

REPORT OF THE MEMBERS OF THE BOARD

The Members of the Board have pleasure in submitting their Report and the audited statement of Accounts for the financial year ended 31 December 2011.

PRINCIPAL ACTIVITIES OF THE GROUP

The principal activities of the Company and its subsidiaries are:

A the operation of a modern railway system with lines from Central to Tsuen Wan (Tsuen Wan Line), from Yau Ma Tei to Tiu Keng Leng (Kwun Tong Line), from Po Lam and LOHAS Park to North Point (Tseung Kwan O Line), from Chai Wan to Sheung Wan (Island Line), from Hong Kong to Tung Chung (Tung Chung Line), from Hong Kong to the Hong Kong International Airport and then AsiaWorld-Expo both at Chek Lap Kok (Airport Express), from Sunny Bay to Disneyland Resort (Disneyland Resort Line), from Hung Hom to the boundary at Lo Wu and Lok Ma Chau (East Rail Line), from Tai Wai to Wu Kai Sha (Ma On Shan Line), from Hung Hom to Tuen Mun (West Rail Line), the North-west Railway (commonly known as Light Rail) in the North-West New Territories of Tuen Mun, Tin Shui Wai and Yuen Long, an intercity railway system between Hong Kong and some major cities in the Mainland of China, and feeder bus services in support of West Rail Line, East Rail Line and Light Rail;

B property development, either as owner or as an agent for KCRC, at locations along the related railway lines including the Tseung Kwan O Line, the Ma On Shan Line, the East Rail Line, the Light Rail, the West Rail Line, the Kwun Tong Line Extension and the South Island Line (East);

C related commercial activities, including the letting of advertising and retail space, enabling telecommunication services on the railway system, asset management and leasing management of investment properties (including shopping malls and offices) and property management of office buildings and residential units;

D the investment in a 50% equity share in the operation of the 7-year UK's London Overground Concession, consisting of 5 London railway lines measuring a total route length of 112 kilometres;

E the investment in the operation (including rolling stock maintenance which is undertaken by a 50:50 joint venture) of the 8-year Sweden's Stockholm Metro Concession, consisting of three lines measuring a total of 110 kilometres, linking the Swedish capital's central areas with surrounding suburbs;

F the investment in a 60% equity share in Metro Trains Melbourne of an 8-year concession for the operation and maintenance of the Melbourne train system, consisting of 15 lines running on 372 kilometres, linking Melbourne's central business district with surrounding suburbs;

G the design and construction of the West Island Line as an extension of the Island Line;

H the design, construction, procurement of services and equipment, and all other matters associated with bringing the Hong Kong section of the Guangzhou-Shenzhen-Hong Kong Express Rail Link into service;

I the design and construction of the Kwun Tong Line Extension and the South Island Line (East) as the system extensions of the railway network;

J the planning and design of the Shatin to Central Link as a major railway project for which the Government has confirmed policy support;

K the operation of the Tung Chung to Ngong Ping Cable Car System and the Theme Village in Ngong Ping, Lantau Island, Hong Kong;

L worldwide consultancy services and contracting opportunities covering all areas of expertise required in the project management, planning, construction, operation, maintenance and up-grading of railways plus fare collection, property integration/development advice including other property related services and advice on generation of non-fare revenues;

M investment in Octopus Holdings Limited, a subsidiary of the Company, which has business activities both in Hong Kong and overseas including the operation of a contactless smart card system by its subsidiary Octopus Cards Limited for the collection of payments for both transport and non-transport applications in Hong Kong;

N equity investments and long term operations and maintenance contracts outside of Hong Kong;

O property management, shopping mall investment and railway related property development business in the Mainland of China;

P the investment in a 49% equity interest in a joint venture for the investment, construction and operations of Beijing Metro Line 4, consisting of 28 kilometres with 24 stations forming the main north-south traffic artery for Beijing, Mainland of China under a 30-year concession agreement with the Beijing Municipal Government, and operations and maintenance of Beijing Metro Daxing Line, an extension to the Beijing Metro Line 4, consisting of 22 kilometres with 11 stations, under a 10-year operations and maintenance concession agreement with Beijing Metro Daxing Line Investment Company Limited, a wholly owned subsidiary of Beijing Municipal Government;

Q the investment in the design, construction and operations of Phase 2 of Shenzhen Metro Line 4; together with the operations of Phase 1. The line is a 20.5 kilometres double-track urban railway running from Futian Checkpoint at the boundary between Hong Kong and Shenzhen, with a total of 15 stations and a train maintenance depot, under a 30-year Build-Operate-Transfer concession agreement with the Shenzhen Municipal Government; and

REPORT OF THE MEMBERS OF THE BOARD

R the acquisition of the land use right of the land lot above the Shenzhen Metro Line 4 Depot by two wholly-owned subsidiaries of the Company in August 2011. The lot with a total gross floor area of approximately 206,167 square metres will be used for residential and commercial development.

In March 2010, a provisional Concession Agreement for a Public-Private Partnership project for the investment, construction and operation of Hangzhou Metro Line 1, for a term of 25 years, was agreed between MTR Hangzhou Line 1 Investment Company Limited (a wholly-owned subsidiary of the Company) and a subsidiary of Hangzhou Metro Group Company Limited together with Hangzhou Municipal Government. The Concession Agreement is pending for the regulatory Central Government approval.

DIVIDEND

The Directors have recommended a final dividend of HK\$0.51 per Ordinary Share to be payable to shareholders whose names appear on the Register of Members of the Company on 14 May 2012. Subject to the passing of the necessary resolutions at the forthcoming Annual General Meeting, such dividend will be payable on or about 29 May 2012, in cash in Hong Kong dollars.

MEMBERS OF THE BOARD

Members of the Board who served during the year were Dr. Raymond Ch'ien Kuo-fung (non-executive Chairman), Mr. Chow Chung-kong (Chief Executive Officer), Mr. Vincent Cheng Hoi-chuen, Ms. Christine Fang Meng-sang, Mr. Edward Ho Sing-tin, Mr. Alasdair George Morrison, Mr. Ng Leung-sing, Mr. Abraham Shek Lai-him, Mr. T. Brian Stevenson, Professor Chan Ka-keung, Ceajer, the Secretary for Transport and Housing (Ms. Eva Cheng) and the Commissioner for Transport (Mr. Joseph Lai Yee-tak).

As announced by the Company in December 2010, Mr. Chow Chung-kong retired from the position of Chief Executive Officer and ceased to be a Member of the Board and a Member of the Executive Directorate on 31 December 2011.

On 22 July 2011 and following a worldwide search for Mr. Chow's replacement, the Company announced the appointment of Mr. Jay Herbert Walder as Chief Executive Officer for an initial term of thirty months with effect from 1 January 2012. He became both a Member of the Executive Directorate and a Member of the Board of Directors with effect from the same date. Before joining the Company, Mr. Walder was Chairman and Chief Executive Officer of the New York Metropolitan Transportation Authority, the largest passenger transportation authority in the United States.

Please refer to the Corporate Governance Report on page 91 for other details.

At the Annual General Meeting on 6 May 2011 and pursuant to the Articles of Association, Mr. Edward Ho Sing-tin, Mr. Ng Leung-sing, Mr. Abraham Shek Lai-him and Mr. Alasdair George Morrison retired under the Articles of Association and were re-elected/elected as Members of the Board.

At the 2012 Annual General Meeting and in accordance with the Articles of Association, Dr. Raymond Ch'ien Kuo-fung, Mr. T. Brian Stevenson and Professor Chan Ka-keung, Ceajer will retire by rotation and will offer themselves for re-election. Mr. Jay Herbert Walder, who was appointed by the Board after the 2011 Annual General Meeting, will retire under Article 85 of the Articles of Association and will offer himself for election at the 2012 Annual General Meeting. Please also refer to page 97 of the Corporate Governance Report.

Biographical details for Board Members are set out on pages 112 to 115.

ALTERNATE DIRECTORS

The Alternate Directors in office during the year were:

- for Professor Chan Ka-keung, Ceajer: Mr. Ying Yiu-hong and Miss Chu Man-ling;
- for the office of the Secretary for Transport and Housing: (i) the Under Secretary for Transport and Housing (Mr. Yau Shing-mu); (ii) the Permanent Secretary for Transport and Housing (Transport) (Mr. Ho Suen-wai); and (iii) the Deputy Secretary for Transport and Housing (Transport) (Ms. Maisie Cheng Mei-sze and Ms. Rebecca Pun Ting-ting); and
- for the Commissioner for Transport: the Deputy Commissioner for Transport/Transport Services and Management (Ms. Carolina Yip Lai-ching).

EXECUTIVE DIRECTORATE

The Members of the Executive Directorate who served during the year were Mr. Chow Chung-kong (Chief Executive Officer and a Member of the Board) (until 31 December 2011), Mr. William Chan Fu-keung (retiring on 17 July 2012), Mr. Chew Tai Chong, Mr. Thomas Ho Hang-kwong (until 30 September 2011), Dr. Jacob Kam Chak-pui, Mr. Lincoln Leong Kwok-kuen, Mr. Leonard Bryan Turk (until 31 August 2011), Ms. Gillian Elizabeth Meller (from 1 September 2011), Ms. Jeny Yeung Mei-chun (from 1 September 2011) and Mr. David Tang Chi-fai (from 1 October 2011).

Please refer to the "Members of the Board" section on this page regarding Mr. Jay Herbert Walder's appointment as the Chief Executive Officer, a Member of the Board and a Member of the Executive Directorate with effect from 1 January 2012.

Ms. Meller and Ms. Yeung, and Mr. Tang were appointed as Members of the Executive Directorate in September and October 2011 respectively. Each of Ms. Meller and Mr. Tang has served the Company for over 7 years. Before being appointed as a Member of the Executive Directorate, Ms. Meller had been Legal Adviser, Legal Manager – General and Deputy Legal Director; and Mr. Tang had held senior management positions in the Legal and Procurement Division and the China and International Business Division before he was transferred to the Property Division in 2009. Ms. Yeung has served the Company for over 12 years. She had been the Marketing Manager and General Manager – Marketing & Station Commercial before she became a Member of the Executive Directorate. Ms. Yeung has also been a member of the Executive Committee since 2004.

Mr. Cheung Siu Wa (also known as Mr. Morris Cheung), currently Human Resources Director – Designate, will be appointed as Human Resources Director and will become a Member of the Executive Directorate, both with effect from 17 July 2012. Before being appointed as Human Resources Director – Designate, Mr. Cheung had been Chief of Operations Engineering.

Biographical details for Members of the Executive Directorate during the year are set out on pages 115 to 117.

INTERNAL AUDIT

The Company's Internal Audit Department provides independent, objective assurance and consulting services designed to add value and improve the Company's operations. Key responsibilities of the Department include:

- Assessment of the adequacy and effectiveness of the Company's system of internal controls over its activities and risk management.
- Identification of opportunities for improving management control, resources utilisation and profitability.
- Special reviews and/or investigations as commissioned by Company management or the Audit Committee.

The Head of Internal Audit reports directly to the Chief Executive Officer and has direct access to the Audit Committee.

BUSINESS ETHICS

Please refer to pages 104 to 105.

POLICIES

The Board has adopted the following risk management strategies and policies:

- A** Construction and Insurance Risk Management Strategy;
- B** Finance Risk Management Strategy;
- C** Treasury Risk Management Strategy;
- D** Safety Risk Management Strategy;
- E** Enterprise Risk Management Strategy;
- F** Security Risk Management Policy; and
- G** Environmental Risk Management Policy.

PUBLIC FLOAT

The Stock Exchange granted to the Company, at the time of its listing on the Main Board of the Stock Exchange in 2000, a waiver from strict compliance with Rule 8.08(1) of the Listing Rules ("Public Float Waiver"). Pursuant to the Public Float Waiver, the Company's prescribed minimum percentage of shares which must be in the hands of the public must not be less than 10% of the total issued share capital of the Company. Based on the information that is publicly available to the Company and within the knowledge of the Directors, the Company has maintained the prescribed amount of public float during the year and up to the date of this report as required by the Public Float Waiver.

BANK OVERDRAFTS, BANK LOANS AND OTHER BORROWINGS

The total borrowings of the Group as at 31 December 2011 amounted to HK\$23,168 million (2010: HK\$21,057 million). Particulars of borrowings are set out in note 42 to the accounts.

ACCOUNTS

The state of affairs of the Company and the Group as at 31 December 2011 and of the Group's results, changes in equity and cash flows for the year are set out in the accounts on pages 147 to 238.

TEN-YEAR STATISTICS

A summary of the results and of the assets and liabilities of the Group together with some major operational statistics for the last ten years are set out on pages 80 to 81.

FIXED ASSETS AND RAILWAY CONSTRUCTION IN PROGRESS

Movements in fixed assets and railway construction in progress during the year are set out in notes 23 to 25 and 27 to the accounts respectively.

REPORT OF THE MEMBERS OF THE BOARD

MOVEMENTS IN RESERVES

Movements in reserves during the year are set out in the Consolidated Statement of Changes in Equity and notes 50 and 51 to the accounts.

SHARE CAPITAL

As at 31 December 2010, the authorised share capital of the Company was HK\$6.5 billion, divided into 6.5 billion Ordinary Shares, 5,772,563,031 of which were issued and credited as fully paid.

