to provide complete and adequate cost data and other materials for those hearings.

The following tables set forth the tariff rates of certain services provided by us, where government fixed tariffs or government guidance tariffs are applicable:

***Mobile Business***

Generally the categories of tariffs we charge our mobile subscribers include, among others, basic monthly fees and local usage charges, roaming charges, long-distance call charges and charges for value-added services. Mobile tariffs are set forth by the MIIT and tariff adjustments are subject to regulation by various government authorities, including the MIIT, the NDRC and the relevant provincial price regulatory authorities. The following table summarizes the current tariffs for post-paid and pre-paid mobile services:

	<b>Post-paid Services (RMB)</b>	<b>Pre-paid Services (RMB)</b>
Basic monthly fee	45-50	0
Local usage charge (per minute)	0.36-0.40	0.54-0.6
Domestic roaming charge (per minute)	0.6 for caller 0.4 for receiver	0.6 for caller 0.4 for receiver





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Intensified competition in our mobile service areas has resulted in tariff discounts and service promotions offered by us and our main competitors from time to time, which may reduce the effective tariffs. These discounts and promotions have taken many forms, including promotional tariff rates, free call minutes, reduced roaming charges, off-peak discounts or discounts for high-usage subscribers and package service plans with fixed monthly fees.

We have introduced a number of package service plans. Under these plans, subscribers typically pay a fixed monthly fee for a specified number of call minutes. The plans vary at the levels of fixed monthly fee, number of specified call minutes and tariff rates for call minutes in excess of the specified call minutes. The terms of these plans also vary depending on the local markets.

In 1997, the PRC Government granted us preferential treatment by allowing us to reduce our tariffs by up to 10% below the State-guidance tariff rates. In the past, this preferential treatment has helped us capture a significant number of mobile subscribers by allowing us to market our mobile services at discounted rates. As we and our main competitors introduced various package service plans and other promotional programs, the tariff structure has become more complex, which, to some extent, has made our price advantages less obvious to subscribers compared to previous tariffs that were largely based on simple per-minute charges.

*Fixed-Line Voice Business*

For our local voice services, we charge an installation and testing fee that varies depending on whether the subscriber is a residential or a business customer, a fixed monthly fee, local call usage fees based on call duration and fees for certain value-added services. For our domestic long distance services, our revenue from domestic long distance services consist of charges based on the duration, time of day and day of the week a call is placed. In addition, we currently charge RMB0.30 per minute in addition to a long distance fee for our VoIP domestic long distance services. For our international long distance services, our charges are subject to the maximum tariffs regulated by the MIIT.

The following table sets forth our current tariffs for (i) local voice services provided on our traditional and PHS network, (ii) domestic long distance telephone services using our traditional network and (iii) our international long distance telephone services using our traditional network:

<b>Local Voice Services</b>	<b>Tariff (RMB)</b>
<b>Monthly fee:</b>	
Residential subscribers in:	
Provincial capitals	20.00 to 25.00
Other cities and counties	12.00 to 18.00
Rural areas	10.00 to 15.00
Business subscribers	25.00 to 35.00
<b>Usage fee:</b>	
Intra-district	0.18 to 0.22 for the first two pulses (first three minutes or less) and 0.09 to 0.11 for each additional pulse (one minute intervals)
Inter-district	up to 0.30 per pulse (one minute intervals)
<b>Communication fee:</b>	
Internet dial-up	0.02 per pulse (one minute intervals)
<b>Domestic long distance services on our traditional network<sup>(1)</sup></b>	<b>0.07 per six seconds</b>
<b>International long distance services on our traditional network<sup>(1)</sup>:</b>	
To Hong Kong, Macau and Taiwan	0.20 per six seconds
To all international destinations	0.80 per six seconds

(1) Subject to filing with the provincial telecommunications administrations, our provincial level headquarters may apply a 10% to 50% discount rate to calls made during off-peak hours.



**Table of Contents***Managed Data Services*

The PRC Government publishes guidance tariffs for certain managed data services, including DDN and frame relay services, provided by operators in China. Tariffs for our ATM services are determined at our discretion, subject to approval by the MIIT. An installation and testing fee is generally charged for installation and testing for our data services, as well as a fixed monthly fee for each of the services.

DDN services. The following table sets forth the monthly fees for DDN services at the bandwidths of 64kbps, 128kbps, 512kbps and 1Mbps:

	Monthly Fee			
	64kbps	128kbps	512kbps	1Mbps
	(RMB)			
Intra-district	1,500	2,000	3,800	5,000
Inter-district	2,000	2,500	5,200	7,500
Domestic long distance	3,500	5,000	7,000	9,000

Frame relay services. The following tables set forth the monthly fees for frame relay services, which include monthly fees for port access and permanent virtual circuits, or PVCs<sup>(1)</sup>:

	Monthly Fee			
	64kbps	256kbps	512kbps	1Mbps
	(RMB)			
Port access				
Monthly fees	260	400	500	750
PVC				
Intra-district	550	800	1,000	1,250
Inter-district	800	1,150	1,450	2,000
Domestic long distance	1,700	2,200	2,500	3,000

(1) One-way tariff for PVCs frame relay services.

*Leased Line Services*

We charge monthly fees for subscribers to our leased line services based on guidance tariffs set by the PRC Government, which vary based on bandwidth and whether the leased line is local or long distance. Leased line tariffs have generally decreased in recent years.

The following table sets forth the tariffs for 2Mbps, 8Mbps, 34Mbps and 155Mbps digital circuits:

	Monthly Fee			
	2Mbps	8Mbps	34Mbps	155Mbps
	(RMB)			
Intra-district	2,000	6,000	16,000	44,000
Inter-district	4,000	11,000	31,000	88,000
Domestic long distance <sup>(1)</sup>	6,000	17,000	47,000	132,000

(1) Does not include the tariffs for local digital circuits and access lines.

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In October 2003, the former Ministry of Information Industry issued Measures on Settlement of Interconnection between Public Telecommunications Networks and Sharing of Relaying Fees, which superseded the Measures on the Settlement of Call Charges between Telecommunications Networks issued by the former Ministry of Information Industry in 2001. These regulations contain specific provisions regarding, among other things, revenue sharing methods and settlement mechanisms and interconnection agreements among telecommunications service providers. Since November 2005, the former Ministry of Information Industry (or the MIIT after March 2008) has issued a number of administrative measures to adjust the settlement arrangement standards with respect to interconnection fees for certain network interconnections between telecommunications operators. In accordance with various administrative measures, Unicom Group or we, as the case may be, have entered into agreements on interconnection with other telecommunications operators, including China Telecom and China Mobile.

The following table sets forth selected interconnection revenue sharing and settlement arrangements for local calls:

<b>Operator from Whose Network Calls are Originated</b>	<b>Operator at Whose Network Calls are Terminated</b>	<b>Current Main Settlement Arrangement</b>
Mobile operator	Local fixed-line operator	(1) Mobile operator collects the usage fees from its subscribers;  (2) Mobile operator pays RMB0.06 per minute to local fixed-line operator. For calls originated from 157 or 188 prefix phone numbers (TD users) during the period from January 1, 2010 to December 31, 2010, mobile operator (China Mobile) pays RMB0.012 per minute to fixed-line operator. From January 1, 2011, for calls originated from 157 or 188 prefix phone numbers (TD users), mobile operator (China Mobile) continues to pay RMB0.012 per minute to fixed-line operator.
Local fixed-line operator	Mobile operator	(1) Local fixed-line operator collects the usage charge from its subscribers;  (2) No revenue sharing or settlement prior to June 1, 2010. Local fixed-line operator pays RMB0.001 per minute to mobile operator after June 1, 2010.
Mobile operator A	Mobile operator B	(1) Mobile operator A collects the cellular usage charge from its subscribers;  (2) Mobile operator A pays RMB0.06 per minute to mobile operator B. For calls originated from 157 or 188 prefix phone numbers (TD users) during the period from January 1, 2010 to December 31, 2010, mobile operator A (China Mobile) pays RMB0.012 per minute to mobile operator B. For calls originated from 157 or 188 prefix phone numbers (TD users) during the period from January 1, 2011, mobile operator A (China Mobile) pays RMB0.012 per minute



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<b>Operator from Whose Network Calls are Originated</b>	<b>Operator at Whose Network Calls are Terminated</b>	<b>Current Main Settlement Arrangement</b>
Local fixed-line operator A	Local fixed-line operator B	<p>(1) Operator A collects the usage fees from its subscribers;</p> <p>(2) In the case of intra-district calls, operator A pays operator B 50% of the intra-district usage fees;</p> <p>(3) (i) In the case of local inter-district calls from operator A using operator B's local inter-district trunk circuit, operator A collects the usage charge from its subscribers and pays RMB0.06 per minute to operator B; (ii) In the case of local inter-district calls from operator A not using operator B's local inter-district trunk circuit, operator A collects the usage charge from its subscribers and pays operator B 50% of the intra-district usage fees.</p>

The following table sets forth selected current major main interconnection revenue sharing and settlement arrangements for domestic long distance calls:

<b>Operator at Whose Network Calls are Originated</b>	<b>Operator at Whose Network Calls are Terminated</b>	<b>Current Main Settlement Arrangement</b>
Local fixed-line or mobile operator A (through the long distance network of operator A) Fixed-line or mobile operator A	Local fixed-line or mobile operator B  Domestic long distance calls made without using the carrier identity code of operator B (through the long distance network of operator B)	<p>Operator A pays RMB0.06 per minute to operator B</p> <p>(1) Operator A collects the tariff from the subscribers;</p> <p>(2) If Operator A is a fixed-line operator, operator A retains RMB0.06 per minute; if operator A is a mobile operator, operator A retains local usage fee and RMB0.06 per minute; and</p> <p>(3) Operator A pays operator B the rest of the domestic long distance tariff.</p> <p>Note: Domestic long distance calls shall be charged at the domestic long distance call tariff of operator B.</p>
Local fixed-line or mobile operator A	Domestic long distance calls made by using the carrier identity code of operator B (through the long distance network of operator B)	<p>(1) Operator B collects the tariff from the subscribers; and</p> <p>(2) Operator B pays operator A RMB0.06 per minute.</p>



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The following table sets forth selected current main interconnection revenue sharing and settlement arrangements for public switched telephone network international long distance calls, including calls originated from and terminated in Hong Kong, Macau and Taiwan:

<b>Operator at Whose Network Calls are Originated</b>	<b>Operator at Whose Network Calls are Terminated</b>	<b>Current Main Settlement Arrangement</b>
Local fixed-line or mobile operator A	International long distance calls (including to Hong Kong, Macau and Taiwan) made without using the carrier identity code of operator B and directed by operator A from the originating network to operator B.	<p>(1) Operator A collects the tariff from the subscribers;</p> <p>(2) If operator A is a fixed-line operator, operator A retains no more than RMB0.54 per minute with the remaining paid to operator B; and</p> <p>(3) If operator A is local usage fees and a mobile operator, operator A retains local usage fees and no more than RMB0.54 per minute with the remaining paid to operator B.</p> <p>Note: International long distance calls shall be charged at the international long distance call tariff of operator B.</p>
Local fixed-line or mobile operator A	International long distance calls made by using the carrier identity code of operator B and through the domestic and international long distance networks of operator B.	<p>(1) Operator B collects the tariff from the subscribers; and</p> <p>(2) Operator B pays operator A RMB0.06 per minute.</p>

The following table sets forth selected current main interconnection revenue sharing and settlement arrangements for VoIP long distance calls:

<b>Operator from Whose Network Calls are Originated</b>	<b>Operator at Whose Network Calls are Terminated</b>	<b>Current Main Settlement Arrangement</b>
Fixed-line or mobile operator A	Fixed-line or mobile operator B through the VoIP network of operator C	<p>(1) Operator A collects local usage fees;</p> <p>(2) Operator C collects the VoIP long distance usage fees from its subscribers;</p> <p>(3) Operator C pays RMB0.06 per minute to operator B on the terminating end;</p> <p>(4) No settlement between operator C and operator A on the originating end.</p>

The following table sets forth selected current main interconnection revenue sharing and settlement arrangements for SMS:

<b>Network from Which SMS Originated</b>	<b>Network at Which SMS Terminated</b>	<b>Current Main Settlement Arrangement</b>
Fixed-line or mobile operator A	Fixed-line or mobile operator B	

(1) Operator A collects the tariff from its subscribers;

(2) Operator A pays RMB0.03 (RMB0.05 prior to January 1, 2010) per SMS to Operator B

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The following table sets forth selected current main interconnection revenue sharing and settlement arrangements for MMS:

<b>Network from Which MMS Originated</b>	<b>Network at Which MMS Terminated</b>	<b>Current Main Settlement Arrangement</b>
Fixed-line or mobile operator A	Fixed-line or mobile operator B	(1) Operator A collects the tariff from its subscribers;
		(2) Operator A pays RMB0.10 (RMB0.15 prior to January 1, 2010) per MMS to Operator B

***Technical Standards***

The MIIT is responsible for promulgating the technical standards for China's telecommunications industry and establishing the technical requirements and testing parameters for telecommunications equipment (including network and end user equipment). The MIIT is also responsible for designating qualified institutes to test telecommunications equipment, which would grant network access licenses (or product standard certificates) for the equipment that has successfully passed the relevant tests. Only telecommunications equipment for which a network access license (or a product standard certificate) has been granted may be sold and used in China.

Most of the standards used in the Chinese telecommunications industry are generally based on the standards issued by the International Telecommunication Union, or ITU, 3rd Generation Partnership Project, Open Mobile Alliance, World Wide Web Consortium, and other international organizations for telecommunications standards, with more specific requirements made in light of China's particular telecommunications industry. On the basis of the technical standards used in China's telecommunications industry, we may formulate our own technical standards based on our own needs and issue additional requirements for telecommunications equipment in order to meet our operational needs. All telecommunications equipment purchased by China's telecommunications operators must have been granted a network access license issued by the MIIT and must meet the standards set forth by the relevant operators.

***Quality of Service***

Under the Telecommunications Regulations, the MIIT and the relevant provincial telecommunications administrations are responsible for supervising and monitoring the quality of services provided by telecommunications operators in China. Under the Telecommunications Regulations, customers of telecommunications operators have the right to submit their complaints to the MIIT and the relevant provincial telecommunications administrations or other relevant government authorities. In addition, the MIIT, together with other governmental authorities, has taken measures to prompt telecommunications operators to screen indecent contents carried through their networks.

***Universal Services***

Telecommunications service providers in China are required to fulfill universal service obligations in accordance with relevant regulations to be promulgated by the PRC Government, and the MIIT has the authority to delineate the scope of its universal service obligations. The MIIT may also select universal service providers through a tendering process. The MIIT, together with the finance and pricing authorities, is also responsible for formulating administrative rules relating to the establishment of a universal service fund and compensation schemes for universal services. Under the Telecommunications Regulations, all PRC telecommunications operators shall provide universal services, and we expect to perform our duties thereunder accordingly.

The MIIT has required major Chinese telecommunications service providers, including Unicom Group and former Netcom Group, to participate in a project to provide telecommunications services in a number of remote villages in certain designated provinces in China as transitional measures prior to the formalization of a universal service obligation framework. In participating in this project, Unicom Group has undertaken the universal service obligation to extend telecommunications service coverage to all administrative-level villages primarily through its transmission networks. Currently, with our assistance, Unicom Group is further extending telecommunications service coverage to natural villages in remote areas in China as designated by the MIIT. We have been assisting Unicom Group in providing mobile telecommunications services to these remote villages and are responsible for the operation and maintenance of the relevant network facilities in our service areas. See

D. Risk Factors Risks Relating to the Telecommunications Industry in China The PRC Government may require us, along with other telecommunications service providers in China, to provide universal services with specified obligations, and we may not be compensated adequately for providing such services. under Item 3.



**Table of Contents*****Convergence Policy of Telecom, Broadcasting and Internet Networks***

In January 2010, the PRC Government announced its decision to accelerate the advancement of convergence of television broadcast, telecommunications and Internet access networks to realize interconnection and resource sharing among the three networks and further develop the provision of voice, data, television and other services. Specifically, the three-network convergence policy will be initially carried out on a trial basis in selective geographic locations during the period from 2010 to 2012 and further implemented across-the-board in the following three years. In June 2010, the PRC Government announced the first batch of cities in China where the three-network convergence policy is carried out on a trial basis. In December 2011, a total number of 44 cities were selected as the second batch of cities where the three-network convergence policy is carried out on a trial basis. The PRC Government may amend relevant policies or promulgate new regulations corresponding to the implementation of the three-network convergence policy in the future.

***Others***

As a company with substantially all of our operations in China, we, along with our controlling shareholder, Unicom Group, are subject to various regulations of the PRC Government in addition to those regulating the telecommunications industry. PRC regulatory authorities, such as the State Bureau of Taxation, National Audit Office, SAIC and local price bureaus, exercise extensive control over various aspects of our businesses and conduct various regular inspections, examinations and/or audits on us and Unicom Group. As required by the relevant PRC laws and regulations, Unicom Group, as one of the key State-owned enterprises under the direct supervision of the SASAC, is also subject to routine audits by the National Audit Office, or the NAO, including the senior management departure audit which involves a mandatory review by the NAO of the economic responsibilities of a departing senior management member of Unicom Group.

In addition, SASAC has an indirect influence over us as our controlling shareholder, Unicom Group, is under the direct supervision of SASAC. In particular, SASAC may designate certain nominees and request Unicom Group to propose the appointment of such nominees as our directors and senior management. SASAC may also request Unicom Group to remove our directors and senior management in accordance with relevant procedures provided by applicable law and our articles of association.

**C. *Organizational Structure***

We are incorporated in Hong Kong and as of April 20, 2012, we were 41.27% owned by Unicom BVI, which was 17.90% owned by Unicom Group and 82.10% owned by the A Share Company, which in turn was 61.50% owned by Unicom Group, 29.74% owned by Netcom BVI, which in turn was 100% owned by Unicom Group, 19.42% owned by public shareholders and 9.57% owned by Telefónica. See A. History and Development of the Company above. Set forth below are details of our wholly owned significant subsidiaries:

<b>Name of Subsidiary</b>	<b>Country of Incorporation</b>	<b>Ownership Interest</b>
China United Network Communications Corporation Limited	China	100%
China Unicom (Hong Kong) Operations Limited	Hong Kong	100%
China Unicom (Americas) Operations Limited	United States	100%
China Unicom (Singapore) Operations Pte. Ltd.	Singapore	100%
China Unicom (Europe) Operations Limited	United Kingdom	100%
China Unicom (Japan) Operations Corporation	Japan	100%
Billion Express Investments Limited	British Virgin Islands	100%

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### ***D. Properties***

Our principal executive offices are located in Hong Kong. We also maintain executive offices in Beijing. We own and lease a large number of offices, retail outlets, equipment rooms and base stations throughout China. In some cases, we have not entered into formal lease agreements with the lessors or the lessors may not possess requisite title certificates. We believe that it is unlikely that we would be denied our right to use a large number of these properties at any given time.

### **Item 4A. Unresolved Staff Comments**

None.

### **Item 5. Operating and Financial Review and Prospects**

You should read the following discussion and analysis in conjunction with the selected financial data set forth in Item 3 and our consolidated financial statements, together with the related notes, included elsewhere in this annual report on Form 20-F.

#### **Acquisitions of Unicom NewSpace, Fixed-Line Business in 21 Provinces in Southern China and Other Assets from Parent Companies**

We completed (i) the 2011 Acquisition in respect of Unicom NewSpace in December 2011 and (ii) the 2009 Acquisition in respect of the acquisition of Target Business in January 2009. See *A. History and Development of the Company* *Unicom Acquisitions and Sales* *2011 Acquisition* and *A. History and Development of the Company* *Unicom Acquisitions and Sales* *Acquisitions of Fixed-Line Business in 21 Provinces in Southern China and Other Assets from Parent Companies and Lease of Telecommunications Networks in 21 Provinces in Southern China* under Item 4, respectively. Because (i) we and Unicom NewSpace were under common control of Unicom Group both prior to and after the 2011 Acquisition and (ii) we and the Target Business were under common control of Unicom Group both prior to and after the 2009 Acquisition, each of the acquisitions is considered as a business combination of entities and businesses under common control and has been accounted for using merger accounting in accordance with AG 5 issued by the HKICPA in November 2005. Upon our adoption of IFRS, we adopted the accounting policy to account for business combination of entities and businesses under common control using the predecessor values method, which is consistent with HKFRS. Given that all the acquired entities and businesses mentioned above in this paragraph had always been under common control during all the periods presented, the assets and liabilities thereof are stated at predecessor values and are included in the consolidated financial statements included in this annual report on Form 20-F as if these entities and their businesses acquired had always been part of our company during all the periods presented.

#### **Overview**

We are an integrated telecommunications operator in China providing mobile voice and value-added, fixed-line voice and value-added, fixed-line broadband, data communications and other telecommunications services to our customers through our two operating segments comprised of mobile services and fixed-line services. Following our acquisition of fixed-line business in 21 provinces in southern China from our parent companies in January 2009, we have extended the coverage of all of our services nationwide. We, China Mobile and China Telecom are the three major telecommunications operators in China. See *A. History and Development of the Company* *Restructurings of the Telecommunications Industry* under Item 4.

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The table below sets forth revenue from our major businesses and their respective percentage of our total revenue in 2009, 2010 and 2011 (excluding fixed-line upfront connection fees of RMB490 million in 2009, RMB192 million in 2010 and RMB15 million in 2011).

	For the Year Ended December 31,					
	2009 (Restated) <sup>(1)</sup>		2010 (Restated) <sup>(1)</sup>		2011	
	RMB in millions	As % of Total	RMB in millions	As % of Total	RMB in millions	As % of Total
Total revenue (excluding fixed-line upfront connection fees) <sup>(2)</sup>	153,536	100.0	171,178	100.0	209,152	100.0
Total service revenue (excluding fixed-line upfront connection fees) <sup>(2)</sup>	151,373	98.6	163,891	95.7	185,870	88.9
Include: Mobile business	70,102	45.7	82,449	48.2	103,307	49.4
Fixed-line business	80,670	52.5	79,750	46.6	81,627	39.0
Out of which:						
Broadband service	23,898	15.6	29,822	17.4	35,226	16.8
Total sales of telecommunications products	2,163	1.4	7,287	4.3	23,282	11.1

(1) The comparative financial data of 2009 and 2010 presented herein was restated to reflect the effects of the 2011 Acquisition. See Note 2.2 to our consolidated financial statements included elsewhere in this annual report on Form 20-F.

(2) Fixed-line upfront connection fees represent the amortization of deferred upfront connection fees received from the customers before July 1, 2001. No upfront connection fee was received from the customers since then. Therefore, we consider that analyses of our operating results excluding upfront connection fees are more relevant to the readers of this report.

Our service revenue primarily consists of the following:

usage fees and monthly fees for our mobile and fixed-line telephone services, which are recognized when we render the service to our customers;

revenue from the provision of value-added services, which is recognized when we render the services to our customers;

revenue from the provision of broadband, data and other Internet-related services are recognized when the services are provided to customers;

revenue from interconnection with other telecommunications operators for calls made from their networks to our networks. We recognize interconnection revenue when the relevant calls are made by subscribers;

revenue for offerings which include the bundled sale of mobile handsets and provision of services. The total contract consideration of such bundled sale is allocated to service revenue and sales of handsets based on their relative fair values. We recognize revenue allocated to the sale of handset when the title of the handset is passed to the customer and recognize revenue allocated to the service element based upon the actual usage of mobile services. The cost of the mobile handset sold is expensed immediately to the statement of income;

revenue from information communications technology services are recognized when goods are delivered to the customers (which generally coincides with the time when the customers have accepted the goods and the related risks and rewards of

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ownership have been transferred to the customers) or when services are rendered to the customers using the percentage of completion method when the outcome of the services provided can be estimated reliably. If the outcome of the services provided cannot be estimated reliably, the treatment should be as follows: (i) if it is probable that the costs incurred for the services provided is recoverable, service revenue should be recognized only to the extent of reasonable costs incurred, and costs should be recognized as current expenses in the period in which they are incurred, or (ii) if it is probable that costs incurred will not be recoverable, costs should be recognized as current expenses immediately and service revenue should not be recognized;

revenue from sales of telecommunications products (which mainly represent handsets and accessories) that are not bundled with mobile services are recognized when title of such products has been passed to the buyers; and



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rental income from leases of customer-end equipment and transmission lines on our networks to business customers and other telecommunications carriers in China. We recognize leased line rental revenue on a straight-line basis over the relevant lease term.

The following table sets forth our major costs and expenses items and income before income tax, both in terms of amount and as a percentage of total revenue in 2009, 2010 and 2011 (excluding fixed-line upfront connection fees of RMB490 million in 2009, RMB192 million in 2010 and RMB15 million in 2011).

