NOTES TO THE ACCOUNTS

1 Statement of Compliance

These accounts have been prepared in compliance with the Hong Kong Companies Ordinance and the applicable disclosure provisions of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules"). These accounts have also been prepared in accordance with all applicable Hong Kong Financial Reporting Standards ("HKFRSs"), which collective term includes all applicable individual Hong Kong Financial Reporting Standards, Hong Kong Accounting Standards ("HKASs") and Interpretations issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA"), and accounting principles generally accepted in Hong Kong. The HKFRSs are fully converged with International Financial Reporting Standards in all material respects. A summary of the principal accounting policies adopted by the Group is set out in note 2.

The HKICPA has issued certain new and revised HKFRSs that are effective for accounting periods beginning on or after 1 January 2011. Changes in accounting policies resulting from the initial application of these developments to the extent that they are relevant to the Group for the current and prior accounting periods reflected in these accounts are disclosed in note 2A(iii).

2 Principal Accounting Policies

A Basis of Preparation of the Accounts

(i) The measurement basis used in the preparation of the accounts is the historical cost basis except that the following assets and liabilities are stated at their fair value as explained in the accounting policies set out below:

- investment properties (note 2F(i));
- self-occupied land and buildings (note 2F(ii));
- financial instruments classified as investments in securities other than those intended to be held to maturity (note 2M); and
- derivative financial instruments (note 2T).

(ii) The preparation of the accounts in conformity with HKFRSs requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets, liabilities, income and expenditure. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements and estimations about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Judgements made by management in the application of HKFRSs that have significant effect on the accounts and estimates are discussed in note 59.

(iii) The HKICPA has issued a number of amendments to HKFRSs and one new Interpretation that are first effective for the current accounting period of the Group. Of these, only HKAS 24 (revised 2009), *Related party disclosures*, is relevant to the Group's accounts.

HKAS 24 (revised 2009) introduces modified disclosure requirements for government-related entities. As a result, the Group has revised the disclosure on material related party transactions with the Hong Kong Special Administrative Region ("HKSAR") Government and entities related to the HKSAR Government for those transactions that are collectively but not individually significant (note 57). HKAS 24 (revised 2009) also revises the definition of a related party. The Group has re-assessed the identification of related parties and concluded that the revised definition does not have any impact on the Group's related party disclosures in the current and previous period.

The Group has not applied any new and revised standard or interpretation that is not yet effective for the current accounting period (note 60).

B Basis of Consolidation

The consolidated accounts include the accounts of the Company and its subsidiaries (together referred to as the "Group") and the Group's interest in non-controlled subsidiaries (note 2D) and associates (note 2E) made up to 31 December each year. The results of subsidiaries acquired or disposed of during the year are included in the consolidated profit and loss account from or to the date of their acquisition or disposal, as appropriate.

C Subsidiaries and Non-controlling Interests

A subsidiary in accordance with the Hong Kong Companies Ordinance is a company in which the Group, directly or indirectly, holds more than half of the issued share capital, or controls more than half of the voting power, or controls the composition of the board of directors. Subsidiaries are considered to be controlled if the Company has the power, directly or indirectly, to govern the financial and operating policies, so as to obtain benefits from their activities.

An investment in a subsidiary is consolidated into the consolidated accounts from the date that control commences until the date that control ceases. Intra-group balances and transactions, and any unrealised profits arising from intra-group transactions, are eliminated in full in preparing the consolidated accounts. Unrealised losses resulting from intra-group transactions are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

2 Principal Accounting Policies *(continued)*

C Subsidiaries and Non-controlling Interests *(continued)*

Non-controlling interests represent the equity in a subsidiary not attributable directly or indirectly to the Company, and in respect of which the Group has not agreed any additional terms with the holders of those interests which would result in the Group as a whole having a contractual obligation in respect of those interests that meets the definition of a financial liability. Non-controlling interests are presented in the consolidated balance sheet within equity, separately from equity attributable to equity shareholders of the Company. Non-controlling interests in the results of the Group are presented on the face of the consolidated profit and loss account and the consolidated statement of comprehensive income as an allocation of the total profit or loss and total comprehensive income for the year between non-controlling interests and the equity shareholders of the Company. Loans from holders of non-controlling interests and other contractual obligations towards these holders are presented as financial liabilities in the consolidated balance sheet depending on the nature of the liability.

Investments in subsidiaries are carried in the Company's balance sheet at cost less any impairment losses (note 2H(ii)).

D Non-controlled Subsidiaries

Non-controlled subsidiaries are not consolidated in the accounts as the Group does not have effective control over their Boards. The investments in non-controlled subsidiaries are accounted for in the consolidated accounts of the Company using the equity method and are initially recorded at cost and adjusted thereafter for the post acquisition change in the Group's share of their net assets. The consolidated profit and loss account reflects the Group's share of the results of those non-controlled subsidiaries for the year.

Unrealised profits and losses resulting from transactions between the Group and the non-controlled subsidiaries are eliminated to the extent of the Group's interest in those subsidiaries, except where unrealised losses provide evidence of an impairment of the asset transferred, in which case they are recognised immediately in the profit and loss account.

In the Company's balance sheet, its investments in non-controlled subsidiaries are stated at cost less impairment losses (note 2H(ii)).

E Associates and Jointly Controlled Entities

An associate is an entity over which the Group or the Company has significant influence, but not control or joint control, over its management, including participation in the financial and operating policy decisions.

A jointly controlled entity is an entity which operates under a contractual arrangement between the Group or the Company and other parties, where the contractual arrangement establishes that the Group or the Company and one or more of the other parties share joint control over the economic activity of the entity.

An investment in an associate or a jointly controlled entity is accounted for in the consolidated accounts of the Company using the equity method and is initially recorded at cost and adjusted thereafter for the post acquisition change in the Group's share of the investees' net assets. The Group's share of the post-acquisition results of the investees for the year is recognised in the consolidated profit and loss account, whereas the Group's share of the post-acquisition items of the investees' other comprehensive income is recognised in the consolidated statement of comprehensive income.

When the Group's share of losses equals or exceeds its interest in the associate or the jointly controlled entity, the Group's interest is reduced to nil and recognition of further losses is discontinued except to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of the investee. For this purpose, the Group's interest in the investee is the carrying amount of the investment under the equity method together with the Group's long-term interests that in substance form part of the Group's net investment in the associate or the jointly controlled entity.

Unrealised profits and losses resulting from transactions between the Group and its associates and jointly controlled entities are eliminated to the extent of the Group's interest in the investee, except where unrealised losses provide evidence of an impairment of the asset transferred, in which case they are recognised immediately in the profit and loss account.

In the Company's balance sheet, investments in associates and jointly controlled entities are stated at cost less impairment losses (note 2H(ii)).

F Fixed Assets

(i) Investment properties are land and/or buildings which are owned or held under a leasehold interest to earn rental income and/or for capital appreciation. These include property that is being constructed or developed for future use as investment property.

Investment properties are stated on the balance sheet at fair value as determined semi-annually by independent professionally qualified valuers. Gains or losses arising from changes in the fair value are recognised in the consolidated profit and loss account in the year in which they arise.

(ii) Leasehold land registered and located in the HKSAR is accounted for as being held under a finance lease and is stated at cost less accumulated depreciation and impairment losses (note 2H(ii)). Land held for own use under operating leases and buildings thereon, where the fair value of the leasehold interest in the land and buildings cannot be measured separately at inception of the lease are accounted for as being held under a finance lease, unless the buildings are also clearly held under an operating lease. For these purposes, inception of the lease is the time that the lease was first entered into by the Group, or taken over from the previous lessee, or at the date of construction of those buildings, if later. The self-occupied land and buildings are stated on the balance sheet at their fair value on the basis of their existing use at the date of revaluation less any subsequent accumulated depreciation. Revaluations are performed by independent qualified valuers semi-annually, with changes in the fair value arising on revaluations recorded as movements in the fixed assets revaluation reserve, except:

2 Principal Accounting Policies *(continued)*

F Fixed Assets *(continued)*

(a) where the balance of the fixed assets revaluation reserve relating to a self-occupied land and building is insufficient to cover a revaluation deficit of that property, the excess of the deficit is charged to the profit and loss account; and

(b) where a revaluation deficit had previously been charged to the profit and loss account and a revaluation surplus subsequently arises, this surplus is firstly credited to the profit and loss account to the extent of the deficit previously charged to the profit and loss account, and thereafter taken to the fixed assets revaluation reserve.

(iii) Civil works and plant and equipment are stated at cost less accumulated depreciation and impairment losses (note 2H(ii)).

(iv) Assets under construction are stated at cost less impairment losses (note 2H(ii)). Cost comprises direct costs of construction, such as materials, staff costs and overheads, together with interest expense capitalised during the period of construction or installation and testing. Capitalisation of these costs ceases and the asset concerned is transferred to the appropriate fixed assets category when substantially all the activities necessary to prepare the asset for its intended use are completed.

(v) Leased Assets

(a) Leases of assets under which the lessee assumes substantially all the risks and rewards of ownership are classified as finance leases. Where the Group acquires the use of assets under finance leases, the amounts representing the fair value of the leased asset, or, if lower, the present value of the minimum lease payments (computed using the rate of interest implicit in the lease), of such assets are included in fixed assets and the corresponding liabilities, net of finance charges, are recorded as obligations under finance leases. Depreciation and impairment losses are accounted for in accordance with the accounting policy as set out in notes 2I(iv) and 2H(ii) respectively. Finance charges implicit in the lease payments are charged to the profit and loss account over the period of the leases so as to produce an approximately constant periodic rate of charge on the remaining balance of the obligations for each accounting period.