During the year, the Company issued a total of 12,308,219 Ordinary Shares. Of this number:

A 792,200 Ordinary Shares were issued by the Company pursuant to the exercise of share options which had been granted under the Company's New Joiners Share Option Scheme (as referred in note 50A to the accounts). In respect of each Ordinary Share issued, the relevant exercise price per share of options are HK\$9.75 and HK\$20.66 to the Company;

B 1,172,500 Ordinary Shares were issued by the Company pursuant to the exercise of share options which had been granted under the Company's 2007 Share Option Scheme (as referred in note 50A to the accounts). In respect of each Ordinary Share issued, the relevant exercise price per share of options are HK\$18.30, HK\$26.52, HK\$26.85, and HK\$27.60 to the Company; and

C 10,343,519 Ordinary Shares were issued by the Company in order to satisfy shareholders' scrip dividend elections in respect of the final dividend of the Company for the year ended 31 December 2010 (for which the cash dividend was HK\$0.45 per Ordinary Share).

As at 31 December 2011, the authorised share capital of the Company was HK\$6.5 billion, divided into 6.5 billion Ordinary Shares, 5,784,871,250 of which were issued and credited as fully paid.

PURCHASE, SALE OR REDEMPTION OF LISTED SECURITIES

Neither the Company nor any of its subsidiaries has purchased, sold or redeemed any of the Group's listed securities during the year ended 31 December 2011.

PROPERTIES

Particulars of the principal investment properties and properties held for sale of the Company are shown on pages 54 to 55.

DONATIONS

During the year, the Company donated a total of approximately HK\$2.7 million to charitable and other organisations.

In addition, the MTR HONG KONG Race Walking 2011 raised over HK\$1.33 million (including over HK\$55,000 from MTR staff) for the Hospital Authority Health InfoWorld to promote good health.

The Company helped raise funds for the Community Chest and the Hong Kong Cancer Fund with a total cash donation of over HK\$304,000 through different activities such as CARE Scheme, Green Day, Love Teeth Day and Dress Casual Day for the former organisation and Dress Pink Day for the latter.

REPORTING AND MONITORING

There is a comprehensive budgeting system for all operational and business activities, with an annual budget approved by the Board. Monthly results of the Company's operations, businesses and projects are reported against the budget to the Board and updated forecasts for the year are prepared regularly.

TREASURY MANAGEMENT

The Company's Treasury Department operates within approved guidelines from the Board. It manages the Company's debt profile with reference to the Preferred Financing Model which defines the preferred mix of financing instruments, fixed and floating rate debts, maturities, interest rate risks, currency exposure and financing horizon. The model is reviewed and refined periodically to reflect changes in the Company's financing requirements and market environment. Derivative financial instruments such as interest rate swaps and cross currency swaps are used only as hedging tools to manage the Group's exposure to interest rate and currency risks. Prudent guidelines and procedures are in place to control the Company's derivatives activities, including a comprehensive credit risk management system for monitoring counterparty credit exposure using the Value-at-Risk approach. There is also appropriate segregation of duties within the Company's Treasury Department.

Major financing transactions and guidelines for derivatives transactions including credit risk management framework are approved at the Board level.

CAPITAL AND REVENUE EXPENDITURE

There are defined procedures for the appraisal, review and approval of major capital and revenue expenditures. All project expenditure over 0.2% of the net assets of the Company and the employment of consultancy services over 0.1% of the net assets of the Company require the approval of the Board.

BONDS AND NOTES ISSUED

The Group issued notes amounting to HK\$2,206 million equivalent during the year ended 31 December 2011, details of which are set out in note 42C to the accounts. Such notes were issued in order to meet the Group's general corporate

funding requirements, including the financing of new capital expenditure and the refinancing of maturing debts.

COMPUTER PROCESSING

There are defined procedures, controls and regular quality reviews on the operation of computer systems to ensure the accuracy and completeness of financial records and efficiency of data processing. The Company's computer centre operation and support, help desk operation and support services, and also software development and maintenance, have been certified under ISO 9001:2008. Disaster recovery rehearsal on critical applications is conducted annually.

INTERESTS IN CONTRACTS OF MEMBERS OF THE BOARD AND THE EXECUTIVE DIRECTORATE

There was no contract of significance, to which the Company

or any of its subsidiaries was a party and in which a Member of the Board or a Member of the Executive Directorate had a material interest (whether direct or indirect), which subsisted at the end of the year or at any time during the year.

BOARD MEMBERS' AND EXECUTIVE DIRECTORATE'S INTERESTS IN SHARES

As at 31 December 2011, the interests or short positions of the Members of the Board and the Executive Directorate in the shares, underlying shares and debentures of the Company (within the meaning of Part XV of the Securities and Futures Ordinance (Cap. 571 of the Laws of Hong Kong) ("SFO")) as recorded in the register required to be kept under section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code were as follows:

LONG POSITIONS IN SHARES AND UNDERLYING SHARES OF THE COMPANY

Member of the Board and/or the Executive Directorate	Derivatives						Percentage of aggregate interests to total issued share capital
	Number of Ordinary Shares held			Share Options	Other		
	Personal* interests	Family [†] interests	Corporate interests	Personal* interests	Personal* interests	Total interests	
Raymond Ch'ien Kuo-fung	52,330	–	–	–	–	52,330	0.00090
Chow Chung-kong	–	–	–	2,130,000 (Note 1)	222,161 (Note 2)	2,352,161	0.04066
Vincent Cheng Hoi-chuen	1,675	1,675	–	–	–	3,350	0.00006
Christine Fang Meng-sang	1,712	–	–	–	–	1,712	0.00003
T. Brian Stevenson	5,153	–	–	–	–	5,153	0.00009
William Chan Fu-keung	126,106	–	–	680,000 (Note 1)	–	806,106	0.01393
Chew Tai Chong	–	–	–	425,000 (Note 1)	–	425,000	0.00735
Jacob Kam Chak-pui	2,283	–	–	425,000 (Note 1)	–	427,283	0.00739
Lincoln Leong Kwok-kuen	23,000	–	23,000 (Note 3)	680,000 (Note 1)	–	726,000	0.01255
Jeny Yeung Mei-chun (Note 5)	13,400	–	–	270,000 (Note 1)	–	283,400	0.00490
Gillian Elizabeth Meller (Note 6)	–	–	–	219,500 (Note 1)	–	219,500	0.00379
David Tang Chi-fai (Note 7)	600	–	–	(i) 22,000 (Note 4) (ii) 238,000 (Note 1)	–	260,600	0.00450

REPORT OF THE MEMBERS OF THE BOARD

LONG POSITIONS IN SHARES AND UNDERLYING SHARES OF THE COMPANY (CONTINUED)

Number of Ordinary Shares held	Derivatives			Percentage of aggregate interests to total issued share capital
	Share Options		Other	
	Personal* interests	Family† interests	Corporate interests	
Member of the Board and the Executive Directorate				
Jay Herbert Walder (Note 8)	–	–	–	300,000 0.00519

Notes

- 1 Further details of the above share options are set out in the table below showing details of the options to subscribe for ordinary shares granted under the 2007 Share Option Scheme.
- 2 Mr. Chow Chung-kong had a derivative interest in respect of 222,161 shares in the Company within the meaning of Part XV of the SFO. That derivative interest represented Mr. Chow's entitlement to receive an equivalent value in cash of 222,161 shares in the Company on completion of his contract on 31 December 2011. An amount of HK\$5,556,802.01 was paid to him on 4 January 2012 (at a price of HK\$25.0125 per share derived in accordance with the terms of the grant by reference to the average closing price of the Company's shares on the 20 business days immediately preceding 31 December 2011).
- 3 The 23,000 shares are held by Linsan Investment Ltd., a private limited company beneficially wholly owned by Mr. Lincoln Leong Kwok-kuen.
- 4 Further details of the above share options are set out in the table below showing details of the options to subscribe for ordinary shares granted under the New Joiners Share Option Scheme.
- 5 Ms. Jeny Yeung Mei-chun became the Commercial Director and a Member of the Executive Directorate on 1 September 2011.
- 6 Ms. Gillian Elizabeth Meller became the Legal Director and Secretary and a Member of the Executive Directorate on 1 September 2011.
- 7 Mr. David Tang Chi-fai became the Property Director and a Member of the Executive Directorate on 1 October 2011.
- 8 Mr. Jay Herbert Walder became Chief Executive Officer, a Member of the Board and a Member of the Executive Directorate on 1 January 2012. Mr. Walder was granted a derivative interest in respect of 300,000 shares in the Company within the meaning of Part XV of the SFO. That derivative interest represents Mr. Walder's entitlement to be paid an equivalent value in cash of 300,000 shares in the Company following 30 June 2014, being the date on which his initial term of office is expected to expire (35% of which shall be deemed to be earned at 31 October 2013 subject to certain conditions specified in his employment contract).

* Interests as beneficial owner

† Interests of spouse or child under 18 as beneficial owner

**OPTIONS TO SUBSCRIBE FOR ORDINARY SHARES GRANTED UNDER THE NEW JOINERS SHARE OPTION SCHEME,
AS REFERRED TO IN NOTES 11B(i) AND 53A(i) TO THE ACCOUNTS**

Executive Directorate and eligible employees	Date granted	Options granted	Period during which rights exercisable (day/month/year)	Options outstanding as at 1 January 2011				Options granted during the year	Options vested during the year	Options lapsed during the year	Options exercised during the year	Exercise price per share of options (HK\$)	Options outstanding as at 31 December 2011	Weighted average closing price of shares immediately before the date(s) on which options were exercised (HK\$)
				Options outstanding as at 1 January 2011	Options granted during the year	Options vested during the year	Options lapsed during the year							
Lincoln Leong Kwok-kuen	1/8/2003	1,066,000	14/7/2004 – 14/7/2013	417,500	–	–	–	417,500	9.75	–	25.55	–	–	–
David Tang Chi-fai	15/5/2006	213,000	25/4/2007 – 25/4/2016	22,000	–	–	–	–	20.66	22,000	–	–	–	–
Other eligible employees	1/8/2003	495,200	14/7/2004 – 14/7/2013	108,200	–	–	–	108,200	9.75	–	29.16	–	–	–
	23/9/2005	213,000	9/9/2006 – 9/9/2015	213,000	–	–	–	–	15.97	213,000	–	–	–	–
	5/10/2006	94,000	29/9/2007 – 29/9/2016	94,000	–	–	–	–	19.732	94,000	–	–	–	–
	12/5/2006	266,500	25/4/2007 – 25/4/2016	266,500	–	–	–	266,500	20.66	–	28.77	–	–	–

Notes

- No option may be exercised later than ten years after its date of offer and no option may be offered to be granted more than five years after the adoption of the New Joiners Share Option Scheme ("New Option Scheme") on 16 May 2002.
- Unless approved by shareholders in the manner as required by the Listing Rules, the total number of shares issued and issuable upon exercise of the options granted to any eligible employee under the New Option Scheme together with the total number of shares issued and issuable upon the exercise of any option granted to such eligible employee under any other share option scheme of the Company (including, in each case, both exercised and outstanding options) in any 12-month period must not exceed 1% of the shares of the Company in issue at the date of offer in respect of such option under the New Option Scheme.
- The proportion of underlying shares in respect of which the above share options will vest is as follows:

Date	Proportion of underlying shares in respect of which an option is vested
Before the first anniversary of the date of offer of the option (the "Offer Anniversary")	none
From the first Offer Anniversary to the date immediately before the second Offer Anniversary	one-third
From the second Offer Anniversary to the date immediately before the third Offer Anniversary	two-thirds
From the third Offer Anniversary and thereafter	all

REPORT OF THE MEMBERS OF THE BOARD

OPTIONS TO SUBSCRIBE FOR ORDINARY SHARES GRANTED UNDER THE 2007 SHARE OPTION SCHEME, AS REFERRED TO IN NOTES 11B(ii) AND 53A(ii) TO THE ACCOUNTS