	For the Year Ended December 31,					
	2009 (Restated) <sup>(1)</sup>		2010 (Restated) <sup>(1)</sup>		2011	
	RMB in millions	% of Total	RMB in millions	% of Total	RMB in millions	% of Total
Total revenue (excluding fixed-line upfront connection fees) <sup>(2)</sup>	153,536	100.0	171,178	100.0	209,152	100.0
Costs, expenses and others	141,870	92.4	166,786	97.4	203,569	97.3
Interconnection charges	12,955	8.4	13,727	8.0	16,380	7.8
Depreciation and amortization	47,745	31.1	54,654	31.9	58,021	27.7
Networks, operations and support expenses	23,740	15.5	26,387	15.4	29,449	14.1
Employee benefit expenses	21,947	14.3	23,348	13.6	26,601	12.7
Selling and marketing	21,020	13.7	23,735	13.9	28,750	13.8
Cost in relation to information communication technology services	839	0.5	896	0.5	1,410	0.7
General, administrative and other expenses	12,192	7.9	12,966	7.6	13,426	6.4
Cost of telecommunications products sold	2,689	1.8	10,688	6.3	29,739	14.2
Finance costs, net of interest income	944	0.6	1,606	0.9	1,244	0.6
Realized gains on changes in fair value of derivative financial instrument	(1,239)	(0.8)	-	-	-	-
Other income-net	(962)	(0.6)	(1,221)	(0.7)	(1,451)	(0.7)

<sup>(1)</sup> The comparative financial data of 2009 and 2010 presented herein was restated to reflect the effects of the 2011 Acquisition and the change in accounting policy for property, plant and equipment upon the adoption of amended IFRS/HKFRS 1 in 2011. See Note 2.2 to our consolidated financial statements included elsewhere in this annual report on Form 20-F.

<sup>(2)</sup> Fixed-line upfront connection fees represent the amortization of deferred upfront connection fees received from the customers before July 1, 2001. No upfront connection fee was received from the customers since then. Therefore, we consider that analyses of our operating results excluding upfront connection fees are more relevant to the readers of this report.

Our major costs and expenses include the following:

interconnection expenses, representing amounts paid to other operators for calls from our networks to their networks and for calls made by our subscribers roaming in their networks;

depreciation and amortization expenses, mainly relating to our property, plant and equipment and other assets;

networks, operations and support expenses, mainly relating to repair, maintenance and operations of our networks;

leasing fee for telecommunications networks in southern China;



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employee benefit expenses, representing staff salaries and wages, bonuses and medical benefits, contributions to defined contribution pension schemes, housing benefits and share-based compensation costs amortized over the vesting period of options;

selling and marketing expenses, including commissions, promotion and advertising expenses, direct incremental costs for activating subscriber services and customer retention costs;

cost in relation to information communication technology services, primarily including cost of hardware sold;

general, administrative and other expenses, primarily including provision for doubtful debts, utilities, general office expenses and travel expenses;

cost of telecommunications products sold; and

finance costs, net of interest income, primarily including interest expenses, net of interest income.

### **Critical Accounting Policies**

The preparation of our financial statements and this annual report on Form 20-F requires us to make estimates and judgments that affect the reported and disclosed amounts of assets and liabilities, including contingent assets and liabilities, as of the relevant dates and revenue and expenses for the relevant periods. We have identified below the areas involving a higher degree of judgment or complexity, or areas where assumptions are significant to the accounting policies and estimates, as critical to our business operations and an understanding of our results of operations and financial position. The impact and any associated risks related to these policies on our business operations are discussed throughout this Item 5 where such policies affect our reported and expected financial results. For a discussion of the application of these and other accounting policies, see Note 4 to our consolidated financial statements included elsewhere in this annual report on Form 20-F. There can be no assurance that actual results will not differ from those estimates and assumptions.

### ***Significant Accounting Policies***

#### ***Revenue Recognition***

Revenue comprises the fair value of the consideration received or receivable for the services and sales of goods or telecommunications products in the ordinary course of our business activities. Revenue is shown net of business tax, government surcharges, returns and discounts and after eliminating sales within our company.

We recognize revenue when the amount of revenue can be reliably measured, it is probable that future economic benefits will flow to the entity and specific criteria have been met for each of our activities as described below. The amount of revenue is not considered to be reliably measurable until all contingencies relating to the sale have been resolved. We base our estimates on historical results, taking into consideration of the type of customer, the type of transaction and the specifics of each arrangement.

#### ***Sales of services and goods***

Usage fees and monthly fees are recognized when the services are rendered;

Revenue from the provision of broadband and other Internet-related services and managed data services are recognized when the services are provided to customers;

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Lease income from leasing of lines and customer-end equipment are treated as operating leases with rental income recognized on a straight-line basis over the lease term;

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Value-added services revenue, which mainly represents revenue from the provision of services such as SMSs, Cool Ringtone, personalized ring, caller number display and secretarial services to subscribers, is recognized when service is rendered;

Standalone sales of telecommunications products, which mainly represent handsets and accessories, are recognized when title has been passed to the buyers;

For offerings which include the bundled sale of mobile handsets and provision of services, the total contract consideration of such bundled sale is allocated to service revenue and sales of handsets based on their relative fair values. Revenue relating to the sale of the handset is recognized when the title is passed to the customer whereas service revenue is recognized based upon the actual usage of mobile services. The cost of the mobile handset is expensed immediately to the statement of income upon revenue recognition; and

Revenue from information communications technology services are recognized when goods are delivered to the customers (which generally coincides with the time when the customers have accepted the goods and the related risks and rewards of ownership have been transferred to the customers) or when services are rendered to the customers using the percentage of completion method when the outcome of the services provided can be estimated reliably. If the outcome of the services provided cannot be estimated reliably, the treatment should be as follows: (i) if it is probable that the costs incurred for the services provided are recoverable, services revenue should be recognized only to the extent of recoverable costs incurred, and costs should be recognized as current expenses in the period in which they are incurred; or (ii) if it is probable that costs incurred will not be recoverable, costs should be recognized as current expenses immediately and services revenue should not be recognized.

### *Interest income*

Interest income from deposits in banks or other financial institutions is recognized on a time proportion basis, using the effective interest method.

### *Dividend income*

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

### *Deferred Revenue, Advances from Customers and Subscriber Points Reward Program*

#### *Deferred revenue*

Deferred revenue mainly represents upfront non-refundable revenue, including upfront connection fees and installation fees of fixed-line business and receipts from the activation of SIM/USIM cards relating to our mobile businesses, which are deferred and recognized over the expected customer service period.

#### *Advances from customers*

Advances from customers are amounts paid by customers for prepaid cards, other calling cards and prepaid service fees, which cover future telecommunications services (over a period of one to twelve months). Advances from customers are stated at the amount of proceeds received less the amount already recognized as revenue upon the rendering of services.

#### *Subscriber points reward program*

The fair value of providing telecommunications services and the subscriber points reward are allocated based on their relative fair values. The allocated portion of fair value for the subscriber points reward is recorded as deferred revenue when the rewards are granted and recognized as revenue when the points are redeemed or expired. The fair value of deferred revenue is estimated based on (i) the value of each bonus point awarded to subscribers, (ii) the number of bonus points related to subscribers who are qualified or expected to be qualified to exercise their redemption right at each balance sheet date, and (iii) the expected bonus points redemption rate. The fair value of the outstanding subscriber points reward is subject to review by management on a periodic basis.



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### ***Critical Accounting Estimates and Judgments***

#### ***Recognition of Upfront Non-Refundable Revenue and Direct Incremental Costs***

We defer and amortize upfront activation fees of SIM/USIM cards of the mobile business over the expected customer service period of 3 years (2009: approximately 3 years; 2010: approximately 3 years). The related direct incremental costs of acquiring and activating mobile subscribers, including costs of SIM/USIM cards and commissions, are also deferred and amortized over the same expected customer service period of 3 years.

We defer and amortize upfront customer installation and testing fees of the fixed-line business over the expected customer service period of 10 years (2009: approximately 10 years; 2010: approximately 10 years). The related direct incremental installation costs are deferred and amortized over the same expected customer service period of 10 years.

We only defer costs to the extent that they will generate future economic benefits. The excess of the direct incremental costs over the corresponding upfront non-refundable revenue, if any, is expensed to the statement of income immediately.

We estimate the expected customer service period based on the historical customer retention experience and after factoring in the expected level of future competition, the risk of technological or functional obsolescence to our services, technological innovation, and the expected changes in the regulatory and social environment. If our estimate of the expected customer service period changes as a result of increased competition, changes in telecommunications technology or other factors, the amount and timing of recognition of the deferred revenue and direct incremental costs may change for future periods.

#### ***Lease of Telecommunications Networks in Southern China***

Pursuant to the initial network lease agreement and the 2011-2012 network lease agreement, Unicom New Horizon has the legal ownership of the Telecommunications Networks in southern China. We believe we only bear the risks associated with the operation of the fixed-line business in southern China during the relevant leasing periods and are free from any ownership risks of the telecommunications networks, and the risks and rewards of ownership of the leased assets rest substantially with the lessor. In addition, at the inception of the initial network lease agreement dated December 16, 2008, there was a high degree of uncertainty related to the market condition and operating results of the fixed-line business in southern China. It was highly uncertain whether we would continue to lease the network in the future, and we were unable to determine whether or not we would exercise the purchase option in the future. In the event that CUCL elects to exercise this purchase option, the parties will discuss and negotiate the purchase price with reference to the appraised value of the telecommunications networks in southern China, which is to be determined in accordance with applicable laws of Hong Kong and China, after taking into account the prevailing market conditions and other factors. Given these uncertainties and due to the fact that the risks associated with the ownership of the Telecommunications Networks in Southern China substantially remained with Unicom New Horizon, accordingly, we accounted for the leasing of the Telecommunications Networks in Southern China as an operating lease.

At the beginning of each lease term, we assess the appropriate classification based on the relevant factors and circumstances at that time. On October 29, 2010, CUCL entered into the 2011-2012 network lease agreement with Unicom New Horizon. The 2011-2012 network lease agreement has an initial term of two years, effective from January 1, 2011 and expiring on December 31, 2012, which is renewable at the option of CUCL with at least two months' prior notice on the same terms and conditions as the initial network lease agreement dated December 16, 2008, except that the annual fee payable by CUCL for such lease for the two years ending December 31, 2011 and 2012 is RMB2.4 billion and RMB2.6 billion, respectively. At the time of entering into the 2011-2012 network lease agreement, we still believed the uncertainties of the fixed-line business in southern China continue to exist, particularly due to the fact that (i) the growth of the fixed-line business in southern China was not significant; (ii) the future success of the fixed-line business in southern China remained uncertain, in light of the keen market competition; and (iii) the technology, technological standards and government regulatory environment in respect of the relevant business are still subject to uncertainties. Accordingly, we were not in a position to determine whether we would renew the lease after the initial two-year lease term or whether we would exercise the purchase option upon the entering into the 2011-2012 network lease agreement. As a result, we considered the risks associated with the ownership of the Telecommunications Networks in Southern China still substantially remain with Unicom New Horizon, and therefore accounted for the leasing of Telecommunications Networks in Southern China under the 2011-2012 network lease agreement as an operating lease. The operating lease expense was recorded in the consolidated statement of income for the years ended December 31, 2009, 2010 and 2011, but the carrying value of the Telecommunications Networks in Southern China and the related liabilities were not reflected in the consolidated balance sheets as of December 31, 2010 and 2011.





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### *Depreciation on Property, Plant and Equipment*

Depreciation on our property, plant and equipment is calculated using the straight-line method to allocate cost up to residual values over the estimated useful lives of the assets. We review the useful lives and residual values periodically to ensure that the method and rates of depreciation are consistent with the expected pattern of realization of economic benefits from property, plant and equipment. We estimate the useful lives of property, plant and equipment based on historical experience, taking into account anticipated technological changes. If there are significant changes from previously estimated useful lives, the amount of depreciation expenses may change.

### *Impairment of Non-Financial Assets*

We test whether non-financial assets have suffered from any impairment, in accordance with the accounting policy stated in Note 2.11 to the audited consolidated financial statements contained elsewhere in this annual report. The recoverable amount of an asset is the higher of its fair value less costs to sell and its value in use. Management estimates value in use based on estimated discounted pre-tax future cash flows of the cash generating unit at the lowest level to which the asset belongs. If there is any significant change in management's assumptions, including discount rates or growth rates in the future cash flow projection, the estimated recoverable amounts of the non-financial assets and our results would be significantly affected. Such impairment losses are recognized in the statement of income. Accordingly, there will be an impact to the future results if there is a significant change in the recoverable amounts of the non-financial assets.

No significant impairment loss on property, plant and equipment was recognized for the years ended December 31, 2009, 2010 and 2011.

### *Income Tax and Deferred Taxation*

We estimate our income tax provision and deferred taxation in accordance with the prevailing tax rules and regulations, taking into account any special approvals obtained from relevant tax authorities and any preferential tax treatment to which we are entitled in each location or jurisdiction in which we operate. There are many transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business. We recognize liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income tax and deferred tax provisions in the period in which such determination is made.

For temporary differences which give rise to deferred tax assets, we have assessed the likelihood that the deferred tax assets could be recovered. Major deferred tax assets relate to unrecognized revaluation surplus on prepayments for the leasehold land and buildings determined under PRC regulations, accruals of expenses not yet deductible for tax purpose, changes in fair value on financial assets through other comprehensive income, and provision for doubtful debts. Due to the effects of these temporary differences on income tax, we have recorded deferred tax assets amounting to approximately RMB5,091 million as at December 31, 2011 (2010: approximately RMB4,940 million). Deferred tax assets are recognized based on our estimates and assumptions that they will be recovered from taxable income arising from continuing operations in the foreseeable future.

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We believe we have recorded adequate income tax provision and deferred taxes based on the prevailing tax rules and regulations and our current best estimates and assumptions. In the event that future tax rules and regulations or related circumstances change, adjustments to income tax and deferred taxation may be necessary which would impact our results or financial position.

**Recently Issued International Financial Reporting Standards/Hong Kong Financial Reporting Standards**

The IASB has issued a number of new and revised IFRSs and interpretations that are first effective for the current accounting period commencing January 1, 2011 or are available for early adoption. The equivalent new and revised HKFRSs and interpretations consequently issued by the HKICPA have the same effective date as those issued by the IASB and are in all material respects identical to the pronouncements issued by the IASB. There have been no other material changes to HKFRSs.

Up to the date of issue of our 2011 financial statements, the following new standard and amendment or revision to existing standard has been issued but not yet effective for the annual accounting period ended December 31, 2011 and has not been adopted by us:

	<b>Effective for annual accounting period beginning on or after</b>
IFRS/HKFRS 7 (amendment) Financial instruments: disclosures	July 1, 2011
IAS/HKAS 1 (amendment) Presentation of financial statements	January 1, 2012
IFRS/HKFRS 10 Consolidated financial statements	January 1, 2013
IFRS/HKFRS 13 Fair value measurements	January 1, 2013

On January 1, 2011, we early adopted IFRS/HKFRS 9 Financial instruments. Upon adoption of this standard, we classified the investments in equity instruments as those measured at fair value and transferred the balance of available-for-sale fair value reserve to investment revaluation reserve. In addition, we made an irrevocable election upon initial adoption of the standard to recognize changes in fair value of these financial assets only through other comprehensive income. Thus, all subsequent fair value or disposal gains or losses will not be recognized in the statement of income. IFRS/HKFRS 9 is applied retrospectively to all periods presented.

In 2011, we adopted the amended IFRS/HKFRS 1 First-Time Adoption of International/Hong Kong Financial Reporting Standards. We had completed our IPO process and merger of businesses under common control before the adoption of IFRS and the property, plant and equipment were revalued for the purpose of the transactions. Such revaluations were event-driven fair value measurements. Accordingly, upon adoption of the amended IFRS/HKFRS 1, we applied such event-driven fair value measurements as deemed cost for the relevant property, plant and equipment (other than buildings and telecommunications equipment of mobile business which were accounted for using the cost model) retrospectively. The restated deemed costs of these assets would be subject to depreciation and impairment assessments. Since subsequent re-measurement at fair value of property, plant and equipment is not necessary to comply with IAS/HKAS 16 Property, Plant and Equipment as a result of the adoption of this standard, we changed our accounting policy and measure all of our property, plant and equipment at cost less accumulated depreciation and accumulated impairment losses. As a result, those revaluation surpluses or deficits recognized as a consequence of the 2006 and 2008 revaluations have been reversed and their impacts on depreciation have been adjusted accordingly.

**Operating Results**

In the 2009 Acquisition, we did not purchase the underlying fixed-line network assets in southern China, but subsequently leased such assets from Unicom New Horizon, a wholly-owned subsidiary of Unicom Group, to operate the acquired fixed-line business. To account for this transaction, we recorded all assets, liabilities, revenue and costs and expenses associated with the acquired fixed-line business in southern China and the underlying network assets in our consolidated financial statements for the historical periods prior to the completion of the transaction in January 2009. Following the completion of this transaction, as we started to lease the fixed-line network assets in southern China, which were retained by the lessor, the assets and liabilities associated with these network assets were treated as a distribution by us to Unicom Group from other reserve using the merger accounting under HKFRS and predecessor values method under IFRS. Accordingly, we no longer include any assets, liabilities, depreciation, finance costs or other costs relating to such assets, but record only revenue generated from the acquired fixed-line business in southern China and the leasing fee for the relevant network assets in our consolidated financial statements for the subsequent periods.

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Unless otherwise noted, the selected consolidated financial statements data as of and for the years ended December 31, 2009 and 2010 under this Item 5 was restated to reflect the effects of the 2011 Acquisition and the change in accounting policy for property, plant and equipment upon the adoption of amended IFRS/HKFRS 1 in 2011. See Note 2.2 to our consolidated financial statements included elsewhere in this annual report on Form 20-F.

### **Year Ended December 31, 2011 Compared to Year Ended December 31, 2010**

#### ***Revenue***

In 2011, we continued to face various challenges, including intensified telecommunications market competition, further downward adjustments in tariffs and decline of fixed-line voice business. We continued to actively develop full-service operation with a focus on 3G mobile services and fixed-line broadband business. Revenue for 2011 was RMB209.17 billion, representing an increase of 22.1% from RMB171.37 billion for 2010. Excluding fixed-line upfront connection fees of RMB192 million and RMB15 million in 2010 and 2011, respectively, our revenue for 2011 would have been RMB209.15 billion, representing an increase of 22.2% from RMB171.18 billion in 2010, of which our service revenue would have been RMB185.87 billion in 2011, representing an increase of 13.4% from 2010.

#### ***Mobile Business Revenue***

Revenue from our mobile business increased by 41.2% from RMB89.62 billion in 2010 to RMB126.53 billion in 2011. Of the revenue from our mobile business in 2010 and 2011, RMB82.45 billion and RMB103.31 billion, respectively, was from service revenue. Service revenue from our mobile business as a percentage of our total service revenue (excluding fixed-line upfront connection fees of RMB192 million and RMB15 million in 2010 and 2011, respectively) increased from 50.3% in 2010 to 55.6% in 2011. The growth in revenue from our mobile business was primarily driven by the growth of our 3G business. Our ARPU increased in 2011 compared to 2010, primarily due to the change in revenue mix between our GSM business and 3G businesses. 3G business has a significantly higher ARPU than GSM business. As the revenue from 3G business increased significantly as a percentage of total service revenue from mobile business from 14.1% in 2010 to 31.7% in 2011, the overall ARPU of our mobile business increased from RMB43.7 in 2010 to RMB47.3 in 2011. In addition, to effectively develop our 3G mobile data business, we sought to enhance customer experiences by incentivizing customers to upgrade their handsets. To this end, we offered a broad range of attractive bundled packages of mid- to high-end 3G handsets and 3G services in 2011. This initiative resulted in a significant increase in our mobile Internet service revenue as well as revenue from the sales of mobile telecommunications products in 2011.

The total number of our mobile subscribers was 199.66 million as of December 31, 2011, with a net addition of 32.23 million subscribers (including 25.96 million 3G subscribers) from the end of 2010. ARPU of our GSM mobile business was RMB37.4 in 2011, representing a decrease of 5.3% from RMB39.5 in 2010. ARPU of our 3G business was RMB110.0 in 2011, representing a decrease of 11.3% from RMB124.0 in 2010.

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The table below sets forth the revenue composition of our mobile business and each revenue item's respective share of total revenue for the years ended December 31, 2010 and 2011.

	2010 (Restated) <sup>(1)</sup>		2011	
	RMB in millions	As % of total	RMB in millions	As % of total
Total revenue from mobile business	89,622	100.0	126,526	100.0
Service revenue	82,449	92.0	103,307	81.6
Usage fees and monthly fees	47,004	52.4	54,186	42.8
Value-added service revenue	25,920	28.9	37,880	29.9
Interconnection revenue	9,022	10.1	10,726	8.5
Other service revenue	503	0.6	515	0.4
Sales of mobile telecommunications products	7,173	8.0	23,219	18.4

<sup>(1)</sup> The financial data of 2010 presented herein was restated to reflect the effects of the 2011 Acquisition. See Note 2.2 to our consolidated financial statements included elsewhere in this annual report on Form 20-F.

*Usage Fees and Monthly Fees.* Primarily as a result of an increase in mobile subscribers, usage fees and monthly fees for our mobile services were RMB54.19 billion in 2011, representing an increase of 15.3% from RMB47.00 billion in 2010.

*Value-Added Service Revenue.* Value-added service revenue consists primarily of revenue from our 3G value-added services and GSM value-added services. In 2011, we continued to actively promote mobile data business of our 3G business and improved the penetration of mobile Internet services. As a result, revenue from our mobile value-added services amounted to RMB37.88 billion in 2011, representing an increase of 46.1% from RMB25.92 billion in 2010 and as a percentage of total mobile revenue increased from 28.9% in 2010 to 29.9% in 2011. Of the total revenue from mobile value-added services, revenue from mobile Internet services increased by 90.4% from RMB7.70 billion in 2010 to RMB14.65 billion in 2011, revenue from our SMS services increased by 4.6% from RMB8.13 billion in 2010 to RMB8.51 billion in 2011 and revenue from Cool Ringtone services increased by 6.7% from RMB3.08 billion in 2010 to RMB3.28 billion in 2011.

*Interconnection Revenue.* Our interconnection revenue increased by 18.9% from RMB9.02 billion in 2010 to RMB10.73 billion in 2011, and represented 8.5% of total mobile revenue in 2011 as compared with 10.1% in 2010. The increase in our interconnection revenue was primarily as a result of the increased total usage of our mobile services due to the increased total number of our mobile subscribers.

*Sales of Telecommunications Products.* Revenue from our sale of mobile telecommunications products increased from RMB7.17 billion in 2010 to RMB23.22 billion in 2011, mainly due to our continuing efforts in promoting a broad range of new bundled packages of mid- to high-end 3G handsets and 3G services in 2011.

*Fixed-Line Business Revenue*

In 2011, we continued to develop our fixed-line broadband services and promoted our mobile and fixed-line bundled services. The trend of mobile substitution continued to have a negative impact on the revenue from our fixed-line voice business. Excluding fixed-line upfront connection fees of RMB192 million and RMB15 million in 2010 and 2011, respectively, our revenue from fixed-line business would have increased by 2.3% from RMB79.86 billion in 2010 to RMB81.69 billion in 2011, of which service revenue would have increased by 2.4% from RMB79.75 billion in 2010 to RMB81.63 billion in 2011. See **D. Risk Factors** We may further lose fixed-line and mobile subscribers and our doubtful debt ratios may increase, which may materially adversely affect our financial condition, results of operations and growth prospects under Item 3.

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The table below sets forth the revenue composition of our fixed-line business and each revenue item's respective share of total revenue from our fixed-line business for the years ended December 31, 2010 and 2011.

	For the Year Ended December 31, 2010 (Restated) <sup>(1)</sup>		2011	
	RMB in millions	As % of Total	RMB in millions	As % of Total
Total revenue from fixed-line business <sup>(2)</sup>	79,864	100.0	81,690	100.0
Service revenue <sup>(2)</sup>	79,750	99.9	81,627	99.9
Usage fee and monthly fee	29,085	36.4	24,116	29.5
Broadband, managed data and other Internet-related services revenue	32,595	40.8	38,500	47.1
Interconnection revenue	5,243	6.6	4,579	5.6
Value-added service revenue	4,860	6.1	4,562	5.6
Leased line service revenue	5,589	7.0	6,859	8.4
Information communication technology services revenue	1,048	1.3	1,634	2.0
Others	1,330	1.7	1,377	1.7
Sales of fixed-line telecommunications products	114	0.1	63	0.1

(1) The financial data of 2010 presented herein was restated to reflect the effects of the 2011 Acquisition. See Note 2.2 to our consolidated financial statements included elsewhere in this annual report on Form 20-F.

(2) Excluding fixed-line upfront connection fees of RMB192 million in 2010 and RMB15 million in 2011. Fixed-line upfront connection fees represent the amortization of deferred upfront connection fees received from the customers before July 1, 2001. No upfront connection fee was received from the customers since then. Therefore, we consider that analyses of our operating results excluding upfront connection fees are more relevant to the readers of this report.