(b) Leases of assets, other than that mentioned in note 2F(ii), under which the lessor has not transferred substantially all the risks and rewards of ownership are classified as operating leases. Where the Group leases out assets under operating leases, the assets are included in the balance sheet according to their nature and, where applicable, are depreciated in accordance with the Group's depreciation policies. Impairment losses are accounted for in accordance with the accounting policies on impairment of assets (note 2H(ii)). Revenue arising from operating leases is recognised in accordance with the Group's revenue recognition policies as set out in note 2Z(ii).

(vi) Subsequent expenditure relating to the replacement of certain parts of an existing fixed asset is recognised in the carrying amount of the asset if it is probable that future economic benefit will flow to the Group and the cost of the item can be measured reliably. The carrying amount of those parts that are replaced is derecognised, with gain or loss arising therefrom dealt with in the profit and loss account.

Expenditure on repairs or maintenance of an existing fixed asset to restore or maintain the originally assessed standard of performance of that asset is charged as an expense when incurred.

Gains or losses arising from the retirement or disposal of a fixed asset or an investment property are determined as the difference between the net disposal proceeds and the carrying amount of the asset. Such gains or losses are recognised as income or expense in the profit and loss account on the date of retirement or disposal. Any related revaluation surplus is transferred from the fixed assets revaluation reserve to retained profits and is not re-classified to profit and loss account.

(vii) Service Concession Assets

Where the Group enters into service concession arrangements under which the Group acquires the right to access, use and operate certain assets for the provision of public services, upfront payments and expenditure directly attributable to the acquisition of the service concession up to inception of the service concession are capitalised as service concession assets and amortised on a straight-line basis over the period of the service concession. Annual payments over the period of the service concession with the amounts fixed at inception are capitalised at their present value, calculated using the incremental long term borrowing rate determined at inception as the discount rate, as service concession assets and amortised on a straight-line basis over the period of the service concession, with a corresponding liability recognised as obligations under service concession. Annual payments for the service concession which are not fixed or determinable at inception and are contingent on future revenues are charged to the profit and loss account in the period when incurred.

Where the Group enters into service concession arrangements under which the Group constructs, uses and operates certain assets for the provision of public services, construction revenues and costs are recognised in the profit and loss account by reference to the stage of completion at the balance sheet date while the fair value of construction service is capitalised initially as service concession assets in the balance sheet and amortised on a straight-line basis over the shorter of the assets' useful lives and the period in which the service concession assets are expected to be available for use by the Group.

Expenditure for the replacement and/or upgrade of the assets subject to service concession is capitalised and amortised on a straight-line basis over the shorter of the assets' useful lives and the remaining period of the service concession.

Service concession assets are carried on the balance sheet as an intangible asset at cost less accumulated amortisation and impairment losses, if any (note 2H(ii)).

Income and expenditure and assets and liabilities in relation to the operation of the service concessions are accounted for in the Group's and the Company's profit and loss accounts and balance sheets.

2 Principal Accounting Policies *(continued)*

G Property Management Rights

Where the Group makes payments for the acquisition of property management rights, the amounts paid are capitalised as intangible assets and stated on the balance sheet at cost less accumulated amortisation and impairment losses (note 2H(ii)). Property management rights are amortised to the profit and loss account on a straight-line basis over the terms of the management rights.

H Impairment of Assets

(i) Impairment of Debtors and Other Receivables

Debtors and other current and non-current receivables are reviewed at each balance sheet date to determine whether there is objective evidence of impairment. If any such evidence exists, the impairment loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition of these assets) where the effect of discounting is material.

If in a subsequent period the amount of an impairment loss decreases, the impairment loss is reversed through the profit and loss account.

(ii) Impairment of Other Assets

Internal and external sources of information are reviewed at each balance sheet date to identify indications that the following assets may be impaired or an impairment loss previously recognised no longer exists or may have decreased:

- fixed assets (including service concession assets but other than assets carried at revalued amounts);
- property management rights;
- railway construction in progress;
- property development in progress;
- deferred expenditure;
- investments in held-to-maturity securities; and
- investments in subsidiaries, non-controlled subsidiaries, associates and jointly controlled entities.

If any such indication exists, the asset's recoverable amount is estimated.

The recoverable amount of an asset is the greater of its fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of time value of money and the risks specific to the asset. Where an asset does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the smallest group of assets that generates cash inflows independently (i.e. a cash-generating unit).

An impairment loss is recognised in the profit and loss account whenever the carrying amount of an asset, or the cash-generating unit to which it belongs, exceeds its recoverable amount.

An impairment loss is reversed if there has been a favourable change in the estimates used to determine the recoverable amount of the asset.

A reversal of impairment losses is limited to the asset's carrying amount that would have been determined had no impairment loss been recognised in prior years. Reversals of impairment losses are credited to the profit and loss account in the year in which the reversals are recognised.

I Depreciation and Amortisation

(i) Investment properties are not depreciated.

(ii) Fixed assets other than investment properties, assets under construction and service concession assets which are amortised over the entire or remaining period of the service concession (note 2F(vii)) are depreciated or amortised on a straight-line basis at rates sufficient to write off their cost or valuation, less their estimated residual value, if any, over their estimated useful lives as follows:

Land and Buildings

Self-occupied land and buildings .... the shorter of 50 years and the unexpired term of the lease

Leasehold land .... the unexpired term of the lease

2 Principal Accounting Policies *(continued)*

I Depreciation and Amortisation *(continued)*

Civil Works

Excavation and boring	Indefinite
Tunnel linings, underground civil structures, overhead structures and immersed tubes	100 years
Station building structures	100 years
Depot structures	80 years
Kiosk structures	20 years
Cableway station tower and theme village structures	27 years

Plant and Equipment

Rolling stock and components	4 – 50 years
Platform screen doors	25 – 35 years
Rail track	7 – 30 years
Environmental control systems, lifts and escalators, fire protection and drainage system	7 – 30 years
Power supply systems	7 – 40 years
Aerial ropeway and cabin	5 – 27 years
Automatic fare collection systems, metal station kiosks, and other mechanical equipment	20 – 25 years
Train control and signalling equipment, station announcement systems, telecommunication systems and advertising panels	5 – 25 years
Station architectural finishes	20 – 30 years
Fixtures and fittings	10 – 25 years
Maintenance equipment	4 – 25 years
Office furniture and equipment	2 – 15 years
Computer software licences and applications	2 – 10 years
Computer equipment	3 – 5 years
Cleaning equipment and tools	5 years
Motor vehicles	4 – 5 years

Where parts of an item of property, plant and equipment have different useful lives, each part is depreciated or amortised separately. The useful lives of the various categories of fixed assets are reviewed annually in the light of actual asset condition, usage experience and the current asset replacement programme.

(iii) No depreciation or amortisation is provided on assets under construction until construction is completed and the assets are ready for their intended use.

(iv) Depreciation on assets held under finance leases is provided at rates designed to write off the cost of the asset in equal annual amounts over the shorter of the lease term or the anticipated useful life of the asset as set out above, except in cases where title to the asset will be acquired by the Group at the end of the lease where depreciation is provided at rates designed to write off the cost of the asset in equal amounts over the anticipated useful life of the asset.

J Construction Costs

(i) Costs incurred by the Group in respect of feasibility studies on proposed railway related construction projects (including consultancy fees, in-house staff costs and overheads) are dealt with as follows:

- where the proposed projects are at a preliminary review stage with no certainty of materialising, the costs concerned are charged to the profit and loss account; and
- where the proposed projects are at a detailed study stage, having been agreed in principle by the Members of the Board based on a feasible financial plan, the costs concerned are recorded as deferred expenditure until such time as a project agreement is reached, whereupon the costs are transferred to railway construction in progress.

(ii) After entering into a project agreement, all costs incurred in the construction of the railway are dealt with as railway construction in progress until commissioning of the railway line, whereupon the relevant construction costs are transferred to fixed assets.

2 Principal Accounting Policies *(continued)*

K Property Development

(i) Costs incurred by the Group in respect of site preparation, land costs and acquisition of development rights as well as notional interest in connection with interest-free loans to property developers are dealt with as property development in progress.

(ii) Payments received from developers in respect of property developments are offset against the amounts in property development in progress attributable to that development. Any surplus amounts of payments received from developers in excess of the balance in property development in progress are transferred to deferred income. In these cases, further costs subsequently incurred by the Group in respect of that development are charged against deferred income.

(iii) Where an interest-free loan is provided to a developer as one of the terms of the development contract, such loan is initially stated at fair value which is its face value discounted at the prevailing market rates of interest at inception. When the repayment schedule of the loan is altered, the fair value is re-calculated and the carrying amount of the loan is adjusted. The difference between the fair value and the face value of the loan is dealt with as property development in progress during construction and transferred to the profit and loss account upon completion of the development. Notional interest income is credited to the profit and loss account and debited to the loan over the period of the loan so that the fair value of the loan at maturity equates its face value.

(iv) Profits arising from the development of properties undertaken in conjunction with property developers are recognised in the profit and loss account as follows:

- where the Group receives payments from developers, profits arising from such payments are recognised when the foundation and site enabling works are complete and acceptable for development, and after taking into account the outstanding risks and obligations, if any, retained by the Group in connection with the development;
- where the Group receives a right to a share of the net surplus from sale of the development and interests in any unsold units, income is initially recognised by the Group upon the issue of occupation permits provided the amounts of revenue and costs can be estimated reliably. The interest in any unsold properties is subsequently remeasured on a basis consistent with the policy set out in note 2K(v); and
- where the Group receives a distribution of the assets of the development, profit is recognised based on the fair value of such assets at the time of receipt and after taking into account any outstanding risks and obligations retained by the Group in connection with the development.

Upon recognition of profit, the balance of deferred income or property development in progress relating to that development is credited or charged to the profit and loss account, as the case may be.