Executive Directorate and eligible employees	Date granted	Options granted	Period during which rights exercisable (day/month/year)	Options outstanding as at 1 January 2011	Options granted during the year	Options vested during the year	Options lapsed during the year	Options exercised during the year	Exercise price per share of options (HK\$)	Options outstanding as at 31 December 2011	Weighted average closing price of shares immediately before the date(s) on which options were exercised
											(HK\$)
Chow Chung-kong	13/12/2007	720,000	10/12/2008 – 10/12/2014	720,000	–	–	–	–	27.60	720,000	–
	9/12/2008	470,000	8/12/2009 – 8/12/2015	470,000	–	156,000	–	–	18.30	470,000	–
	9/12/2009	470,000	8/12/2010 – 8/12/2016	470,000	–	157,000	–	–	26.85	470,000	–
	17/12/2010	470,000	16/12/2011 – 16/12/2017	470,000	–	157,000	–	–	28.84	470,000	–
William Chan Fu-keung	13/12/2007	170,000	10/12/2008 – 10/12/2014	170,000	–	–	–	–	27.60	170,000	–
	9/12/2008	170,000	8/12/2009 – 8/12/2015	170,000	–	56,000	–	–	18.30	170,000	–
	10/12/2009	170,000	8/12/2010 – 8/12/2016	170,000	–	57,000	–	–	26.85	170,000	–
	17/12/2010	170,000	16/12/2011 – 16/12/2017	170,000	–	57,000	–	–	28.84	170,000	–
Chew Tai Chong	18/6/2009	85,000	12/6/2010 – 12/6/2016	85,000	–	28,500	–	–	24.50	85,000	–
	10/12/2009	170,000	8/12/2010 – 8/12/2016	170,000	–	57,000	–	–	26.85	170,000	–
	17/12/2010	170,000	16/12/2011 – 16/12/2017	170,000	–	57,000	–	–	28.84	170,000	–
Jacob Kam Chak-pui	13/12/2007	75,000	10/12/2008 – 10/12/2014	75,000	–	–	–	–	27.60	75,000	–
	8/12/2008	65,000	8/12/2009 – 8/12/2015	65,000	–	21,000	–	–	18.30	65,000	–
	14/12/2009	65,000	8/12/2010 – 8/12/2016	65,000	–	22,000	–	–	26.85	65,000	–
	21/7/2010	50,000	28/6/2011 – 28/6/2017	50,000	–	17,000	–	–	27.73	50,000	–
	17/12/2010	170,000	16/12/2011 – 16/12/2017	170,000	–	57,000	–	–	28.84	170,000	–
Lincoln Leong Kwok-kuen	12/12/2007	170,000	10/12/2008 – 10/12/2014	170,000	–	–	–	–	27.60	170,000	–
	9/12/2008	170,000	8/12/2009 – 8/12/2015	170,000	–	56,000	–	–	18.30	170,000	–
	10/12/2009	170,000	8/12/2010 – 8/12/2016	170,000	–	57,000	–	–	26.85	170,000	–
	17/12/2010	170,000	16/12/2011 – 16/12/2017	170,000	–	57,000	–	–	28.84	170,000	–
Jeny Yeung Mei-chun (Note 4)	12/12/2007	75,000	10/12/2008 – 10/12/2014	75,000	–	–	–	–	27.60	75,000	–
	10/12/2008	65,000	8/12/2009 – 8/12/2015	65,000	–	21,000	–	–	18.30	65,000	–
	10/12/2009	65,000	8/12/2010 – 8/12/2016	65,000	–	22,000	–	–	26.85	65,000	–
	17/12/2010	65,000	16/12/2011 – 16/12/2017	65,000	–	22,000	–	–	28.84	65,000	–
Gillian Elizabeth Meller (Note 5)	12/12/2007	55,000	10/12/2008 – 10/12/2014	18,000	–	–	–	–	27.60	18,000	–
	11/12/2008	70,000	8/12/2009 – 8/12/2015	46,500	–	23,000	–	–	18.30	46,500	–
	10/12/2009	65,000	8/12/2010 – 8/12/2016	65,000	–	22,000	–	–	26.85	65,000	–
	17/12/2010	90,000	16/12/2011 – 16/12/2017	90,000	–	30,000	–	–	28.84	90,000	–
David Tang Chi-fai (Note 6)	13/12/2007	65,000	10/12/2008 – 10/12/2014	65,000	–	–	–	–	27.60	65,000	–
	12/12/2008	65,000	8/12/2009 – 8/12/2015	43,000	–	21,000	–	–	18.30	43,000	–
	15/12/2009	65,000	8/12/2010 – 8/12/2016	65,000	–	22,000	–	–	26.85	65,000	–
	17/12/2010	65,000	16/12/2011 – 16/12/2017	65,000	–	22,000	–	–	28.84	65,000	–
Other eligible employees	11/12/2007	45,000	10/12/2008 – 10/12/2014	45,000	–	–	–	–	27.60	45,000	–
	12/12/2007	2,430,000	10/12/2008 – 10/12/2014	2,025,000	–	320,000	65,000	27.60	1,640,000	28.15	
	13/12/2007	775,000	10/12/2008 – 10/12/2014	775,000	–	65,000	–	27.60	710,000	–	
	14/12/2007	1,005,000	10/12/2008 – 10/12/2014	872,000	–	52,000	–	27.60	820,000	–	
	15/12/2007	435,000	10/12/2008 – 10/12/2014	343,000	–	75,000	40,000	27.60	228,000	29.20	
	17/12/2007	835,000	10/12/2008 – 10/12/2014	751,000	–	21,000	–	27.60	730,000	–	
	18/12/2007	445,000	10/12/2008 – 10/12/2014	288,000	–	13,000	–	27.60	275,000	–	
	19/12/2007	115,000	10/12/2008 – 10/12/2014	80,000	–	–	–	27.60	80,000	–	
	20/12/2007	190,000	10/12/2008 – 10/12/2014	190,000	–	–	–	27.60	190,000	–	
	21/12/2007	45,000	10/12/2008 – 10/12/2014	15,000	–	15,000	–	27.60	–	–	
	22/12/2007	35,000	10/12/2008 – 10/12/2014	35,000	–	–	–	27.60	35,000	–	
	24/12/2007	118,000	10/12/2008 – 10/12/2014	118,000	–	–	–	27.60	118,000	–	
	28/12/2007	35,000	10/12/2008 – 10/12/2014	35,000	–	–	–	27.60	35,000	–	
	31/12/2007	130,000	10/12/2008 – 10/12/2014	130,000	–	–	–	27.60	130,000	–	
	2/1/2008	75,000	10/12/2008 – 10/12/2014	48,000	–	13,000	–	27.60	35,000	–	
	3/1/2008	40,000	10/12/2008 – 10/12/2014	40,000	–	–	–	27.60	40,000	–	
	7/1/2008	125,000	10/12/2008 – 10/12/2014	125,000	–	15,000	30,000	27.60	80,000	28.90	
	28/3/2008	255,000	26/3/2009 – 26/3/2015	204,000	–	75,000	5,000	–	26.52	199,000	–
	31/3/2008	379,000	26/3/2009 – 26/3/2015	349,000	–	117,000	20,000	6,000	26.52	323,000	28.95

**OPTIONS TO SUBSCRIBE FOR ORDINARY SHARES GRANTED UNDER THE 2007 SHARE OPTION SCHEME,
AS REFERRED TO IN NOTES 11B(ii) AND 53A(ii) TO THE ACCOUNTS (CONTINUED)**

Executive Directorate and eligible employees	Date granted	Options granted	Period during which rights exercisable (day/month/year)	Options outstanding as at 1 January 2011	Options granted during the year	Options vested during the year	Options lapsed during the year	Options exercised during the year	Exercise price per share of options (HK\$)	Options outstanding as at 31 December 2011	Weighted average closing price of shares immediately before the date(s) on which options were exercised (HK\$)
Other eligible employees	1/4/2008	261,000	26/3/2009 – 26/3/2015	249,000	–	79,000	–	–	26.52	249,000	–
	2/4/2008	296,000	26/3/2009 – 26/3/2015	276,000	–	84,000	–	–	26.52	276,000	–
	3/4/2008	171,000	26/3/2009 – 26/3/2015	159,000	–	52,000	–	19,000	26.52	140,000	28.50
	4/4/2008	23,000	26/3/2009 – 26/3/2015	23,000	–	7,000	–	–	26.52	23,000	–
	5/4/2008	17,000	26/3/2009 – 26/3/2015	17,000	–	5,000	–	–	26.52	17,000	–
	7/4/2008	390,000	26/3/2009 – 26/3/2015	342,000	–	110,000	12,000	–	26.52	330,000	–
	8/4/2008	174,000	26/3/2009 – 26/3/2015	116,000	–	40,000	–	6,000	26.52	110,000	29.35
	9/4/2008	85,000	26/3/2009 – 26/3/2015	85,000	–	26,000	–	–	26.52	85,000	–
	10/4/2008	58,000	26/3/2009 – 26/3/2015	58,000	–	18,000	–	–	26.52	58,000	–
	11/4/2008	134,000	26/3/2009 – 26/3/2015	117,000	–	36,000	–	–	26.52	117,000	–
	12/4/2008	48,000	26/3/2009 – 26/3/2015	48,000	–	15,000	–	–	26.52	48,000	–
	14/4/2008	40,000	26/3/2009 – 26/3/2015	40,000	–	12,000	–	–	26.52	40,000	–
	15/4/2008	34,000	26/3/2009 – 26/3/2015	34,000	–	10,000	–	–	26.52	34,000	–
	16/4/2008	57,000	26/3/2009 – 26/3/2015	40,000	–	12,000	–	–	26.52	40,000	–
	17/4/2008	147,000	26/3/2009 – 26/3/2015	124,000	–	38,000	–	–	26.52	124,000	–
	18/4/2008	32,000	26/3/2009 – 26/3/2015	15,000	–	5,000	–	–	26.52	15,000	–
	19/4/2008	25,000	26/3/2009 – 26/3/2015	25,000	–	8,000	–	–	26.52	25,000	–
	21/4/2008	66,000	26/3/2009 – 26/3/2015	66,000	–	20,000	–	–	26.52	66,000	–
	23/4/2008	34,000	26/3/2009 – 26/3/2015	19,000	–	6,000	–	–	26.52	19,000	–
	8/12/2008	90,000	8/12/2009 – 8/12/2015	45,000	–	14,000	–	–	18.30	45,000	–
	9/12/2008	653,000	8/12/2009 – 8/12/2015	623,000	–	184,000	21,000	53,000	18.30	549,000	27.73
	10/12/2008	2,111,400	8/12/2009 – 8/12/2015	1,975,900	–	681,400	50,000	93,000	18.30	1,832,900	27.23
	11/12/2008	2,394,200	8/12/2009 – 8/12/2015	2,244,700	–	768,200	29,000	269,000	18.30	1,946,700	26.03
	12/12/2008	1,416,500	8/12/2009 – 8/12/2015	1,249,000	–	462,500	–	151,000	18.30	1,098,000	25.01
	13/12/2008	84,500	8/12/2009 – 8/12/2015	84,500	–	27,500	–	6,500	18.30	78,000	28.95
	14/12/2008	88,200	8/12/2009 – 8/12/2015	79,700	–	22,200	6,000	21,500	18.30	52,200	25.63
	15/12/2008	1,084,700	8/12/2009 – 8/12/2015	930,200	–	322,700	15,000	42,000	18.30	873,200	29.08
	16/12/2008	581,500	8/12/2009 – 8/12/2015	487,500	–	157,000	14,500	23,000	18.30	450,000	27.52
	17/12/2008	513,500	8/12/2009 – 8/12/2015	485,500	–	167,500	–	15,000	18.30	470,500	27.85
	18/12/2008	611,500	8/12/2009 – 8/12/2015	483,000	–	177,500	–	12,500	18.30	470,500	27.04
	19/12/2008	198,000	8/12/2009 – 8/12/2015	198,000	–	64,000	–	–	18.30	198,000	–
	20/12/2008	19,000	8/12/2009 – 8/12/2015	19,000	–	6,000	–	–	18.30	19,000	–
	22/12/2008	772,500	8/12/2009 – 8/12/2015	689,500	–	253,500	67,000	135,500	18.30	487,000	26.67
	23/12/2008	306,000	8/12/2009 – 8/12/2015	246,500	–	85,000	6,000	22,500	18.30	218,000	28.88
	24/12/2008	500,500	8/12/2009 – 8/12/2015	455,500	–	163,500	–	88,000	18.30	367,500	28.49
	25/12/2008	45,000	8/12/2009 – 8/12/2015	45,000	–	15,000	–	–	18.30	45,000	–
	29/12/2008	148,000	8/12/2009 – 8/12/2015	133,000	–	48,000	15,000	–	18.30	118,000	–
	30/12/2008	19,000	8/12/2009 – 8/12/2015	19,000	–	6,000	–	–	18.30	19,000	–
	18/6/2009	170,000	12/6/2010 – 12/6/2016	90,000	–	30,000	–	–	24.50	90,000	–
	6/7/2009	45,000	12/6/2010 – 12/6/2016	45,000	–	15,000	–	–	24.50	45,000	–
	9/7/2009	45,000	12/6/2010 – 12/6/2016	30,000	–	15,000	–	–	24.50	30,000	–
	9/12/2009	200,000	8/12/2010 – 8/12/2016	115,000	–	39,000	–	–	26.85	115,000	–
	10/12/2009	2,211,000	8/12/2010 – 8/12/2016	2,114,000	–	700,500	108,000	–	26.85	2,006,000	–
	11/12/2009	2,362,000	8/12/2010 – 8/12/2016	2,322,000	–	788,000	87,000	–	26.85	2,235,000	–
	12/12/2009	610,000	8/12/2010 – 8/12/2016	610,000	–	205,500	44,500	–	26.85	565,500	–
	13/12/2009	19,000	8/12/2010 – 8/12/2016	12,500	–	6,500	–	–	26.85	12,500	–
	14/12/2009	2,443,000	8/12/2010 – 8/12/2016	2,379,000	–	802,500	6,500	–	26.85	2,372,500	–
	15/12/2009	2,773,000	8/12/2010 – 8/12/2016	2,739,000	–	869,000	252,500	45,500	26.85	2,441,000	28.24
	16/12/2009	1,550,000	8/12/2010 – 8/12/2016	1,491,000	–	486,000	55,000	22,000	26.85	1,414,000	29.20
	17/12/2009	1,000,000	8/12/2010 – 8/12/2016	975,000	–	329,500	–	–	26.85	975,000	–
	18/12/2009	389,000	8/12/2010 – 8/12/2016	380,500	–	131,500	–	–	26.85	380,500	–