*Usage Fees and Monthly Fees.* Usage fees include local usage fees charged for local telephone calls and VoIP long distance calls, long distance usage fees for domestic and international long distance calls originated by our fixed-line subscribers, users of our pre-paid phone cards and certain other customers. Monthly fees represent the fixed amount of service charges to our customers for using our fixed-line telephone services.

As a result of further implementation of the Calling-Party-Pays tariff policy for mobile services and continuing downward adjustments of tariffs for fixed-line services, the substitution effect of fixed-line local services by mobile services became more intense. In 2011, we experienced continuing decline in the number of fixed-line local telephone subscribers and revenue. Our local telephone subscribers decreased in 2011 by 3.9% from 96.64 million at the end of 2010 to 92.85 million at the end of 2011. ARPU of the local telephone business decreased by 11.1% from 2010 to RMB25.7 in 2011. Total usage of local calls decreased by 19.5% from 2010 to 125.28 billion pulses in 2011 (excluding Internet dial-up usage) and total usage of long distance calls decreased by 19.5% from 26.79 billion minutes in 2010 to 21.55 billion minutes in 2011. As a result, revenue from our usage fees and monthly fees in 2011 decreased by 17.1% from RMB29.09 billion in 2010 to RMB24.12 billion in 2011.

*Broadband, managed data and other Internet-related services revenue.* Revenue from our broadband, managed data and other Internet-related services include revenue generated from DSL, LAN, and broadband-related value-added services, fees that we charge for our DDN, frame relay, ATM, MPLS-VPN and X.25 services and revenue from the provision of Internet dial-up services (other than communication fees) and dedicated Internet access services. Revenue from our broadband, managed data and other Internet-related services increased by 18.1% from RMB32.60 billion in 2010 to RMB38.50 billion in 2011, primarily as a result of the increase in revenue from fixed-line broadband services.

In light of the continuing effect of mobile substitution, fixed-line broadband service has become the main growth driver of our fixed-line business revenue. In 2011, our fixed-line broadband business continued to maintain a rapid growth as a result of our efforts in improving broadband access speed, adopting multi-service bundling strategy, enriching application contents and implementing diversified sales strategies. The number of our fixed-line broadband subscribers increased by 17.8% from 47.22 million in 2010 to 55.65 million in 2011. ARPU of our fixed-line broadband business decreased by 1.2% from RMB57.1 in 2010 to RMB56.4 in 2011. However, revenue from our fixed-line broadband service increased by 18.2% from RMB29.80 billion in 2010 to RMB35.23 billion in 2011, and as a percentage of the total fixed-line revenue, increased from 37.3% in 2010 to 43.1% in 2011. Revenue from our managed data and other Internet-related services increased by 18.1% from RMB2.77 billion in 2010 to RMB3.27 billion in 2011.

*Interconnection Revenue.* Revenue from our interconnection services consists of interconnection fees charged to other domestic telecommunications operators, principally China Mobile and China Telecom, for both local and long distance calls. Revenue from our interconnection services decreased by 12.7% from RMB5.24 billion in 2010 to RMB4.58 billion in 2011. The decrease in interconnection revenue was mainly due to a decrease in voice traffic from other telecommunications operators as a result of the mobile substitution effect.

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**Value-Added Service Revenue.** Revenue from our value-added services consists of fees that we charge our customers for the provision of caller identification, personalized ring, telephone information services, video- and tele-conferencing and other value-added services. Revenue from our value-added services decreased by 6.1% from RMB4.86 billion in 2010 to RMB4.56 billion in 2011, mainly due to the decrease in the usage of our caller identification, Personalized Ring, and PHS SMS services as a result of the significant reduction of our fixed-line telephone subscribers, including PHS subscribers.

**Leased Line Service Revenue.** Revenue from our leased line services consists of fees that we receive from our government, corporate and carrier customers for leasing circuit capacity to them, including the lease of digital circuits, digital trunk lines and optic fibers. Revenue from our leased line services increased by 22.7% from RMB5.59 billion in 2010 to RMB6.86 billion in 2011, which was primarily due to the increased demand of leased line services from our local government and corporate customers.

**Information Communication Technology Services Revenue.** Information communication technology services revenue increased by 55.9% from RMB1.05 billion in 2010 to RMB1.63 billion in 2011, mainly as a result of our new system integration projects in 2011 for government and large corporate customers.

**Others.** Other fixed-line related revenue mainly consists of miscellaneous revenue items. Other fixed-line related revenue increased by 3.5% from RMB1.33 billion in 2010 to RMB1.38 billion in 2011.

**Sales of Telecommunications Products.** Revenue from our sales of fixed-line telecommunications products decreased by 44.7% from RMB0.11 billion in 2010 to RMB0.06 billion in 2011, mainly due to the decrease in sales of telecommunications terminal products such as telephone sets associated with local voice services in 2011.

**Costs, Expenses and Others**

Total costs, expenses and others in 2011 were RMB203.57 billion, representing an increase of 22.1% from RMB166.79 billion in 2010.

**Mobile Business Operating Costs and Expenses**

Operating costs and expenses for our mobile business in 2011 were RMB92.26 billion, representing an increase of 46.5% from RMB62.98 billion in 2010. The table below sets forth the principal items of operating costs and expenses from mobile business and their respective percentage of service revenue from mobile business for the years 2010 and 2011:

	For the Year Ended December 31,			
	2010 (Restated) <sup>(1)</sup>		2011	
	RMB in millions	% of Total	RMB in millions	% of Total
Service revenue from mobile business	82,449	100.0	103,307	100.0
Mobile business costs and expenses	62,980	76.3	92,262	89.3
Interconnection charges	14,452	17.5	17,442	16.9
Depreciation and amortization	23,362	28.3	26,151	25.3
Networks, operations and support expenses	3,106	3.8	4,270	4.1
Selling and marketing expenses	9,390	11.4	12,284	11.9
General, administrative and other expenses	2,175	2.6	2,489	2.4
Cost of telecommunications products sold	10,495	12.7	29,626	28.7

<sup>(1)</sup> The financial data of 2010 presented herein was restated to reflect the effects of the 2011 Acquisition and the change in accounting policy for property, plant and equipment upon the adoption of amended IFRS/HKFRS 1 in 2011. See Note 2.2 to our consolidated financial statements included elsewhere in this annual report on Form 20-F.

**Interconnection Charges.** Interconnection charges from mobile business were RMB17.44 billion in 2011, up by 20.7% from 2010, primarily due to an increase in mobile interconnection traffic volume resulting from the increased total usage of our mobile services. Interconnection charges

from mobile business as a percentage of service revenue from mobile business were 16.9% and 17.5% in 2011 and 2010, respectively.



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*Depreciation and Amortization.* Our depreciation and amortization expenses from mobile business were RMB26.15 billion in 2011, up by 11.9% from 2010. The increase was primarily due to our efforts in improving our 3G network capacity, expanding the 3G network coverage and optimizing our GSM network, which increased the relevant fixed assets that are subject to depreciation. As a percentage of service revenue from mobile business, our depreciation and amortization expenses from mobile business decreased from 28.3% in 2010 to 25.3% in 2011.

*Networks, Operations and Support Expenses.* Due to various factors, including the expansion of networks coverage, the increase in network assets and the increase in infrastructure charges such as utilities charges and rental expenses, we incurred networks, operations and support expenses from mobile business of RMB4.27 billion in 2011, up by 37.5% from 2010. Networks, operations and support expenses from mobile business, as a percentage of service revenue from mobile business, increased from 3.8% in 2010 to 4.1% in 2011. As a result of an increase in the lease of underlying telecommunications networks from other telecommunications operators, the related line leasing fees was RMB0.74 billion, up by 116.2% from 2010.

*Selling and Marketing Expenses.* Due to various factors, including the increased promotion of our key businesses, such as 3G business, and the increased costs of customer retention and channel subsidies, our selling and marketing expenses from mobile business reached RMB12.28 billion in 2011, up by 30.8% from 2010, and as a percentage of service revenue from mobile business, increased from 11.4% in 2010 to 11.9% in 2011.

*General, Administrative and Other Expenses.* We continued to closely control the increase in general and administrative expenses from mobile business. Our general, administrative and other expenses from mobile business were RMB2.49 billion in 2011, up by 14.4% compared with 2010, and, as a percentage of service revenue from mobile business, slightly decreased from 2.6% in 2010 to 2.4% in 2011.

*Cost of Telecommunications Products Sold.* In 2011, we continued to proactively promote 3G handsets subsidy policies and launched a number of newly defined 3G handsets models. As a result, the cost of mobile telecommunications products sold amounted to RMB29.63 billion, up by 182.3% from 2010. Correspondingly, revenue from sales of mobile telecommunications products in 2011 amounted to RMB23.22 billion, up by 223.7% from 2010.

*Fixed-Line Business Operating Costs and Expenses*

Operating costs and expenses for our fixed-line business in 2011 were RMB52.07 billion, representing an increase of 2.8% from RMB50.63 billion in 2010. The table below sets forth the principal items of operating costs and expenses from fixed-line business and their respective percentage of the total telecommunications services revenue for the years 2010 and 2011:

	For the Year Ended December 31,			
	2010 (Restated) <sup>(1)</sup>		2011	
	RMB in millions	% of Total	RMB in millions	% of Total
Services revenue from fixed-line business <sup>(2)</sup>	79,750	100.0	81,627	100.0
Fixed-line business costs and expenses	50,634	63.4	52,071	63.7
Interconnection charges	3,706	4.7	3,533	4.3
Depreciation and amortization	29,028	36.4	29,358	36.0
Networks, operations and support expenses	9,409	11.8	9,467	11.6
Selling and marketing	6,647	8.3	7,416	9.1
Cost in relation to information communication technology services	897	1.1	1,410	1.7
General, administrative and other expenses	754	0.9	774	0.9
Cost of telecommunications products sold	193	0.2	113	0.1

<sup>(1)</sup> The financial data of 2010 presented herein was restated to reflect the effects of the 2011 Acquisition and the change in accounting policy for property, plant and equipment upon the adoption of amended IFRS/HKFRS 1 in 2011. See Note 2.2 to our consolidated financial statements included elsewhere in this annual report on Form 20-F.

(2) Excludes fixed-line upfront connection fees of RMB192 million in 2010 and RMB15 million in 2011.

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*Interconnection Charges.* Interconnection charges from fixed-line business were RMB3.53 billion in 2011, down by 4.7% from 2010, primarily due to a decrease in fixed-line voice interconnection traffic volume. This was as a result of the decrease in the total usage of our fixed-line voice services. The decrease in interconnection charges is consistent with the decrease in interconnection revenues. Interconnection charges as a percentage of service revenue from fixed-line business (excluding fixed-line upfront connection fees) were 4.3% and 4.7% in 2011 and 2010, respectively.

*Depreciation and Amortization.* Our depreciation and amortization expenses from fixed-line business were RMB29.36 billion in 2011, up by 1.1% from 2010. The increase was primarily because we increased investments in upgrading broadband network and expanding our coverage. These investments resulted in an increase in our broadband network assets that are subject to depreciation. As a percentage of service revenue from fixed-line business (excluding fixed-line upfront connection fees), our depreciation and amortization expenses from fixed-line business decreased from 36.4% in 2010 to 36.0% in 2011.

*Networks, Operations and Support Expenses.* We incurred networks, operations and support expenses from fixed-line business of RMB9.47 billion in 2011, up by 0.6% from 2010. As a percentage of service revenue from fixed-line business (excluding fixed-line upfront connection fees), networks, operations and support expenses from fixed-line business decreased from 11.8% in 2010 to 11.6% in 2011.

*Selling and Marketing Expenses.* Primarily due to (i) the adoption of various marketing initiatives to retain our fixed-line subscribers, participating broadband services subscribers, and (ii) an increase in costs of channel subsidies, our selling and marketing expenses from fixed-line business were RMB7.42 billion in 2011, up by 11.6% from 2010, and as a percentage of service revenue from fixed-line business (excluding fixed-line upfront connection fees), increased from 8.3% in 2010 to 9.1% in 2011.

*Cost in Relation to Information Communication Technology Services.* Cost in relation to information communication technology in 2011 was RMB1.41 billion, up by 57.2% from 2010. Correspondingly, revenue from ICT services in 2011 was RMB1.63 billion, up by 55.9% from 2010.

*General, Administrative and Other Expenses.* We continued to closely control the increase in general and administrative expenses. Our general, administrative and other expenses from fixed-line business were RMB0.77 billion in 2011, up by 2.7% compared with 2010. Our general, administrative and other expenses from fixed-line business as a percentage of service revenue from fixed-line business (excluding fixed-line upfront connection fees) remained stable at 0.9% in 2010 and 2011.

*Cost of Telecommunications Products Sold.* The cost of fixed-line telecommunications products sold was RMB0.11 billion in 2011, down by 41.5% from 2010. Correspondingly, revenue from sales of fixed-line telecommunications products in 2011 amounted to RMB0.06 billion, down by 44.7% from 2010.

### *Unallocated Costs and Expenses*

The unallocated costs and expenses primarily represent corporate and shared service expenses that are not directly attributable to any of our operating segments. The unallocated costs and expenses also include certain statement of income items, such as employee benefit expenses, interest income, finance costs and other income, that cannot be directly identified to specific operating segments.

*Employee Benefit Expenses.* As the average social wages continued to increase in China and due to the implementation of our employee incentive, evaluation and allocation mechanism, our employee benefit expenses increased by 13.9% from 2010 to RMB26.60 billion in 2011, and as a percentage of service revenue (excluding fixed-line upfront connection fees), increased from 14.2% in 2010 to 14.3% in 2011.

*Finance Costs, Net of Interest Income.* Our finance costs, net of interest income, decreased by 22.5% from RMB1.61 billion in 2010 to RMB1.24 billion in 2011, which was primarily due to the increase in gain from foreign currency exchanges driven by the appreciation of RMB, partially offset by an increase of 22.2% in interest expenses from RMB1.91 billion in 2010 to RMB2.33 billion in 2011. The increase in our interest expenses was mainly due to the increase in our overall cost of capital from 3.1% in 2010 to 3.7% in 2011, as a result of the increase in the financing costs in the PRC financial market.

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*Depreciation and Amortization Expenses.* Depreciation and amortization expenses that are unallocated to mobile and fixed-line businesses were RMB2.63 billion in 2011, up by 12.6% from RMB2.34 billion in 2010. The increase was primarily as a result of an increase in our information system assets.

*Networks, Operations and Support Expenses.* Networks, operations and support expenses that are unallocated to mobile and fixed-line businesses were RMB15.72 billion in 2011, up by 13.3% from RMB13.88 in 2010, which was primarily due to the increases in utility charges and rental expenses as a result of our increased number of base stations and business premises.

*Other Operating Expenses.* Other operating expenses consist of selling and marketing expenses, general, administrative and other expenses and cost in relation to information communication technology services. Other operating expenses that are unallocated to mobile and fixed-line businesses were RMB19.58 billion in 2011, up by 8.5% from RMB18.04 in 2010, which was mainly due to the increase in expenses for advertisement and customer retention initiatives.

*Other Income-Net.* In 2011, other income-net was RMB1.45 billion, up by 18.7% from 2010. The increase was primarily as a result of the dividends of RMB0.87 billion received from our investment in Telefónica and others, up by RMB0.39 billion from 2010.

### ***Income Before Income Tax***

In 2011, our income before income tax was RMB5.60 billion, up by 22.1% from 2010, mainly due to the increase in our revenue from mobile business, especially 3G business.

In order to ensure the comparability of income before income tax and income for the year, we exclude the non-comparable factor of deferred fixed-line upfront connection fees of RMB15 million for 2011 and RMB192 million for 2010 for additional analysis purposes. After excluding the above factor, our income before income tax would have been RMB5.58 billion, up by 27.1% from 2010.

### ***Income Tax***

Our income tax was RMB1.37 billion in 2011, up by 55.3% from 2010, and our effective tax rate in 2011 was 24.5%, up by 5.2 percentage points from 2010. The increase in our income tax was largely due to the increases in our income before income tax and our effective tax rate. The increase in our effective tax rate is mainly due to the significant decrease in non-taxable deferred fixed-line upfront connection fees and the unavailability of certain one-off favorable tax treatments, such as the utilization of tax loss from the previous years of a subsidiary of our company against the current year taxable income. Excluding the factors discussed under Income Before Income Tax above, our effective tax rate in 2010 and 2011 would have been 20.1% and 24.6%, respectively.

### ***Net Income for the Year***

In 2011, our net income reached RMB4.23 billion, up by 14.2% from 2010. Our basic earnings per share was RMB0.18 in 2011. Excluding the factors discussed under the subsection Income Before Income Tax above, our net income would have been RMB4.21 billion, up by 20.0% from 2010.

**Table of Contents****Year Ended December 31, 2010 Compared to Year Ended December 31, 2009****Revenue**

2010 is the second year that we had a full-year operation following our merger with China Netcom. Although China's economy experienced recovery from the global financial crisis, we continued to face various challenges, including intensified telecommunications market competition, further downward adjustments in tariffs and decline of fixed-line voice business. We continued to actively develop full-service operation with a focus on mobile and fixed-line broadband businesses. Revenue for 2010 was RMB171.37 billion, an increase of 11.3% from RMB154.03 billion for 2009. Excluding the effects of fixed-line upfront connection fees of RMB0.19 billion and RMB0.49 billion in 2010 and 2009, respectively, our revenue for 2010 would have been RMB171.18 billion, representing an increase of 11.5% from RMB153.54 billion in 2009, of which our service revenue would have been RMB163.89 billion in 2010, up by 8.3% from 2009.

**Mobile Business Revenue**

Revenue from our mobile business increased by 24.4% from RMB72.07 billion in 2009 to RMB89.62 billion in 2010. Of the revenue from our mobile business in 2009 and 2010, RMB70.10 billion and RMB82.45 billion, respectively, was from service. Service revenue from our mobile business as a percentage of our total service revenue (excluding fixed-line upfront connection fees of RMB0.19 billion and RMB0.49 billion in 2010 and 2009, respectively) increased from 46.3% in 2009 to 50.3% in 2010. The growth in revenue from our mobile business is primarily due to the continued increase in the total number of our mobile subscribers, as well as an increase in our subscribers' ARPU. The increase in ARPU was due to the change of revenue mix between our GSM business and 3G business. 3G business has a significantly higher ARPU than GSM business. Therefore, despite the ARPU of each of our GSM and 3G businesses decreased in 2010 compared to 2009, as the revenue from 3G business increased significantly as a percentage of total service revenue from mobile business from 1.1% in 2009 to 21.0% in 2010, the overall ARPU of our mobile business increased. In 2010, service revenue from 3G business was RMB11.60 billion.

Our total number of mobile subscribers was 167.43 million as of December 31, 2010, with a net addition of 19.84 million subscribers (including 11.32 million 3G subscribers) from the end of 2009. ARPU of our GSM mobile business was RMB39.5 in 2010, a decrease of 4.1% from RMB41.2 in 2009. ARPU of our 3G business was RMB124.0 in 2010, a decrease of 12.5% from RMB141.7 in 2009.

The table below sets forth the revenue composition of our mobile business and each revenue item's respective share of total revenue for the years ended December 31, 2009 and 2010.

	2009 (Restated) <sup>(1)</sup>		2010 (Restated) <sup>(1)</sup>	
	RMB in millions	% of total	RMB in millions	As % of total
Total revenue from mobile business	72,072	100.0	89,622	100.0
Service revenue	70,102	97.3	82,449	92.0
Usage fees and monthly fees	42,297	58.7	47,004	52.4
Value-added service revenue	19,150	26.6	25,920	28.9
Interconnection revenue	8,220	11.4	9,022	10.1
Other service revenue	435	0.6	503	0.6
Sales of mobile telecommunications products	1,970	2.7	7,173	8.0

<sup>(1)</sup> The financial data of 2009 and 2010 presented herein was restated to reflect the effects of the 2011 Acquisition. See Note 2.2 to our consolidated financial statements included elsewhere in this annual report on Form 20-F.

**Usage Fees and Monthly Fees.** As a result of an increase in mobile subscribers, partially offset by the decrease in effective tariffs, usage fees and monthly fees for our mobile services were RMB47.00 billion in 2010, an increase of 11.1% from RMB42.30 billion in 2009.

**Value-Added Service Revenue.** Value-added service revenue consists primarily of revenue from our 3G value-added services and GSM value-added services. In 2010, we continued to actively promote mobile value-added services and mobile data business, and improved the penetration of SMS, Cool Ringtone and mobile Internet services. As a result, revenue from our mobile value-added services amounted to RMB25.92 billion in 2010, representing an increase of 35.4% from RMB19.15 billion in 2009 and as a percentage of total mobile revenue increased from 26.6% in 2009 to 28.9% in 2010. Of the total revenue from mobile value-added services, revenue from our SMS services increased by 1.6% from RMB8.00 billion in 2009 to RMB8.13 billion in 2010, revenue from Cool Ringtone services increased by 6.8% from

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RMB2.88 billion in 2009 to RMB3.08 billion in 2010 and revenue from mobile Internet services increased by 390.0% from RMB2.80 billion in 2009 to RMB7.70 billion in 2010.

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*Interconnection Revenue.* Our interconnection revenue increased by 9.8% from RMB8.22 billion in 2009 to RMB9.02 billion in 2010, and represented 10.1% of total mobile revenue in 2010 as compared with 11.4% in 2009. This increase is primarily as a result of the increased total usage of our mobile services due to the increased total number of our mobile subscribers.

*Sales of Telecommunications Products.* Revenue from our sale of mobile telecommunications products increased from RMB1.97 billion in 2009 to RMB7.17 billion in 2010, mainly due to our continuing efforts in promoting our bundled sale of 3G mobile handsets and provision of 3G mobile services.

*Fixed-Line Business Revenue*

In 2010, as mobile substitution further intensified and the declining trend of the fixed-line voice business continued, we further developed our fixed-line broadband services and promoted our mobile and fixed-line bundled services. Excluding fixed-line upfront connection fees of RMB0.49 billion and RMB0.19 billion in 2009 and 2010, respectively, our revenue from fixed-line business would have decreased by 1.2% from RMB80.86 billion in 2009 to RMB79.86 billion in 2010, of which service revenue would have decreased by 1.1% from RMB80.67 billion in 2009 to RMB79.75 billion in 2010. See *D. Risk Factors* We may further lose fixed-line and mobile subscribers and our doubtful debt ratios may increase, which may materially adversely affect our financial condition, results of operations and growth prospects under Item 3.

The table below sets forth the revenue composition of our fixed-line business and each revenue item's respective share of total revenue from our fixed-line business for the years ended December 31, 2009 and 2010.

	For the Year Ended December 31,			
	2009 (Restated) <sup>(1)</sup>		2010 (Restated) <sup>(1)</sup>	
	RMB in millions	As % of Total	RMB in millions	As % of Total
Total revenue from fixed-line business <sup>(2)</sup>	80,863	100.0	79,864	100.0
Service revenue <sup>(2)</sup>	80,670	99.8	79,750	99.9
Usage fee and monthly fee	34,369	42.5	29,085	36.4
Broadband, managed data and other Internet-related services revenue	26,364	32.6	32,595	40.8
Interconnection revenue	5,599	6.9	5,243	6.6
Value-added service revenue	5,238	6.5	4,860	6.1
Leased line service revenue	5,683	7.0	5,589	7.0
Information communication technology services revenue	1,035	1.3	1,048	1.3
Others	2,382	3.0	1,330	1.7
Sales of fixed-line telecommunications products	193	0.2	114	0.1

(1) The financial data of 2009 and 2010 presented herein was restated to reflect the effects of the 2011 Acquisition. See Note 2.2 to our consolidated financial statements included elsewhere in this annual report on Form 20-F.

(2) Excluding fixed-line upfront connection fees of RMB490 million in 2009 and RMB192 million in 2010. Fixed-line upfront connection fees represent the amortization of deferred upfront connection fees received from the customers before July 1, 2001. No upfront connection fee was received from the customers since then. Therefore, we consider that analyses of our operating results excluding upfront connection fees are more relevant to the readers of this report.

*Usage Fees and Monthly Fees.* Usage fees include local usage fees charged for local telephone calls and VoIP long distance calls, long distance usage fees for domestic and international long distance calls originated by our fixed-line subscribers, users of our pre-paid phone cards and certain other customers. Monthly fees represent the fixed amount of service charges to our customers for using our fixed-line telephone services.