(v) Where properties are received as a profit distribution upon completion of development and are held for sale, those properties are stated at fair value upon receipt and subsequently carried at their estimated net realisable value. Net realisable value represents the estimated selling price less costs to be incurred in selling the properties. When properties are sold, the carrying amount of those properties is recognised as cost of properties sold in the period in which the related revenue is recognised. The amount of any write-down of properties to net realisable value is recognised as an expense in the period the write-down occurs. The amount of any reversal of any write-down of properties arising from an increase in net realisable value is recognised as a reduction in the cost of properties sold in the period in which the reversal occurs.

(vi) Where properties under construction are received from a development for investment purpose, these properties are recognised as investment properties at fair value. Further costs incurred in the construction of those assets are capitalised in investment properties.

L Jointly Controlled Operations

The arrangements entered into by the Group with developers for property developments without establishing separate entities are considered to be jointly controlled operations pursuant to HKAS 31, *Interests in joint ventures*. Under the development arrangements, the Group is normally responsible for its own costs, including in-house staff costs and the costs of enabling works, and the developers normally undertake to pay for all other project costs such as land premium (or such remaining portion as not already paid by the Group), construction costs, professional fees, etc. Such costs are deductible from the proceeds of sale before surplus proceeds are shared. In respect of its interests in such operations, the Group accounts for the purchase consideration of development rights, costs of enabling works (including any interest accrued) and land costs (including any land premiums) paid net of payments received as property development in progress. In cases where payments received from developers exceed the related expenditures incurred by the Group, such excess is recorded as deferred income. Expenses incurred by the Group on staff, overhead and consultancy fees in respect of these developments are also capitalised as property development in progress. The Group's share of income earned from such operations is recognised in the profit and loss account on the basis of note 2K(iv) after netting off any related balance in property development in progress at that time.

2 Principal Accounting Policies *(continued)*

M Investments in Securities

The Group's policies for investments in securities (other than investments in its subsidiaries, non-controlled subsidiaries, associates and jointly controlled entities) are as follows:

(i) Investments in securities held for trading purpose are initially stated at fair value. At each balance sheet date the fair value is remeasured, with any resultant unrealised gain or loss being recognised in the profit and loss account.

(ii) Investments in debt securities and bank medium term notes on which the Group has the ability and intention to hold to maturity are classified as held-to-maturity securities, which are stated at amortised cost less impairment losses (note 2H(ii)).

(iii) Investments are recognised/derecognised on the date the Group commits to purchase/sell the investments.

(iv) Interest income in relation to investment in securities is recognised as it accrues using the effective interest method.

(v) Profit or loss on disposal of investments in securities are determined as the difference between the estimated net disposal proceeds and the carrying amount of the investments and are accounted for in the profit and loss account as they arise.

N Stores and Spares

Stores and spares used for railway and business operation are categorised as either revenue or capital. Revenue spares are stated in the balance sheet at cost, using the weighted average cost method and are recognised in the year in which the consumption occurred. Provision is made for obsolescence where appropriate. Capital items are included in fixed assets and stated at cost less accumulated depreciation and impairment losses (note 2H(ii)). Depreciation is charged at the rates applicable to the relevant fixed assets against which the capital spares are held in reserve.

O Long-term Contracts

The accounting policy for contract revenue is set out in note 2Z(iii). When the outcome of a fixed-price long-term contract can be estimated reliably, contract costs are recognised as expenses by reference to the stage of completion of the contract activity at the balance sheet date. When it is probable that total contract costs will exceed total contract revenue, the expected loss is recognised as an expense immediately. When the outcome of a long-term contract cannot be estimated reliably, contract costs are recognised as expenses in the period in which they are incurred.

Long-term contracts in progress at the balance sheet date are recorded in the balance sheet at the net amount of costs incurred plus recognised profits less recognised losses and progress billings, and are presented in the balance sheet as the "Gross amount due from customers for contract work" (as an asset) or the "Gross amount due to customers for contract work" (as a liability), as applicable. Progress billings not yet paid by the customer are included in the balance sheet under "Debtors, deposits and payments in advance". Amounts received before the related work is performed are included in the balance sheet as a liability under "Creditors and accrued charges".

P Cash and Cash Equivalents

Cash and cash equivalents comprise cash at banks and on hand, demand deposits with banks and other financial institutions, and short-term highly liquid investments that are readily convertible into known amounts of cash and subject to an insignificant risk of changes in value with a maturity at acquisition within three months. Bank overdrafts that are repayable on demand and form an integral part of the Group's cash management are also included as a component of cash and cash equivalents for the purpose of the consolidated cash flow statement.

Q Debtors, Deposits and Payments in Advance

Debtors, deposits and payments in advance are initially recognised at fair value and thereafter stated at amortised cost using the effective interest method less impairment losses for bad and doubtful debts (note 2H(i)), except where the effect of discounting would be immaterial or the discount is not measurable as the receivables are interest-free loans made to related parties without any fixed repayment terms. In such cases, the receivables are stated at cost less impairment losses for bad and doubtful debts.

R Interest-bearing Borrowings

Interest-bearing borrowings are recognised initially at fair value net of transaction costs incurred. The unhedged portion of interest-bearing borrowings is subsequently stated at amortised costs. Any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the profit and loss account over the period of the borrowings using the effective interest method.

Subsequent to initial recognition, the carrying amount of the hedged portion of interest-bearing borrowings is remeasured and the change in fair value attributable to the risk being hedged is recognised in the profit and loss account to offset the effect of the gain or loss on the related hedging instrument.

S Creditors and Accrued Charges

Creditors and accrued charges are stated at amortised cost if the effect of discounting would be material, otherwise they are stated at cost.

2 Principal Accounting Policies *(continued)*

T Derivative Financial Instruments and Hedging Activities

The Group uses derivative financial instruments such as interest rate swaps and currency swaps to manage its interest rate and foreign exchange exposure. Based on the Group's policies, these instruments are used solely for reducing or eliminating financial risks associated with the Group's investments and liabilities and not for trading or speculation purposes.

Derivatives are initially recognised at fair value and are subsequently remeasured at their fair value at each balance sheet date. The method of recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument and the nature of the item being hedged.

Where hedge accounting applies, the Group designates derivatives employed as either: (1) a fair value hedge: to hedge the fair value of recognised liabilities; or (2) a cash flow hedge: to hedge the variability in cash flows of a recognised liability or the foreign currency risk of a firm commitment.

(i) Fair Value Hedge

Changes in the fair value of derivatives that are designated and qualified as fair value hedges are recorded in the profit and loss account, together with any changes in the fair value of the hedged assets or liabilities that are attributable to the hedged risk.

(ii) Cash Flow Hedge

The effective portion of changes in the fair value of derivatives that are designated and qualified as cash flow hedges is recognised in other comprehensive income which is accumulated separately in equity in the hedging reserve. The gain or loss relating to the ineffective portion is recognised immediately in the profit and loss account.

Amounts previously recognised in other comprehensive income and accumulated in equity are transferred to the profit and loss account in the periods when the hedged item is recognised in the profit and loss account. However, when the transaction in respect of the hedged item results in the recognition of a non-financial asset or liability, the associated gains and losses that were previously recognised in other comprehensive income and accumulated in equity are transferred from equity and included in the initial cost or carrying amount of the non-financial asset or liability.

When a hedging instrument expires or is sold, terminated or exercised, or the Group revokes designation of the hedge relationship but the transaction in respect of the hedged item is still expected to occur, the cumulative gain or loss existing in equity at that time remains in equity until the transaction occurs and it is recognised in accordance with the above policy. However, if the transaction in respect of the hedged item is no longer expected to occur, the gain or loss accumulated in equity is immediately transferred to the profit and loss account.

(iii) Derivatives That Do Not Qualify for Hedge Accounting

Changes in the fair value of any derivative instruments that do not qualify for hedge accounting are recognised immediately in the profit and loss account.

U Employee Benefits

(i) Salaries, annual leave, leave passage allowance, contributions to defined contribution retirement plans, including contributions to Mandatory Provident Funds ("MPF") as required under the Hong Kong Mandatory Provident Fund Schemes Ordinance, and other costs of non-monetary benefits are accrued in the year in which the associated services are rendered by employees of the Group. Where these benefits are incurred for staff relating to construction projects, capital works and property developments, they are capitalised as part of the cost of the qualifying assets. In other cases, they are recognised as expenses in the profit and loss account as incurred.

(ii) The Group's net obligation in respect of defined benefit retirement plans is calculated separately for each plan by estimating the amount of future benefit that employees have earned in return for their service in the current and prior years; that benefit is discounted to determine the present value, and the fair value of any plan assets is deducted. The discount rate is the yield at balance sheet date on high quality corporate bonds that have maturity dates approximating the terms of the Group's obligations. If there is no deep market in such bonds, the market yield on government bonds would be used. The calculation is performed annually by a qualified actuary using the Projected Unit Credit Method.

When the benefits of a plan are improved, the portion of the increased benefit relating to past service by employees is recognised either as an expense in the profit and loss account, or capitalised as part of the cost of the relevant construction projects, capital works or property developments, as the case may be, on a straight-line basis over the average period until the benefits become vested. To the extent that the benefits vest immediately, the expense is recognised immediately in a similar manner.

In calculating the Group's obligation in respect of a plan, to the extent that any cumulative unrecognised actuarial gain or loss exceeds ten percent of the greater of the present value of the defined benefit obligation and the fair value of plan assets, that portion is recognised in the profit and loss account over the expected average remaining working lives of the employees participating in the plan. Otherwise, the actuarial gain or loss is not recognised.

Where the calculation of the Group's net obligation results in a negative amount, the asset recognised is limited to the net total of any cumulative unrecognised net actuarial losses and past service costs and the present value of any future refunds from the plan or reductions in future contributions to the plan.