REPORT OF THE MEMBERS OF THE BOARD

OPTIONS TO SUBSCRIBE FOR ORDINARY SHARES GRANTED UNDER THE 2007 SHARE OPTION SCHEME, AS REFERRED TO IN NOTES 11B(ii) AND 53A(ii) TO THE ACCOUNTS (CONTINUED)

Executive Directorate and eligible employees	Date granted	Options granted	Period during which rights exercisable (day/month/year)	Options outstanding as at 1 January 2011					Exercise price per share of options (HK\$)	Options outstanding as at 31 December 2011	Weighted average closing price of shares immediately before the date(s) on which options were exercised (HK\$)
				Options granted during the year	Options vested during the year	Options lapsed during the year	Options exercised during the year				
Other eligible employees	19/12/2009	70,000	8/12/2010 – 8/12/2016	70,000	–	23,500	–	–	26.85	70,000	–
	20/12/2009	75,000	8/12/2010 – 8/12/2016	75,000	–	25,500	–	–	26.85	75,000	–
	21/12/2009	520,000	8/12/2010 – 8/12/2016	520,000	–	169,500	12,500	6,500	26.85	501,000	29.85
	22/12/2009	256,000	8/12/2010 – 8/12/2016	237,000	–	80,500	22,000	–	26.85	215,000	–
	21/7/2010	305,000	28/6/2011 – 28/6/2017	305,000	–	94,000	25,000	–	27.73	280,000	–
	16/12/2010	194,000	16/12/2011 – 16/12/2017	194,000	–	65,500	–	–	28.84	194,000	–
	17/12/2010	4,097,000	16/12/2011 – 16/12/2017	4,097,000	–	1,347,000	140,500	–	28.84	3,956,500	–
	18/12/2010	673,000	16/12/2011 – 16/12/2017	673,000	–	227,500	–	–	28.84	673,000	–
	19/12/2010	174,000	16/12/2011 – 16/12/2017	174,000	–	59,000	–	–	28.84	174,000	–
	20/12/2010	4,854,500	16/12/2011 – 16/12/2017	4,854,500	–	1,627,000	126,500	–	28.84	4,728,000	–
	21/12/2010	3,020,000	16/12/2011 – 16/12/2017	3,020,000	–	1,015,500	19,000	–	28.84	3,001,000	–
	22/12/2010	975,000	16/12/2011 – 16/12/2017	975,000	–	322,000	19,000	–	28.84	956,000	–
	23/12/2010	189,000	16/12/2011 – 16/12/2017	189,000	–	64,000	–	–	28.84	189,000	–
	7/7/2011	215,000	27/6/2012 – 27/6/2018	–	215,000	–	–	–	26.96	215,000	–

Notes

- No option may be exercised later than seven years after its date of offer and no option may be offered to be granted more than seven years after the adoption of the 2007 Share Option Scheme ("2007 Option Scheme") on 7 June 2007.
- Unless approved by shareholders in the manner as required by the Listing Rules, the total number of shares issued and issuable upon exercise of the options granted to any eligible employee under the 2007 Option Scheme together with the total number of shares issued and issuable upon the exercise of any option granted to such eligible employee under any other share option scheme of the Company (including, in each case, both exercised and outstanding options) in any 12-month period must not exceed 0.2% of the shares of the Company in issue at the date of offer in respect of such option under the 2007 Option Scheme.
- The proportion of underlying shares in respect of which the above share options will vest is as follows:

Date	Proportion of underlying shares in respect of which an option is vested
Before the first anniversary of the date of offer of the option (the "Offer Anniversary")	none
From the first Offer Anniversary to the date immediately before the second Offer Anniversary	one-third
From the second Offer Anniversary to the date immediately before the third Offer Anniversary	two-thirds
From the third Offer Anniversary and thereafter	all

- Ms. Jeny Yeung Mei-chun became the Commercial Director and a Member of the Executive Directorate on 1 September 2011.
- Ms. Gillian Elizabeth Meller became the Legal Director and Secretary and a Member of the Executive Directorate on 1 September 2011.
- Mr. David Tang Chi-fai became the Property Director and a Member of the Executive Directorate on 1 October 2011.

During the year ended 31 December 2011, 215,000 options to subscribe for shares of the Company were granted to 5 employees under the 2007 Share Option Scheme. Details of the grant are set out in the tables above. The closing price per share immediately before the date of grant of the options is set out below. Pursuant to the terms of the Scheme, each grantee undertakes to pay HK\$1.00, on demand, to the

Company, in consideration for the grant of the options. The share options granted are recognised on an accrued vesting basis in the accounts. The weighted average value per option granted, estimated at the date of grant using the Black-Scholes pricing model is as follows:

Date granted	Closing price per share immediately before the date of grant (HK\$)	Estimated risk-free interest rate (%)	Expected life (Years)	Estimated Volatility	Expected dividend per share (HK\$)	Weighted average value per option granted (HK\$)
7/7/2011	27.70	0.84	3.5	0.28	0.70	5.01

The Black-Scholes option pricing model was developed for use in estimating the fair value of traded options and requires input of highly subjective assumptions, including the expected life and stock price volatility. Since the Company's share options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimates, the Black-Scholes option pricing model does not necessarily provide a reliable measure of the fair value of the share options.

Save as disclosed above:

- A** none of the Members of the Board or the Executive Directorate of the Company had any interest or short position in the shares, underlying shares or debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO); and
- B** during the year ended 31 December 2011, no Member of the Board or the Executive Directorate nor any of their spouses or children under 18 years of age held any rights to subscribe for equity or debt securities of the Company nor had there been any exercises of any such rights by any of them,

as recorded in the register kept by the Company under section 352 of the SFO or otherwise notified to the Company and the HKSE pursuant to the Model Code.

DIRECTORS' SERVICE CONTRACTS

No director proposed for election or re-election at the forthcoming Annual General Meeting has a service contract which is not determinable by the Company or any of its subsidiaries within one year without payment of compensation, other than statutory compensation.

No Director has a service contract with the Company or any of its subsidiaries which is for a duration which may exceed three years or which requires the Company to, in order to terminate such contract, give a notice period in excess of one year or pay or make other payments equivalent to more than one year's emoluments.

SUBSTANTIAL SHAREHOLDERS' INTERESTS

Set out below is the name of the party which was interested in 5% or more of the nominal value of the share capital of the Company and the number of shares in which it was interested as at 31 December 2011 as recorded in the register kept by the Company under section 336 of the SFO:

Name	No. of Ordinary Shares	Percentage of Ordinary Shares to total issued share capital
The Financial Secretary Incorporated (in trust on behalf of the Government)	4,434,552,207	76.66

The Company has been informed by the Government that, as at 31 December 2011, approximately 0.47% of the shares of the Company were held for the account of the Exchange Fund. The Exchange Fund is a fund established under the Exchange Fund Ordinance (Cap. 66 of the Laws of Hong Kong) under the control of the Financial Secretary.

LOAN AGREEMENTS WITH COVENANT RELATING TO SPECIFIC PERFORMANCE OF THE CONTROLLING SHAREHOLDER

As at 31 December 2011, the Group had borrowings of HK\$19,543 million with maturities ranging from 2012 to 2020 and available uncommitted banking and other facilities of HK\$10,469 million, which were subject to the condition that the Government, being the Company's controlling shareholder, owns more than half in nominal value of the voting share capital of the Company during the lives of the borrowings and the undrawn facilities. Otherwise, immediate repayment of borrowings may be demanded and cancellation of the undrawn facilities may result.

REPORT OF THE MEMBERS OF THE BOARD

MAJOR SUPPLIERS AND CUSTOMERS

Less than 30% in value of supplies (which were not of a capital nature) purchased during the year ended 31 December 2011 was attributable to the Company's five largest suppliers. Less than 30% in value of the Company's turnover during the year ended 31 December 2011 was attributable to the Company's five largest customers combined by value.

GOING CONCERN

The accounts on pages 147 to 238 have been prepared on a going concern basis. The Board has reviewed the Company's budget for 2012, together with the longer-term forecast for the following five years and is satisfied that the Company has sufficient resources to continue as a going concern for the foreseeable future.

CONTINUING CONNECTED TRANSACTIONS

During the year under review, the following transactions and arrangements described below involved the provision of goods or services on an ongoing basis with the Government and/or KCRC, the Airport Authority (the "AA"), United Group Rail Services Limited ("UGL"), Leighton Contractors (Asia) Limited ("LCAL") and John Holland Pty Limited ("JHL"). The Government is a substantial shareholder of the Company for the purposes of the Listing Rules. KCRC and the AA are both associates of the Company as defined in the Listing Rules. As explained under Section III below, UGL and John Holland Melbourne Rail Franchise Pty Ltd. ("John Holland") are substantial shareholders of a subsidiary of the Company and John Holland, JHL and LCAL are indirect wholly-owned subsidiaries of Leighton Holdings Limited. On this basis, JHL and LCAL are both associates of John Holland for the purposes of the Listing Rules. The Government, KCRC, the AA, UGL, LCAL and JHL are therefore each "connected persons" for the purposes of the Listing Rules and each transaction set out at paragraphs I, II and III below constitutes a continuing connected transaction for the Company under the Listing Rules.

I Merger-related Continuing Connected Transactions

Each of the transactions listed in paragraphs A to D below and which formed part of the Rail Merger, was approved by the independent shareholders of the Company at an Extraordinary General Meeting held on 9 October 2007. These paragraphs should be read in conjunction with the paragraphs contained in the section below headed "Additional Information in respect of the Rail Merger".

As disclosed in the circular issued by the Company on 3 September 2007 in connection with the Rail Merger, the Stock Exchange granted a waiver to the Company from strict compliance with the requirements under Chapter 14A of the Listing Rules which would otherwise apply to continuing connected transactions between the Company, the Government and/or KCRC arising as a result of the Rail Merger, subject to certain conditions (the "Merger-related Waiver").

A Merger Framework Agreement

The Merger Framework Agreement was entered into on 9 August 2007 between the Company, KCRC and the Secretary for Transport and Housing and the Secretary for Financial Services and the Treasury for and on behalf of the Government.

The Merger Framework Agreement contains provisions for the overall structure and certain specific aspects of the Rail Merger, including in relation to:

- a seamless interchange programme;
- corporate governance of the Company Post-Rail Merger;
- payments relating to property enabling works;
- arrangements relating to the establishment of a rolling programme on the level of flat production arising from tenders for railway property development;
- arrangements in relation to the assessment of land premium amounts;
- arrangements in relation to the employees of the Company and KCRC, including provisions preventing the Company from terminating the employment of relevant frontline staff for any reason that relates to the process of integrating the operations of the Company and KCRC;
- the implementation of certain fare reductions;
- arrangements in relation to the proposed Shatin to Central Link;
- KCRC's continuing responsibility for its existing financial arrangements;
- treatment of KCRC's cross border leases;
- the payment of HK\$7.79 billion in respect of the Property Package (as described on pages 131 to 133 and in paragraph D below);
- the allocation of liability for any Pre-Rail Merger and Post-Rail Merger claims by third parties; and
- the Company's retention of its English name and (pursuant to the Rail Merger Ordinance) the change of its Chinese name to "香港鐵路有限公司".

B West Rail Agency Agreement

The West Rail Agency Agreement and related agreements were entered into on 9 August 2007 between the Company, KCRC and certain KCRC subsidiary companies ("West Rail Subsidiaries"). Pursuant to the terms of the West Rail Agency Agreement, the Company was appointed:

- to act as KCRC's agent, and donee under powers of attorney, to exercise certain rights and perform certain obligations relating to specified development sites along West Rail; and

- to act as agent for, and donee under powers of attorney from, each of the West Rail Subsidiaries to exercise certain rights and perform certain obligations relating to specified development sites along West Rail.

The Company will receive an agency fee of 0.75% of the gross sale proceeds in respect of the unawarded West Rail development sites and 10% of the net profits accrued to the West Rail Subsidiaries under the development agreements in respect of the awarded West Rail development sites. The Company will also recover from the West Rail Subsidiaries its costs (including internal costs) incurred in respect of the West Rail development sites plus 16.5% on-cost, together with interest accrued thereon.

C KCRC Cross Border Lease Agreements

US CBL Assumption Agreements

Separate US CBL Assumption Agreements were entered into on 30 November 2007 between the Company, KCRC and, variously, Wilmington Trust Company, Buoyant Asset Limited, BA Leasing & Capital Corporation, Utrecht-America Finance Co., Cooperatieve Centrale Raiffeisen-Boerenleenbank B.A., Advanced Asset Limited, Washoe Asset Management Company, Quality Asset Limited, Kasey Asset Limited, Key Equipment Finance Inc., Mercantile Leasing Company (No. 132) Limited, Landesbank Sachsen Aktiengesellschaft, Barclays Bank PLC, Bayerische Landesbank Girozentrale, U.S. Bank National Association, Circuit Asset Limited, Citicorp USA Inc., Shining Asset Limited, Banc of America FSC Holdings Inc., Fluent Asset Limited, Anzef Limited, Societe Generale, Australia and New Zealand Banking Group Limited, Statesman Asset Limited, State Street Bank and Trust Company and Bowman Asset Limited and became effective on 3 December 2007, with respect to each of the US cross border leases originally entered into between KCRC and certain counterparties (each, a "CBL"). Pursuant to each US CBL Assumption Agreement, the Company undertakes to perform, on a joint and several basis with KCRC, the obligations of KCRC under the respective CBLs. As a result thereof, the Company is generally liable to the CBL counterparties in respect of KCRC's obligations under the CBLs and has the right to exercise certain of KCRC's rights under the CBLs.