As a result of further implementation of the *Calling-Party-Pays* tariff policy for mobile services and continuing downward adjustments of tariffs for fixed-line services, the substitution effect of fixed-line local services by mobile services became more intense. We experienced significant decline in the number of our fixed-line local telephone subscribers and substantial decline in revenue. Our local telephone subscribers decreased in 2010 by 6.0% from 102.82 million at the end of 2009 to 96.64 million at the end of 2010. ARPU of the local telephone business decreased by 8.0% from 2009 to RMB28.9 in 2010. Total usage of local calls decreased by 16.2% from 2009 to 155.56 billion pulses in 2010 (excluding Internet dial-up usage) and total usage of long distance calls decreased by 20.2% from 33.58 billion minutes in 2009 to 26.79 billion minutes in

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2010. As a result, revenue from our usage fees and monthly fees in 2010 decreased by 15.4% from RMB34.37 billion in 2009 to RMB29.09 billion in 2010.



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*Broadband, managed data and other Internet-related services revenue.* Revenue from our broadband, managed data and other internet-related services include revenue generated from DSL, LAN, and broadband-related value-added services, fees that we charge for our DDN, frame relay, ATM, MPLS-VPN and X.25 services and revenue from the provision of Internet dial-up services (other than communication fees) and dedicated Internet access services. Revenue from our broadband, managed data and other Internet-related services increased by 23.6% from RMB26.36 billion in 2009 to RMB32.60 billion in 2010, as a result of increases in both revenue from fixed-line broadband services and from managed data and other Internet-related services.

In 2010, our fixed-line broadband business continued to maintain a rapid growth as a result of our efforts in improving broadband access speed, adopting multi-service bundling strategy, enriching application contents and implementing diversified sales strategies. The number of our fixed-line broadband subscribers increased by 22.5% from 2009 to 47.22 million in 2010. ARPU of our fixed-line broadband business remained stable at RMB57.2 in 2009 and RMB57.1 in 2010. However, revenue from our fixed-line broadband service increased significantly by 24.8% from 2009 to RMB29.82 billion in 2010, and as a percentage of total fixed-line revenue, increased from 29.6% in 2009 to 37.3% in 2010. Fixed-line broadband service has become the main factor in counteracting the effect of mobile substitution in the decline of our fixed-line voice business. Revenue from our managed data services and other Internet-related services increased by 12.1% from RMB2.47 billion in 2009 to RMB2.77 billion in 2010.

*Interconnection Revenue.* Revenue from our interconnection services consists of interconnection fees charged to other domestic telecommunications operators, principally China Mobile and China Telecom, for both local and long distance calls. Revenue from our interconnection services decreased by 6.4% from RMB5.60 billion in 2009 to RMB5.24 billion in 2010. The decrease in interconnection revenue was mainly due to a decrease in voice traffic from other telecommunications operators as a result of the mobile substitution effect.

*Value-Added Service Revenue.* Revenue from our value-added services consists of fees that we charge our customers for the provision of caller identification, personalized ring, telephone information services, video- and tele-conferencing and other value-added services. Revenue from our value-added services decreased by 7.2% from RMB5.24 billion in 2009 to RMB4.86 billion in 2010, mainly due to the decrease in the usage of our caller identification, Personalized Ring, and PHS SMS services as a result of the significant reduction of our fixed-line telephone subscribers, including PHS subscribers.

*Leased Line Service Revenue.* Revenue from our leased line services consists of fees that we receive from our government, corporate and carrier customers for leasing circuit capacity to them, including the lease of digital circuits, digital trunk lines and optic fibers. Revenue from our leased line services decreased by 1.7% from RMB5.68 billion in 2009 to RMB5.59 billion in 2010.

*Information Communication Technology Services Revenue.* Information communication technology services revenue increased by 1.3% from RMB1.04 billion in 2009 to RMB1.05 billion in 2010.

*Others.* Other fixed-line related revenue mainly consists of miscellaneous revenue items. Other fixed-line related revenue decreased by 44.2% from RMB2.38 billion in 2009 to RMB1.33 billion in 2010.

*Sales of Telecommunications Products.* Revenue from our sales of fixed-line telecommunications products decreased by 40.9% from RMB0.19 billion in 2009 to RMB0.11 billion in 2010, mainly due to the decrease in sales of telecommunications terminal products such as telephone sets associated with local voice services in 2010.

**Costs, Expenses and Others**

Total costs, expenses and others in 2010 were RMB166.79 billion, representing an increase of 17.6% from RMB141.87 billion in 2009. Excluding the effects of the realized gains of RMB1.24 billion on changes in fair value of derivative financial instrument in 2009, our total costs, expenses and others in 2010 increased by 16.5% from RMB143.11 billion in 2009.

**Table of Contents***Mobile Business Operating Costs and Expenses*

Operating costs and expenses for our mobile business in 2010 were RMB62.98 billion, representing an increase of 39.5% from RMB45.13 billion in 2009. The table below sets forth the principal items of operating costs and expenses from mobile business and their respective percentage of the telecommunications services revenue from mobile business for the years 2009 and 2010:

	<b>For the Year Ended December 31,</b>			
	<b>2009 (Restated)<sup>(1)</sup></b>		<b>2010 (Restated)<sup>(1)</sup></b>	
	<b>RMB in millions</b>	<b>% of Total</b>	<b>RMB in millions</b>	<b>% of Total</b>
Service revenue from mobile business	70,102	100.0	82,449	100.0
Mobile business costs and expenses	45,134	64.4	62,980	76.3
Interconnection charges	13,104	18.7	14,452	17.5
Depreciation and amortization	17,851	25.4	23,362	28.3
Networks, operations and support expenses	2,508	3.6	3,106	3.8
Selling and marketing	7,708	11.0	9,390	11.4
General, administrative and other expenses	1,533	2.2	2,175	2.6
Cost of telecommunications products sold	2,430	3.5	10,495	12.7

<sup>(1)</sup> The financial data of 2009 and 2010 presented herein was restated to reflect the effects of the 2011 Acquisition and the change in accounting policy for property, plant and equipment upon the adoption of amended IFRS/HKFRS 1 in 2011. See Note 2.2 to our consolidated financial statements included elsewhere in this annual report on Form 20-F.

*Interconnection Charges.* Interconnection charges from mobile business were RMB14.45 billion in 2010, up by 10.3% from 2009, primarily due to an increase in mobile interconnection traffic volume resulting from the increase of total usage of our mobile services. The increase in interconnection charges is consistent with the increase in interconnection revenues. Interconnection charges as a percentage of service revenue from mobile business were 17.5% and 18.7% in 2010 and 2009, respectively.

*Depreciation and Amortization.* Our depreciation and amortization expenses from mobile business were RMB23.36 billion in 2010, up by 30.9% from 2009. The increase was primarily because we focused on improving our 3G network capacity and expanding the 3G network coverage. Meanwhile, we continued to optimize our GSM network. As a percentage of service revenue from mobile business, our depreciation and amortization expenses increased from 25.4% in 2009 to 28.3% in 2010.

*Networks, Operations and Support Expenses.* Due to various factors, including the expansion of networks, facilities and base stations and the increases in utilities charges and rental expenses, we incurred networks, operations and support expenses from mobile business of RMB3.11 billion in 2010, up by 23.8% from 2009. Networks, operations and support expenses, as a percentage of service revenue from mobile business, increased from 3.6% in 2009 to 3.8% in 2010. As a result of an increase in the lease of underlying telecommunications networks from other telecommunications operators, the related line leasing fees was RMB0.34 billion, up by 47.8% from 2009.

*Selling and Marketing Expenses.* Due to various factors, including the increased promotion of our 3G business and the increased costs of customer retention and channel subsidies, in 2010, our total selling and marketing expenses from mobile business reached RMB9.39 billion, up by 21.8% from 2009, and as a percentage of service revenue from mobile business, increased from 11.0% in 2009 to 11.4% in 2010.

*General, Administrative and Other Expenses.* We continued to closely monitor the increase in general and administrative expenses. Our general, administrative and other expenses from mobile business were RMB2.18 billion in 2010, up by 41.9% compared with last year, and as a percentage of service revenue from mobile business, increased from 2.2% in 2009 to 2.6% in 2010.

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*Cost of Telecommunications Products Sold.* In 2010, we launched a number of custom-made 3G handsets (including iPhone 4), proactively implemented handsets subsidies packages and developed 3G contracting subscribers. As a result, the cost of telecommunications products sold from mobile business amounted to RMB10.50 billion, up by 331.9% from 2009. Correspondingly, revenue from sales of mobile telecommunications products in 2010 amounted to RMB7.17 billion, up by 264.1% from 2009.

*Fixed-Line Business Operating Costs and Expenses*

Operating costs and expenses for our fixed-line business in 2010 were RMB50.63 billion, representing an increase of 2.8% from RMB49.25 billion in 2009. The table below sets forth the principal items of operating costs and expenses from fixed-line business and their respective percentage of the telecommunications services revenue from fixed-line business for the years 2009 and 2010:

	For the Year Ended December 31,			
	2009 (Restated) <sup>(1)</sup>		2010 (Restated) <sup>(1)</sup>	
	RMB in millions	% of Total	RMB in millions	% of Total
Service revenue from fixed-line business <sup>(2)</sup>	80,670	100.0	79,750	100.0
Fixed-line business costs and expenses	49,254	61.0	50,634	63.4
Interconnection charges	4,292	5.3	3,706	4.7
Depreciation and amortization	28,399	35.2	29,028	36.4
Networks, operations and support expenses	7,780	9.7	9,409	11.8
Selling and marketing	6,733	8.3	6,647	8.3
Cost in relation to information communication technology services	805	1.0	897	1.1
General, administrative and other expenses	986	1.2	754	0.9
Cost of telecommunications products sold	259	0.3	193	0.2

<sup>(1)</sup> The financial data of 2009 and 2010 presented herein was restated to reflect the effects of the 2011 Acquisition and the change in accounting policy for property, plant and equipment upon the adoption of amended IFRS/HKFRS 1 in 2011. See Note 2.2 to our consolidated financial statements included elsewhere in this annual report on Form 20-F.

<sup>(2)</sup> Excludes fixed-line upfront connection fees of RMB490 million in 2009 and RMB192 million in 2010.

*Interconnection Charges.* Interconnection charges from fixed-line business were RMB3.71 billion in 2010, down by 13.7% from 2009, primarily due to a decrease in fixed-line voice interconnection traffic volume resulting from the decrease of total usage of our fixed-line voice services. The decrease in interconnection charges is consistent with the decrease in interconnection revenues. Interconnection charges as a percentage of service revenue from fixed-line business (excluding fixed-line upfront connection fees) were 4.7% and 5.3% in 2010 and 2009, respectively.

*Depreciation and Amortization.* Our depreciation and amortization expenses from fixed-line business were RMB29.03 billion in 2010, up by 2.2% from 2009. The increase was primarily because we continued to expedite broadband network upgrade. As a percentage of service revenue from fixed-line business (excluding fixed-line upfront connection fees), our depreciation and amortization expenses increased from 35.2% in 2009 to 36.4% in 2010.

*Networks, Operations and Support Expenses.* Due to various factors, including the expansion of networks, facilities and base stations and the increases in utilities charges and rental expenses, we incurred networks, operations and support expenses of RMB9.41 billion in 2010, up by 20.9% from 2009. Networks, operations and support expenses, as a percentage of service revenue from fixed-line business (excluding fixed-line upfront connection fees), increased from 9.7% in 2009 to 11.8% in 2010. As a result of an increase in the lease of underlying telecommunications networks from other telecommunications operators, the related line leasing fees was RMB1.2 billion, up by 24.8% from 2009. We completed an acquisition of fixed-line business of 21 provinces in southern China in January 2009. As the underlying telecommunications networks for such business are retained by Unicom Group, we operated those networks through an operating lease from Unicom Group from January 2009. As a result, we incurred a lease fee of RMB2.20 billion for leasing those telecommunications networks in 2010.



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*Selling and Marketing Expenses.* Due to various factors, including the increased promotion of our broadband services and the increased costs of customer retention and channel subsidies, in 2010, our total selling and marketing expenses from fixed-line business reached RMB6.65 billion, down by 1.3% from 2009, and as a percentage of service revenue from fixed-line business (excluding fixed-line upfront connection fees), remained stable at 8.3% in 2009 and 2010.

*Cost in Relation to Information Communication Technology Services.* Cost in relation to information communication technology in 2010 was RMB0.90 billion, up by 11.4% from last year. Correspondingly, revenue from ICT services in 2010 was RMB1.05 billion, up by 1.2% from last year.

*General, Administrative and Other Expenses.* We continued to closely control the growth of general and administrative expenses. Our general, administrative and other expenses from fixed-line business were RMB0.75 billion in 2010, down by 23.5% compared with last year and, as a percentage of service revenue from fixed-line business (excluding fixed-line upfront connection fees), decreased from 1.2% in 2009 to 0.9% in 2010.

*Cost of Telecommunications Products Sold.* The cost of fixed-line telecommunications products sold amounted to RMB0.19 billion, down by 25.5% from 2009. Correspondingly, revenue from sales of fixed-line telecommunications products in 2010 amounted to RMB0.11 billion, down by 40.9% from 2009.

### *Unallocated Costs and Expenses*

The unallocated costs and expenses primarily represent corporate and shared service expenses that are not directly attributable to any of our operating segments. The unallocated costs and expenses also include statement of income items, such as employee benefit expenses, interest income, finance costs and other income, which cannot be directly identified to specific operating segments.

*Employee Benefit Expenses.* Due to various factors, such as increased employee insurance premium expenses and housing fund resulting from new regulations and generally improved social average wages in China, our employee benefit expenses increased by 6.4% from 2009 to RMB23.35 billion in 2010, and as a percentage of service revenue (excluding fixed-line upfront connection fees), decreased from 14.5% in 2009 to 14.2% in 2010.

*Finance Costs, Net of Interest Income.* In 2010, we adopted a low cost fund raising strategy including the issuance of commercial papers, promissory notes and convertible bonds to decrease our overall cost of capital to 3.2% from 4.1% in 2009. However, due to various factors including the increase in our interest-bearing debt, our finance costs, net of interest income, increased by 70.1% from RMB0.94 billion in 2009 to RMB1.61 billion in 2010.

*Realized Gain on Changes in Fair Value of Derivative Financial Instrument.* In order to strengthen our cooperation with Telefónica, we entered into a subscription agreement with Telefónica on September 6, 2009, pursuant to which each party completed the mutual investment of an equivalent of US\$1 billion in each other through an acquisition of the other party's shares on October 21, 2009. At the inception of the subscription agreement on September 6, 2009, our agreement to undertake the above mutual investment with Telefónica was accounted for as a derivative financial instrument in accordance with IAS/HKAS 39 *Financial instrument: Recognition and measurement*, as it represents a forward contract for the purchase of shares by Telefónica and us in each other at predetermined fixed prices and is denominated in a foreign currency. The derivative financial instrument was derecognized upon completion of the transaction on October 21, 2009. The changes in the fair value of the derivative financial instrument during the period from September 6, 2009 to October 21, 2009 resulted in a fair value gain of approximately RMB1.24 billion, which has been recorded in the consolidated statement of income for the year ended December 31, 2009.

*Depreciation and Amortization Expenses.* Depreciation and amortization expenses that are unallocated to mobile and fixed-line businesses were RMB2.34 billion in 2010, up by 53.3% from RMB1.52 billion in 2009. The increase was primarily due to an increase in office and business premises.

*Networks, Operations and Support Expenses.* Networks, operations and support expenses that are unallocated to mobile and fixed-line businesses were RMB13.88 billion in 2010, up by 3.0% from RMB13.47 in 2009, which was primarily due to increases in utility charges and rental expenses as a result of our increased number of base stations and an increase in electricity prices.

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*Other Operating Expenses.* Other operating expenses consist of selling and marketing expenses, general, administrative and other expenses and cost in relation to information communication technology services. Other operating expenses that are unallocated to mobile and fixed-line businesses were RMB18.04 billion in 2010, up by 3.2% from RMB17.48 in 2009, which was mainly due to an increase in customer retention expenses as a result of our adoption of various customer retention initiatives.

*Other Income-Net.* In 2010, other income-net was RMB1.22 billion, up by 26.9% from 2009. The increase was primarily as a result of dividends of RMB0.48 billion received from our investment in Telefónica, up by RMB0.27 billion from 2009.

### ***Income Before Income Tax***

In 2010, our income before income tax was RMB4.58 billion, down by 62.3% from 2009, mainly due to our initial development of the 3G business, in respect of which the related revenue is not yet sufficient to cover the increased costs and expenses, including depreciation and amortization charges, networks, operations and support expenses and selling and marketing expenses related to 3G handset subsidy cost.

In order to ensure the comparability of income before income tax and income for the year, we exclude the following non-comparable factors that are reflected in the figures of 2009 and 2010 for additional analysis purpose:

- (1) deferred fixed-line upfront connection fees of RMB0.19 billion for 2010 and RMB0.49 billion for 2009; and
- (2) realized gain of RMB1.24 billion on changes in fair value of derivative financial instrument in 2009.

Excluding the above factors, our income before income tax would have been RMB4.39 billion, down by 57.9% from 2009.

### ***Income Tax***

Our income tax was RMB0.88 billion in 2010, down by 67.2% from 2009, and our effective tax rate in 2010 was 19.3%. Such decrease is mainly due to various factors, including the utilization of tax loss from the previous years of a subsidiary of our company against the current year taxable income and other favorable tax treatments. Excluding the factors discussed under Income Before Income Tax above, our effective tax rate in 2009 and 2010 would have been 25.8% and 20.1%, respectively.

### ***Net Income for the Year***

In 2010, our net income was RMB3.70 billion, down by 60.9% from 2009. Our basic earnings per share was RMB0.157 in 2010. Excluding the factors discussed under the subsection Income Before Income Tax above, our net income would be RMB3.51 billion, down by 54.6% from 2009.

**Table of Contents****Liquidity and Capital Resources****Working Capital and Cash Flows**

As of December 31, 2011, we had RMB15.11 billion of cash and cash equivalents, as compared with RMB22.60 billion as of December 31, 2010 and RMB7.90 billion as of December 31, 2009. As of December 31, 2011, we had RMB0.30 billion of short-term bank deposits, as compared with RMB0.27 billion as of December 31, 2010 and RMB1.00 billion as of December 31, 2009. As of December 31, 2011, we had a working capital deficit (current liabilities less current assets) of RMB175.12 billion, representing an increase by 12.3% from the working capital deficit of RMB155.91 billion as of December 31, 2010. The increase in working capital deficit in 2011 primarily resulted from the increase in commercial papers and the increase in advances from customer due to our business expansion. The decrease in cash and cash equivalents was primarily as a result of our efforts to increase capital turnover ratio.

In recent years, although the PRC Government introduced measures to avoid overheating of the economy, including tightening bank lending policies, we, due to our enterprise nature and our good credit records with PRC banks, generally have not experienced and do not expect to experience in the foreseeable future significant difficulties in obtaining bank financing in China. As of December 31, 2011, we had RMB206.8 billion revolving banking facilities and registered quota of commercial papers, of which RMB136.5 billion was unutilized. There is no term of the facilities that materially restricts our ability to draw down the unutilized banking facilities. In addition, we believe we have the ability to raise funds from short, medium and long-term perspectives and maintain reasonable financing costs through appropriate financing portfolio. Therefore, we believe that we will be able to fund our anticipated capital and liquidity needs with our access to debt and equity financing, in particular bank financing in China, and net cash inflows from our operations.

The following table sets forth cash inflows and outflows in 2009, 2010 and 2011.

	<b>For the Year Ended December 31,</b>		
	<b>2009</b> <b>(Restated)<sup>(1)</sup></b>	<b>2010</b> <b>(Restated)<sup>(1)</sup></b>	<b>2011</b>
	<b>RMB in</b> <b>millions</b>	<b>RMB in millions</b>	<b>RMB in millions</b>
Net cash inflow from operating activities of continuing operations	57,732	66,376	66,491
Net cash outflow from investing activities of continuing operations	(85,310)	(76,619)	(82,970)
Net cash inflow from financing activities of continuing operations	30,197	19,824	8,988
<b>Net cash inflow/(outflow) from continuing operations</b>	<b>2,619</b>	<b>9,581</b>	<b>(7,491)</b>
<b>Net cash (outflow)/inflow from discontinued operations</b>	<b>(5,039)</b>	<b>5,121</b>	<b>-</b>
<b>Net (decrease)/increase in cash and cash equivalents</b>	<b>(2,420)</b>	<b>14,702</b>	<b>(7,491)</b>

<sup>(1)</sup> The comparative financial data of 2009 and 2010 presented herein was restated to reflect the effects of the 2011 Acquisition and the change in accounting policy for property, plant and equipment upon the adoption of amended IFRS/HKFRS 1 in 2011. See Note 2.2 to our consolidated financial statements included elsewhere in this annual report on Form 20-F.

Our net cash inflow from operating activities of continuing operations increased by 15.0% from RMB57.73 billion in 2009 to RMB66.38 billion in 2010, and further increased by 0.2% to RMB66.49 billion in 2011. The increase in net cash inflow from operating activities in 2010 was mainly due to an increase in cash generated from operations as a result of 3G business development and a decrease in the amount of income tax paid as a result of the lower income before income tax. The increase in net cash inflow from operating activities in 2011 was mainly due to an increase in cash generated from our growing 3G business, partially offset by an increase in interest paid.

Our net cash outflow from investing activities of continuing operations decreased by 10.2% from RMB85.31 billion in 2009 to RMB76.62 billion in 2010, and increased by 8.3% to RMB82.97 billion in 2011. The decrease in 2010 was mainly due to the effect that we no longer have

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any cash outflow from investing activities associated with the consideration for purchase of entities and businesses under common control. The increase in 2011 was mainly due to an amount of RMB3.37 billion used to increase our investment in Telefónica pursuant to the Agreement to Enhance the Strategic Alliance with Telefónica and an increase of US\$2.30 billion in the purchase of property, plant and equipment.



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Our net cash inflow from financing activities decreased from RMB30.20 billion in 2009 to RMB19.82 billion in 2010, primarily as a result of a decrease in the net increase of our indebtedness in 2010 from 2009, reflecting our decreased needs for new financings, primarily due to the increase in our net cash inflow from operating activities and the decrease in our net cash outflow from investing activities. Our net cash inflow from financing activities further decreased to RMB8.99 billion in 2011, primarily due to our decreased needs for new financings as a result of our improved overall cash flow position.

Our net cash outflow from discontinued operations changed from RMB5.04 billion in 2009 to net cash inflow of RMB5.12 billion in 2010, mainly resulting from our payment made in 2009 of the income tax in relation to the sale of our CDMA business in 2008 and our receipt of proceeds in 2010 in relation to the disposal of our CDMA business in 2008. There was no cash inflow or outflow from discontinued operations in 2011.

**Indebtedness and Capital Structure**

The following table sets forth the amount of cash, cash equivalents, assets, short-term and long-term debt and equity as well as debt-to-capitalization and debt-to-equity ratios as of the end of 2009, 2010 and 2011.

	As of December 31,		
	2009 (Restated) <sup>(1)</sup>	2010 (Restated) <sup>(1)</sup>	2011
	(RMB in millions, except percentages)		
Cash and cash equivalents and short-term bank deposits	8,891	22,870	15,410
Total assets	417,008	441,269	456,233
Short-term debt	66,601	61,944	72,606
Short-term bank loans	63,909	36,727	32,322
Commercial papers	-	23,000	38,000
Current portion of long-term bank loans	62	58	50
Amounts due to related parties	2,104	2,033	2,156
Notes payables included in accounts payable and accrued liabilities	500	-	-
Current portion of obligations under finance lease included in other obligations	26	126	78
Long-term debt	7,862	35,098	34,502
Promissory notes	-	15,000	15,000
Corporate bonds	7,000	7,000	7,000
Convertible bonds	-	11,558	11,118
Non-current portion of long-term bank loans	759	1,462	1,384
Non-current portion of obligations under finance lease included in other obligations	103	78	-
Equity attributable to owners of the parent	206,435	205,661	205,898
Debt-to-capitalization ratio <sup>(2)</sup>	26.5%	32.1%	34.2%
Debt-to-equity ratio <sup>(3)</sup>	36.1%	47.2%	52.0%

(1) The comparative financial data of 2009 and 2010 presented herein was restated to reflect the effects of the 2011 Acquisition and the change in accounting policy for property, plant and equipment upon the adoption of amended IFRS/HKFRS 1 in 2011.

(2) Debt-to-capitalization ratio = (long-term interest-bearing debt + short-term interest-bearing debt)/(long-term interest-bearing debt + short-term interest-bearing debt + equity attributable to owners of the parent).

(3) Debt-to-equity ratio = (long-term interest-bearing debt + short-term interest-bearing debt)/equity attributable to owners of the parent.

Our debt-to-capitalization ratio was 34.2% at the end of 2011, compared to 32.1% at the end of 2010 and 26.5% at the end of 2009. Our debt-to-equity ratio was 52.0% at the end of 2011, compared to 47.2% at the end of 2010 and 36.1% at the end of 2009. The sum of our long-term and short-term interest-bearing debt exceeds the amount of our cash and cash equivalents and short-term bank deposits by RMB91.70 billion as of December 31, 2011, compared to RMB74.17 billion as of December 31, 2010 and RMB65.57 billion as of December 31, 2009. The increases in our debt-to-capitalization ratio and debt-to-equity ratio was primarily due to our issuance of commercial papers, promissory notes

and convertible bonds to finance the telecommunications networks construction, which was partially offset by our repayment of short-term bank loans. We continue to seek to optimize our capital structure, develop multiple financing sources and reduce overall financing costs. In addition, we seek to increase our capital turnover ratio and control the amount of monetary assets.