2 Principal Accounting Policies *(continued)*

U Employee Benefits *(continued)*

(iii) Equity-settled share-based payments are measured at fair value at the date of grant. The fair value determined at the grant date is recognised as a staff cost, unless the relevant employee expenses qualify for recognition as an asset, on a straight-line basis over the vesting period and taking into account the probability that the options will vest, with a corresponding increase in the employee share-based capital reserve within equity. Fair value is measured by use of a Black-Scholes model, taking into account the terms and conditions upon which the options are granted. The expected life used in the model is adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions, and behavioural considerations.

During the vesting period, the number of share options that is expected to vest is reviewed. Any adjustment to the cumulative fair value recognised in prior years is charged/credited to the profit and loss account for the year of the review, unless the original employee expenses qualify for recognition as an asset, with a corresponding adjustment to the capital reserve. On vesting date, the amount recognised as an expense is adjusted to reflect the actual number of share options that vest (with a corresponding adjustment to the capital reserve). The equity amount is recognised in the capital reserve until either the option is exercised (when it is transferred to the share premium account) or the option expires (when it is released directly to retained profits).

For cash-settled share-based payments, a liability equal to the portion of the services received is recognised at the fair value of the shares determined at each balance sheet date.

(iv) Termination benefits are recognised when, and only when, the Group demonstrably commits itself to terminate employment or to provide benefits as a result of voluntary redundancy by having a detailed formal plan which is without realistic possibility of withdrawal.

V Retirement Schemes

The Group operates both defined contribution and defined benefit retirement schemes.

Employer's contributions to defined contribution retirement schemes including MPF Schemes are recognised in the accounts in accordance with the policy set out in note 2U(i).

Employer's contributions paid and payable in respect of employees of defined benefit retirement schemes as calculated annually by independent actuaries in accordance with the Retirement Scheme Rules and provisions of the Occupational Retirement Schemes Ordinance are used to satisfy the pension expenses recognised in the accounts according to note 2U(ii). Any deficit or surplus thereof will be dealt with in the balance sheet as accrued or prepaid benefit expenses, as the case may be.

W Income Tax

(i) Income tax for the year comprises current tax and movements in deferred tax assets and liabilities. Income tax is recognised in the profit and loss account except to the extent that it relates to items recognised in other comprehensive income or directly in equity, in which case it is recognised in other comprehensive income or directly in equity respectively.

(ii) Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

(iii) Deferred tax assets and liabilities arise from deductible and taxable temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and their tax bases. Deferred tax assets also arise from unused tax losses and unused tax credits.

Apart from certain limited exceptions, all deferred tax liabilities and deferred tax assets to the extent that it is probable that future taxable profits will be available against which the asset can be utilised, are recognised. Future taxable profits that may support the recognition of deferred tax assets arising from deductible temporary differences include those that will arise from the reversal of existing taxable temporary differences, provided those differences relate to the same taxation authority and the same taxable entity, and are expected to reverse either in the same period as the expected reversal of the deductible temporary difference or in periods into which a tax loss arising from the deferred tax asset can be carried back or forward. The same criteria are adopted when determining whether existing taxable temporary differences support the recognition of deferred tax assets arising from unused tax losses and credits, that is, those differences are taken into account if they relate to the same taxation authority and the same taxable entity, and are expected to reverse in a period, or periods, in which the tax loss or credit can be utilised.

The limited exceptions to recognition of deferred tax assets and liabilities are those temporary differences arising from the initial recognition of assets or liabilities that affect neither accounting nor taxable profit (provided they are not part of a business combination) and investments in subsidiaries to the extent that, in the case of taxable differences, the Group controls the timing of the reversal and it is probable that the differences will not reverse in the foreseeable future, or in the case of deductible differences, unless it is probable that they will reverse in the future.

The amount of deferred tax recognised is measured based on the expected manner of realisation or settlement of the carrying amount of the assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date. Deferred tax assets and liabilities are not discounted.

The carrying amount of a deferred tax asset is reviewed at each balance sheet date and is reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow the related tax benefit to be utilised. Any such reduction is reversed to the extent that it becomes probable that sufficient taxable profits will be available.

2 Principal Accounting Policies *(continued)*

W Income Tax *(continued)*

(iv) Current tax balances and deferred tax balances, and movements therein, are presented separately from each other and are not offset. Current tax assets are offset against current tax liabilities, and deferred tax assets against deferred tax liabilities if, and only if, the Company or the Group has the legally enforceable right to set off current tax assets against current tax liabilities and the following additional conditions are met:

- in the case of current tax assets and liabilities, the Company or the Group intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously; or
- in the case of deferred tax assets and liabilities, if they relate to income taxes levied by the same taxation authority on either:
  - the same taxable entity; or
  - different taxable entities, which, in each future period in which significant amounts of deferred tax liabilities or assets are expected to be settled or recovered, intend to realise the current tax assets and settle the current tax liabilities on a net basis or realise and settle simultaneously.

X Financial Guarantee Contracts

Financial guarantees are contracts that require the issuer to make specified payments to reimburse the holder of the guarantee for a loss it incurs because a specified debtor fails to make payment to the holder when due in accordance with the original or modified terms of a debt instrument.

When the Group issues a financial guarantee, where the effect is material, the fair value of the guarantee (being the transaction price, unless the fair value can otherwise be reliably estimated) after netting off any consideration received or receivable at inception is initially debited to the profit and loss account and recognised as deferred income within creditors and accrued charges.

The amount of the guarantee initially recognised as deferred income is amortised in the profit and loss account over the term of the guarantee as income from financial guarantees issued. In addition, provisions are recognised in accordance with note 2Y if and when (i) it becomes probable that the holder of the guarantee will call upon the Group under the guarantee, and (ii) the amount of that claim on the Group is expected to exceed the amount currently carried in creditors and accrued charges in respect of that guarantee, i.e. the amount initially recognised less accumulated amortisation.

Y Provisions and Contingent Liabilities

Provisions are recognised for liabilities of uncertain timing or amount when the Company or Group has a legal or constructive obligation arising as a result of a past event, it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made. Where the time value of money is material, provisions are stated at the present value of the expenditure expected to settle the obligation.

Where it is not probable that an outflow of economic benefits will be required, or the amount cannot be estimated reliably, the obligation is disclosed as a contingent liability, unless the probability of outflow of economic benefits is remote. Possible obligations, whose existence will only be confirmed by the occurrence or non-occurrence of one or more future events are also disclosed as contingent liabilities unless the probability of outflow of economic benefits is remote.

Z Revenue Recognition

Revenue is measured at the fair value of the consideration received or receivable. Provided it is probable that the economic benefits associated with the transactions will flow to the Group and the amount of revenue can be measured reliably, revenue is recognised in the profit and loss account as follows:

(i) Fare revenue is recognised when the journey is provided.

(ii) Rental income from investment properties, station kiosks and other railway premises under operating leases is accounted for in accordance with the terms of the leases. Lease incentives granted are recognised in the profit and loss account as an integral part of the aggregate net lease payments receivable. Contingent rentals are recognised as income in the accounting period in which they are earned.

(iii) Contract revenue is recognised when the outcome of a consultancy, construction or service contract can be estimated reliably. Contract revenue is recognised using the percentage of completion method, measured by reference to the percentage of contract costs incurred to date to the estimated total contract costs for the contract. When the outcome of a consultancy, construction or service contract cannot be estimated reliably, revenue is recognised only to the extent of contract costs incurred that it is probable to be recovered.

(iv) Incomes from other station commercial businesses, property management and franchise revenue from service concessions are recognised when the services are provided.

2 Principal Accounting Policies *(continued)*

AA Operating Lease Charges

Rentals payable under operating leases are charged on a straight-line basis over the period of the lease to the profit and loss account, except for rentals payable in respect of railway construction, property development in progress and proposed capital projects which are capitalised as part of railway construction in progress, property development in progress and deferred expenditure respectively.

BB Interest and Finance Charges

Interest income and expense directly attributable to the financing of capital projects prior to their completion or commissioning are capitalised. Exchange differences arising from foreign currency borrowings relating to the acquisition of assets are capitalised to the extent that they are regarded as an adjustment to capitalised interest costs. Interest expense attributable to other purposes is charged to the profit and loss account.

Finance charges implicit in the lease payments on assets held under finance leases are charged to the profit and loss account over the period of the lease so as to produce an approximately constant periodic rate of charge on the remaining balance of the obligations for each accounting period.

CC Foreign Currency Translation

Foreign currency transactions during the year are translated into Hong Kong dollars and recorded at exchange rates ruling at the transaction dates. Foreign currency monetary assets and liabilities are translated into Hong Kong dollars at the exchange rates ruling at the balance sheet date. Exchange gains and losses are recognised in the profit and loss account.

The results of foreign enterprises are translated into Hong Kong dollars at the average exchange rates for the year. Balance sheet items are translated into Hong Kong dollars at the closing exchange rates at the balance sheet date. The resulting exchange differences are recognised in other comprehensive income and accumulated separately in equity in the exchange reserve.

DD Segment Reporting

Operating segments, and the amounts of each segment item reported in the financial statements, are identified from the financial information provided regularly to the Group's most senior executive management for the purposes of allocating resources to, and assessing the performance of, the Group's various lines of business and geographical locations.

Individually material operating segments are not aggregated for financial reporting purposes unless the segments have similar economic characteristics and are similar in respect of the nature of services and products, the type or class of customers, the methods used to provide the services or distribute the products, and the nature of the regulatory environment. Operating segments which are not individually material may be aggregated if they share a majority of these criteria.

EE Related Parties

For the purposes of these accounts, a person, or a close member of that person's family, is related to the Group if that person is a member of the key management personnel of the Group. An entity is related to the Group if the entity and the Group are members of the same group, or the entity is an associate or joint venture of the Group, or post-employment benefit plans which are for the benefit of employees of the Group or of any entity that is a related party of the Group, or an individual who is a related party of the Group has control, jointly control, significant influence over that entity or is a member of the key management personnel of that entity.