US CBL Allocation Agreement

The US CBL Allocation Agreement was entered into between the Company, KCRC and the subsidiaries of KCRC (the "KCRC Subsidiaries") on 2 December 2007. Pursuant to the US CBL Allocation Agreement, rights, obligations and responsibility for risks relating to the CBLs are delineated and allocated between KCRC and the Company (each of which is jointly and severally liable to specified CBL counterparties, as referred to in the paragraph above headed "US CBL Assumption Agreements"). Under the terms of the US CBL Allocation Agreement, as between the Company and KCRC, the Company is responsible for specified obligations. The Company and KCRC each made representations under the US CBL Allocation Agreement, which include, in the case of those

made by KCRC, representations with respect to the status of the CBLs. The Company and KCRC agreed to indemnify each other for certain losses in relation to the CBLs.

D Property Package Agreements

Category 2A Properties

On 9 August 2007, the Government entered into an undertaking that it would, within twelve months of the Merger Date or such further period of time as the Government and the Company may agree, issue to KCRC an offer for the grant at nil premium of Government leases in respect of the land upon which certain properties (the "Category 2A Properties") are situated (the "said Government Leases"). The Category 2A Properties were held by KCRC as vested land under the Kowloon-Canton Railway Corporation Ordinance (Cap. 372 of the Laws of Hong Kong) ("KCRC Ordinance"). On 9 August 2007, KCRC entered into an undertaking that it would, immediately after the grant of the said Government Leases referred to in the preceding sentence, enter into agreements for sale and purchase to sell the Category 2A Properties to the Company (the "said Agreements for Sale and Purchase"). Assignments of the Category 2A Properties to the Company shall then take place pursuant to the said Agreements for Sale and Purchase (the said "Assignments"). Pursuant to the KCRC undertaking and as interim arrangements until the grant of the Government leases, on 9 August 2007 the following agreements were entered into between KCRC and the Company:

- an agreement that KCRC (as lessor) shall enter into tenancy agreements with the Company (as lessee) at market rent in respect of the Category 2A Properties' vacant units (with the intention that the Company will then sub-let the vacant units to sub-tenants);
- two licence agreements in respect of the common areas within the Category 2A Properties, pursuant to which KCRC granted the Company the right to use certain common areas until the execution of the Category 2A Properties assignment referred to above;
- a lease enforcement agency agreement appointing the Company as its enforcement agent to enforce KCRC's current Category 2A Properties tenancy agreements against tenants; and
- an assignment of rental proceeds whereby the proceeds received under KCRC's current Category 2A Properties tenancy agreements with tenants are assigned to the Company.

The said Government Leases were issued to KCRC respectively on 27 March 2009 and 31 March 2009. The said Agreements for Sale and Purchase were entered into between KCRC and the Company on 27 March 2009 and 31 March 2009 respectively and the said Assignments to the Company were executed on 27 March 2009 and 31 March 2009 respectively.

REPORT OF THE MEMBERS OF THE BOARD

Deeds of Mutual Grant were also entered into between the Company and KCRC on 27 March 2009 and 31 March 2009 respectively setting out the easements, rights, entitlements, privileges and liberties of the Company and KCRC in the land on which the Category 2A Properties are situated.

Category 2B Property

On 9 August 2007, the Government entered into an undertaking that it would, within twenty four months of the Merger Date or such further period of time as the Government and the Company may agree, issue to the Company an offer for the grant of a Government Lease of a certain property (the "Category 2B Property") on terms to be agreed. The Category 2B Property is currently held by KCRC as vested land under the KCRC Ordinance for use as staff quarters and a recreational club.

On 9 August 2007, KCRC entered into an undertaking relating to interim arrangements to ensure that, as from the Merger Date, the Company shall be responsible for KCRC's obligations under licence agreements relating to the Category 2B Property, and for enforcing such agreements. The Company is entitled to proceeds received by KCRC in respect of those licence agreements. The interim arrangements include, inter alia, as from the Merger Date:

- an agreement that KCRC (as licensor) shall grant to the Company (as licensee) possession of the Category 2B Property (without payment of any licence fee or premium), subject to existing licences and the Second Schedule of the KCRC Ordinance, with the right of the Company to sub-license all or any part of the Category 2B Property (subject to it being used as staff quarters and a recreation club);
- until the grant of the Government lease of the Category 2B Property, KCRC has appointed the Company as its enforcement agent to enforce KCRC's current Category 2B Property licence agreements against licensees; and
- KCRC has assigned to the Company the proceeds received under KCRC's current Category 2B Property licence agreements with licensees.

The basic terms offer for the Category 2B Property (i.e. Trackside Villas) was issued and accepted by the Company on 31 December 2009 and the Government Lease in respect of Tai Po Town Lot No. 199 dated 29 March 2010 was issued for a term of 50 years from 2 December 2007.

Category 3 Properties

On 9 August 2007, the Company entered into three agreements (the "Category 3 Agreements") and related powers of attorney with KCRC. Each Category 3 Agreement relates to a certain property (each a "Category 3 Property"). KCRC has previously entered into a development agreement in respect of each Category 3 Property. None of the rights and obligations granted to or undertaken by the Company under the Category 3 Agreements may be exercised or performed

by the Company if they relate exclusively to concession property situate on any Category 3 Property. Matters affecting the concession property situate on any Category 3 Property are dealt with under the terms of the Service Concession Agreement (as defined and summarised on pages 142 to 143).

Pursuant to the terms of each Category 3 Agreement, the Company has been appointed to act as KCRC's agent, and donee under powers of attorney, to exercise rights and to perform obligations of KCRC which relate to the Category 3 Property (but excluding the right or obligation to dispose of the relevant Category 3 Property).

The Company is required at all times to comply with statutory restrictions and obligations binding on KCRC which relate to the Category 3 Property, and shall pay all amounts due and payable from KCRC which have been incurred by KCRC as a result of the Company's actions.

In acting as KCRC's agent, the Company is required to act according to prudent commercial principles, and aim to maximise gross profits under the Category 3 Property and to run a safe and efficient railway. In order to assist the Company in performing its agency functions, KCRC has granted powers of attorney to the Company. The Company may only use the powers of attorney to exercise rights and perform obligations conferred or undertaken by it under the relevant Category 3 Agreement. As well as acting as KCRC's agent, the Company has the right to give KCRC instructions in respect of any action or matter relating to each Category 3 Property (including its related development agreement) which the Company is unable to take by reason of the limitation of the scope of its agency powers. KCRC is required to comply promptly with those instructions provided that it is permitted under law, and under the relevant Government grant, to carry out those instructions.

KCRC is required to account for revenue received in respect of a Category 3 Property by way of balance sheet movement (rather under its profit and loss account), provided that such treatment is permitted under law and accounting principles and practices.

KCRC shall not take any action in respect of a Category 3 Property which is not carried out by the Company (acting as KCRC's agent), or according to the Company's instructions, or otherwise in accordance with the terms of the Category 3 Agreement.

As consideration for acting as KCRC's agent, the Company shall be paid a fee which is expected to be similar in quantum to the profits made by KCRC in respect of the relevant Category 3 Property (after deducting certain initial and upfront payments and consultant contribution costs, in each case paid or to be paid by the relevant developer to KCRC). Generally, the Company's fee shall be payable in instalments promptly following receipt of relevant funds by KCRC (but subject to specified deductions of amounts due from KCRC to the relevant Category 3 Property developer).

The Company has agreed to give certain indemnities to KCRC in respect of each Category 3 Property.

The Company shall be the first manager, or shall ensure that a manager is appointed in respect of, each Category 3 Property (once developed).

The Company's appointment as agent shall terminate when KCRC ceases to have any undivided share in the relevant Category 3 Property, other than concession property, and neither KCRC nor the developer nor the guarantors have any further rights to exercise, or obligations to perform, under the development agreement relating to the relevant Category 3 Property.

In relation to the Merger Framework Agreement, the West Rail Agency Agreement (and related powers of attorney), the US CBL Assumption Agreements, the US CBL Allocation Agreement and the agreements in relation to Category 2A, Category 2B and Category 3 Properties (together the "Merger-related Continuing Connected Transactions") and in accordance with paragraph B(I)(i) of the Merger-related Waiver, the Company confirms that the Independent Non-executive Directors of the Company have reviewed each of the Merger-related Continuing Connected Transactions and confirmed that the Merger-related Continuing Connected Transactions were entered into:

- (1) in the ordinary and usual course of business of the Company;
- (2) on normal commercial terms or on terms which are no less favourable to the Company than terms available to or from independent third parties; and
- (3) in accordance with the relevant agreement governing them on terms that are fair and reasonable and in the interests of the shareholders of the Company as a whole.

The Company has engaged the auditors of the Company to carry out a review of each of the Merger-related Continuing Connected Transactions in accordance with Hong Kong Standard on Assurance Engagements 3000 "Assurance Engagements Other Than Audits or Reviews of Historical Financial Information" and with reference to Practice Note 740 "Auditor's Letter on Continuing Connected Transactions under the Hong Kong Listing Rules" issued by the Hong Kong Institute of Certified Public Accountants. In accordance with paragraph B(I)(ii) of the Merger-related Waiver, the auditors have provided a letter to the Board confirming that:

- (a) nothing has come to their attention that causes them to believe that the Merger-related Continuing Connected Transactions have not been approved by the Board; and
- (b) nothing has come to their attention that causes them to believe that the Merger-related Continuing Connected Transactions were not entered into, in all material respects, in accordance with the relevant agreements governing such transactions.

II Non Merger-related Continuing Connected Transactions with Government and/or its Associates

As disclosed in the announcement of the Company dated 13 January 2005, the Stock Exchange has granted a waiver to the Company from strict compliance with the requirements under Chapter 14A of the Listing Rules which would otherwise apply to connected transactions and continuing connected transactions between the Company and the Government, subject to certain conditions (the "Waiver").

The following disclosures are made in accordance with paragraph (B)(I) of the Waiver and Rule 14A.46 of the Listing Rules.

A1 Entrustment Agreement for Design and Site Investigation in Relation to the Shatin to Central Link

The Entrustment Agreement for Design and Site Investigation in Relation to the Shatin to Central Link (the "First SCL Agreement") was entered into on 24 November 2008 between the Company and the Secretary for Transport and Housing for and on behalf of the Government.

The First SCL Agreement contains provisions for the design of and site investigation and procurement activities in relation to the proposed Shatin to Central Link, including in relation to:

- the Government's obligation to pay the Company up to a maximum aggregate amount of HK\$1,500 million in respect of certain costs incurred by the Company pursuant to the First SCL Agreement, including the Company's in-house design costs and certain on-costs and preliminary costs;
- the Government's obligation to bear and finance the total cost of the design and site investigation activities under the First SCL Agreement (subject to the limit noted above in respect of payments to the Company) and arrangements for the payment of these costs directly by the Government;
- the Company's obligation to carry out or procure the carrying out of the design and site investigation activities in relation to the proposed Shatin to Central Link;
- the limitation of the Company's liability to the Government under the First SCL Agreement, except in respect of death or personal injury caused by the negligence of the Company, to HK\$600 million; and
- should the railway scheme for the Shatin to Central Link be authorised under the Railways Ordinance (Cap. 519 of the Laws of Hong Kong), the execution of a further agreement by the Government and the Company setting out each of their rights, obligations, duties and powers with respect to the financing, construction, completion, testing, commissioning and putting into service the works necessary for the construction and operation of the Shatin to Central Link.

REPORT OF THE MEMBERS OF THE BOARD

A2 Entrustment Agreement for Advance Works Relating to the Shatin to Central Link

The Entrustment Agreement for Advance Works Relating to the Shatin to Central Link (the "Second SCL Agreement") was entered into on 17 May 2011 between the Company and the Secretary for Transport and Housing for and on behalf of the Government.