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Our outstanding short-term and long-term bank loans, denominated in RMB, U.S. dollar, HK dollar and Euro, was RMB33.76 billion at the end of 2011, compared to RMB38.25 billion at the end of 2010 and RMB64.73 billion at the end of 2009. The decreases in 2011 and 2010 were primarily because we replaced certain of our short-term bank loans with short-term commercial papers and other debts. The loan agreement does not include financial performance or other covenants which may materially restrict our operations or those of CUCL, our principal operating subsidiary in China. As of December 31, 2011, no short-term bank loans or long-term bank loans were guaranteed by Unicom Group.

In order to further rationalize our debt structure and reduce our interest expense, we may continue to finance a portion of our business operations and capital expenditures through short-term borrowings. Our liquidity in the future will primarily depend on our ability to maintain adequate cash inflow from operations and obtain adequate external financing to meet our debt service obligations and planned capital expenditures. Our operating cash flows could be adversely affected by numerous factors beyond our control, including, but not limited to, changes in telecommunications tariffs, decreased demand for our telecommunications services and further intensified competition. Our ability to obtain external financing also depends on numerous factors, including, but not limited to, our financial condition and creditworthiness as well as our relationship with lenders. See **D. Risk Factors Risks Relating to Our Business**. If we are unable to fund our capital expenditure and debt service requirements, our financial condition, results of operations and growth prospects will be adversely affected under Item 3.

On June 8, 2007, we issued RMB2 billion 10-year corporate bonds, bearing interest at 4.5% per annum. The corporate bonds are secured by a guarantee issued by Bank of China Limited. On September 3, 2008, we issued another RMB5 billion 5-year corporate bonds, bearing interest at 5.29% per annum. The corporate bonds are secured by a guarantee issued by State Grid Corporation of China.

In addition, prior to our merger with China Netcom, China Netcom's wholly-owned subsidiary, CNC China (which merged with, and was absorbed by, our wholly-owned subsidiary, CUCL, in January 2009), issued RMB10 billion unsecured commercial paper in the PRC capital market with payment period of 365 days on October 6, 2008. The effective interest rate is 4.47% per annum. The commercial paper was fully repaid in October 2009.

On April 1, 2010, CUCL completed the issue of the first tranche of commercial paper for the year 2010 in an amount of RMB15 billion, with a maturity period of 365 days and at an interest rate of 2.64% per annum. The commercial paper was fully repaid in March 2011. On April 2, 2010, CUCL completed the issue of the first tranche of promissory note for the year 2010 in an amount of RMB3 billion, with a maturity period of 3 years and at an interest rate of 3.73% per annum.

On September 20, 2010, CUCL completed the issue of the second tranche of commercial paper for the year 2010 in an amount of RMB8 billion, with a maturity period of 365 days and at an interest rate of 2.81% per annum. On the same date, CUCL completed the issue of the second tranche of promissory note for the year 2010 in an amount of RMB12 billion, with a maturity period of 3 years and at an interest rate of 3.31% per annum. The commercial paper was fully repaid in September 2011.

On October 18, 2010, Billion Express Investments Limited, a wholly-owned subsidiary of our company, issued the 2015 Convertible Bonds in aggregate principal amount of US\$1,838,800,000 (at the fixed exchange rate of US\$1 equivalent to HK\$7.7576), which are guaranteed by our company and are exchangeable into ordinary shares of our company. Pursuant to the subscription agreement with respect to the 2015 Convertible Bonds, the holders of the 2015 Convertible Bonds may, beginning on November 28, 2010, elect to convert its bonds into our ordinary shares at an initial conversion price of HK\$15.85 per share, subject to certain adjustments. Pursuant to the relevant terms and conditions, the conversion price of the 2015 Convertible Bonds will be adjusted to HK\$15.58 per share upon the payment of the 2011 final dividend, which is expected to be June 6, 2012. As of April 20, 2012, none of the 2015 Convertible Bonds has been converted into our ordinary shares.

On March 10, 2011, CUCL completed the issue of the first and second tranches of super and short-term commercial paper for the year 2011 in an amount of RMB8 billion for each tranche, each with a maturity period of 180 days and at an interest rate of 3.88% per annum. The first and second tranches of super and short-term commercial paper were fully repaid in September 2011.

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On August 25, 2011, CUCL completed the issue of the first tranche of commercial paper for the year 2011 in an amount of RMB15 billion, with a maturity period of 366 days and at an interest rate of 5.23% per annum.

On September 16, 2011, CUCL completed the issue of the third and fourth tranches of super and short-term commercial paper for the year 2011 in an amount of RMB4 billion for each tranche, each with a maturity period of 30 days and at an interest rate of 5.35% per annum. The third and fourth tranches of super and short-term commercial papers were fully repaid in October 2011.

On October 20, 2011, CUCL completed the issue of the second tranche of commercial paper for the year 2011 in an amount of RMB8 billion, with a maturity period of 366 days and at an interest rate of 5.78% per annum.

On November 21, 2011, CUCL completed the issue of the fifth tranche of super and short-term commercial paper for the year 2011 in an amount of RMB15 billion, with a maturity period of 180 days and at an interest rate of 4.65% per annum.

**Contractual Obligations and Commercial Commitments**

The following table sets forth the amounts of our outstanding contractual cash obligations as of December 31, 2011.

	<b>Total</b>	<b>Less than 1 year</b>	<b>Between 1 and 3 years</b>	<b>Between 3 and 5 years</b>	<b>Over 5 years</b>
Short-term bank loans <sup>(1)*</sup>	32,877	32,877	-	-	-
Commercial papers <sup>(2)*</sup>	39,150	39,150	-	-	-
Long-term bank loans <sup>(3)*</sup>	1,553	101	953	108	391
Corporate bonds <sup>(4)*</sup>	7,932	355	5,358	180	2,039
Convertible bonds <sup>(5)*</sup>	11,916	87	174	11,655	-
Promissory notes <sup>(6)*</sup>	15,820	509	15,311	-	-
Other obligations*	2,676	2,588	12	11	65
Capital commitments <sup>(7)</sup>	8,817	5,596	1,371	301	1,549
Operating leases commitments <sup>(7)</sup>					
Telecommunications networks leasing arrangement in 21 provinces in southern China	2,600	2,600	-	-	-
Other commitments	7,007	1,833	2,756	1,817	601
<b>Total obligations</b>	<b>130,348</b>	<b>85,696</b>	<b>25,935</b>	<b>14,072</b>	<b>4,645</b>

\* Interest included

(1) See Note 27 Short-Term Bank Loans to our consolidated financial statements included elsewhere in this annual report on Form 20-F.

(2) See Note 26 Commercial Papers to our consolidated financial statements included elsewhere in this annual report on Form 20-F.

(3) See Note 20 Long-Term Bank Loans to our consolidated financial statements included elsewhere in this annual report on Form 20-F.

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- (4) See Note 23 Corporate Bonds to our consolidated financial statements included elsewhere in this annual report on Form 20-F.
- (5) See Note 22 Convertible Bonds to our consolidated financial statements included elsewhere in this annual report on Form 20-F.
- (6) See Note 21 Promissory Notes to our consolidated financial statements included elsewhere in this annual report on Form 20-F.
- (7) See Note 41 Contingencies and Commitments to our consolidated financial statements included elsewhere in this annual report on Form 20-F.

### ***Trend Information***

Please refer to the discussion in sections headed Overview and Operating Results under this Item 5.

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As of December 31, 2011, except for the operating lease of the telecommunications networks in 21 provinces in southern China set forth above in Contractual Obligations and Commercial Commitments, we did not have any other off-balance sheet arrangement.

**Capital Expenditures**

The following table sets forth our historical and planned capital expenditure requirements for the periods indicated. Actual future capital expenditures may differ from the amounts indicated below.

	For the Year Ended December 31,					
	2010		2011		2012	
	(RMB in billions)	As a Percentage	(RMB in billions)	As a Percentage	(RMB in billions)	As a percentage
Mobile business	23.17	33.0%	25.99	33.9%	38.7	38.7%
Broadband and data business	22.45	32.0%	25.71	33.5%	25.8	25.8%
Infrastructure and transmission network	16.96	24.2%	15.42	20.1%	25.6	25.6%
Others <sup>(1)</sup>	7.61	10.8%	9.54	12.5%	9.9	9.9%
<b>Total</b>	<b>70.19</b>	<b>100.0%</b>	<b>76.66</b>	<b>100.0%</b>	<b>100.00</b>	<b>100.0%</b>

<sup>(1)</sup> Other expenditures consist of innovation and value-added platform, IT system, fixed-line business and procurement of miscellaneous assets, equipment and spare parts.

Our capital expenditure totaled RMB76.66 billion in 2011, which mainly consisted of investment in mobile business, broadband and data business, and infrastructure and transmission networks. In 2011, capital expenditure attributable to mobile business was RMB25.99 billion; capital expenditure attributable to broadband and data business was RMB25.71 billion; capital expenditure attributable to infrastructure and transmission networks was RMB15.42 billion.

Our projected capital expenditure for 2012 is estimated to be approximately RMB100.00 billion, a significant portion of which will continue to be used for investments in our 3G business and data business as well as infrastructure and transmission networks that support the development of our 3G and fixed-line broadband businesses.

We expect to fund our capital expenditure needs through a combination of cash generated from operating activities, granted and unused banking facilities and other available financing sources. See D. Risk Factors Risks Relating to Our Business. If we are unable to fund our capital expenditure and debt service requirements, our financial condition, results of operations and growth prospects will be adversely affected. under Item 3.

**Item 6. Directors, Senior Management and Employees****A. Directors and Senior Management**

The following table sets forth certain information concerning our current directors and executive officers.

Name	Age	Position
Chang Xiaobing	55	

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		Chairman of the Board of Directors and Chief Executive Officer
Lu Yimin	48	Executive Director and President
Tong Jilu	54	Executive Director and Senior Vice President
Li Fushen	49	Executive Director and Chief Financial Officer
Cesareo Alierta Izuel	66	Non-Executive Director
Cheung Wing Lam Linus	63	Independent Non-Executive Director
Wong Wai Ming	54	Independent Non-Executive Director
John Lawson Thornton	58	Independent Non-Executive Director

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<b>Name</b>	<b>Age</b>	<b>Position</b>
Chung Shui Ming Timpson	60	Independent Non-Executive Director
Cai Hongbin	44	Independent Non-Executive Director
Li Jianguo	58	Senior Vice President
Li Gang	54	Senior Vice President
Zhang Junan	55	Senior Vice President
Jiang Zhengxin	55	Senior Vice President
Shao Guanglu	48	Senior Vice President

**Mr. Chang Xiaobing** was appointed in December 2004 as an Executive Director, Chairman and Chief Executive Officer of the Company. Mr. Chang, a professor level senior engineer, graduated in 1982 from the Nanjing Institute of Posts and Telecommunications with a bachelor's degree in telecommunications engineering and received a master's degree in business administration from Tsinghua University in 2001. He received a doctor's degree in business administration from the Hong Kong Polytechnic University in 2005. Prior to joining China United Telecommunications Corporation, Mr. Chang served as a Deputy Director of the Nanjing Municipal Posts and Telecommunications Bureau of Jiangsu Province and a Deputy Director General of the Directorate General of Telecommunications of the Ministry of Posts and Telecommunications and a Deputy Director General and Director General of the Department of Telecommunications Administration of the former Ministry of Information Industry, Vice President of China Telecommunications Corporation, as well as Executive Director and President of China Telecom Corporation Limited. Mr. Chang was appointed the Chairman of China United Telecommunications Corporation in November 2004. In December 2008, China United Telecommunications Corporation changed its company name to China United Network Communications Group Company Limited (Unicom Group). Mr. Chang has served as a Director of Telefónica since May 2011. He also serves as the Chairman of Unicom Group, A Share Company and CUCL, respectively. Mr. Chang has extensive operational and managerial experience in the telecommunications industry.

**Mr. Lu Yimin** was appointed as an Executive Director of the Company in October 2008 and President of the Company in February 2009. Mr. Lu, a researcher level senior engineer, graduated from Shanghai Jiao Tong University with a bachelor's degree in computer science in 1985 and then was awarded a master's degree in public administration by the John F. Kennedy School of Government at Harvard University. Mr. Lu joined Netcom Group in December 2007, serving as senior management. Mr. Lu has served as a Non-Executive Director of PCCW Limited (listed on the Hong Kong Stock Exchange with an American Depositary Receipt trading on the Pink Sheets OTC Market in the U.S.) since May 2008 and the Deputy Chairman of PCCW Limited since November 2011. Mr. Lu has served as a Non-Executive Director of HKT Limited (listed on the Hong Kong Stock Exchange) and HKT Management Limited (the trustee-manager of the HKT Trust, which is listed on the Hong Kong Stock Exchange) since November 2011. Prior to joining the Netcom Group, Mr. Lu was a member of the Secretary Bureau of the General Office of the Chinese Communist Party Central Committee, serving as the Deputy Director and the Director of the Information Processing Office since 1992, Secretary at deputy director general level since 2001 and Secretary at director general level since 2005. Mr. Lu is Vice Chairman and President of Unicom Group. Mr. Lu is also a Director and President of A Share Company, and a Director and President of CUCL. Mr. Lu has extensive experience in government administration and business management.

**Mr. Tong Jilu** was appointed as an Executive Director of the Company in February 2004 and Senior Vice President of the Company in March 2011. Mr. Tong graduated in 1987 from the Department of Economic Management at the Beijing University of Posts and Telecommunications. He received a doctor's degree in management from the Hong Kong Polytechnic University in 2009. Mr. Tong was Deputy Director General of the Posts and Telecommunications Administration of Liaoning Province, as well as the Posts Office of Liaoning Province. Mr. Tong joined China United Telecommunications Corporation in July 2000. He served first as Chief Accountant and later a Vice President and, from September 2003, a Director of China United Telecommunications Corporation. In December 2008, China United Telecommunications Corporation changed its company name to China United Network Communications Group Company Limited (Unicom Group). From February 2004 to March 2011, Mr. Tong served as Chief Financial Officer of the Company. Mr. Tong now serves as a Director and Vice President of Unicom Group. He is also a Director of A Share Company, and a Director and Senior Vice President of CUCL. Mr. Tong has extensive operation and financial management experience in telecommunications companies.



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**Mr. Li Fushen** was appointed in March 2011 as an Executive Director and Chief Financial Officer of the Company. Mr. Li graduated from the Jilin Engineering Institute with a degree in engineering management in 1988, and from the Australian National University with a master's degree in management in 2004. From November 2001 to October 2003, Mr. Li served as Deputy General Manager of the former Jilin Provincial Telecommunications Company and Jilin Communications Company. From October 2003 to August 2005, Mr. Li served as General Manager of the Finance Department of Netcom Group. Since October 2005, he has served as the Chief Accountant of Netcom Group. He has served as Chief Financial Officer of China Netcom since September 2005 and has served as Executive Director of China Netcom since January 2007. From December 2006 to March 2008, Mr. Li served as Joint Company Secretary of China Netcom. From February 2009 to March 2011, Mr. Li served as a Senior Vice President of the Company. In addition, Mr. Li has served as a Non-Executive Director of PCCW Limited (listed on the Hong Kong Stock Exchange with an American Depository Receipt trading on the Pink Sheets OTC Market in the U.S.) since July 2007, and a Non-Executive Director of HKT Limited (listed on the Hong Kong Stock Exchange) and HKT Management Limited (the trustee-manager of the HKT Trust, which is listed on the Hong Kong Stock Exchange) since November 2011. Mr. Li is a Director, Vice President and Chief Accountant of Unicom Group, a Director of A Share Company, as well as Director and Senior Vice President of CUCL. Mr. Li has worked in the telecommunications industry for a long period of time and has extensive management experience.

**Mr. Cesareo Alierta Izuel** was appointed in October 2008 as a Non-Executive Director of the Company. Mr. Alierta has been a member of the Board of Directors of Telefónica (listed on various stock exchanges including Madrid, New York and London) from January 1997 and has been Chairman of Telefónica since July 2000. Mr. Alierta is a member of the Board of Directors of Telecom Italia (listed on the stock exchange of Milan) and of International Consolidated Airlines Group (IAG, listed on the stock exchanges of Madrid and London). He is also the Chairman of the Social Board of the UNED (National Long Distance Spanish University) and a member of the Columbia Business School Board of Overseers. Between 1970 and 1985, he was the General Manager of the Capital Markets division at Banco Urquijo in Madrid. He has been the founder and Chairman of Beta Capital. As from 1991, he has also acted as the Chairman of the Spanish Financial Analysts Association. He has also been a member of the Board of Directors and the Standing Committee of the Madrid Stock Exchange. Between 1996 and 2000, he held the post of Chairman of Tabacalera, S.A., and subsequently Altadis following the company's merger with the French group Seita. Mr. Alierta served as a Non-Executive Director of China Netcom during the period from December 2007 to November 2008. In September 2005, Mr. Alierta received The Global Spanish Entrepreneur award from the Spanish/US Chamber of Commerce. Mr. Alierta holds a degree in law from the University of Zaragoza and received a master's degree of business administration at the University of Columbia (New York) in 1970.

**Mr. Cheung Wing Lam Linus** was appointed in May 2004 as an Independent Non-Executive Director of the Company. Mr. Cheung is Chairman of the University of Hong Kong School of Professional and Continuing Education. Besides, Mr. Cheung is a Non-Executive Director of HKR International Limited (listed on the Hong Kong Stock Exchange). Mr. Cheung was Chairman of Asia Television Limited, Deputy Chairman of PCCW Limited, an independent Non-Executive Director of Taikang Life Insurance Company Limited and President of the Chartered Institute of Marketing (Hong Kong Region). Prior to the merger of Pacific Century Cyberworks Limited and Cable & Wireless HKT Limited, or Hongkong Telecom, Mr. Cheung was the Chief Executive of Hongkong Telecom and an Executive Director of Cable & Wireless plc in the United Kingdom. Mr. Cheung also worked at Cathay Pacific Airways for 23 years, before departing as Deputy Managing Director. He was appointed an Official Justice of the Peace in 1990 and a Non-official Justice of the Peace in 1992. Mr. Cheung received a bachelor's degree in social sciences and a diploma in management studies from the University of Hong Kong. He is also an Honorary Fellow of the University of Hong Kong and of The Chartered Institute of Marketing in the United Kingdom.

**Mr. Wong Wai Ming** was appointed in January 2006 as an Independent Non-Executive Director of the Company. Mr. Wong is Senior Vice President and Chief Financial Officer of Lenovo Group Limited (listed on the Hong Kong Stock Exchange and the New York Stock Exchange). Besides, Mr. Wong is a Non-Executive Director of Linmark Group (listed on the Hong Kong Stock Exchange). Prior to his current executive position at Lenovo Group Limited, Mr. Wong was a Chief Executive Officer and Executive Director of Roly International Holdings Limited and an Executive Director of Linmark Group. Mr. Wong was also a Non-Executive Director of Kingsoft Corporation Limited and an Independent Non-Executive Director of I.T Limited (listed on the Hong Kong Stock Exchange). Mr. Wong was previously an investment banker with over 15 years of experience in investment banking business in Greater China and was a member of the Listing Committee of The Stock Exchange of Hong Kong Limited. Mr. Wong is a chartered accountant and holds a bachelor's degree (with Honors) in management science from the Victoria University of Manchester in the United Kingdom.

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**Mr. John Lawson Thornton** was appointed in October 2008 as an Independent Non-Executive Director of the Company and is currently a Professor and Director of the Global Leadership Program at the Tsinghua University School of Economics and Management in Beijing. He is also the Chairman of the Board of Trustees of the Brookings Institution in Washington, D.C. He is a Director and Non-Executive Chairman of HSBC North America Holdings Inc., as well as a Director of HSBC Holdings plc (listed on the Hong Kong Stock Exchange, London Stock Exchange, New York Stock Exchange, Paris Stock Exchange and Bermuda Stock Exchange). He is also a Director of the Ford Motor Company (listed on the New York Stock Exchange) and News Corporation, Inc. (listed on the NASDAQ Global Select Market and the Australian Stock Exchange). Mr. Thornton is a trustee, advisory board member or member of the Asia Society, China Foreign Affairs University, China Institute, China Investment Corporation, China Reform Forum, China Securities Regulatory Commission, Council on Foreign Relations, General Atlantic, The Hotchkiss School, McKinsey Knowledge Council, Morehouse College, and the National Committee on U.S.-China Relations. He is the Chairman of the Advisory Board of the Tsinghua University School of Economics and Management. Mr. Thornton served as a Director of Intel Corporation from July 2003 to May 2010, an Independent Non-Executive Director of China Netcom from October 2004 to November 2008. Mr. Thornton retired in July 2003 as President, Co-Chief Operating Officer and a Director of The Goldman Sachs Group, Inc. Mr. Thornton received an A.B. in history from Harvard College in 1976, a B.A. and M.A. in jurisprudence from Oxford University in 1978 and an M.P.P.M. from the Yale School of Management in 1980.

**Mr. Chung Shui Ming Timpson** was appointed in October 2008 as an Independent Non-Executive Director of the Company. Mr. Chung is a member of the National Committee of the 11th Chinese People's Political Consultative Conference. He is also the Chairman of the Advisory Committee on Arts Development. Besides, Mr. Chung is an Independent Non-Executive Director of Glorious Sun Enterprises Limited, The Miramar Hotel & Investment Co. Limited, Nine Dragons Paper (Holdings) Limited and China Overseas Grand Oceans Group Limited (all listed on the Hong Kong Stock Exchange). Mr. Chung is also an Independent Director of China State Construction Eng. Corp. Ltd. and China Everbright Bank Company Limited (both listed on the Shanghai Stock Exchange) and an Outside Director of China Mobile Communications Corporation. From October 2004 to November 2008, Mr. Chung served as an Independent Non-Executive Director of China Netcom. Formerly, he was the Chairman of China Business of Jardine Fleming Holdings Limited and the Deputy Chief Executive Officer of BOC International Limited. He was also the Director-General of Democratic Alliance for the Betterment and Progress of Hong Kong, the Chairman of the Council of the City University of Hong Kong, the Chairman of the Hong Kong Housing Society, a member of the Executive Council of the Hong Kong Special Administrative Region, the Vice Chairman of the Land Fund Advisory Committee of Hong Kong Special Administrative Region Government, a member of the Managing Board of the Kowloon-Canton Railway Corporation, a member of the Hong Kong Housing Authority and a member of the Disaster Relief Fund Advisory Committee. Mr. Chung holds a bachelor of science degree from the University of Hong Kong and a master's degree of business administration from the Chinese University of Hong Kong. Mr. Chung also received an honorary doctoral degree in Social Science from the City University of Hong Kong in 2010. Mr. Chung is a fellow member of the Hong Kong Institute of Certified Public Accountants.

**Mr. Cai Hongbin** was appointed in May 2010 as an Independent Non-Executive Director of the Company. Mr. Cai is currently the Dean of and a Professor in Applied Economics at Guanghua School of Management at Peking University. Besides, Mr. Cai is an Independent Director of China Everbright Bank Company Limited (listed on the Shanghai Stock Exchange). Prior to joining Guanghua School of Management at Peking University, Mr. Cai served as an Assistant Professor of the Economics Department at University of California, Los Angeles. He was also an Independent Non-Executive Director of Concord Medical Services Holdings Limited and Beijing Venustech Inc. Mr. Cai received a bachelor's degree in Mathematics from Wuhan University in 1988, a master's degree in Economics from Peking University in 1991, and a doctoral degree in Economics from Stanford University in 1997. In addition, Mr. Cai was awarded New Century Excellent Talents in University from Ministry of Education of the PRC, or the Ministry of Education, in 2006, the National Outstanding Young Researcher from National Science Foundation of China in 2007 and the National Changjiang Scholar from the Ministry of Education in 2008. Mr. Cai has carried out extensive research in the areas of, among others, game theory, industrial organization, corporate finance and Chinese economy, and has published many academic papers in top international and national journals.

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**Ms. Li Jianguo** was appointed as Senior Vice President of the Company in February 2009. Ms. Li graduated from the Xiangtan University with a bachelor's degree in Chemical Engineering in 1982 and received a master's degree in business administration from the Hong Kong Polytechnic University in 2006. From June 2000 to July 2007, Ms. Li held various senior positions in China United Telecommunications Corporation, including serving as a Director and Chairperson of the Labour Union. Ms. Li also served as the Chairperson of the Board of Supervisors of A Shares Company from December 2001 to July 2007 and as Executive Director of the Company from April 2006 to July 2007. Ms. Li served as Senior Management in Netcom Group since July 2007. She has also served as Executive Director of China Netcom since July 2007. Ms. Li holds a senior managerial position in Unicom Group. Ms. Li is the Chairman of the Supervisory Board of A Share Company, as well as Director and Senior Vice President of CUCL. Ms. Li held leading positions in various enterprises, local governments and state ministries and committees for long period of time, and she has extensive working and management experiences in government, authorities and enterprises.