FF Government Grants

Government grants are assistance by governments in the form of transfer of resources in return for the Group's compliance to the conditions attached thereto. Government grants which represent compensation for the cost of an asset are deducted from the cost of the asset in arriving at its carrying value to the extent of the amounts received and receivable as at the date of the balance sheet. Government grants which represent compensation for expenses or losses are deducted from the related expenses. Any excess of the amount of grant received or receivable over the cost of the asset or the expenses or losses at the balance sheet date are carried forward as advance receipts or deferred income to set off against the future cost of the asset or future expenses or losses.

3 Rail Merger with Kowloon-Canton Railway Corporation ("KCRC")

On 2 December 2007 (the "Appointed Day"), the Company's operations merged with those of KCRC ("Rail Merger"). The structure and key terms of the Rail Merger were set out in a series of transaction agreements entered into between, inter alia, HKSAR Government, KCRC and the Company including the Service Concession Agreement, Property Package Agreements and Merger Framework Agreement. Key elements of the Rail Merger included the following:

- The expansion of the Company's existing franchise under the Mass Transit Railway Ordinance ("MTR Ordinance") to cover the construction, operation and regulation of railways in addition to the MTRC railway for an initial period of 50 years from the Appointed Day ("Franchise Period"), which may be extended pursuant to the provisions of the MTR Ordinance (note 57C);
- The Service Concession Agreement ("SCA") pursuant to which KCRC granted the Company the right to access, use and operate the KCRC system for an initial term of 50 years (the "Concession Period"), which will be extended if the Franchise Period (as it relates to the KCRC railway) is extended. The SCA also sets out the basis on which the KCRC system will be returned at the end of the Concession Period. In accordance with the terms of the SCA, the Company paid an upfront lump sum to KCRC on the Appointed Day and is obliged to pay an annual fixed payment to KCRC for the duration of the Concession Period. Additionally, commencing after three years from the Appointed Day, the Company is obliged to pay a variable annual payment to KCRC based on the revenue generated from the KCRC system above certain thresholds;
- Under the SCA, the Company is responsible for the expenditure incurred in relation to the maintenance, repair, replacement and upgrade of the KCRC system (with any new assets acquired being classified as "additional concession property"). To the extent that such expenditure exceeds an agreed threshold ("Capex Threshold"), the Company will be reimbursed for any above threshold expenditure at the end of the Concession Period with such reimbursement to be on the basis of depreciated book value;
- In the event that the Concession Period is extended, the fixed annual payment and the variable annual payment will continue to be payable by the Company. On such extension, the Capex Threshold may also be adjusted; and
- Property Package Agreements and Merger Framework agreement setting out the acquisition of certain properties, property management rights and property development rights by the Company as well as the framework for the Rail Merger including the implementation of the Fare Adjustment Mechanism.

4 Revenue from Hong Kong Transport Operations

Revenue from Hong Kong transport operations comprises:

in HK$ million	**2011**	2010
Fare Revenue:		
– Domestic Service	**9,300**	8,668
– Cross-boundary Service	**2,633**	2,487
– Airport Express	**751**	694
– Light Rail, Bus and Intercity	**673**	610
	13,357	12,459
Other rail-related income	**152**	176
	13,509	12,635

The Domestic Service comprises the Kwun Tong, Tsuen Wan, Island, Tung Chung, Tseung Kwan O, Disneyland Resort, East Rail (excluding Cross-boundary Service), West Rail and Ma On Shan lines. Other rail-related income includes mainly ancillary service income from Intercity, by-law infringement surcharge and Octopus load agent fees.

5 Revenue from Hong Kong Station Commercial Business

Revenue from Hong Kong station commercial business comprises:

in HK$ million	**2011**	2010
Duty free shops and kiosk rental	**1,905**	1,716
Advertising	**893**	734
Telecommunication income	**500**	290
Other station commercial income	**124**	113
	3,422	2,853

6 Revenue from Property Rental and Management Businesses

Revenue from property rental and management businesses comprises:

in HK$ million	**2011**	2010
Property rental income from:		
– Telford Plaza	**672**	614
– Elements	**634**	509
– Maritime Square	**389**	377
– Luk Yeung Galleria	**161**	153
– Paradise Mall	**124**	118
– Citylink Plaza	**120**	112
– International Finance Centre	**410**	390
– Ginza Mall – Beijing	**123**	105
– Other properties	**383**	380
	3,016	2,758
Property management income	**199**	203
	3,215	2,961

7 Revenue and Expenses of Railway Subsidiaries outside of Hong Kong

On 16 June 2011, Shenzhen Metro Longhua Line ("Shenzhen Longhua Line") Phase 2 commenced revenue operation. Revenue and expenses relating to railway subsidiaries outside of Hong Kong comprise:

in HK$ million	Stockholm Metro	Melbourne Train	Shenzhen Longhua Line	Total
2011				
Revenue				
– Railway operations related	**3,166**	**6,177**	**185**	**9,528**
– Project related	**–**	**2,748**	**3**	**2,751**
	3,166	**8,925**	**188**	**12,279**
Expenses				
– Railway operations related	**3,111**	**5,967**	**254**	**9,332**
– Project related	**–**	**2,558**	**2**	**2,560**
– Utilisation of government grant	**–**	**–**	**(62)**	**(62)**
	3,111	**8,525**	**194**	**11,830**
2010				
Revenue				
– Railway operations related	2,858	5,226	20	8,104
– Project related	–	2,013	27	2,040
	2,858	7,239	47	10,144
Expenses				
– Railway operations related	2,864	5,043	62	7,969
– Project related	–	1,870	26	1,896
	2,864	6,913	88	9,865

8 Revenue from Other Businesses

Revenue from other businesses comprises incomes from:

in HK$ million	2011	2010
Ngong Ping 360	270	239
Consultancy business	105	113
Project management for KCRC and HKSAR Government	588	540
Miscellaneous businesses	35	33
	998	925

9 Other Net Income

Other net income relates to the construction of Shenzhen Longhua Line Phase 2 and comprises:

in HK$ million	2011	2010
Construction revenue	1,933	1,719
Construction cost	(1,933)	(1,719)
	–	–

Construction revenue is recognised by reference to the total construction cost incurred since signing of the Project Concession Agreement on 18 March 2009 up to the date of operation commencement on 16 June 2011. As of 31 December 2011, such cost amounted to HK$5,541 million (31 December 2010: HK$3,608 million). There was no cumulative net profit or loss recognised in respect of the construction as at 31 December 2011 and 2010.

10 Operating Expenses

A Total staff costs include:

in HK$ million	2011	2010
Amount charged to profit and loss account under:		
– staff costs and related expenses for Hong Kong transport operations	3,673	3,398
– maintenance and related works for Hong Kong transport operations	70	78
– other expense line items for Hong Kong transport operations	50	59
– expenses relating to Hong Kong station commercial business	53	47
– expenses relating to property rental and management businesses	88	73
– expenses relating to railway subsidiaries outside of Hong Kong	4,837	3,848
– expenses relating to other businesses	690	561
– project study and business development expenses	96	142
Amount capitalised under:		
– railway construction in progress before offset by government grant	452	183
– property development in progress	93	90
– assets under construction and other projects	242	399
– service concession assets	284	251
Amount recoverable	591	542
Total staff costs	11,219	9,671

Amount recoverable relates to property management, entrustment works and other agreements.

10 Operating Expenses *(continued)*

A Total staff costs include: *(continued)*

The following expenditures are included in total staff costs:

in HK$ million	2011	2010
Share-based payments	**113**	61
Contributions to defined contribution retirement plans and Mandatory Provident Fund	**409**	362
Expenses recognised in respect of defined benefit retirement plans	**144**	173
	666	596

B The costs of maintenance and related works for Hong Kong transport operations relate mainly to contracted maintenance and revenue works. Other routine repairs and maintenance works are performed by in-house operations and the costs of which are included under staff costs and related expenses as well as stores and spares consumed.

C Project study and business development expenses comprise:

in HK$ million	2011	2010
Business development expenses	**114**	192
Miscellaneous project study expenses and project cost written off	**9**	24
	123	216

Business development expenses relate mainly to new business opportunities in the Mainland of China, Europe and Australia.