The Second SCL Agreement contains the following provisions:

- in consideration of the Company executing or procuring the execution of certain entrustment activities as set out in the Second SCL Agreement and carrying out its other obligations under the Second SCL Agreement, the Government shall pay to the Company the Company's project management cost. The amount of such project management cost is to be agreed between the Company and the Government and prior to such agreement, the project management cost shall be paid by the Government to the Company on a provisional basis calculated in accordance with the Second SCL Agreement;
- the Company and the Government may agree that the Company will carry out (or procure the carrying out of) certain additional works for the Government (such agreed additional works being "miscellaneous works"). Miscellaneous works (if any) are to be carried out by the Company in the same manner as if they had formed part of the activities specified to be carried out under the Second SCL Agreement and in consideration of the Company executing or procuring the execution of such miscellaneous works (if any) and carrying out its other obligations under the Second SCL Agreement in relation to such miscellaneous works (if any), the Government shall pay to the Company an amount to be agreed between the Company and the Government as being the project management fee payable to the Company for designing and constructing such miscellaneous works;
- the Government shall bear all of the "Works Cost" (as defined in the Second SCL Agreement). In this connection, the Government will make payments to the Company in respect of the Works Cost on a provisional basis, subject to adjustments when the final outturn cost of the Works Cost is determined;
- the Government shall bear land acquisition, clearance and related costs and those costs which are incurred by the Lands Department in connection with the Shatin to Central Link project;
- the maximum aggregate amount payable by the Government to the Company under the Second SCL Agreement is limited to approximately HK\$3,000 million per annum and a total in aggregate of approximately HK\$15,000 million;
- the Company shall carry out or procure the carrying out of certain enabling works on the expanded Admiralty Station and the to be constructed Ho Man Tin Station, the reprovisioning of the International Mail Centre from Hung Hom to Kowloon Bay and other works as described under the Second SCL Agreement;
- the Company's total liability to the Government under the First SCL Agreement and the Second SCL Agreement, except in respect of death or personal injury caused by the negligence of the Company, is limited to the aggregate fees that have been and will be received by the Company from the Government under the First SCL Agreement and the Second SCL Agreement;
- the Company will provide to Government by the end of each calendar month, a progress report on the activities under the Second SCL Agreement that were carried out in the immediately preceding calendar month and, within three months following the completion of the relevant works, a final report on the activities required to be carried out under the Second SCL Agreement;
- the Company shall be responsible for the care of all works constructed under the Shatin to Central Link project from the commencement of construction until the date of handover of those works to the Government and for completing or procuring the completion of any outstanding works and/or defective works identified prior to the handover of the works;
- during the period of twelve years following the issue of a certificate of completion by the Company in respect of work carried out under any contract with any third party, the Company shall be responsible for the repair of any defects in such work that are identified following the expiry of any defects liability period under the relevant contract;
- the Company warrants that:
 - in the case of those activities under the Second SCL Agreement that relate to the provision of project management services, such activities shall be carried out with the skill and care reasonably to be expected of a professional and competent project manager;
 - in the case of those activities under the Second SCL Agreement that relate to the provision of design services, such activities shall be carried out with the skill and care reasonably to be expected of a professional and competent design engineer; and
 - in the case of those activities under the Second SCL Agreement that relate to the carrying out of construction activities, such activities shall be carried

out with the skill and care reasonably to be expected of, and by utilising such plant, goods and materials reasonably to be expected from, a competent and workmanlike construction contractor; and

- the Government further undertakes to use reasonable endeavours to provide the Company with assistance of a non-financial nature, including taking all reasonable steps to procure that all necessary licences and consents, required in connection with the design, construction and operation of the Shatin to Central Link are given or granted.

B1 Entrustment Agreement for Design and Site Investigation in Relation to the Express Rail Link (Hong Kong Section of the Guangzhou-Shenzhen-Hong Kong Express Rail Link)

The Entrustment Agreement for Design and Site Investigation in Relation to the Express Rail Link (the "First XRL Agreement") was entered into on 24 November 2008 between the Company and the Secretary for Transport and Housing for and on behalf of the Government.

The First XRL Agreement contains provisions for the design of and site investigation and procurement activities in relation to the proposed Express Rail Link, including in relation to:

- the Government's obligation to pay the Company, up to a maximum aggregate amount of HK\$1,500 million, in respect of certain costs incurred by the Company pursuant to the First XRL Agreement, including the Company's in-house design costs and certain on-costs, preliminary costs and recruited staff costs;
- the Government's obligation to bear and finance the total cost of the design and site investigation activities under the First XRL Agreement (subject to the limit noted above in respect of payments to the Company) and arrangements for the payment of these costs directly by the Government;
- the Company's obligation to carry out or procure the carrying out of the design and site investigation activities in relation to the proposed Express Rail Link;
- the limitation of the Company's liability to the Government under the First XRL Agreement, except in respect of death or personal injury caused by the negligence of the Company, to HK\$700 million; and
- should the railway scheme for the Express Rail Link be authorised under the Railways Ordinance (Cap. 519 of the Laws of Hong Kong), the execution of a further agreement by the Government and the Company setting out each of their rights, obligations, duties and powers with respect to the financing, construction, completion, testing, commissioning and putting into service the works necessary for the construction and operation of the Express Rail Link.

B2 Entrustment Agreement for Construction, Testing and Commissioning of the Express Rail Link

The Entrustment Agreement for the construction and commissioning of the Express Rail Link was entered into on 26 January 2010 between the Company and the Secretary for Transport and Housing for and on behalf of the Government (the "Second XRL Agreement").

The scheme in respect of the Express Rail Link was first gazetted under the Railways Ordinance (Cap. 519 of the Laws of Hong Kong) on 28 November 2008, with amendments and corrections gazetted on 30 April 2009. The scheme, as amended with such minor modifications as deemed necessary, was authorised by the Chief Executive in Council on 20 October 2009 and funding support approved by the Finance Committee on 16 January 2010.

The Second XRL Agreement contains the following provisions:

- in consideration of the Company executing or procuring the execution of certain entrustment activities as set out in the Second XRL Agreement and carrying out its other obligations under the Second XRL Agreement and the First XRL Agreement, the Government shall pay to the Company HK\$4,590 million, to be paid in cash quarterly in advance on a scheduled basis as such sum may be varied in accordance with the Second XRL Agreement, subject to the maximum payment limits stated in the Second XRL Agreement (being HK\$2,000 million annually and HK\$10,000 million in total) (the "Maximum Payment Limits");
- the Company and the Government may agree that the Company will carry out (or procure the carrying out of) certain additional works for the Government (such agreed additional works being "miscellaneous works"). Miscellaneous works (if any) are to be carried out by the Company in the same manner as if they had formed part of the activities specified to be carried out under the Second XRL Agreement and in consideration of the Company executing or procuring the execution of the miscellaneous works (if any) and carrying out its other obligations under the Second XRL Agreement in relation to the miscellaneous works (if any), the Government shall pay to the Company an amount equal to an agreed fixed percentage of third party costs attributable to the miscellaneous works from time to time subject to the Maximum Payment Limits;
- the Company will provide to the Government by the end of each calendar month, a progress report on the activities under the Second XRL Agreement that were carried out in the immediately preceding calendar month and, within three months following the earlier of handover of the Express Rail Link project to the Government or termination of the Second XRL Agreement, a final report on the activities required to be carried out under the Second XRL Agreement;

REPORT OF THE MEMBERS OF THE BOARD

- the Company shall be responsible for the care of all works constructed under the Express Rail Link project from the commencement of construction until the date of handover of those works to the Government (or to a third party directed by the Government) and for completing or procuring the completion of any outstanding works and/or defective works identified prior to the handover of the works;
- during the period of twelve years following the issue of a certificate of completion by the Company in respect of work carried out under any contract with any third party, the Company shall be responsible for the repair of any defects in such work that are identified following the expiry of any defects liability period under the relevant contract;
- the Company warrants that:
 - in the case of those activities under the Second XRL Agreement that relate to the provision of project management services, such activities shall be carried out with the skill and care reasonably to be expected of a professional and competent project manager;
 - in the case of those activities under the Second XRL Agreement that relate to the provision of design services, such activities shall be carried out with the skill and care reasonably to be expected of a professional and competent design engineer; and
 - in the case of those activities under the Second XRL Agreement that relate to the carrying out of construction activities, such activities shall be carried out with the skill and care reasonably to be expected of, and by utilising such plant, goods and materials reasonably to be expected from, a competent and workmanlike construction contractor;
- the Government is required to bear (i) any costs payable to third parties, (ii) any charges, costs or amounts payable to any Government department, bureau, agency or body in relation to the activities to be carried out under the Second XRL Agreement, (iii) any and all amounts payable to KCRC as compensation for damage arising as a result of the Company and/or a third party contractor carrying out activities under the Second XRL Agreement; and (iv) all land acquisition, clearance and related costs (including all amounts arising as a result of any claim for compensation by any third party) and those costs which are incurred by the Lands Department in connection with the Express Rail Link project; and

- the Government further undertakes to use reasonable endeavours to provide the Company with assistance of a non-financial nature, including taking all reasonable steps to procure that all necessary licences and consents, required in connection with the design, construction and operation of the Express Rail Link are given or granted.

The Government has agreed that the Company has been asked to proceed with the construction, testing and commissioning of the Express Rail Link (pursuant to and on the terms of the Second XRL Agreement) on the understanding that the Company will be invited to undertake the operation of the Express Rail Link under the concession approach.

The Second XRL Agreement remains in full force and effect until the completion of the activities set out in the Second XRL Agreement or until terminated earlier in accordance with the terms of the Second XRL Agreement. The Company expects that the substantial majority of the activities to be carried out under the Second XRL Agreement will be complete by the time of the projected handover of the completed Express Rail Link in mid-2015. However certain activities involve the provision of specified administrative services to the Government, the Company expects to provide these services for a number of years following the completion of the Express Rail Link project. Notwithstanding this, certain provisions will remain in force following completion of the activities set out in the Second XRL Agreement, for example, provisions regarding confidentiality and dispute resolution.

C Renewal of the existing Maintenance Agreement for the Automated People Mover System at the Hong Kong International Airport

The Company has had entered into a Maintenance Agreement with the AA for the maintenance of the Automated People Mover system at the Hong Kong International Airport since 2002. It was signed on 18 March 2002 for a period of three years, which expired on 6 July 2005. A Supplemental Agreement was agreed with the AA, and approved by the Board in June 2005, to extend the Maintenance Agreement for another three years until 6 July 2008, which also included options for the Automated People Mover serving the Sky Plaza and Sky Pier terminal buildings.

On 21 August 2008, the Company entered into a new Maintenance Agreement with the AA, for the renewal of the then expired Maintenance Agreement for the Automated People Mover system for a five year period (the "New Maintenance Agreement"), effective from 6 July 2008. It is expected that the highest amount per year receivable from the AA under the New Maintenance Agreement will be HK\$37 million.

The New Maintenance Agreement contains provisions relating to the operation and maintenance by the Company of the automated people mover system installed at Hong Kong International Airport (the "System") and the carrying out by

the Company of certain specified services in respect of the System, they including the following:

- provisions stating that the duration of the New Maintenance Agreement shall be five years from 6 July 2008 up to and including 5 July 2013;
- provisions relating to the performance of scheduled maintenance works and overhaul of the System by the Company;
- provisions relating to monitoring the System for any breakdown and the Company providing repair services where necessary;
- provisions relating to the standards to which the Company must operate the System; and
- provisions relating to the carrying out by the Company (as additional services), in certain circumstances, of upgrade work on the System.

D Project Agreement for the Financing, Design, Construction and Operation of the West Island Line

The Project Agreement for the Financing, Design, Construction and Operation of the West Island Line (the "WIL Project Agreement") was entered into on 13 July 2009 between the Company and the Secretary for Transport and Housing for and on behalf of the Government.

The WIL Project Agreement contains provisions for the financing of and the carrying out, or procuring the carrying out, of the design, construction, completion, testing and commissioning by the Company of the railway works required in order to bring the West Island Line into operation in accordance with the MTR Ordinance, the Operating Agreement between the Company and the Secretary for Transport and Housing for and on behalf of the Government dated 9 August 2007 and the WIL Project Agreement. The West Island Line will be owned, operated and maintained by the Company for its own account for the period of the Company's railway franchise. The WIL Project Agreement includes provisions in relation to:

- payment by the Government of HK\$12,252 million to the Company in consideration of the Company's obligations under the WIL Project Agreement, such sum constituting funding support from the Government for the Company to implement the West Island Line project;
- within 24 months of commercial operations commencing on the West Island Line on a revenue earning basis and providing scheduled transport for the public, payment by the Company to the Government of any "Repayment Amounts" for any over-estimation of certain capital expenditure, price escalation costs, land costs and the amount of contingency in relation to the railway works and reprovisioning, remedial and improvement works (together with interest);

- the design, construction and completion of the associated reprovisioning, remedial and improvement works (the cost of which shall be the responsibility of the Company) and the associated essential public infrastructure works (the cost of which shall be the responsibility of the Government);
- the Company's responsibility for costs relating to land acquisition, clearance and related costs arising from the implementation of the West Island Line project (save for costs arising from certain claims for compensation by third parties) and all costs, expenses and other amounts incurred or paid by the Lands Department pursuant to the involvement of the Lands Department in connection with the implementation of the West Island Line project; and
- the Company carrying out measures specified in the environmental impact assessment and the environmental permit issued by the Government to the Company in relation to the West Island Line on 12 January 2009.

The construction of the West Island Line is scheduled to take place between the date of the WIL Project Agreement and 2014.

In relation to the First SCL Agreement, the Second SCL Agreement, the First XRL Agreement, the Second XRL Agreement, the New Maintenance Agreement and the WIL Project Agreement (together the "Non Merger-related Continuing Connected Transactions") and in accordance with paragraph B(I)(iii)(a) of the Waiver, the Company confirms that the Independent Non-executive Directors of the Company have reviewed each of the Non Merger-related Continuing Connected Transactions and confirmed that the Non Merger-related Continuing Connected Transactions were entered into:

- (1) in the ordinary and usual course of business of the Company;
- (2) on normal commercial terms or on terms which are no less favourable to the Company than terms available to or from independent third parties; and
- (3) in accordance with the relevant agreement governing them on terms that are fair and reasonable and in the interests of the shareholders of the Company as a whole.