**Mr. Li Gang** was appointed as Vice President of the Company in April 2006 and Senior Vice President of the Company in February 2009. Mr. Li graduated from Beijing University of Posts and Telecommunications in 1985 and received a master's degree in business administration from the Department of Advanced Business Administration of Jinan University in 2004. Mr. Li previously served as a Deputy Director of the Telecommunications Division, a Deputy Director of the Telecommunications Department, a Deputy Director of the Rural Telephone Bureau, a Deputy Director and a Director of the Telecommunications Operation and Maintenance Department of the Posts and Telecommunications Administration Bureau in Guangdong Province and as a Director of the Mobile Communication Bureau in Guangdong Province. From 1999 to 2005, he served as the Deputy Chairman, General Manager and Chairman of Guangdong Mobile Communication Co., Limited and as the Chairman and General Manager of Beijing Mobile Communication Co., Limited. From 2000 to 2005, he also served as an Executive Director of China Mobile (Hong Kong) Limited. Mr. Li joined China United Telecommunications Corporation in December 2005 and served as Vice President. In December 2008, China United Telecommunications Corporation changed its company name to China United Network Communications Group Company Limited (Unicom Group). From April 2006 to October 2008, Mr. Li served as an Executive Director of the Company. In addition, Mr. Li has served as a Non-Executive Director of PCCW Limited since November 2011. Mr. Li is a Vice President of Unicom Group, as well as a Director and Senior Vice President of CUCL. Mr. Li has worked in the telecommunications industry for a long period of time and has extensive management experience.

**Mr. Zhang Junan** was appointed as Vice President of the Company in April 2006 and Senior Vice President of the Company in February 2009. Mr. Zhang graduated from the Nanjing University of Posts and Telecommunications majoring in carrier communication in 1982. He received a master's degree in business administration from the Australian National University in 2002 and a doctor's degree in business administration from the Hong Kong Polytechnic University in 2008. He previously served as a Director of the Bengbu Municipal Posts and Telecommunications Bureau in Anhui Province and a Deputy Director of the Anhui Provincial Posts and Telecommunications Bureau. From 2000 to 2005, he served as a Deputy General Manager and General Manager of the Anhui Provincial Telecommunications Company and the Chairman and General Manager of the Anhui Provincial Telecommunications Co., Limited. Mr. Zhang joined the China United Telecommunications Corporation in December 2005 and served as Vice President. In December 2008, China United Telecommunications Corporation changed its company name to China United Network Communications Group Company Limited (Unicom Group). From April 2006 to October 2008, Mr. Zhang served as the Executive Director of the Company. In addition, Mr. Zhang serves as a Non-Executive Director of China Communications Services Corporation Limited. Mr. Zhang also serves as Vice President of Unicom Group, as well as Director and Senior Vice President of CUCL. Mr. Zhang has worked in the telecommunications industry for a long period of time and has extensive management experience.

**Mr. Jiang Zhengxin** was appointed as Senior Vice President of the Company in February 2009. Mr. Jiang is a senior engineer of professor level. He received a bachelor's degree in radio engineering from Beijing University of Posts and Telecommunications in 1982, a master's degree in business administration from Jilin University in 2001, and a PhD in political economy from Jilin University in 2006. Mr. Jiang served as Deputy Director of the Bureau of Telecommunications Administration in Changchun of Jilin Province from February 1998 to July 1999. He was the Deputy General Manager of Jilin Mobile Communication Company from July 1999 to March 2004. He served as the Deputy General Manager of South Communication Co. Limited of Netcom Group from March 2004 to June 2004, and he was the General Manager of Zhejiang Branch of Netcom Group from June 2004 to September 2007. He has served as Deputy General Manager of Netcom Group since September 2007. Mr. Jiang is a Vice President of Unicom Group, as well as Director and Senior Vice President of CUCL. Mr. Jiang has worked in the telecommunications industry for a long period of time and has extensive management experience.

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**Mr. Shao Guanglu** was appointed as Senior Vice President of the Company in April 2011. Mr. Shao is a senior engineer. He received a bachelor's degree from Harbin Institute of Technology in 1985, a master's degree in engineering and a master's degree in economics from Harbin Institute of Technology in 1988 and 1990, respectively, a master's degree in management from BI Norwegian Business School in 2002 and a doctor's degree in management from Nankai University in 2009. Mr. Shao joined China United Telecommunications Corporation in February 1995. In December 2008, China United Telecommunications Corporation changed its company name to China United Network Communications Group Company Limited (Unicom Group). Mr. Shao was Deputy General Manager of Tianjin Branch, Deputy General Manager of Henan Branch, General Manager of Guangxi Branch, as well as Head and General Manager of Human Resource Department of Unicom Group. Mr. Shao also serves as a Vice President of Unicom Group, as well as a Director and Senior Vice President of CUCL. Mr. Shao has worked in the telecommunications industry for a long period of time and has extensive management experience.

**B. Compensation**

The aggregate compensation and other benefits paid by us to our directors as a group in 2011 was approximately RMB5.527 million, while retirement benefits paid by us were approximately RMB118,000. Each of our executive directors participated in a bonus scheme with us that ties the amount of bonus he or she will receive at the end of a year to our operating results of the year and his or her job performance. Some of our directors also hold options to purchase shares in our company. See E. Share Ownership below for detailed descriptions of our share option schemes and options granted to our directors as well as compensation for the year 2011.

**C. Board Practices****General**

Pursuant to our articles of association, at each annual general meeting, one-third of our directors retire from office by rotation. The retiring directors are eligible for re-election. The Board may at any time appoint a new director to fill a vacancy or as an additional director. The Board may also appoint and remove our executive officers. No benefits are payable to our directors or executive officers upon termination of their service with us in accordance with the provisions of their service agreements, except certain statutory compensation. The following table sets forth certain information concerning our current directors and former directors who served as directors in 2011.

Name	Appointment Date	Re-appointment Date	Resignation or Retirement Date
<b>Current Directors</b>			
		May 12, 2006 and	
Chang Xiaobing	December 21, 2004	May 26, 2009	
Lu Yimin	October 15, 2008	May 26, 2009 and	
		May 24, 2011	
Tong Jilu	February 1, 2004	May 12, 2004,	
		May 12, 2006,	
		May 16, 2008 and	
		May 12, 2010	
Li Fushen	March 30, 2011	May 24, 2011	
Cesareo Alierta Izuel	October 15, 2008	May 26, 2009 and	



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<b>Name</b>	<b>Appointment Date</b>	<b>Re-appointment Date</b>	<b>Resignation or Retirement Date</b>
Cheung Wing Lam Linus	May 12, 2004	May 12, 2006, May 16, 2008 and May 12, 2010	
Wong Wai Ming	January 19, 2006	May 12, 2006, May 26, 2009 and May 24, 2011	
John Lawson Thornton	October 15, 2008	May 26, 2009	
Chung Shui Ming Timpson	October 15, 2008	May 26, 2009	
Cai Hongbin	May 13, 2010	May 24, 2011	
<b>Former Directors</b>			
Zuo Xunsheng	October 15, 2008	May 26, 2009 and May 12, 2010	March 30, 2011

**Audit Committee**

The audit committee reviews and supervises our financial reporting process and internal controls. The duties of the audit committee include, among others:

as the key representative body for overseeing our relationship with the independent auditor, considering and approving the appointment, resignation and removal of our independent auditor and the auditor's fees;

reviewing our quarterly, interim and annual financial statements and disclosures before submission to the board of directors;

coordinating and discussing with the independent auditor with respect to any issues identified and recommendations made during the audit;

reviewing any correspondence from the independent auditor to our management and the responses of our management;

reviewing the relevant reports concerning our internal controls and procedures;

discussing our internal control system with our management to ensure that our management perform their duties to have an effective internal control system in place;

pre-approving the audit and non-audit services to be provided by the external auditor, and determining whether any non-audit services would affect the independence of the auditor;

discussing with our management the schedule and procedures for the rotation of the partner of the auditing firm who will principally be responsible for the audit of our company and the partners who will actively participate in the audit of our company;

supervising the internal audit department, which will directly report to the committee; and

having the right to approve the appointment or removal of the head of internal audit department.

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As of April 20, 2012, the members of the audit committee are Mr. Wong Wai Ming (Chairman of the audit committee), Mr. Cheung Wing Lam Linus, Mr. John Lawson Thornton, Mr. Chung Shui Ming Timpson and Mr. Cai Hongbin, all being independent non-executive directors of our company.

**Remuneration Committee**

The remuneration committee meets regularly to consider human resources issues, issuance of options and other matters relating to compensation. The primary duties of the remuneration committee include considering and approving the remuneration policies and structure for directors and senior management's remuneration, considering and making recommendations to the Board regarding the remuneration packages of the directors and senior management, and considering and approving our employee share option scheme and any other incentive scheme as they apply to the executive directors, including determining the granting of options to executive directors. The remuneration committee also conducts performance review of the Chief Executive Officer and determines the Chief Executive Officer's year-end bonus pursuant to the performance target contract entered into between the Board and the Chief Executive Officer. The Chief Executive Officer is responsible for the performance review and determination of performance-based year-end bonuses for the other members of our management, which is subject to the review of the remuneration committee. In addition, the remuneration committee consults the Chairman of the Board on the remuneration proposals for other executive directors. As of April 20, 2012, the members of the remuneration committee are Mr. Cheung Wing Lam Linus (Chairman of the remuneration committee), Mr. Wong Wai Ming, Mr. John Lawson Thornton, Mr. Chung Shui Ming Timpson and Mr. Cai Hongbin, all being independent non-executive directors of our company.

**Nomination Committee**

The nomination committee meets regularly to consider the nomination of our directors and senior management personnel. The primary duties of the nomination committee are to (i) review the structure, size and composition of the Board at least annually and make recommendations on any proposed changes to the Board; (ii) identify individuals suitably qualified to become Board members and select or make recommendations to the Board; (iii) assess the independence of independent non-executive directors; (iv) make recommendations to the Board on the appointment or re-appointment of directors and succession planning for directors; and (v) provide opinion to the Board on candidates nominated by our Chief Executive Officer to become our senior management personnel and on changes to our senior management personnel. As of April 20, 2012, the members of the nomination committee are Mr. Cai Hongbin (Chairman of the nomination committee), Mr. Chang Xiaobing, Mr. John Lawson Thornton and Mr. Chung Shui Ming Timpson. Except for Mr. Chang Xiaobing, who is our Chairman and Chief Executive Officer, each of the members of the nomination committee is an independent non-executive director of our company.

**D. Employees**

As of December 31, 2009, 2010 and 2011, we had a total number of 321,772, 310,030 and 297,210 employees, respectively. The employees as of December 31, 2011 are classified by function as follows:

<b>By Function</b>	<b>Number of Employees</b>
Employees	215,945
Management and administration	23,380
Sales and customer service	63,135
Product and Marketing	18,073
Network construction and maintenance	79,835
Support	26,675
Others	4,856
Temporary employees	81,256
<b>Total</b>	<b>297,210</b>



**Table of Contents****E. Share Ownership**

As of April 20, 2012, our directors who own shares in our company are listed as follows:

Name	Capacity and Nature	Ordinary Shares Held	Percentage of Total Issued Shares
Cheung Wing Lam Linus	Beneficial Owner ( <i>Personal</i> )	400,000	0.0017%
Chung Shui Ming Timpson	Beneficial Owner ( <i>Personal</i> )	6,000	0.0000%

Apart from those disclosed herein, as of April 20, 2012, our other directors as a group do not own any shares in our company.

As of April 20, 2012, our directors as a group hold options for 2,619,840 shares, or approximately 0.01% of our issued and outstanding share capital, including the following options granted under our share option scheme and special purpose share option scheme:

Name Directors	Capacity and Nature	Number of Shares Covered <sup>(1)</sup>	Expiration Date	Exercise Price	Consideration Paid	Compensation for 2011 (RMB in thousands)
Chang Xiaobing	Beneficial Owner ( <i>Personal</i> )	526,000	December 20, 2013 <sup>(3)</sup>	HK\$6.20	HK\$1.00	995
		746,000	February 14, 2014 <sup>(3)</sup>	HK\$6.35	HK\$1.00	
Lu Yimin						984
Tong Jilu	Beneficial Owner ( <i>Personal</i> )	92,000	July 19, 2013 <sup>(3)</sup>	HK\$5.92	HK\$1.00	868
		460,000	February 14, 2014 <sup>(3)</sup>	HK\$6.35	HK\$1.00	
	Beneficial Owner ( <i>Spouse</i> )	32,000	July 19, 2013 <sup>(3)</sup>	HK\$5.92	HK\$1.00	
		40,000	February 14, 2014 <sup>(3)</sup>	HK\$6.35	HK\$1.00	
Li Fushen	Beneficial Owner ( <i>Personal</i> )	723,840	November 16, 2013 <sup>(3)</sup>	HK\$5.57		657
Cesareo Alierta Izuel						248
Cheung Wing Lam Linus						339
Wong Wai Ming						348
John Lawson Thornton						329
Chung Shui Ming Timpson						329
Cai Hongbin						335
<b>Employees<sup>(2)</sup></b>						
		8,956,000	May 20, 2013 <sup>(3)</sup>	HK\$4.30	HK\$1.00	
		40,900,000	July 19, 2013 <sup>(3)</sup>	HK\$5.92	HK\$1.00	
		128,000	December 20, 2013 <sup>(3)</sup>	HK\$6.20	HK\$1.00	
		150,310,000	February 14, 2014 <sup>(3)</sup>	HK\$6.35	HK\$1.00	
		99,637,850	November 16, 2013 <sup>(3)</sup>	HK\$5.57	HK\$1.00	
		88,929,468	December 5, 2013 <sup>(3)</sup>	HK\$8.26	HK\$1.00	

(1) Each option gives the holder the right to subscribe for one share.

- (2) In 2009, the exercise periods of approximately 25,000,000 options were extended by one year by the Board pursuant to the terms of the Share Option Scheme. The reasons for such extension were that (i) the holders of those options were determined by the Board as Transferred Personnel under the terms of the Share Option Scheme due to the transfers of those option holders to other telecommunications operators as part of the 2008 industry restructuring and (ii) those options were not exercisable due to a Mandatory Moratorium under the terms of the Share Option Scheme. Due to the Mandatory Moratorium continuing to be in force, the Board further extended the exercise periods of certain options by one year in each of March 2010, 2011 and 2012 under the terms of the Share Option Scheme. As of December 31, 2011, approximately 23,440,000 share options held by Transferred Personnel remained valid.

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- (3) In each of March 2010, 2011 and 2012, the expiry dates for certain options were extended by one year by the Board pursuant to the terms of each of the Share Option Scheme and the Special Purpose Share Option Scheme, because those options were not exercisable due to a Mandatory Moratorium, which is still in force, under the respective terms of each of the Share Option Scheme and the Special Purpose Share Option Scheme.

**Stock Incentive Schemes**

*Share Option Scheme.* We adopted a share option scheme on June 1, 2000, and amended the scheme on each of May 13, 2002, May 11, 2007 and May 26, 2009. The amended scheme provides for the grant of options to our employees, including executive directors and non-executive directors. Any grant of options to a connected person (as defined in the HKSE Listing Rules) of Unicom requires approval by our independent non-executive directors, excluding any independent non-executive director who is the grantee of the option. The option period commences on any date after the date on which an option is offered, but may not exceed 10 years from the offer date. The subscription price of a share in respect of any particular option granted under this share option scheme will be determined by our board of directors in its discretion at the grant date, which shall be no less than the higher of: (i) the nominal value of the shares; (ii) the closing price of the shares on the HKSE on the grant date of such option; and (iii) the average closing price of the shares on the HKSE for the five trading days immediately preceding the grant date. As of April 20, 2012, 202,190,000 options granted by us under the share option scheme were outstanding and held by two directors and approximately 2,800 of our employees. The share option scheme expired on June 21, 2010. Following the expiry of the share option scheme, no further option may be granted under the share option scheme, but the provisions of the share option scheme will remain in full force and effect to the extent necessary to give effect to the exercise of the options granted prior to the expiry or otherwise as may be required in accordance with the provisions of the share option scheme. As of April 20, 2012, 4,310,000 options (with an exercise price of HK\$15.42), 34,131,200 options (with an exercise price of HK\$6.18), 92,398,800 options (with an exercise price of HK\$4.3), 366,000 options (with an exercise price of HK\$4.66), 67,084,000 options (with an exercise price of HK\$5.92) and 10,652,000 options (with an exercise price of HK\$6.35) had been exercised.

*Special Purpose Share Option Scheme.* We also adopted a special purpose share option scheme on September 16, 2008, in connection with our merger with China Netcom and amended the scheme on May 26, 2009. The special purpose share option scheme provides for the grant of options to the optionholders of China Netcom, in consideration for the cancellation of their outstanding China Netcom options (whether vested or not) on October 14, 2008. There are two exercise periods for the options granted under the special purpose share option scheme, one of which commenced on October 15, 2008, and will end on November 16, 2013 (as extended by the Board), with an exercise price of HK\$5.57 and the other commenced on October 15, 2008, and will end on December 5, 2013 (as extended by the Board), with an exercise price of HK\$8.26. No amount was payable on acceptance of the grant of options under the special purpose share option scheme. As of April 20, 2012, 189,291,158 options granted under this scheme were outstanding and held by one director and approximately 690 of our employees. As of April 20, 2012, 265,408 options (with an exercise price of HK\$5.57) granted under the Special Purpose Share Option Scheme had been exercised.

**Item 7. Major Shareholders and Related Party Transactions****A. Major Shareholders**

As of April 20, 2012, our controlling shareholder, Unicom Group, through its 17.90% direct interest in Unicom BVI, 61.50% direct interest in the A Share Company (which in turn holds 82.10% of Unicom BVI) and 100% direct interest in Netcom BVI, indirectly and beneficially owned approximately 16.7 billion shares of Unicom, or 71.01% of our total outstanding shares. See A. History and Development of the Company under Item 4. Unicom Group's shares are held by the SASAC and a group of companies, most of which are state-owned enterprises in China. Shares beneficially owned by Unicom Group do not carry voting rights different from our other issued shares. In addition, Telefónica held 9.57% of our total outstanding shares.

As of April 20, 2012, most of our shareholders of record were located outside of the United States. In addition, as of April 20, 2012, there were approximately 52,106,177 ADSs outstanding, each representing 10 shares and together representing 2.21% of our total outstanding shares or 7.63% of our total outstanding shares not beneficially owned by our controlling shareholder.

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### ***B. Related Party Transactions***

Prior to our merger with China Netcom, Netcom BVI and Netcom Group (which was the 100% owner of Netcom BVI) did not have any shareholding interest in us. Upon completion of the merger, China Netcom became one of our wholly-owned subsidiaries and Netcom BVI currently owns 29.74% of our total outstanding shares. Accordingly, the related party transactions between China Netcom and its subsidiaries, namely, CNC China (which merged with, and was absorbed by, CUCL in January 2009 after the completion of our merger with China Netcom) and China Unicom System Integration (formerly known as China Netcom System Integration, which became one of our wholly-owned subsidiaries upon the completion of our merger with China Netcom), on one hand and Netcom Group (which merged with, and was absorbed by, Unicom Group in January 2009 after the completion of our merger with China Netcom) on the other hand in effect before our merger with China Netcom became our related party transactions upon the completion of the merger.

There were transactions between certain of our subsidiaries and Netcom Group in existence before our merger with China Netcom. Upon completion of the merger, these transactions became our related party transactions. On August 12, 2008, CUCL and Netcom Group entered into various framework agreements to record the principles governing, and the principal terms of, these continuing transactions that would take effect upon the completion of our merger with China Netcom. All of these framework agreements expired by the end of 2010.

In addition, before our merger with China Netcom, we had entered into a number of service arrangements with Unicom Group and/or its subsidiaries (other than us and our subsidiaries) with respect to the provision of ongoing telecommunications and ancillary services between Unicom Group and us. On October 26, 2006, we entered into a comprehensive services agreement with Unicom Group to record such related party transactions. In order to include CNC China as a party to the service arrangements and to facilitate our business and operations after our merger with China Netcom, Unicom Group and the A Share Company entered into a comprehensive services agreement on August 12, 2008, and the A Share Company, CUCL and CNC China entered into a transfer agreement on August 12, 2008, to amend the terms of the continuing related party transactions between us and Unicom Group in existence before our merger with China Netcom, with effect upon the completion of the merger. On October 29, 2010, CUCL and Unicom Group entered into the 2010 comprehensive services agreement to renew certain continuing related party transactions for a term of three years commencing on January 1, 2011 and expiring on December 31, 2013.

In January 2009, subsequent to our merger with China Netcom and the disposal of our CDMA business, we completed our acquisitions, through CUCL, of certain telecommunications business and assets from Unicom Group and Netcom Group, including the telecommunications business across 21 provinces in southern China.

### **2011 Acquisition**

In December 2011, we completed our acquisitions through Broadband Online, a wholly-owned subsidiary of CUCL, of the entire equity interest in Unicom NewSpace from Unicom Group for a total cash consideration of RMB158 million. Unicom NewSpace primarily engages in mobile value-added business in China.

### **Continuing Related Party Transactions under the 2010 Comprehensive Services Agreement**

Under the two-step approach described under *A. History and Development of the Company Two-Step Voting Arrangements* of Item 4, the continuing transactions between CUCL and Unicom Group under the comprehensive services agreement entered into in 2006 were amended, or the amended comprehensive services agreement, effective upon the completion of our merger with China Netcom, with CNC China added as party to such transactions. In January 2009, CNC China merged into CUCL. Pursuant to the amended comprehensive services agreement, Unicom Group agreed to provide certain services to CUCL and CNC China, being the supply of telephone cards, the provision of equipment procurement services, interconnection arrangements, the mutual provision of premises, the provision of international telecommunications network gateway, the provision of operator-based value-added services, the provision of value-added telecommunications services, the provision of 10010/10011 customer services, the provision of agency services and the provision of engineering design and technical services, until December 31, 2010.

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On October 29, 2010, CUCL and Unicom Group entered into the 2010 comprehensive services agreement to renew certain continuing connected transactions for a term of three years commencing on January 1, 2011 and expiring on December 31, 2013. Unless CUCL notifies Unicom Group at least 60 days prior to the expiration of such agreement of their intention not to renew the 2010 comprehensive services agreement, such agreement shall automatically be renewed for a further period of three years.

Details of the continuing related party transactions under the 2010 comprehensive services agreement are summarized below.

### ***Telecommunications Resources Leasing***

Unicom Group agrees to lease to CUCL certain international telecommunications resources and certain other telecommunications facilities required by CUCL for its operations.

The rental charges for the leasing of international telecommunications resources and other telecommunications facilities are based on the annual depreciation charges of such resources and telecommunications facilities, provided that such charges would not be higher than market rates. CUCL will be responsible for the on-going maintenance of the leased international telecommunications resources. CUCL and Unicom Group will determine and agree which party is to provide maintenance service to the leased telecommunications facilities. Unless otherwise agreed by CUCL and Unicom Group, such maintenance service charges would be borne by CUCL. If Unicom Group is responsible for maintaining any leased telecommunications facilities, CUCL will pay to Unicom Group the relevant maintenance service charges which will be determined with reference to market rates, or where there are no market rates, be agreed between the parties and determined on a cost-plus basis. The net rental charges and service charges due to Unicom Group for the provision of the leased telecommunications resources leasing will be settled between CUCL and Unicom Group on a quarterly basis. In 2011, the total charges paid by CUCL to Unicom Group amounted to approximately RMB307 million.

### ***Property Leasing***

CUCL and Unicom Group agree to lease to each other properties and ancillary facilities belonging to CUCL or Unicom Group (including their respective branch companies and subsidiaries).

The rental charges payable by CUCL or Unicom Group are based on market rates or the depreciation charges and taxes in respect of each property, provided that such rental charges will not be higher than the market rates. The rental charges are payable quarterly in arrears and are subject to review every year to take into account the then prevailing market rates of the properties leased in that year. In 2011, the rental charges paid by CUCL to Unicom Group amounted to approximately RMB954 million and the rental charges paid by Unicom Group to CUCL was negligible.

### ***Provision of Value-added Telecommunications Services***

Unicom Group (or its subsidiaries) agrees to provide the customers of CUCL with various types of value-added telecommunications services.

CUCL will settle the revenue generated from the value-added telecommunications services with the branches of Unicom Group (or its subsidiaries) on the condition that such settlement will be based on the average revenue for independent value-added telecommunications content providers who provide value-added telecommunications content to CUCL in the same region. The revenue will be settled on a monthly basis. In 2011, the total revenue allocated to Unicom Group in relation to value-added services amounted to approximately RMB51 million.