D Auditors' remuneration charged to the profit and loss account include:

in HK$ million	2011	2010
Audit services	**10**	10
Tax services	**1**	1
Other audit related services	**3**	3
	14	14

E The following charges/(credits) are included in operating expenses:

in HK$ million	2011	2010
Loss on disposal of fixed assets	**32**	50
Derivative financial instruments:		
– foreign exchange contracts – ineffective portion of cash flow hedges	**–**	(1)
– transfer from hedging reserve (note 22B)	**(5)**	(1)
Unrealised loss on revaluation of investments in securities	**4**	2

F Operating lease expenses charged to the profit and loss account comprise:

in HK$ million	2011	2010
Shopping centre, office building, staff quarters and bus depot	**78**	84
Rolling stock, stations, office buildings, depots, depot equipment and other minor assets for railway subsidiaries	**1,066**	935
Amount capitalised	**(4)**	(20)
	1,140	999

11 Remuneration of Members of the Board and the Executive Directorate

A Remuneration of Members of the Board and the Executive Directorate

(i) The emoluments of Members of the Board and the Executive Directorate of the Company were as follows:

in HK$ million	Fees	Base pay, allowances and benefits in kind	Retirement scheme contribution	Variable remuneration related to performance	Total
2011					
Members of the Board					
– Raymond Ch'ien Kuo-fung	**1.2**	**–**	**–**	**–**	**1.2**
– Vincent Cheng Hoi-chuen	**0.3**	**–**	**–**	**–**	**0.3**
– Christine Fang Meng-sang	**0.3**	**–**	**–**	**–**	**0.3**
– Edward Ho Sing-tin	**0.4**	**–**	**–**	**–**	**0.4**
– Alasdair George Morrison	**0.3**	**–**	**–**	**–**	**0.3**
– Ng Leung-sing	**0.3**	**–**	**–**	**–**	**0.3**
– Abraham Shek Lai-him	**0.3**	**–**	**–**	**–**	**0.3**
– T. Brian Stevenson	**0.4**	**–**	**–**	**–**	**0.4**
– Ceajer Chan Ka-keung	**0.3**	**–**	**–**	**–**	**0.3**
– Eva Cheng	**0.3**	**–**	**–**	**–**	**0.3**
– Joseph Lai Yee-tak	**0.3**	**–**	**–**	**–**	**0.3**
Members of the Executive Directorate					
– Chow Chung-kong (retired on 31 December 2011)	**–**	**7.8**	**–***	**7.0**	**14.8**
– William Chan Fu-keung	**–**	**4.6**	**0.2**	**1.9**	**6.7**
– Chew Tai-chong	**–**	**4.3**	**–***	**1.8**	**6.1**
– Thomas Ho Hang-kwong (retired on 30 September 2011)	**–**	**4.5**	**0.2**	**1.5**	**6.2**
– Jacob Kam Chak-pui (appointed on 1 January 2011)	**–**	**3.7**	**0.6**	**1.5**	**5.8**
– Lincoln Leong Kwok-kuen	**–**	**5.1**	**0.8**	**2.1**	**8.0**
– Gillian Elizabeth Meller (appointed on 1 September 2011)**	**–**	**1.1**	**0.2**	**0.3**	**1.6**
– David Tang Chi-fai (appointed on 1 October 2011)**	**–**	**0.8**	**0.2**	**0.3**	**1.3**
– Leonard Bryan Turk (retired on 31 August 2011)	**–**	**3.9**	**0.1**	**1.5**	**5.5**
– Jeny Yeung Mei-chun (appointed on 1 September 2011)**	**–**	**1.1**	**0.2**	**0.3**	**1.6**
	4.4	**36.9**	**2.5**	**18.2**	**62.0**

* During the year ended 31 December 2011, the total contributions paid by the Company for C K Chow and T C Chew, who participated in the MTR MPF Scheme, were HK$12,000 each.

** Gillian E Meller and Jeny M C Yeung were appointed as Members of the Executive Directorate since 1 September 2011 while David C F Tang was appointed as Member of the Executive Directorate since 1 October 2011. The amount of their emoluments shown in the above table covered the period from the date of their appointment to 31 December 2011.

11 Remuneration of Members of the Board and the Executive Directorate *(continued)*

A Remuneration of Members of the Board and the Executive Directorate *(continued)*

in HK$ million	Fees	Base pay, allowances and benefits in kind	Retirement scheme contribution	Variable remuneration related to performance	Total
2010					
Members of the Board					
– Raymond Ch'ien Kuo-fung	1.2	–	–	–	1.2
– Vincent Cheng Hoi-chuen	0.3	–	–	–	0.3
– Christine Fang Meng-sang	0.3	–	–	–	0.3
– Edward Ho Sing-tin	0.4	–	–	–	0.4
– Alasdair George Morrison (appointed on 9 July 2010)	0.1	–	–	–	0.1
– Ng Leung-sing	0.3	–	–	–	0.3
– Abraham Shek Lai-him	0.3	–	–	–	0.3
– T. Brian Stevenson	0.4	–	–	–	0.4
– Ceajer Chan Ka-keung	0.3	–	–	–	0.3
– Eva Cheng	0.3	–	–	–	0.3
– Joseph Lai Yee-tak	0.3	–	–	–	0.3
Members of the Executive Directorate					
– Chow Chung-kong	–	6.8	–*	7.1	13.9
– Russell John Black (retired on 31 January 2010)	–	0.8	–*	0.1	0.9
– William Chan Fu-keung	–	4.7	0.2	1.9	6.8
– Chew Tai-chong (appointed on 1 February 2010)**	–	3.8	–*	1.6	5.4
– Thomas Ho Hang-kwong	–	4.5	0.2	1.9	6.6
– Lincoln Leong Kwok-kuen	–	5.0	0.8	2.0	7.8
– Andrew McCusker (retired on 31 December 2010)	–	4.6	0.2	1.8	6.6
– Leonard Bryan Turk	–	4.4	0.2	1.9	6.5
	4.2	34.6	1.6	18.3	58.7

* During the year ended 31 December 2010, the total contributions paid by the Company for C K Chow and T C Chew, who participated in the MTR MPF Scheme, were HK$12,000 and HK$7,000 respectively. The contribution paid by the Company for Russell J Black, who participated in the MTR Retirement Scheme, was HK$17,484.

** T C Chew was appointed as Member of the Executive Directorate since 1 February 2010. The amount of the emoluments shown in the above table covered the period from the date of his appointment to 31 December 2010.

Russell J Black, Andrew McCusker, Thomas H K Ho and Leonard B Turk received a lump sum benefit payment of HK$20.8 million, HK$20.7 million, HK$24.3 million and HK$24.3 million respectively from the MTR Retirement Scheme upon their retirements in January 2010 for Russell J Black, December 2010 for Andrew McCusker, August 2011 for Leonard B Turk and September 2011 for Thomas H K Ho.

Andrew McCusker, who retired on 31 December 2010, received a pro-rated discretionary award of HK$153,510 in July 2011 in respect of his service from 1 July 2010 to 31 December 2010.

On 12 April 2010, Lincoln K K Leong was paid HK$4.6 million, representing the derivative interest granted to him on 12 April 2007 to receive an equivalent value in cash of 160,000 shares (note 53B(iii)). On 4 January 2012, C K Chow was paid HK$5.6 million, representing his entitlement to receive an equivalent value in cash of 222,161 shares on completion of his two-year contract ended on 31 December 2011 (note 53B(i)).

The above emoluments do not include the fair value of share options, as estimated at the date of grant which is defined as the date of acceptance of the offer to grant the option.

11 Remuneration of Members of the Board and the Executive Directorate *(continued)*

A Remuneration of Members of the Board and the Executive Directorate *(continued)*

Share options were granted to Members of the Executive Directorate under the Company's 2007 Option Scheme, which were offered to them on 10 December 2007, 8 December 2008, 12 June 2009, 8 December 2009, 28 June 2010 and 16 December 2010. The entitlements of each of the Members are as follows:

- C K Chow was granted options in respect of 720,000 shares on 13 December 2007 and 470,000 shares each on 9 December 2008, 9 December 2009 and 17 December 2010, of which 470,000 options were vested in 2011 (2010: 554,000), and the respective fair value of the share-based payments recognised for the year ended 31 December 2011 was HK$3.4 million (2010: HK$2.5 million);
- Russell J Black was granted options in respect of 170,000 shares each on 12 December 2007 and 9 December 2008 and 42,500 shares on 10 December 2009, of which 127,500 options were vested in 2010, and the respective fair value of the share-based payments recognised for the year ended 31 December 2010 was HK$0.5 million;
- William F K Chan was granted options in respect of 170,000 shares each on 13 December 2007, 9 December 2008, 10 December 2009 and 17 December 2010, of which 170,000 options were vested in 2011 (2010: 170,000), and the respective fair value of the share-based payments recognised for the year ended 31 December 2011 was HK$1.2 million (2010: HK$0.8 million);
- T C Chew was granted options in respect of 85,000 shares on 18 June 2009 and 170,000 shares each on 10 December 2009 and 17 December 2010, of which 142,500 options were vested in 2011 (2010: 85,500), and the respective fair value of the share-based payments recognised for the year ended 31 December 2011 was HK$1.3 million (2010: HK$0.5 million);
- Thomas H K Ho was granted options in respect of 170,000 shares each on 12 December 2007, 11 December 2008 and 14 December 2009 and 127,500 shares on 17 December 2010, of which 155,500 options were vested in 2011 (2010: 170,000), and the respective fair value of the share-based payments recognised for the year ended 31 December 2011 was HK$1.1 million (2010: HK$0.8 million);
- Jacob C P Kam was granted options in respect of 75,000 shares on 13 December 2007, 65,000 shares each on 8 December 2008 and 14 December 2009, 50,000 shares on 21 July 2010 and 170,000 shares on 17 December 2010, of which 117,000 options were vested in 2011 (2010: 69,000), and the respective fair value of the share-based payments recognised for the year ended 31 December 2011 was HK$1.0 million (2010: HK$0.3 million);
- Lincoln K K Leong was granted options in respect of 170,000 shares each on 12 December 2007, 9 December 2008, 10 December 2009 and 17 December 2010, of which 170,000 options were vested in 2011 (2010: 170,000), and the respective fair value of the share-based payments recognised for the year ended 31 December 2011 was HK$1.2 million (2010: HK$0.7 million);
- Andrew McCusker was granted options in respect of 170,000 shares each on 12 December 2007, 12 December 2008 and 10 December 2009, of which 170,000 options were vested in 2010, and the respective fair value of the share-based payments recognised for the year ended 31 December 2010 was HK$0.7 million;
- Gillian E Meller was granted options in respect of 55,000 shares on 12 December 2007, 70,000 shares on 11 December 2008, 65,000 shares on 10 December 2009 and 90,000 shares on 17 December 2010, of which 75,000 options were vested in 2011 (2010: 63,500), and the respective fair value of the share-based payments recognised for the year ended 31 December 2011 was HK$0.6 million (2010: HK$0.3 million);
- David C F Tang was granted options in respect of 65,000 shares each on 13 December 2007, 12 December 2008, 15 December 2009 and 17 December 2010, of which 65,000 options were vested in 2011 (2010: 65,000), and the respective fair value of the share-based payments recognised for the year ended 31 December 2011 was HK$0.5 million (2010: HK$0.3 million);
- Leonard B Turk was granted options in respect of 170,000 shares each on 12 December 2007, 9 December 2008 and 10 December 2009 and 127,500 shares on 17 December 2010, of which 155,500 options were vested in 2011 (2010: 170,000), and the respective fair value of the share-based payments recognised for the year ended 31 December 2011 was HK$1.1 million (2010: HK$0.7 million); and
- Jeny M C Yeung was granted options in respect of 75,000 shares on 12 December 2007 and 65,000 shares each on 10 December 2008, 10 December 2009 and 17 December 2010, of which 65,000 options were vested in 2011 (2010: 69,000), and the respective fair value of the share-based payments recognised for the year ended 31 December 2011 was HK$0.5 million (2010: HK$0.3 million).