The Company has engaged the auditors of the Company to carry out a review of each of the Non Merger-related Continuing Connected Transactions in accordance with Hong Kong Standard on Assurance Engagements 3000 "Assurance Engagements Other Than Audits or Reviews of Historical Financial Information" and with reference to Practice Note 740 "Auditor's Letter on Continuing Connected Transactions under the Hong Kong Listing Rules" issued by the Hong Kong Institute of Certified Public Accountants. In accordance with paragraph B(I)(iii)(b) of the Waiver, the auditors have provided a letter to the Board confirming that:

REPORT OF THE MEMBERS OF THE BOARD

- (a) nothing has come to their attention that causes them to believe that the Non Merger-related Continuing Connected Transactions have not been approved by the Board; and
- (b) nothing has come to their attention that causes them to believe that the Non Merger-related Continuing Connected Transactions were not entered into, in all material respects, in accordance with the relevant agreements governing such transactions.

III Non Merger-related Continuing Connected Transactions with parties other than Government and/or its Associates

The following disclosures are made in accordance with Rule 14A.46 of the Listing Rules.

A Pre-Existing UGL Contract and Pre-Existing Supplemental UGL Contract for the provision of maintenance and other services for certain trains

Metro Trains Melbourne Pty Ltd ("MTM") is a joint venture company incorporated in Australia. The Company controls 60% of the voting power at any general meeting of MTM and each of UGL and John Holland controls 20% of the voting power at any general meeting of MTM. Accordingly, subsequent to the Company entering into the Pre-Existing UGL Contract as amended by the Pre-Existing Supplemental UGL Contract (each, as defined below), UGL is treated as a substantial shareholder of MTM (a subsidiary of the Company) and therefore a "connected person" of the Company within the meaning of Chapter 14A of the Listing Rules. The Pre-Existing UGL Contract (as amended by the Pre-Existing Supplemental UGL Contract) is therefore a "continuing connected transaction" within the meaning of Rule 14A.14 of the Listing Rules.

On 11 January 2002, the Company entered into a contract with UGL for the provision of maintenance and other services in respect of trains at certain depots for a period of seven years commencing on or around 1 October 2002 to 30 September 2009 (the "Pre-Existing UGL Contract"). The commencement date was subsequently advanced by three months. On 14 April 2009, the Company entered into a supplemental agreement with UGL for the extension of the Pre-Existing UGL Contract for a further period of seven years from 1 August 2009 and for the transfer of the provision of certain services to the Kowloon depot (the "Pre-Existing Supplemental UGL Contract").

The Pre-Existing UGL Contract (as amended by the Pre-Existing Supplemental UGL Contract) provides for the provision of maintenance and other services by UGL in respect of 15 G/H stock trains used by the Company on the Kwun Tong Line, the Island Line, the Tsuen Wan Line and the Tseung Kwan O Line, in each case at the Tseung Kwan O depot and the Kowloon depot, including provisions in relation to:

- payment by the Company of a total sum of approximately HK\$171,966,450 to UGL (including for variations and additional works) in consideration of UGL providing certain services between 1 August 2002 and 31 July 2009 and payment by the Company of HK\$152,940,000 to UGL for the extended term of seven years pursuant to the Pre-Existing Supplemental UGL Contract (which amount is to be paid on a scheduled basis), subject to certain adjustments, including for the level of performance by the relevant trains;
- indemnification by UGL of the Company against certain losses and expenses sustained by the Company arising out of or in connection with UGL carrying out its obligations under the Pre-Existing UGL Contract (as amended by the Pre-Existing Supplemental UGL Contract);
- maintenance by UGL of insurance in relation to certain liabilities to the Company;
- the Company effecting and maintaining third party insurance covering the legal liability of both UGL and the Company for accidental death or injury to persons or accidental loss of or damage to property, in each case, arising out of the UGL's obligations under the Pre-Existing UGL Contract (as amended by the Pre-Existing Supplemental UGL Contract); and
- the Company maintaining "Contractors All Risks" insurance covering loss or damage to certain goods, equipment and temporary buildings at the Tseung Kwan O depot and the Kowloon depot.

The terms of the Pre-existing UGL Contract were agreed upon subsequent to a tender process that invited submissions from a number of contractors, including UGL. UGL was selected by the Company in accordance with the Company's established procedures for the assessment of tenders.

The Company regularly outsources certain services to third parties that specialise in the type of work outsourced, thereby improving the efficiency of the Company's operations and allowing the Company to concentrate its resources on its core business areas. UGL is a specialist in the provision of construction, refurbishment and maintenance services to the railway industry.

B Supplemental Agreement for the extension of the Original Contract for the Mid-Life Refurbishment of Phase 1 Light Rail Vehicles

The Supplemental Agreement for the extension of the Original Contract (defined below) for the Mid-Life Refurbishment of Phase 1 Light Rail Vehicles ("Phase 1 LRVs"), was entered into on 26 February 2010 between the Company and UGL (the "Supplemental Agreement").

On 30 November 2007, KCRC entered into the Original Contract with UGL (the "Original Contract"), for the refurbishment of the Phase 1 LRVs for a period of 45 months from 30 November 2007 to 31 August 2011. On 2 December 2007, the rights and obligations of KCRC under the Original Contract were vested in the Company pursuant to section 52(B) of the MTR Ordinance. The Supplemental Agreement extends the Original Contract for a further period of 16 months from 31 August 2011 until 31 December 2012. The Original Contract (as amended and supplemented by the Supplemental Agreement) is in substantially the same form as KCRC's standard conditions of contract for engineering works and contains the following provisions:

- in consideration of UGL providing the Refurbishment Works (defined below) under the Original Contract, the Company is obliged to pay UGL a total sum of approximately HK\$48,260,000 (excluding amounts for variations and additional works). The Supplemental Agreement, inter alia, extended the scope of the Refurbishment Works of the Original Contract and the consideration payable by the Company to UGL for such extension is HK\$83,736,143, as adjusted by an additional HK\$14,435,327 (the "Contract Sum"). The total sum under the Original Contract plus the Contract Sum is to be paid progressively based on materials delivered and on works completed as set out in the Supplemental Agreement, subject to adjustments to take account of variations made by the Company's Chief Electrical and Mechanical Engineer (the "Engineer") to the scope of the Refurbishment Works. The maximum aggregate amount payable annually by the Company under the Original Contract plus the Contract Sum is approximately HK\$78,632,000;
- the Company is obliged to effect "Contractor's All Risks" and "Third Party Liability" insurance with a third party liability limit of not less than HK\$30 million;
- UGL shall carry out a carbody structure review to assess the mechanical condition of the Phase 1 LRVs; refurbish the drivers' consoles, the operators' seats and the passenger saloons of the Phase 1 LRVs; conduct a brake software upgrade of the Phase 1 LRVs; and carry out further miscellaneous repairs to the Phase 1 LRVs (together the "Refurbishment Works");
- UGL shall indemnify the Company against any certain losses or expenses which may arise out of or in connection with the Refurbishment Works, subject to any proportionate reduction in liability on account of any related negligence by the Company, its employees or agents, the Engineer or those appointed by the Engineer;
- UGL shall indemnify the Company against certain damages, compensation, costs and expenses in respect of any damages or compensation payable at law in respect of or in consequence of any accident, injury or illness to any person in the employment of UGL arising out of and in the course of such employment;
- UGL shall effect and maintain insurance with a limit of not less than HK\$100 million in relation to certain of its liabilities for the period commencing on 30 November 2007 until the date of the completion of the Refurbishment Works;
- UGL's liability to indemnify the Company is reduced proportionally to the extent that any act or omission of the Company, its employees or agents, the Engineer or those appointed by the Engineer, caused or contributed to the relevant death, illness, injury, loss or damage and the total liability of UGL shall not exceed 100% of the total sum payable under the Original Contract, save and except for UGL's liability for death, personal injury, wilful misconduct, fraud and infringement of third party intellectual property rights; and
- the total liability of UGL to the Company for liquidated damages arising as a result of delay is limited to 10% of the total sum payable under the Original Contract and, subject to the provisions regarding liquidated damages, UGL is not liable for any kind of economic, financial, indirect or consequential loss or damage, including but not limited to loss of profit, loss of use, loss of production, loss of any contract and the like, suffered by the Company.

Pursuant to the Original Contract, a bank guarantee issued by HSBC Bank Australia Limited has been provided to the Company in respect of the obligations of UGL under the Original Contract.

If UGL fails to complete the Refurbishment Works within the contract period, the Engineer may terminate the contract by notice in writing to UGL.

C Contract 903 between the Company and LCAL relating to certain works on the South Island Line (East)

As mentioned above, MTM is a joint venture company incorporated in Australia. MTM is a non-wholly owned subsidiary of the Company and each of UGL and John Holland controls 20% of the voting power at any general meeting of MTM.

Accordingly, John Holland is treated as a substantial shareholder of MTM. John Holland, JHL and LCAL are indirect wholly-owned subsidiaries of Leighton Holdings Limited. On this basis, JHL and LCAL are both associates of John Holland under the Listing Rules. Therefore, each of John Holland, JHL and LCAL is a "connected person" of the Company within the meaning of Chapter 14A of the Listing Rules. Contract 903 (as defined below) is therefore a "continuing connected transaction" within the meaning of Rule 14A.14 of the Listing Rules.

REPORT OF THE MEMBERS OF THE BOARD

On 17 May 2011, the Company and LCAL entered into Contract 903 ("Contract 903") for the construction of certain works relating to the Aberdeen Channel Bridge, Wong Chuk Hang Station and Ocean Park Station in respect of the South Island Line (East) (the "Contract 903 Works").

Contract 903 is in substantially the same form as the Company's standard conditions of contract for engineering works and contains the following provisions:

- the principal obligation of LCAL under Contract 903 is the construction of the Contract 903 Works;
- LCAL shall indemnify the Company against any loss or expense sustained by the Company and against all losses and claims in respect of death or injuries or damage to any person or property whatsoever which may arise out of or in consequence of the execution of the Contract 903 Works and against all claims, proceedings, damages, costs, charges and expenses whatsoever in respect of or in relation thereto, except for compensation or damages related to the permanent use or occupation of land by the Contract 903 Works, or the right of the Company to execute the Contract 903 Works on any part of the land, or on account of any negligence by the Company, its agents, servants or other contractors, not being employed by LCAL;
- LCAL shall indemnify the Company against all damages and compensation and against all claims, demands, proceedings, costs, charges and expenses whatsoever in respect of any damages or compensation payable at law in respect of or in consequence of any accident, injury or illness to any workman or other person in the employment of LCAL or its sub-contractors or suppliers arising out of and in the course of such employment;
- LCAL shall effect and maintain insurance with a limit of not less than HK\$200 million in relation to certain of its liabilities for the period commencing on 29 April 2011 until 30 June 2016;
- a bond issued by Chartis Insurance Hong Kong Limited will be provided to the Company in respect of the obligations of LCAL under Contract 903;
- LCAL's liability to indemnify the Company is reduced proportionally to the extent that any act or neglect of the Company, the Engineer or any other person employed by the Company in connection with the Contract 903 Works, their respective agents, employees or representatives, may have contributed to the relevant death, illness, or damage. The total liability of LCAL to the Company for all damages (liquidated damages and general) for delay shall not exceed 10% of the target cost plus fees as calculated under Contract 903;

- the total amount payable by the Company to LCAL under Contract 903 is HK\$2,513,394,379, which includes the target cost for the Contract 903 Works and fees to LCAL. From time to time the scope of the Contract 903 Works may vary and the Company will be obliged to revise the fees payable to LCAL in accordance with the terms of the Contract;
- the Company is obliged to pay the target cost for the Contract 903 Works to LCAL on a scheduled basis set out in Contract 903. If the final total cost of the Contract 903 Works exceeds or is less than the target cost for the Works, the deficit or, as the case may be, the excess will be borne by or, as the case may be, distributed to the Company and LCAL on a basis calculated in accordance with Contract 903;
- the maximum aggregate amount payable annually by the Company under Contract 903 is approximately HK\$1,400 million. As payments by the Company to LCAL are paid on a scheduled basis as set out in Contract 903, the maximum aggregate annual amount is set by reference to the highest amount payable by the Company in any given year under such schedule;
- the Company is obliged to effect "Contractor's All Risks" and "Third Party Liability" insurance with a third party liability limit of not less than HK\$700 million; and
- the Company may at any time, by giving 30 days' notice in writing to LCAL, terminate Contract 903 but without prejudice to any claims by the Company for breach of contract.

D Contract 904 between the Company, LCAL and JHL relating to certain works on the South Island Line (East)

On 17 May 2011, the Company, LCAL and JHL (LCAL and JHL being "the Contractors") entered into Contract 904 ("Contract 904") for the construction of certain works relating to Lei Tung Station and South Horizons Station in respect of the South Island Line (East) (the "Contract 904 Works").

As explained above, as the Contractors are "connected persons" under the Listing Rules, Contract 904 is a "continuing connected transaction" within the meaning of Rule 14A.14 of the Listing Rules.