### ***Provision of Equipment Procurement Services***

Unicom Group agrees to provide comprehensive procurement services for imported and domestic telecommunications equipment and other domestic non-telecommunications equipment to CUCL. Unicom Group also agrees to provide services on management of tenders, verification of technical specifications, installation, consulting and agency services.

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In addition, Unicom Group will sell cable, modem and other materials operated by itself to CUCL and will also provide storage and logistics services in relation to the above equipment and materials procurement.

Charges for the provision of equipment procurement services are calculated at the rate of:

(a) up to 3% of the contract value of those procurement contracts in the case of domestic equipment procurement; and

(b) up to 1% of the contract value of those procurement contracts in the case of imported equipment procurement.

The charges for the provision of materials operated by Unicom Group are determined by reference to the following pricing principles:

(A) the government fixed price;

(B) where there is no government fixed price but a government guidance price exists, the government guidance price;

(C) where there is neither a government fixed price nor a government guidance price, the market price; or

(D) where none of the above is applicable, the price to be agreed between the parties and determined on a cost-plus basis.

The charges for the provision of storage and logistics services are determined by reference to the market price, which is determined by reference to the following:

(I) the price charged by an independent third party providing the services in the same or nearby location in an ordinary business transaction; or

(II) the price charged by an independent third party providing the services in mainland China in an ordinary business transaction.

The service charges due to Unicom Group will be settled on a monthly basis. In 2011, the total charges paid by CUCL to Unicom Group amounted to approximately RMB227 million.

### ***Provision of Engineering Design and Construction Services***

Unicom Group agrees to provide engineering design, construction and supervision services and IT services to CUCL. Engineering design services include planning and design, engineering inspection, telecommunications electronic engineering, telecommunications equipment engineering and corporate telecommunications engineering. Construction services include services relating to telecommunications equipment, telecommunications routing, power supplies, telecommunications conduit, and technical support systems. IT services include services relating to office automation, software testing, network upgrading, research and development of new business, and development of support systems.

The charges for the provision of engineering design and construction services are determined by reference to the market price, which is determined by reference to the following:

(a) the price charged by an independent third party providing the services in the same or nearby location in an ordinary business transaction; or

- (b) the price charged by an independent third party providing the services in mainland China in an ordinary business transaction.

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The service charges will be settled between CUCL and Unicom Group as and when the relevant services are provided. In 2011, the total charges paid by CUCL to Unicom Group amounted to approximately RMB2,728 million.

### ***Provision of Ancillary Telecommunications Services***

Unicom Group agrees to provide ancillary telecommunications services to CUCL. These services include certain telecommunications pre-sale, on-sale and after-sale services such as assembling and repairing of certain telecommunications equipment, sales agency services, printing and invoice delivery services, maintenance of telephone booths, customers acquisitions and servicing and other customers services.

The charges payable for the provision of ancillary telecommunications services are determined by reference to the following pricing principles:

- (a) the government fixed price;
- (b) where there is no government fixed price but a government guidance price exists, the government guidance price;
- (c) where there is neither a government fixed price nor a government guidance price, the market price; or
- (d) where none of the above is applicable, the price to be agreed between the parties and determined on a cost-plus basis.

The service charges will be settled between CUCL and Unicom Group as and when the relevant services are provided. In 2011, the total charges paid by CUCL to Unicom Group amounted to approximately RMB1,174 million.

### ***Provision of Comprehensive Support Services***

Unicom Group and CUCL agree to provide comprehensive support services to each other, including dining services, facilities leasing services (excluding those facilities which are provided under the paragraph headed *Provision of Telecommunications Resources Leasing* above), vehicle services, health and medical services, labor services, security services, hotel and conference services, gardening services, decoration and renovation services, sales services, construction agency, equipment maintenance services, market development, technical support services, research and development services, sanitary services, parking services, staff trainings, storage services, advertising services, marketing, property management services, information and communications technology services (including construction and installation services, system integration services, software development, product sales and agent services, operation and maintenance services, and consultation services).

The service charges are determined by reference to the following pricing principles:

- (a) the government fixed price;
- (b) where there is no government fixed price but a government guidance price exists, the government guidance price;
- (c) where there is neither a government fixed price nor a government guidance price, the market price; or
- (d) where none of the above is applicable, the price to be agreed between the parties and determined on a cost-plus basis.



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The service charges will be settled between CUCL and Unicom Group as and when the relevant services are provided. In 2011, the total services charges paid by CUCL to Unicom Group amounted to approximately RMB171 million and the total services charges paid by Unicom Group to CUCL was RMB108 million.

### ***Provision of Shared Services***

Unicom Group and CUCL agree to provide shared services to each other, including, but not limited to, the following:

- (a) CUCL will provide headquarter human resources services to Unicom Group;
- (b) Unicom Group and CUCL will provide central business support services to each other;
- (c) CUCL will provide trust services related to the services referred to in paragraphs (a) and (b) above to Unicom Group; and
- (d) Unicom Group will provide premises to CUCL and other shared services requested by its headquarters.

In relation to the central business support services, CUCL will provide support services, such as billing and settlement services provided by the business support center and operational statistics reports. Unicom Group will provide support services, including telephone card production, development and related services, maintenance and technical support and management services in relation to the telecommunications card operational system.

Unicom Group and CUCL will share the costs related to the shared services proportionately in accordance with their respective total assets value, except that the total assets value of the overseas subsidiaries and the listed company of Unicom Group will be excluded from the total asset value of Unicom Group, and the shared costs proportion will be agreed between Unicom Group and CUCL in accordance with the total assets value set out in the financial statements provided to each other, as adjusted in accordance with their respective total assets value on an annual basis. In 2011, the total services charges paid by CUCL to Unicom Group amounted to approximately RMB177 million and the total services charges paid by Unicom Group to CUCL was negligible.

### **Acquisitions of Fixed-Line Business in 21 Provinces in Southern China and Other Assets from Parent Companies and Lease of Telecommunications Networks in 21 Provinces in Southern China**

Under the two-step voting mechanism described in *A. History and Development of the Company Two-Step Voting Arrangements* under Item 4, we completed our acquisitions, through CUCL, of certain telecommunications business and assets, including the telecommunications business across 21 provinces in southern China, from Unicom Group and Netcom Group pursuant to (1) an acquisition agreement entered into among Unicom Group, Netcom Group and the A Share Company on December 16, 2008, under which the A Share Company agreed to acquire the relevant business and assets and (2) a transfer agreement entered into between the A Share Company and CUCL on December 16, 2008, under which the A Share Company agreed to transfer all of its rights and obligations under the acquisition agreement to CUCL. In addition, in order to operate the fixed-line business in the 21 provinces in southern China, on December 16, 2008, CUCL entered into the initial network lease agreement with Unicom Group, Netcom Group and Unicom New Horizon, a wholly-owned subsidiary of Unicom Group, to lease on an exclusive basis the telecommunications networks in those provinces, which are held by Unicom New Horizon and are necessary for the operation of the fixed-line business in southern China. The initial network lease agreement expired at the end of 2010.

On October 29, 2010, CUCL entered into the 2011-2012 network lease agreement, with Unicom New Horizon, which became effective on January 1, 2011. The 2011-2012 network lease agreement is for an initial term of two years effective from January 1, 2011 and is renewable at the option of CUCL with at least two months' prior notice on the same terms and conditions, except for the future lease fee which will remain subject to further negotiations between the parties. The annual lease fee payable by CUCL under the 2011-2012 network lease agreement for the years ending December 31, 2011 and 2012 is RMB2.4 billion and RMB2.6 billion, respectively. In connection with the 2011-2012 network lease agreement, Unicom New Horizon also granted CUCL an option, but not an obligation, to purchase the telecommunications networks leased in southern China. The purchase option may be exercised, at the discretion of CUCL, at any time during the term of the lease. No premium has been paid or will be payable by CUCL for such purchase option. In the event that CUCL elects to exercise this purchase option, the parties will discuss and negotiate the purchase price with reference to the appraised value of the telecommunications networks in southern China, which is to

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be determined in accordance with applicable laws of Hong Kong and China, after taking into account the prevailing market conditions and other factors. Under the 2011-2012 network lease agreement, CUCL is responsible for the ongoing cost and expenses incurred in respect of the maintenance and management which may arise from the use of the leased telecommunications networks in southern China. See A. History and Development Acquisitions of Fixed-Line Business in 21 Provinces in Southern China and Other Assets from Parent Companies and Lease of Telecommunications Networks in 21 Provinces in Southern China under Item 4.

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### **Mergers of Parent Companies and Subsidiaries**

As part of our integration with China Netcom, our wholly-owned subsidiary, CUCL, merged with CNC China, a wholly-owned subsidiary of China Netcom, with effect from January 2009, and upon such merger becoming effective, CUCL assumed all the rights and obligations of CNC China, and all the assets, liabilities and business of CNC China were vested in CUCL. In addition, China Netcom's parent, Netcom Group, also merged with our parent, Unicom Group, with effect from January 2009, and upon such merger becoming effective, Unicom Group assumed all the rights and obligations of Netcom Group, and all the assets, liabilities and business of Netcom Group were vested in Unicom Group.

### **Certain Agreements Relating to Our Initial Public Offering**

#### ***The Reorganization Agreement***

In relation to the restructuring in connection with our initial public offering, our wholly-owned subsidiary, CUCL, entered into a reorganization agreement with Unicom Group, dated April 21, 2000. This agreement includes the following terms:

Unicom Group's agreement to transfer to CUCL certain assets and liabilities;

mutual warranties and indemnities given by Unicom Group and CUCL in relation to the assets and liabilities transferred to CUCL and in relation to the restructuring;

undertakings by Unicom Group in favor of CUCL, including, among other things:

to hold and maintain all licenses received from the former Ministry of Information Industry in connection with any of our businesses for our benefit, and to allocate spectrum and to provide other resources to us;

subject to applicable Chinese laws and regulations in effect at the relevant time, to take all actions necessary to obtain, maintain, renew and otherwise extend to or for our benefit such governmental or regulatory licenses, consents, permits or other approvals as we shall require to continue to operate our businesses;

to arrange for us to participate in its international roaming arrangements;

not to engage in any business that competes with our businesses, except for the existing competing businesses of Unicom Group;

to grant us a right of first refusal in relation to any governmental authorization, license or permit, or other business opportunity to develop any new telecommunications technology, product or service;

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to ensure that we can continue to use the premises for which title documentation cannot be obtained at this time, for a period of three years following the restructuring;

not to dispose of any of our shares it beneficially owns or to take or permit any other actions, including primary issuances of securities by us or CUCL, which would result in us or CUCL no longer constituting majority-owned subsidiaries of Unicom Group; and

not to seek an overseas listing for any of its businesses or the businesses of its subsidiaries in which we are engaged or may engage in the future except through us;

an option granted by Unicom Group to us to acquire Unicom Group's interest in any telecommunications interest, such as Unicom Paging, Unicom Xingye and Unicom Group's CDMA telephony license and business; and

a commitment by Unicom Group that it will provide continuous financial support to us when necessary.

The 2010 comprehensive services agreement provides that the determination of whether we or CUCL would constitute majority-owned subsidiaries of the Unicom Group shall be made in accordance with the PRC Enterprise Accounting Standards, as amended by the Ministry of Finance from time to time.

### ***Trademark Agreement***

Unicom Group is the registered owner of the Unicom trademark in English, the trademark bearing the Unicom logo and the trademark of the word "Unicom" in Chinese ( ), which are registered at the PRC State Trademark Bureau. Under a PRC trademark license agreement entered into on May 25, 2000 between Unicom Group and CUCL, CUCL and our affiliates were granted the right to use these trademarks on a royalty-free basis for an initial period of five years, renewable at the option of CUCL. Under the terms of this agreement, we and our affiliates are the exclusive licensees of these trademarks, provided that Unicom Group may also license these trademarks to any of its existing or future subsidiaries. Unicom Group also agreed to license to CUCL any trademark that it registers in China in the future that incorporates the word "Unicom."

### **C. Interests of Experts and Counsel**

Not Applicable.

### **Item 8. Financial Information**

See Item 18 Financial Statements. Other than as disclosed elsewhere in this annual report, no significant change has occurred since the date of the annual financial statements.

### **Legal Proceedings**

We are not involved in any material litigation, arbitration or administrative proceedings. We are not aware of any pending or threatened litigation, arbitration or administrative proceedings expected to have a material effect on our financial condition and results of operations.

In 2011, the NDRC initiated an anti-monopoly investigation relating to the price charged for Internet dedicated leased line access service provided by us to Internet service providers. In response to the NDRC's investigation, we (i) provided the NDRC with pricing, volume, turnover and other information relevant to our Internet access bandwidth leasing business with Internet service providers for the year 2010, (ii) conducted a comprehensive self-inspection of our operations and (iii) submitted to the NDRC a proposal for enhancement initiatives and an application for suspension of the NDRC's investigation. Through our comprehensive self-inspection of our operations, we have identified room for improvement in pricing management and relatively wide pricing variation, in respect of our business relating to the Internet dedicated leased line access service provided by us to the Internet service providers. In addition, the quality of interconnection between us and other backbone network operators also requires further improvement. As of the date of this annual report, the NDRC has not informed us of any results or conclusions of the investigation.



**Table of Contents****Policy on Dividend Distribution**

The objective of our dividend policy is to achieve a long-term, sustainable and steadily increasing dividend, with a view to maximize our shareholders' value. The declaration and payment of future dividends will depend upon, among other things, financial condition, business prospects, future earnings, cash flow, liquidity level and cost of capital. We believe such policy will provide our shareholders with a stable return in the long term along with the growth of our company. We may only pay dividends out of our distributable profits.

Based on the Company's financial position in 2011 and taking into account the development needs of the mobile and fixed-line broadband businesses, our board of directors recommended the payment of a final dividend of RMB0.10 per share for the year ended December 31, 2011, compared to RMB0.08 per share for the fiscal year ended December 31, 2010.

**Item 9. The Offer and Listing  
Market Price Information**

Our ADSs, each representing ten ordinary shares, are listed and traded on the NYSE. Our ordinary shares are listed and traded on the HKSE. The NYSE and the HKSE are the principal trading markets for our ADSs and ordinary shares, which are not listed on any other exchanges in or outside the United States.

The high and low closing prices of our ordinary shares on the HKSE and of our ADSs on the NYSE since listing are as follows:

	Price per Ordinary Share (HK\$)		Price per ADS (US\$)	
	High	Low	High	Low
<b>Annual:</b>				
2007	18.80	9.18	24.52	11.75
2008	19.58	8.53	25.07	10.27
2009	12.34	6.84	15.75	8.72
2010	12.16	8.31	15.54	10.58
2011	17.40	11.04	22.39	14.11
<b>Quarterly:</b>				
First Quarter, 2010	10.40	8.31	13.41	10.58
Second Quarter, 2010	10.76	8.84	13.55	11.09
Third Quarter, 2010	12.16	9.96	15.54	12.55
Fourth Quarter, 2010	11.68	10.32	15.06	13.34
First Quarter, 2011	13.58	11.04	17.49	14.11
Second Quarter, 2011	17.36	13.40	22.08	17.26
Third Quarter, 2011	17.40	13.40	22.39	17.45
Fourth Quarter, 2011	16.80	14.58	21.70	19.12
First Quarter, 2012	16.78	14.26	21.58	16.33
<b>Monthly:</b>				
October 2011	16.20	14.58	20.82	19.12
November 2011	16.80	15.76	21.61	19.86
December 2011	16.78	15.44	21.70	20.07
January 2012	16.78	14.20	21.58	18.23
February 2012	14.76	13.66	18.80	17.47
March 2012	14.26	12.86	18.47	16.33
April 2012 (through April 24, 2012)	13.50	12.70	17.37	16.32



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**Item 10. Additional Information**

**A. *Share Capital***

Not Applicable.

**B. *Memorandum and Articles of Association***  
**General**

Under our Articles of Association, we have the capacity, rights, powers, liabilities and privileges of a natural person and, in addition to and without limiting the forgoing, we may do anything which is permitted or required to be done by any enactment or rule of law. The following is a summary of selected provisions of our Articles of Association:

**Directors**

***Material Interests and Voting***

A director shall not vote (or be counted in the quorum) on any resolution of our board of directors in respect of any contract or arrangement or proposal in which he or any of his associates (as defined in the HKSE Listing Rules) is, to his knowledge, materially interested, and if he shall do so, his vote shall not be counted (nor shall he be counted in the quorum for that resolution), but this prohibition does not apply to any contract, arrangement or other proposal for or concerning:

the giving of any security or indemnity either (i) to the director or any of his associates (as defined in the HKSE Listing Rules) in respect of money lent or obligations incurred or undertaken by him or any of them at the request of or for the benefit of Unicom or any of its subsidiaries or (ii) to a third-party in respect of a debt or obligation of Unicom or any of its subsidiaries for which the director or any of his associates has assumed responsibility in whole or in part and whether alone or jointly under a guarantee or indemnity or by the giving of security;

an offer of shares or debentures or other securities of or by Unicom (or any other company which Unicom may promote or be interested in) where the director or any of his associates is or will be an interested participant in the underwriting or sub-underwriting of the offer;

any contract or arrangement in which the director or any of his associates is interested in the same manner as other holders of shares or debentures or other securities of Unicom by virtue only of his interest in shares or debentures or other securities of Unicom;

any other company in which the director or any of his associates is interested only, whether directly or indirectly, as an officer or shareholder or in which the director or any of his associates is beneficially interested in shares of that company, provided that he, together with any of his associates, is not beneficially interested in 5% or more of (i) the issued shares of any class of such company (or of any third company through which such interest is derived), or (ii) the voting rights attached to such issued shares or securities (excluding for the purpose of calculating such 5% interest, any indirect interest of such director or any of his associates by virtue of Unicom's interest in such company); or



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the benefit of employees of Unicom or any of its subsidiaries, including (i) the adoption, modification or operation of a pension fund or retirement, death or disability benefits scheme which relates to directors, their associates and employees of Unicom or any of its subsidiaries and does not provide in respect of the director or any of his associates any privilege or advantage not generally accorded to the class of persons to which such scheme or fund relates; or (ii) the adoption, modification or operation of any employee share scheme involving the issue or grant of options over shares or other securities by Unicom to, or for the benefit of, the employees of Unicom or its subsidiaries under which the director or any of his associates may benefit.

### ***Remuneration and Pensions***

The directors of Unicom are entitled to receive by way of remuneration for their services such sum as is from time to time determined by Unicom in a general meeting. The directors are also entitled to have reimbursed all traveling, hotel and other expenses reasonably incurred by them in or about the performance of their duties as directors. The board of directors may grant special remuneration to any director who performs services that, in the opinion of the board, are outside the scope of the ordinary duties of a director.

The board may establish and maintain any contributory or non-contributory pension or superannuation funds for the benefit of, or give donations, gratuities, pensions, allowances or emoluments to, any persons (i) who are or were at any time in the employment or service of Unicom, or of any company which is a subsidiary of Unicom, or is allied or associated with Unicom or with any such subsidiary company, or (ii) who are or were at any time directors or officers of Unicom or of any such other company above, and have or who have had any salaried employment or had held office in Unicom or such other company, and the wives, widows, families and dependents of any such persons. The board may also establish and subsidize or subscribe to any institutions, associations, clubs or funds calculated to be for the benefit of or to advance the interests and well being of Unicom or of any such other company above or of any such persons above, and may make payments for or towards the insurance of any such persons, and subscribe or guarantee money for charitable or benevolent objects or for any exhibition or for any public, general or useful object. Any director holding any such employment or office is entitled to participate in, and retain for his own benefit, any such donation, gratuity, pension, allowance or emolument.

### ***Borrowing Powers***

The directors may exercise all the powers of Unicom to borrow money and to mortgage or charge all or any part of the undertaking, property and assets (present and future) and uncalled capital of Unicom and to issue debentures, debenture stocks, bonds and other securities, whether outright or as collateral security for any debt, liability or obligation of Unicom or of any third-party.

### ***Qualification of Directors***

A director of Unicom is not required to hold any qualification shares.

### ***Rotation of Directors***

At every annual general meeting, one-third of the directors for the time being, or, if the number is not three or a multiple of three, then the number nearest one-third, shall retire from office by rotation, except for any director holding office as chairman or chief executive officer. The directors to retire in every year shall be those who have been in office the longest since their last election. In addition, a director appointed by the board to fill in a casual vacancy or as an addition to the board shall retire at the next following annual general meeting and shall then be eligible for re-election, but shall not be taken into account in determining the number of directors who are to retire by rotation at each annual general meeting. The retiring directors shall be eligible for re-election.

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### **Rights Attached to Ordinary Shares**

#### ***Voting Rights***

Under the Companies Ordinance, any action to be taken by the shareholders at a general meeting requires an affirmative vote by either an ordinary or a special resolution passed at the meeting. An ordinary resolution is one passed by the majority of such shareholders as are entitled to, and do, vote in person or by proxy at a general meeting. A special resolution is one passed by not less than three-quarters of such shareholders as are entitled to, and do, vote in person or by proxy at a general meeting. Most shareholders' decisions are passed by ordinary resolutions. However, the Companies Ordinance and our articles of association stipulate that certain matters may only be passed by special resolutions.

In accordance with the HKSE Listing Rules, any vote of shareholders at a general meeting will be taken by poll.

In a poll, every shareholder present in person or, if the shareholder is a corporation, by duly authorized representative, or by proxy has one vote for every share of which he or she is the shareholder, and which is fully paid up or credited as fully paid up. However, no amount paid up or credited as paid up on a share in advance of calls or installments is treated for the foregoing purposes as paid up on the share.

Any action to be taken by the shareholders requires the affirmative vote of a majority of the shares at a meeting of shareholders. There are no cumulative voting rights. Accordingly, the holders of a majority of the shares voting for the election of directors can elect all the directors if they choose to do so.

#### ***Issue of Shares***

Under the Companies Ordinance, our board of directors may, without prior approval of our shareholders, offer to issue new shares to existing shareholders proportionately according to their shareholdings. Our board of directors may not offer to issue new shares in any other manner without the prior approval of our shareholders at a general meeting. Any such approval given at a general meeting will continue in force until the conclusion of the following annual general meeting or the expiration of the period within which the next annual general meeting is required by law to be held or when revoked or varied by an ordinary resolution of our shareholders in a general meeting, whichever comes first. If such approval is given, the unissued shares shall be at the disposal of our board of directors, which may offer, allot, grant options over or otherwise dispose of them to such persons at such times and for such consideration and upon such terms and conditions as our board of directors may determine.

In accordance with the HKSE Listing Rules, any such approval given by the shareholders must be limited to shares with aggregate nominal value not exceeding 20 per cent of the aggregate nominal value of our share capital in issue plus the aggregate nominal amount of share capital repurchased by us since the granting of such approval.

#### ***Dividends***

Subject to the Companies Ordinance and as set out in our articles of association, our shareholders at a general meeting may from time to time by ordinary resolution declare dividends to be paid to our shareholders according to their rights and interests in the profits available for distribution, but no dividend shall be declared in excess of the amount recommended by our board of directors.

In addition to any dividends declared at a general meeting upon the recommendation of the board of directors, our board of directors may, as they deem appropriate, from time to time resolve to pay to our shareholders such interim dividends as appear to our board of directors to be justified by our financial position. Our board of directors may also pay any fixed dividend that is payable on any of our shares on any other dates, whenever our financial position, in the opinion of our board of directors, justifies such payments.

All dividends or bonuses unclaimed for one year after having become payable may be invested or otherwise made use of by the board for the benefit of Unicom until claimed. All dividends or bonuses unclaimed for six years after having been declared may be forfeited by the board and will revert to Unicom.

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### ***Winding Up***

If we are wound up, the surplus assets remaining after payment to all creditors shall be divided among the shareholders in proportion to the capital paid up on the shares held by them, subject to the rights of the holders of any shares that may be issued on special terms or conditions.

If we are wound up, the liquidator may, with the sanction of a special resolution, divide among our shareholders in specie or in kind the whole or any part of our assets or vest any part of our assets in trustees upon such trusts for the benefit of our shareholders or any of them as the resolution shall provide.

### ***Miscellaneous***

Shareholders are not entitled to any redemption rights, conversion rights or preemptive rights on the transfer of ordinary shares.

The transfer agent and registrar for the shares is Hong Kong Registrars Limited, 46th Floor, Hopewell Centre, 183 Queen's Road East, Hong Kong.

### ***Modification of Rights***

Subject to the Companies Ordinance, any of the rights from time to time attaching to any class of shares may, subject to the provisions of the Companies Ordinance, be varied or abrogated with the consent in writing of the holders of not less than three-fourths of the issued shares of that class or with the sanction of a special resolution passed at a separate general meeting of the holders of shares of that class. The provisions of our Articles of Association relating to general meetings apply to such separate general meetings, except that the necessary quorum is not less than two persons holding or representing by proxy one-third in nominal value of the issued shares of that class, and that any holder of the shares of the class present in person or by proxy may demand a poll.