Jay H Walder replaced C K Chow, who retired from the Company on 31 December 2011, as a Member of the Executive Directorate with effect from 1 January 2012. As a transitional arrangement, Jay H Walder was appointed Chief Executive Officer (Designate) during 1 November 2011 to 31 December 2011. The emolument of Jay H Walder during the year ended 31 December 2011 was HK$2.1 million. Jay H Walder was granted a derivative interest in respect of 300,000 shares in the Company within the meaning of Part XV of the Securities and Futures Ordinance. The derivative interest represents Jay H 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).

The details of Board Members' and Executive Directorate's interest in the Company's shares are disclosed in the Report of the Members of the Board and note 53.

(ii) The aggregate emoluments of Members of the Board and the Executive Directorate for the year pursuant to section 161 of the Hong Kong Companies Ordinance was HK$79.5 million (2010: HK$70.5 million).

(iii) Non-executive directors of the Company are not appointed for a specific term but are subject (save for those appointed pursuant to Section 8 of the Mass Transit Railway Ordinance (Chapter 556 of the Laws of Hong Kong)) to retirement by rotation and re-election at the Company's annual general meetings in accordance with Articles 87 and 88 of the Company's Articles of Association. Dr. Raymond Ch'ien Kuo-fung, a Member of the Board and the non-executive Chairman of the Company since 1998 and 2003 respectively, was re-appointed by the HKSAR Government as the non-executive Chairman of the Company with effect from 2 December 2009 until 31 December 2012.

All of the five individuals with the highest emoluments are Members of the Executive Directorate whose emoluments are disclosed above.

11 Remuneration of Members of the Board and the Executive Directorate *(continued)*

B Share Options

Options exercised and outstanding in respect of each Member of the Executive Directorate as at 31 December 2011 are set out in the Report of the Members of the Board. Details of the options granted to Members of the Executive Directorate are as follows:

(i) New Joiners Share Option Scheme

Under the New Joiners Share Option Scheme (the "New Option Scheme") as described in note 53A(i), Lincoln K K Leong and David C F Tang, Members of the Executive Directorate, were granted options to acquire 1,066,000 shares on 1 August 2003 and 213,000 shares on 15 May 2006 respectively.

Under the vesting terms of the New Option Scheme, Lincoln K K Leong must continue to beneficially own (i) at all times on and after 4 August 2004, at least 23,000 shares; and (ii) at all times on and after 4 August 2005, at least 46,000 shares, up to and including the date on which he has exercised his option in full or the date on which his option lapses (whichever is earlier).

(ii) 2007 Share Option Scheme

Under the 2007 Share Option Scheme (the "2007 Option Scheme") as described in note 53A(ii), all Members of the Executive Directorate were granted options to acquire shares in each year from 2007 to 2010. C K Chow was granted options to acquire 720,000 shares in 2007 and 470,000 shares each in 2008, 2009 and 2010. Russell J Black was granted options to acquire 170,000 shares in both 2007 and 2008 and 42,500 shares in 2009. William F K Chan and Lincoln K K Leong were each granted options to acquire 170,000 shares in each year from 2007 to 2010. T C Chew was granted options to acquire 85,000 shares in June 2009 and 170,000 shares each in December 2009 and 2010. Thomas H K Ho and Leonard B Turk were each granted options to acquire 170,000 shares in each of 2007, 2008 and 2009 and 127,500 shares in 2010. Andrew McCusker was granted options to acquire 170,000 shares in each of 2007, 2008 and 2009. Jacob C P Kam was granted options to acquire 75,000 shares in December 2007, 65,000 shares each in December 2008 and 2009, 50,000 shares in July 2010 and 170,000 shares in December 2010. Gillian E Meller was granted options to acquire 55,000 shares in 2007, 70,000 shares in 2008, 65,000 shares in 2009 and 90,000 shares in 2010. David C F Tang was granted options to acquire 65,000 shares each year from 2007 to 2010. Jeny M C Yeung was granted options to acquire 75,000 shares in 2007 and 65,000 shares each year from 2008 to 2010.

Under the vesting terms of the options granted each year from 2007 to 2010, options granted will be evenly vested in respect of their underlying shares over a period of three years from the date of offer to grant such options (note 11A(i)).

12 Profit on Property Developments

Profit on property developments comprises:

in HK$ million	**2011**	2010
Transfer from deferred income on:		
– payments received from developers (note 48)	**468**	–
– sharing in kind (note 29B)	**–**	17
Share of surplus from development	**3,889**	990
Income recognised from sharing in kind	**572**	3,026
Miscellaneous income net of other overhead costs	**5**	1
	4,934	4,034

13 Depreciation and Amortisation

Depreciation and amortisation comprise:

in HK$ million	**2011**	2010
Depreciation charge on assets relating to:		
Hong Kong transport operations	**2,517**	2,517
Hong Kong station commercial business	**121**	93
Property rental and management businesses	**11**	9
Railway subsidiaries outside of Hong Kong	**46**	24
Other businesses	**62**	63
	2,757	2,706
Amortisation charge on service concession assets relating to:		
KCRC Rail Merger	**434**	400
Railway subsidiaries outside of Hong Kong	**169**	14
	603	414
Utilisation of government subsidy for Shenzhen Metro Longhua Line operation	**(154)**	–
	449	414
	3,206	3,120

14 Variable Annual Payment

Commencing after the third year from the Appointed Day of the Rail Merger, i.e. 2 December 2010, the Company is obliged to pay variable annual payments to KCRC, calculated on a tiered basis by reference to the revenue generated from the operation of the KCRC service concession over certain thresholds. For the year ended 31 December 2011, the variable annual payment amounted to HK$647 million (2010: HK$45 million).

15 Interest and Finance Charges

in HK$ million	2011		2010	
Interest expenses in respect of:				
Bank loans, overdrafts and capital market instruments wholly repayable within 5 years	**315**		560	
Bank loans and capital market instruments not wholly repayable within 5 years	**268**		206	
Obligations under service concession	**723**		721	
Other obligations (note 24E)	**16**		15	
Finance charges	**18**		27	
Exchange loss/(gain)	**32**		(37)	
		1,372		1,492
Utilisation of government subsidy for Shenzhen Metro Longhua Line operation		**(133)**		–
Derivative financial instruments:				
Fair value hedges	**(15)**		–	
Cash flow hedges:				
– transfer from hedging reserve	**63**		86	
– ineffective portion	**–**		(1)	
		48		85
Interest expenses capitalised		**(176)**		(178)
		1,111		1,399
Interest income in respect of:				
Deposits with banks and other financial institutions	**(199)**		(114)	
Investment in bank medium term notes	**(45)**		(34)	
Loans to associates	**(1)**		–	
		(245)		(148)
Interest income capitalised		**80**		78
		946		1,329
Accreted interest on loan to a property developer		**(25)**		(92)
		921		1,237

During the year ended 31 December 2011, interest expenses capitalised were calculated on a monthly basis at the pre-determined cost of borrowings and/or the relevant group company's net borrowing cost which varied from 0.8% to 5.8% per annum (2010: 0.6% to 5.3% per annum), while interest income capitalised was calculated on a monthly basis at the average return from deposits and investments in bank medium term notes which varied from 1.1% to 1.6% per annum (2010: 0.8% to 1.2% per annum).

During the year ended 31 December 2011, interest and finance charges net of interest expenses capitalised in relation to the Shenzhen Metro Longhua Line was HK$133 million (2010: HK$3 million). This amount was fully offset by the subsidy received from the Shenzhen Municipal Government in 2011.

During the same year, the gain resulting from fair value changes of the underlying financial assets and liabilities being hedged was HK$24 million (2010: HK$119 million of loss) and the loss resulting from fair value changes of hedging instruments comprising interest rate and cross currency swaps was HK$9 million (2010: HK$119 million of gain), resulting in a net gain of HK$15 million (2010: nil).

16 Share of Profits of Non-controlled Subsidiaries and Associates

Share of profits of non-controlled subsidiaries and associates comprises:

in HK$ million	2011	2010
Share of profit before taxation of non-controlled subsidiaries (note 31)	**208**	148
Share of profit before taxation of associates (note 33)	**152**	22
	360	170
Share of income tax of non-controlled subsidiaries (note 31)	**(26)**	(22)
Share of income tax of associates (note 33)	**(37)**	(9)
	297	139

17 Income Tax

A Income tax in the consolidated profit and loss account represents:

in HK$ million	2011	2010
Current tax		
– Provision for Hong Kong Profits Tax at 16.5% (2010: 16.5%) for the year	**1,619**	1,495
– Overseas tax for the year	**56**	93
	1,675	1,588
Deferred tax		
– Origination and reversal of temporary differences on:		
– investment property revaluation	**840**	672
– (provision)/utilisation of tax losses	**(9)**	10
– depreciation allowances in excess of related depreciation	**316**	287
– provision and others	**(1)**	33
	1,146	1,002
	2,821	2,590

The provision for Hong Kong Profits Tax for the year ended 31 December 2011 is calculated at 16.5% (2010: 16.5%) on the estimated assessable profits for the year after deducting accumulated tax losses brought forward, if any. Current tax for the Mainland of China and overseas subsidiaries is charged at the appropriate current rates of taxation ruling in the relevant countries.