Contract 904 is in substantially the same form as the Company's standard conditions of contract for engineering works and contains the following provisions:

- the principal obligation of the Contractors is the construction of the Contract 904 Works. The obligations of the Contractors under Contract 904 are joint and several;

- the Contractors shall indemnify the Company against any loss or expense sustained by the Company and against all losses and claims in respect of death or injuries or damage to any person or property whatsoever which may arise out of or in consequence of the execution of the Contract 904 Works and against all claims, proceedings, damages, costs, charges and expenses whatsoever in respect of or in relation thereto, except for compensation or damages related to the permanent use or occupation of land by the Contract 904 Works, or the right of the Company to execute the Contract 904 Works on any part of the land, or on account of any negligence by the Company, its agents, servants or other contractors, not being employed by the Contractors;
 - the Contractors shall indemnify the Company against all damages and compensation and against all claims, demands, proceedings, costs, charges and expenses whatsoever in respect of any damages or compensation payable at law in respect of or in consequence of any accident, injury or illness to any workman or other person in the employment of the Contractors or their subcontractors or suppliers arising out of and in the course of such employment;
 - the Contractors shall effect and maintain insurance with a limit of not less than HK\$200 million in relation to certain of its liabilities for the period commencing on 29 April 2011 until 30 June 2016;
 - a bond issued by Chartis Insurance Hong Kong Limited will be provided to the Company in respect of the obligations of the Contractors under Contract 904;
 - the Contractors' liability to indemnify the Company is reduced proportionally to the extent that any act or neglect of the Company, the Engineer or any other person employed by the Company in connection with the Contract 904 Works, their respective agents, employees or representatives, may have contributed to the relevant death, illness, or damage;
 - the total liability of the Contractors to the Company for all damages (liquidated damages and general) for delay shall not exceed 10% of the contract sum under the Contract (the contract sum being HK\$1,755,018,490);
 - the total amount payable by the Company to the Contractors under Contract 904 is the Contract Sum. From time to time the scope of Works may vary and the Company will be obliged to revise the Contract Sum in accordance with the terms of Contract 904;
 - the maximum aggregate amount payable annually by the Company under Contract 904 is approximately HK\$1,400 million. As payments by the Company to the Contractors are paid on a scheduled basis as set out in Contract 904, the maximum aggregate annual amount is set by reference to the highest amount payable by the Company in any given year under such schedule;
 - the Company is obliged to effect "Contractor's All Risks" and "Third Party Liability" insurance with a third party liability limit of not less than HK\$700 million. In addition, the Contractors have agreed to separately purchase additional cover for "Third Party Liability" insurance in the amount of AU\$485 million; and
 - the Company may at any time, by giving 30 days' notice in writing to the Contractors, terminate Contract 904 but without prejudice to any claims by the Company for breach of contract.
- In relation to the Pre-Existing UGL Contract as amended by the Pre-Existing Supplemental UGL Contract, the Original Contract (as amended), Contract 903 and Contract 904 (together the "Continuing Connected Transactions with Parties other than Government and/or its Associates") and in accordance with Rule 14A.37 of the Listing Rules, the Company confirms that the Independent Non-executive Directors of the Company have reviewed the Continuing Connected Transactions with Parties other than Government and/or its Associates and confirmed that each of the Continuing Connected Transactions with Parties other than Government and/or its Associates was entered into:
- (1) in the ordinary and usual course of business of the Company;
 - (2) on normal commercial terms or on terms which are no less favourable to the Company than terms available to or from independent third parties; and
 - (3) in accordance with the relevant agreement governing them on terms that are fair and reasonable and in the interests of the shareholders of the Company as a whole.
- The Company has engaged the auditors of the Company to carry out a review of the Continuing Connected Transactions with Parties other than Government and/or its Associates in accordance with Hong Kong Standard on Assurance Engagements 3000 "Assurance Engagements Other Than Audits or Reviews of Historical Financial Information" and with reference to Practice Note 740 "Auditor's Letter on Continuing Connected Transactions under the Hong Kong Listing Rules" issued by the Hong Kong Institute of Certified Public Accountants. In accordance with Rule 14A.38 of the Listing Rules, the auditors have provided a letter to the Board confirming that:

REPORT OF THE MEMBERS OF THE BOARD

- (a) nothing has come to their attention that causes them to believe that the Continuing Connected Transactions with Parties other than Government and/or its Associates have not been approved by the Board;
- (b) for transactions involving the provision of goods or services by the Group, nothing has come to their attention that causes them to believe that the Continuing Connected Transactions with Parties other than Government and/or its Associates were not, in all material respects, in accordance with the pricing policies of the Group;
- (c) nothing has come to their attention that causes them to believe that the Continuing Connected Transactions with Parties other than Government and/or its Associates were not entered into, in all material respects, in accordance with the relevant agreements governing such transactions; and
- (d) with respect to the aggregate amount of each of the Continuing Connected Transactions with Parties other than Government and/or its Associates, nothing has come to their attention that causes them to believe that the Continuing Connected Transactions with Parties other than Government and/or its Associates have exceeded the maximum aggregate annual value disclosed in the previous announcements dated 1 September 2009, 26 February 2010, 18 May 2011 and 18 May 2011 made by the Company in respect of each of the Continuing Connected Transactions with Parties other than Government and/or its Associates.

Additional Information in respect of the Rail Merger

The Rail Merger consisted of a number of separate agreements, each of which was detailed in the circular issued by the Company on 3 September 2007 in connection with the Rail Merger, and which together formed a complete package deal which was approved by the independent shareholders of the Company at an Extraordinary General Meeting held on 9 October 2007. The information set out at paragraph A below describes the payment framework adopted in respect of the Rail Merger and paragraphs B to H below set out, summaries of the various agreements entered into by the Company in respect of the Rail Merger in addition to those agreements disclosed above under the heading "Merger-related Continuing Connected Transactions".

A Payments in connection with Merger-related Agreements

In connection with the Rail Merger, the following initial payments were made by the Company to KCRC on 2 December 2007 (being the Merger Date):

- an upfront payment of HK\$4.25 billion, payable under the Service Concession Agreement (as described in paragraph B below), being the upfront fee for the right to operate the Service Concession (as defined in paragraph B below) and the consideration for the purchased rail assets; and

- an upfront payment of HK\$7.79 billion payable under the Merger Framework Agreement (as described on page 130) in consideration for the execution of the Property Package Agreements (as described on pages 131 to 133 and in paragraph E below) and the sale of the shares in the KCRC Subsidiaries (as defined on page 131) that were transferred to the Company under the Sale and Purchase Agreement which was entered into on 9 August 2007 between the Company and KCRC.

In addition to the initial payments above, the Company is also required to make the following payments to KCRC going forward:

- fixed annual payments of HK\$750 million payable under the Service Concession Agreement, for the right to use and operate the concession property for the operation of the service concession, in arrears on the day immediately preceding each anniversary of the Merger Date which falls during the concession period in respect of the 12 month period up to and including the date on which such payment falls due; and
- variable annual payments payable under the Service Concession Agreement, for the right to use and operate the concession property for the operation of the service concession, in each case, calculated on a tiered basis by reference to the amount of revenue from the KCRC system (as determined in accordance with the Service Concession Agreement) for each financial year of the Company. No variable annual payment is payable in respect of the first 36 months following the Merger Date.

As a complete package deal, other than the payment elements described above and unless stated otherwise in the relevant paragraph below, no specific allocation was made between the various elements of the Rail Merger.

B Service Concession Agreement

The Service Concession Agreement was entered into on 9 August 2007 between the Company and KCRC.

The Service Concession Agreement contains provisions in relation to the grant and operation of a service concession and licence granted by KCRC to the Company ("Service Concession"), including in relation to:

- the grant of the Service Concession to the Company to access, use and operate the concession property (other than KCRC railway land referred to immediately below) to certain specified standards;
- the grant of a licence to access and use certain KCRC railway land;

- the term (being an initial period of 50 years from the Merger Date) of the Service Concession and redelivery of the KCRC system upon expiry or termination of the concession period. The Service Concession will end if the Company's franchise relating to the KCRC railway is revoked;
- the payments of an upfront payment of HK\$4.25 billion and fixed annual payments and variable annual payments (as described in paragraph A above);
- KCRC remaining the legal and beneficial owner of the concession property as at the Merger Date and the Company being the legal and beneficial owner of certain future concession property ("Additional Concession Property");
- the regime for compensation payable by KCRC to the Company if Additional Concession Property is returned to KCRC at the end of the concession period;
- the rights and restrictions of the Company and KCRC in relation to the concession property; and
- subject to certain conditions, the Company bearing all risks, liabilities and/or costs whatsoever associated with or arising from the concession property and the land on which any of the concession property is located during the concession period.

C Sale and Purchase Agreement

The Sale and Purchase Agreement was entered into on 9 August 2007 between the Company and KCRC.

The Sale and Purchase Agreement provides the terms pursuant to which the Company acquired certain assets and contracts (the "Purchased Rail Assets") from KCRC.

The consideration for the sale of the Purchased Rail Assets (excluding the shares in the KCRC Subsidiaries) formed part of the upfront payment of HK\$4.25 billion. The consideration for the sale of the shares in the KCRC Subsidiaries (which own the Category 1A Properties referred to at paragraph E below and act as property managers) formed part of the payment of HK\$7.79 billion for the property package (as described in paragraph A above and in paragraph E below).

D Operating Agreement

The Operating Agreement was entered into on 9 August 2007 between the Company and the Secretary for Transport and Housing for and on behalf of the Government as contemplated in the MTR Ordinance.

The Operating Agreement is based on the previous Operating Agreement which was signed on 30 June 2000. The Operating Agreement differs from the previous Operating Agreement to provide for, amongst other things, the nature of the combined MTRC railway and KCRC railway. The Operating Agreement includes terms relating to:

- the extension of the Company's franchise under the MTR Ordinance;
- the design, construction and maintenance of the railway;
- passenger services,
- a framework for the award of new projects and the operation and ownership structure of new railways;
- the adjustment mechanism to be applied to certain of the Company's fares; and
- compensation which may be payable under the MTR Ordinance to the Company in relation to a suspension, expiry or termination of the franchise.

E Additional Property Package Agreements

Category 1A Properties

The Category 1A Properties are held by the KCRC Subsidiaries. Under the terms of the Sale and Purchase Agreement, the Company acquired from KCRC the shares in the KCRC Subsidiaries (and thereby indirectly acquired the "Category 1A Properties").

Category 1B Properties

On 9 August 2007, KCRC and the Company entered into an agreement for sale of purchase under which KCRC agreed to assign certain properties (the "Category 1B Properties") to the Company on the Merger Date. The relevant assignment was executed between KCRC and the Company on 2 December 2007.

Category 4 Properties

On 9 August 2007, the Government entered into an undertaking that it would, within periods to be agreed between the Company and the Government, offer to the Company a private treaty grant in respect of certain development sites ("Category 4 Properties"). The terms of each private treaty grant shall generally be determined by the Government, and the premium for each private treaty grant shall be assessed on a full market value basis ignoring the presence of the railway other than the Tin Shui Wai Terminus, Light Rail, Yuen Long, New Territories.

On 9 August 2007, the Company issued a letter to KCRC confirming that, if there should be any railway premises on the Category 4 Properties, the Company would assign the railway premises to KCRC.

REPORT OF THE MEMBERS OF THE BOARD

Metropolis Equity Sub-participation Agreement

The Metropolis Equity Sub-participation Agreement was entered into on 9 August 2007 between KCRC and the Company. KCRC is obliged to act on the Company's instructions, and pay to the Company any distributions, or proceeds of sale, relating to its shareholding in the property management company The Metropolis Management Company Limited ("Metropolis"). The issued share capital of Metropolis is 25,500 A shares (which are held by KCRC) and 24,500 B shares (which are held by Cheung Kong Property Management Limited). Metropolis' business is property management.

F Liaison Committee Letter

The Liaison Committee Letter was issued on 9 August 2007 by KCRC, the terms of which were acknowledged and agreed to by the Company and the Government.

The letter sets out the agreement between the parties regarding a "Liaison Committee" established for the purposes of governing certain matters of KCRC between 9 August 2007 and the Merger Date. Upon the completion of the Rail Merger, the Liaison Committee was dissolved.

G Outsourcing Agreement

An Outsourcing Agreement was entered into on 9 August 2007 between the Company and KCRC. For the period from 2 December 2007 to 2 December 2009 (subsequently extended to 31 December 2009), KCRC, pursuant to the terms of the Outsourcing Agreement, outsourced certain financial and administrative functions to the Company for an annual fee of not more than HK\$20 million from KCRC. On 6 November 2009, a new Outsourcing Agreement was entered into for the period from 2 December 2009 to 1 December 2011.

H KSL Project Management Agreement

The KSL Project Management Agreement was entered into between the Company and KCRC on 9 August 2007.

Pursuant to the terms of the KSL Project Management Agreement (as amended), the Company was appointed, inter alia, to manage the performance of KCRC's principal obligations to the Government in relation to the design and construction of the Kowloon Southern Link (other than obligations relating to payment).

In return for the performance of these services under the KSL Project Management Agreement (as amended), the Company has received a project management fee of approximately HK\$710.8 million. In addition, given that the final outturn cost of the KSL was under budget, the Company received an incentive payment (calculated with reference to the amount by which the final outturn cost of the project was under budget) of HK\$110 million.

I Application of Merger-related Waiver

In relation to the Operating Agreement and the Service Concession Agreement, pursuant to paragraph A of the Merger-related Waiver, the Stock Exchange granted a waiver to the Company from strict compliance with all the continuing connected transaction requirements of Chapter 14A of the Listing Rules.

AUDITORS

The retiring auditors, KPMG, have signified their willingness to continue in office. A resolution will be proposed at the Annual General Meeting to reappoint them and to authorise the Directors to fix their remuneration.

By order of the Board

Gillian Elizabeth Meller
Secretary to the Board
Hong Kong, 8 March 2012