### **Annual General and Extraordinary General Meetings**

We must hold in each year a general meeting as our annual general meeting in addition to any other meetings in that year. The annual general meeting is held at such time (within a period of not more than 15 months, or such longer period as the Registrar of Companies of Hong Kong may authorize in writing, after the holding of the last preceding annual general meeting) and place as may be determined by the board of directors. All other general meetings are called extraordinary general meetings. The board of directors may call an extraordinary general meeting at any time or upon request in accordance with the Hong Kong Companies Ordinance.

Subject to the Companies Ordinance and the HKSE Listing Rules, an annual general meeting and a meeting called for the passing of a special resolution can be called by not less than 21 days' notice in writing, and any other general meeting can be called by not less than 14 days' notice in writing. The notice must specify the place, date and time of the meeting, and, in the case of special business, the general nature of that business. The HKSE Listing Rules provide that notice shall be given to shareholders at least 20 clear business days before an annual general meeting and at least ten clear business days before all other general meetings.

### **Limitations on Rights to Own Securities**

There are no limitations on the rights to own securities, including the rights of non-resident or foreign shareholders to hold or exercise voting rights on the securities, imposed by Hong Kong law or by our Memorandum of Association or our Articles of Association.

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### **Changes in Capital**

We may exercise any powers conferred or permitted by the Companies Ordinance to purchase or otherwise acquire our own shares and warrants at any price or to give, directly or indirectly, by means of a loan, guarantee, the provision of security or otherwise, financial assistance for the purpose of or in connection with a purchase made by any person of any shares or warrants in Unicom. Repurchases of our own shares may be made either by way of a general offer to all shareholders in proportion to their shareholdings, by purchasing our shares on a stock exchange or by an off-market contract with individual shareholders. Any such purchase or other acquisition or financial assistance must be made or given in accordance with any relevant rules or regulations issued by the HKSE or the Securities and Futures Commission of Hong Kong.

We may, in a general meeting, from time to time, by ordinary resolution increase our authorized share capital by the creation of new shares, and prescribe the amount of new capital and number of new shares. We may, from time to time, by ordinary resolution:

consolidate and divide all or any of our share capital into shares of a larger amount than our existing shares;

divide our shares into several classes and attach to them any preferential, deferred, qualified or special rights, privileges or conditions;

cancel any shares that at the date of the passing of the resolution have not been taken or agreed to be taken by any person, and diminish the amount of our share capital by the amount of the shares so cancelled;

sub-divide our shares or any of them into shares of a smaller amount than is fixed by our Memorandum of Association, subject nevertheless to the provisions of the Companies Ordinance; and

make provision for the issue and allotment of shares which do not carry any voting rights.

### **Miscellaneous**

We keep our share register with our share registrar, which is Hong Kong Registrars Limited, Shops 1712-1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong. In addition, we also file certain documents with the Registrar of Companies, Hong Kong, in accordance with the requirements of the Companies Ordinance. Our company number is 703499.

#### **C. *Material Contracts***

In addition to the contracts described in B. Related Party Transactions under Item 7, Unicom Group, we or our subsidiaries have entered into the following contracts that are not in the ordinary course of business within the two years preceding the date of this annual report that are or may be material:

Share subscription agreement between us and Telefónica, dated September 6, 2009, relating to the mutual investment of an equivalent of US\$1 billion by the parties in each other.

Strategic Alliance Agreement between us and Telefónica, dated September 6, 2009, relating to strengthening the business of each of the companies by cooperation based on the network, business model and experience of each other.

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Irrevocable Offer by SK Telecom, dated September 25, 2009, to the Company, for the sale of our shares held by SK Telecom to us.

Irrevocable voting undertaking from China Netcom Group Corporation (BVI) Limited in favor of SK Telecom, dated September 25, 2009.

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Share Repurchase Agreement, dated November 3, 2009, entered into between the Company and SK Telecom.

Amendment Agreement to Share Repurchase Agreement, dated November 3, 2009, entered into between the Company and SK Telecom.

Network Leasing Agreement, dated October 29, 2010, entered into between CUCL and Unicom New Horizon.

Comprehensive Services Agreement, dated October 20, 2010, entered into between CUCL and Unicom Group.

Agreement to Enhance the Strategic Alliance, dated January 23, 2011, entered into between the Company and Telefónica.

***D. Exchange Controls***

The ability of our operating subsidiary, CUCL, to satisfy its foreign exchange obligations and to pay dividends to us depends on existing and future exchange control regulations in China. Under the current relevant regulations, Renminbi is convertible under the current account, which includes trade-and service-related foreign exchange transactions, but is not convertible under the capital account, which includes foreign direct investment. CUCL, our wholly-owned subsidiary that holds substantially all of our assets, is a foreign investment enterprise. The foreign investment enterprise status will allow it to purchase foreign exchange at designated foreign exchange banks for settlement of current account transactions without the approval of the State Administration for Foreign Exchange of the PRC, or the SAFE. These current account transactions include payment of dividends. However, the relevant PRC Government authorities may in the future limit or eliminate the authorizations for a foreign investment enterprise to retain its foreign exchange to satisfy its foreign exchange obligations or to pay dividends in the future. Furthermore, certain foreign exchange transactions of CUCL under the capital account still require approvals from the SAFE. This requirement affects our subsidiary's ability to obtain foreign exchange through equity financing, including by means of capital contributions from us.

Under existing Hong Kong law, (i) there are no foreign exchange controls or other laws that restrict the import or export of capital and that would affect the availability of cash and cash equivalents for our use, (ii) there are no foreign exchange controls or other laws, decrees or regulations that affect the remittance of interest, dividends or other payments on our outstanding debt and equity securities to U.S. residents and (iii) there are no limitations on the rights of non-resident or foreign owners to hold our debt or equity securities.

***E. Taxation***

The taxation of income and capital gains of holders of ordinary shares or ADSs is subject to the laws and practices of the PRC, Hong Kong and jurisdictions in which holders of ordinary shares or ADSs are resident or otherwise subject to tax. The following summary of certain relevant taxation provisions is based on current law and practice, is subject to change and does not constitute legal or tax advice. The discussion does not deal with all possible tax consequences relating to an investment in the ordinary shares or ADSs. In particular, the discussion does not address the tax consequences under state, local and other laws, such as non-PRC, non-Hong Kong and non-U.S. federal laws. The discussion is based upon laws and relevant interpretations in effect as of the date of this annual report.

**People's Republic of China**

This section describes certain PRC tax consequences of the ownership and disposition of our ordinary shares or ADSs. This section does not address all possible PRC tax considerations that may be relevant to an investment in our ordinary shares or ADSs in light of an investor's specific circumstances, and is based on PRC tax laws and relevant interpretations as in effect as of the date of this annual report on Form 20-F, which are subject to change, possibly with retroactive effect. Accordingly, each prospective investor should consult its own tax advisor regarding the PRC and other tax consequences of an investment in our ordinary shares or ADSs applicable under its particular circumstances.

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### ***Taxation of Dividends***

Under the PRC Enterprise Income Tax, or the EIT, Law and its implementing rules that became effective on January 1, 2008, a non-resident enterprise is generally subject to PRC enterprise income tax with respect to PRC-sourced income, including dividends received from an enterprise that is domiciled in China. The PRC enterprise income tax with respect to such dividends is currently required to be withheld at the rate of 10%, unless there is an applicable tax treaty between China and the jurisdiction in which such non-resident enterprise resides that reduces or exempts the tax.

On April 22, 2009, the PRC State Administration of Taxation, or the SAT, issued the Notice Regarding the Determination of Tax Residence Status of Chinese-Controlled Offshore-Incorporated Enterprises on the Basis of De Facto Management Bodies, or the 2009 Notice, which was retroactively effective as of January 1, 2008. Pursuant to the 2009 Notice, an enterprise incorporated under the laws of a jurisdiction outside China but controlled by a PRC enterprise or enterprise group may be determined to be a PRC resident enterprise with its de facto management bodies located within China for PRC tax purposes if certain criteria specified under the 2009 Notice are met. Under the 2009 Notice, dividends paid by such an off-shore incorporated enterprise are deemed to be PRC-sourced income and subject to PRC enterprise income tax. On November 11, 2010, we were notified by the SAT that we are determined to be a PRC resident enterprise since January 1, 2008 for PRC tax purposes. Accordingly, we are required to withhold the 10% EIT when we distribute dividends to our non-resident enterprise shareholders.

Accordingly, we will withhold the 10% EIT when we distribute our final dividend for the fiscal year ended December 31, 2011 in respect of the non-resident enterprise shareholders for PRC tax purposes whose names appear on our register of members as of the record date for such dividends, and who are not individuals, unless such non-individual shareholders are able to provide documents from the relevant PRC tax authorities confirming that we are not required to withhold the 10% EIT in respect of the dividends that such shareholders are entitled to, on the basis that dividend income between two PRC resident enterprises is exempted from enterprise income tax, subject to certain conditions, under the EIT Law. In addition, certain investors hold our shares or ADSs through custodians, nominees, corporate trustees or other intermediaries and the names of these investors do not appear on our register of members. Payments of dividends to such investors are also subject to the 10% EIT withholding. These investors should enquire about the relevant procedures with the relevant custodians, nominees, trustees or other intermediaries if they wish to change the identities of the shareholders on our register of members.

### ***Taxation of Capital Gains***

Under the PRC EIT Law and its implementing rules, a non-resident enterprise is generally subject to PRC enterprise income tax with respect to PRC-sourced income, but there remain substantial uncertainties as to their interpretation and application by the relevant PRC tax authorities. We intend to comply with any interpretation or notice in relation to the taxation of capital gains issued by the PRC tax authorities in the future.

### ***Additional PRC Tax Considerations***

*Stamp duty.* Under the Provisional Regulations of the PRC Concerning Stamp Duty and its implementing rules, both of which became effective on October 1, 1988, PRC stamp duty should not apply to acquisitions or dispositions of our ordinary shares or ADSs outside of China as the PRC stamp duty is imposed only on documents executed or received within China that are legally binding in China and protected under PRC law.

*Estate tax.* China does not currently levy estate tax.

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### **Hong Kong**

#### ***Taxation of Dividends***

Under the current practices of the Hong Kong Inland Revenue Department, no tax is payable in Hong Kong in connection with dividends paid by us, either by withholding or otherwise, unless such dividends are attributable to a trade, profession or business carried on in Hong Kong.

#### ***Profits***

No tax is imposed in Hong Kong in respect of capital gains from the sale of shares and ADSs. Trading gains from the sale of shares or ADSs by persons carrying on a trade, profession or business in Hong Kong where such gains are derived from or arise in Hong Kong from such trade, profession or business will be chargeable to Hong Kong income tax rates of 16.5% on corporations and 15.0% on individuals. Gains from sales of shares effected on the HKSE will be considered to be derived from or arise in Hong Kong. Liability for Hong Kong profits tax would thus arise in respect of trading gains from sales of shares or ADSs realized by persons carrying on a business of trading or dealing in securities in Hong Kong.

#### ***Stamp Duty***

Hong Kong stamp duty, currently charged at the rate of 0.1% of the higher of the consideration for or the value of the shares, will be payable by the purchaser on every purchase and by the seller on every sale of shares. In addition, a fixed duty of HK\$5 is currently payable on any instrument of transfer of shares. If one of the parties to the sale is a non-resident of Hong Kong and does not pay the required stamp duty, the duty not paid will be assessed on the instrument of transfer (if any) and the transferee will be liable for payment of such duty.

The withdrawal of shares upon the surrender of American Depository Receipts, or ADRs, and the issuance of ADRs upon the deposit of shares, will also attract stamp duty at the rate described above unless such withdrawal or deposit does not result in a change in the beneficial ownership of the shares under Hong Kong law. The issuance of the ADRs upon the deposit of shares issued directly to The Bank of New York, as depository of the ADSs, or for the account of The Bank of New York does not attract stamp duty. No Hong Kong stamp duty is payable upon the transfer of ADSs outside Hong Kong.

#### ***Estate Duty***

The Revenue (Abolition of Estate Duty) Ordinance 2005 became effective on February 11, 2006 in Hong Kong. No Hong Kong estate duty is payable and no estate duty clearance papers are needed for an application for a grant of representation in respect of a holder of the shares whose death occurs on or after February 11, 2006.

### **United States**

#### ***United States Federal Income Taxation***

This section describes the material United States federal income tax consequences to a U.S. holder (as defined below) of owning shares or ADSs. It applies to you only if you hold your shares or ADSs as capital assets for tax purposes. This section does not apply to you if you are a member of a special class of holders subject to special rules, including:

a dealer in securities or currencies,

a trader in securities that elects to use a mark-to-market method of accounting for your securities holdings,

a tax-exempt organization,



an insurance company,

a person liable for alternative minimum tax,

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a person that actually or constructively owns 10% or more of our voting stock,

a person that holds shares or ADSs that are a hedge or as part of a straddle or a conversion transaction,

a person that purchases or sells shares or ADSs as part of a wash sale for tax purposes, or

a person whose functional currency is not the U.S. dollar.

This section is based on the Internal Revenue Code of 1986, as amended, or the Code, its legislative history, existing and proposed regulations, published rulings and court decisions, all as currently in effect. These laws are subject to change, possibly on a retroactive basis. In addition, this section is based in part upon the representations of the Depositary and the assumption that each obligation in the deposit agreement and any related agreement will be performed in accordance with its terms.

You are a U.S. holder if you are a beneficial owner of shares or ADSs and you are:

a citizen or resident of the United States,

a corporation organized under the laws of the United States, any States thereof, or the District of Columbia,

an estate whose income is subject to United States federal income tax regardless of its source, or

a trust if a United States court can exercise primary supervision over the trust's administration and one or more United States persons are authorized to control all substantial decisions of the trust.

If a partnership holds the shares or ADSs, the United States federal income tax treatment of a partner will generally depend on the status of the partner and the activities of the partnership. A partner in a partnership holding the shares or ADSs should consult its tax advisor with regard to the United States federal income tax treatment of its investment in the shares or ADSs.

You should consult your own tax advisor regarding the United States federal, state and local tax consequences of owning and disposing of shares and ADSs in your particular circumstances.

This discussion addresses only United States federal income taxation.

In general, taking into account the earlier assumptions, for United States federal income tax purposes, if you hold ADRs evidencing ADSs, you will be treated as the owner of the shares represented by those ADRs. Exchanges of shares for ADRs, and ADRs for shares, generally will not be subject to United States federal income tax.

***Taxation of Dividends***

Under the United States federal income tax laws, and subject to the passive foreign investment company rules discussed below, if you are a U.S. holder, the gross amount of any dividend we pay out of our current or accumulated earnings and profits (as determined for United States federal income tax purposes) is subject to United States federal taxation. If you are a non-corporate U.S. holder, dividends paid to you in taxable years beginning before January 1, 2013 that constitute qualified dividend income will be taxable to you at a maximum tax rate of 15%, provided that you hold the shares or ADSs for more than 60 days during the 121-day period beginning 60 days before the ex-dividend date and meet other holding period requirements. Dividends we pay with respect to the shares or ADSs will be qualified dividend income, provided that, in the year that you receive the dividend, the shares or ADSs are readily tradable on an established securities market in the United States.



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The dividend is taxable to you when you, in the case of shares, or the Depositary, in the case of ADSs, receive the dividend, actually or constructively. The dividend will not be eligible for the dividends-received deduction generally allowed to United States corporations in respect of dividends received from other United States corporations. The amount of the dividend distribution that you must include in your income as a U.S. holder will be the U.S. dollar value of the Hong Kong Dollar payments made, determined at the spot Hong Kong/U.S. dollar rate on the date the dividend distribution is includible in your income, regardless of whether the payment is in fact converted into U.S. dollars. Generally, any gain or loss resulting from currency exchange fluctuations during the period from the date you include the dividend payment in income to the date you convert the payment into U.S. dollars will be treated as ordinary income or loss and will not be eligible for the special tax rate applicable to qualified dividend income. The gain or loss generally will be income or loss from sources within the United States for foreign tax credit limitation purposes. Distributions in excess of current and accumulated earnings and profits, as determined for United States federal income tax purposes, will be treated as a non-taxable return of capital to the extent of your basis in the shares or ADSs and thereafter as capital gain.

Special rules apply in determining the foreign tax credit limitation with respect to dividends that are subject to the maximum 15% tax rate. Dividends will be income from sources outside the United States and, depending on your circumstances, will be either passive income or general income for purposes of computing the foreign tax credit allowable to you. If you are subject to PRC withholding tax (as discussed in *People's Republic of China Taxation of Dividends*, above), you must include any such tax withheld from the dividend payment in your gross income, even though you do not in fact receive it. The PRC tax withheld and paid over to the PRC will be creditable against your United States federal income tax liability. To the extent a refund of the tax withheld is available under PRC law, the amount of tax withheld that is refundable will not be eligible for credit against your United States federal income tax liability.

### ***Taxation of Capital Gains***

Subject to the passive foreign investment company rules discussed below, if you are a U.S. holder and you sell or otherwise dispose of your shares or ADSs, you will recognize capital gain or loss for United States federal income tax purposes equal to the difference between the U.S. dollar value of the amount that you realize and your tax basis, determined in U.S. dollars, in your shares or ADSs. Capital gain of a non-corporate U.S. holder is generally taxed at preferential rates where the property is held for more than one year. Subject to the paragraph immediately below regarding gain subject to PRC tax, the gain or loss will generally be income or loss from sources within the United States for foreign tax credit limitation purposes. Your ability to deduct capital losses is subject to limitations. Any Hong Kong stamp duty that you pay will not be a creditable tax for United States federal income tax purposes, but you may be able to deduct such stamp duty subject to limitations under the Code.

However, in the event we are deemed to be a Chinese resident enterprise under PRC tax law, we may be eligible for the benefits of the income tax treaty between the United States and China. Under that treaty, if PRC tax were to be imposed on any gain from the disposition of your shares or ADSs (as discussed above in *People's Republic of China Taxation of Capital Gains*), the gain may be treated as PRC source income. U.S. Holders should consult their tax advisors regarding the tax consequences if a foreign withholding tax is imposed on a disposition of shares or ADSs, including the availability of the foreign tax credit under your particular circumstances.

***Passive Foreign Investment Company Rules.*** We believe that we should not be treated as a passive foreign investment company, or PFIC, for United States federal income tax purposes, but this conclusion is a factual determination that is made annually and thus may be subject to change.

In general, if you are a U.S. holder, we will be a PFIC with respect to you if for any taxable year in which you held our ADSs or shares:

at least 75% of our gross income for the taxable year is passive income; or

at least 50% of the value, determined on the basis of a quarterly average, of our assets is attributable to assets that produce or are held for the production of passive income.

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Passive income generally includes dividends, interest, royalties, rents (other than certain rents and royalties derived in the active conduct of a trade or business), annuities and gains from assets that produce passive income. If a foreign corporation owns, directly or indirectly, at least 25% by value of the stock of another corporation, the foreign corporation is treated for purposes of the PFIC tests as owning its proportionate share of the assets of the other corporation, and as receiving directly its proportionate share of the other corporation's income.

If we are treated as a PFIC and you are a U.S. holder that does not make a mark-to-market election, as described below, you will be subject to special rules with respect to:

any gain you realize on the sale or other disposition of your shares or ADSs; and

any excess distribution that we make to you (generally, any distributions to you during a single taxable year that are greater than 125% of the average annual distributions received by you in respect of the shares or ADSs during the three preceding taxable years or, if shorter, your holding period for the shares or ADSs).

Under these rules:

the gain or excess distribution will be allocated ratably over your holding period for the shares or ADSs;

the amount allocated to the taxable year in which you realized the gain or excess distribution will be taxed as ordinary income;

the amount allocated to each prior year, with certain exceptions, will be taxed at the highest tax rate in effect for that year; and

the interest charge generally applicable to underpayments of tax will be imposed in respect of the tax attributable to each such year.

Special rules apply for calculating the amount of the foreign tax credit with respect to excess distributions by a PFIC.

If you own shares or ADSs in a PFIC that are treated as marketable stock, you may make a mark-to-market election. If you make this election, you will not be subject to the PFIC rules described above. Instead, in general, you will include as ordinary income each year the excess, if any, of the fair market value of your shares or ADSs at the end of the taxable year over your adjusted basis in your shares or ADSs. You will also be allowed to take an ordinary loss in respect of the excess, if any, of the adjusted basis of your shares or ADSs over their fair market value at the end of the taxable year (but only to the extent of the net amount of previously included income as a result of the mark-to-market election). Your basis in the shares or ADSs will be adjusted to reflect any such income or loss amounts. Your gain, if any, recognized upon the sale of your shares or ADSs will be taxed as ordinary income.

In addition, notwithstanding any election you make with regard to the shares or ADSs, dividends that you receive from us will not constitute qualified dividend income to you if we are a PFIC either in the taxable year of the distribution or the preceding taxable year. Moreover, your shares or ADSs will be treated as stock in a PFIC if we were a PFIC at any time during your holding period in your shares or ADSs, even if we are not currently a PFIC. For purposes of this rule, if you make a mark-to-market election with respect to your shares or ADSs, you will be treated as having a new holding period in your shares or ADSs beginning on the first day of the first taxable year beginning after the last taxable year for which the mark-to-market election applies. Dividends that you receive that do not constitute qualified dividend income are not eligible for taxation at the 15% maximum rate applicable to qualified dividend income. Instead, you must include the gross amount of any such dividend paid by us out of our accumulated earnings and profits (as determined for United States federal income tax purposes) in your gross income, and it will be subject to tax at rates applicable to ordinary income.



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If you own shares or ADSs during any year that we are a PFIC, you must file Internal Revenue Service Form 8621. In addition, pursuant to recently enacted legislation, if you are a U.S. person that is a shareholder in a PFIC, you will generally be required to file an annual report with the Internal Revenue Service. The content of this required statement and potential exemptions to this requirement are under development by the Internal Revenue Service.

### ***F. Dividends and Paying Agents***

Not Applicable.

### ***G. Statement by Experts***

Not Applicable.

### ***H. Documents on Display***

You can read and copy documents referred to in this annual report that have been filed with the U.S. Securities and Exchange Commission at the SEC's public reference room located at 100 Fifth Street, N.E., Room 1580, Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information on the public reference rooms and their copy charges. The SEC also maintains a web site at <http://www.sec.gov> that contains reports, proxy statements and other information regarding registrants that are filed electronically with the SEC.

The SEC allows us to incorporate by reference the information we file with the SEC. This means that we can disclose important information to you by referring you to another document filed separately with the SEC. The information incorporated by reference is considered to be part of this annual report on Form 20-F.

### ***I. Subsidiary Information***

Not Applicable.

## **Item 11. Quantitative and Qualitative Disclosures about Market Risks**

Our exposure to financial market risks relates primarily to changes in interest rates and currency exchange rates.

### **Interest Rate Risk**

The People's Bank of China has the sole authority in China to establish the official interest rates for Renminbi-denominated loans. Financial institutions in China set their effective interest rates within the range established by the People's Bank of China. Interest rates and payment methods in China on loans denominated in foreign currencies are set by the financial institutions based on interest rate changes in the international financial market, cost of funds, risk levels and other factors. The fair value of our borrowings is approximately the same as the carrying value. These bank loans, denominated in Renminbi, are mainly borrowed from domestic banks at interest rates that vary in accordance with the standard guidance interest rates announced by relevant PRC Government authorities.

We are subject to risks arising from interest-bearing borrowings, including bank loans, commercial papers, promissory notes, convertible bonds, corporate bonds and related party loans. The majority of our interest-bearing borrowings are loans from banks in China, the majority of which bear fixed interest rates. A rise in interest rates will increase the cost of new borrowings and interest expenses of outstanding floating rate debt. Accordingly, fluctuations in interest rates can lead to significant fluctuations in the fair value of these instruments, and, therefore, could have a material adverse effect on our financial position. To mitigate our exposure to interest rate risks in connection with our borrowings denominated in foreign currencies, we may enter into designed interest rate swap agreements from time to time in the future.

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The following table provides information, by maturity date, regarding our interest rate-sensitive financial instruments, including short-term and long-term debt obligations and convertible bonds, as well as the expected maturity profile of such instruments as of December 31, 2011.

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	Expected Maturity						As of December 31, 2011	Fair Value
	2012	2013	2014	2015	2016	Thereafter	Total	
<b>Liabilities:</b>								
RMB-denominated loans								
Fixed rate	1,000	-	-	-	-	-	1,000	1,000
Average rate <sup>(1)</sup>	2.28%	-	-	-	-	-	-	-
Variable rate	16,810	800	-	-	-	-	17,610	17,600
Average rate	6.10%	5.65%	-	-	-	-	-	-
HK dollar-denominated loans								
Variable rate	16,668	-	-	-	-	-	16,668	16,668
Average rate	1.86%	-	-	-	-	-	-	-
U.S. dollar-denominated loans								