Provision for deferred tax on temporary differences arising in Hong Kong is calculated at the Hong Kong Profits Tax rate at 16.5% (2010: 16.5%) while that arising in the Mainland of China and overseas is calculated at the appropriate current rates of taxation ruling in the relevant countries.

B Reconciliation between tax expense and accounting profit at applicable tax rates:

	2011		2010	
	HK$ million	%	HK$ million	%
Profit before taxation	**17,669**		14,762	
Notional tax on profit before taxation, calculated at the rates applicable to profits in the tax jurisdictions concerned	**2,957**	**16.7**	2,451	16.6
Tax effect of non-deductible expenses	**106**	**0.6**	200	1.4
Tax effect of non-taxable revenue	**(215)**	**(1.2)**	(90)	(0.6)
Tax effect of unused tax losses not recognised	**(27)**	**(0.2)**	29	0.2
Actual tax expenses	**2,821**	**15.9**	2,590	17.6

18 Profit Attributable to Equity Shareholders

A The consolidated profit attributable to equity shareholders includes a profit of HK$14,415 million (2010: HK$11,878 million) which has been dealt with in the accounts of the Company. Details of dividend paid and payable to equity shareholders of the Company are set out in note 19.

B Profit attributable to equity shareholders of the Company arising from underlying businesses represents profits excluding impact of investment property revaluation net of related deferred tax, calculated as follows:

in HK$ million	2011	2010
Profit attributable to equity shareholders	**14,716**	12,059
Investment property revaluation	**(5,088)**	(4,074)
Deferred tax on investment property revaluation (note 17A)	**840**	672
	10,468	8,657

Within the profit arising from underlying businesses, the amount attributable to property development has taken into account the effect of related income tax expense of HK$720 million (2010: HK$785 million) and net interest income of HK$11 million (2010: HK$11 million) in relation to the loan to a property developer.

19 Dividends

During the year, dividends paid and proposed to equity shareholders of the Company comprised:

in HK$ million	2011	2010
Dividends paid/payable attributable to the year		
– Interim dividend of 25 cents (2010: 14 cents) per share approved and paid during the year	**1,446**	807
– Final dividend proposed after the balance sheet date of 51 cents (2010: 45 cents) per share	**2,950**	2,598
	4,396	3,405
Dividends paid attributable to the previous year		
– Final dividend of 45 cents (2009: 38 cents) per share approved and paid during the year	**2,598**	2,177

The final dividend proposed after the balance sheet date has not been recognised as a liability at the balance sheet date. For the dividends attributable to the year ended 31 December 2010, scrip dividend elections were offered to all shareholders except shareholders with registered addresses in the United States of America or any of its territories or possessions. No scrip dividend election was offered for the dividends attributable to the year ended 31 December 2011. Details of dividends paid to the Company's majority shareholder, The Financial Secretary Incorporated, are disclosed in note 57N.

20 Earnings Per Share

A Basic Earnings Per Share

The calculation of basic earnings per share is based on the profit for the year attributable to equity shareholders of HK$14,716 million (2010: HK$12,059 million) and the weighted average number of ordinary shares of 5,780,030,171 in issue during the year (2010: 5,751,035,100), calculated as follows:

	2011	2010
Issued ordinary shares at 1 January	**5,772,563,031**	5,727,833,692
Effect of scrip dividends issued	**6,461,157**	20,911,122
Effect of share options exercised	**1,005,983**	2,290,286
Weighted average number of ordinary shares at 31 December	**5,780,030,171**	5,751,035,100

20 Earnings Per Share *(continued)*

B Diluted Earnings Per Share

The calculation of diluted earnings per share is based on the profit for the year attributable to equity shareholders of HK$14,716 million (2010: HK$12,059 million) and the weighted average number of ordinary shares of 5,783,905,064 in issue during the year (2010: 5,756,548,816) after adjusting for the number of dilutive potential ordinary shares under the employee share option schemes, calculated as follows:

	2011	2010
Weighted average number of ordinary shares at 31 December	**5,780,030,171**	5,751,035,100
Effect of dilutive potential shares under the Company's share option schemes	**3,874,893**	5,513,716
Weighted average number of ordinary shares (diluted) at 31 December	**5,783,905,064**	5,756,548,816

C Both basic and diluted earnings per share would have been HK$1.81 (2010: HK$1.51) if the calculation is based on profit attributable to equity shareholders arising from underlying businesses of HK$10,468 million (2010: HK$8,657 million) (note 18B).

21 Segmental Information

The Group manages its businesses by the various business executive committees. In a manner consistent with the way in which information is reported internally to the Group's most senior executive management for the purposes of resource allocation and performance assessment, the Group has identified the following six reportable segments:

(i) Hong Kong transport operations: The provision of passenger operation and related services on the urban mass transit railway system in Hong Kong, the Airport Express serving both the Hong Kong International Airport and the AsiaWorld-Expo at Chek Lap Kok, cross-boundary railway connection with the border of Mainland of China at Lo Wu and Lok Ma Chau, light rail and bus feeder with railway system in the north-west New Territories and intercity railway transport with certain cities in the Mainland of China.

(ii) Hong Kong station commercial business: Commercial activities including the letting of advertising, retail and car parking space at railway stations, the provision of telecommunication and bandwidth services in railway premises and other commercial activities within the Hong Kong transport operations network.

(iii) Property rental and management businesses: The letting of retail, office and car parking space and the provision of estate management services in Hong Kong and the Mainland of China.

(iv) Railway subsidiaries outside of Hong Kong: The operation and maintenance of mass transit railway systems including station commercial activities outside of Hong Kong.

(v) Other businesses: Businesses not directly relating to transport operations or properties such as Ngong Ping 360, which comprises cable car operations in Tung Chung and related businesses at the Ngong Ping Theme Village, railway consultancy business and the provision of project management services to HKSAR Government and KCRC.

(vi) Property developments: Property development activities at locations relating to the railway systems.

During the year ended 31 December 2011, the Group re-categorised certain business activities not directly relating to transport operations or properties including Ngong Ping 360, railway consultancy business and the provision of project management services to the HKSAR Government and KCRC under a new business segment "Other Businesses". The re-categorisation amounted to HK$925 million in revenue and HK$751 million in expenses for the year ended 31 December 2010. Accordingly, the comparatives of the consolidated profit and loss account and segmental information are reclassified.

21 Segmental Information *(continued)*

The results of the reportable segments and reconciliation to the corresponding consolidated totals in the accounts are shown below:

in HK$ million	Hong Kong transport operations	Hong Kong station commercial business	Property rental and manage-ment businesses	Railway subsidiaries outside of Hong Kong	Other businesses	Property develop-ments	Total
2011							
Revenue	**13,509**	**3,422**	**3,215**	**12,279**	**998**	**–**	**33,423**
Operating expenses before depreciation, amortisation and variable annual payment	**(7,354)**	**(358)**	**(721)**	**(11,830)**	**(913)**	**–**	**(21,176)**
	6,155	**3,064**	**2,494**	**449**	**85**	**–**	**12,247**
Profit on property developments	**–**	**–**	**–**	**–**	**–**	**4,934**	**4,934**
Operating profit before depreciation, amortisation and variable annual payment	**6,155**	**3,064**	**2,494**	**449**	**85**	**4,934**	**17,181**
Depreciation and amortisation	**(2,934)**	**(138)**	**(11)**	**(61)**	**(62)**	**–**	**(3,206)**
Variable annual payment	**(520)**	**(127)**	**–**	**–**	**–**	**–**	**(647)**
	2,701	**2,799**	**2,483**	**388**	**23**	**4,934**	**13,328**
Project studies and business development expenses							**(123)**
Operating profit before interest and finance charges							**13,205**
Interest and finance charges							**(921)**
Investment property revaluation			**5,088**				**5,088**
Share of profits of non-controlled subsidiaries and associates				**115**	**182**		**297**
Income tax							**(2,821)**
Profit for the year ended 31 December 2011							**14,848**
Assets							
Operational assets *	**73,588**	**1,726**	**52,332**	**3,714**	**1,124**	**1,211**	**133,695**
Assets under construction	**2,030**	**18**	**–**	**–**	**–**	**–**	**2,048**
Service concession assets	**16,169**	**–**	**–**	**7,759**	**–**	**–**	**23,928**
Property management rights	**–**	**–**	**31**	**–**	**–**	**–**	**31**
Railway construction in progress	**3,566**	**–**	**–**	**–**	**–**	**–**	**3,566**
Property development in progress	**–**	**–**	**–**	**–**	**–**	**11,964**	**11,964**
Deferred expenditure	**–**	**–**	**14**	**–**	**–**	**–**	**14**
Deferred tax assets	**–**	**19**	**3**	**5**	**–**	**–**	**27**
Investments in securities	**–**	**–**	**–**	**–**	**348**	**–**	**348**
Properties held for sale	**–**	**–**	**–**	**–**	**–**	**3,757**	**3,757**
Interests in non-controlled subsidiaries	**–**	**–**	**–**	**–**	**579**	**–**	**579**
Interests in associates	**–**	**–**	**–**	**948**	**–**	**–**	**948**
	95,353	**1,763**	**52,380**	**12,426**	**2,051**	**16,932**	**180,905**
Unallocated assets							**16,968**
Total assets							**197,873**

21 Segmental Information *(continued)*

in HK$ million	Hong Kong transport operations	Hong Kong station commercial business	Property rental and management businesses	Railway subsidiaries outside of Hong Kong	Other businesses	Property developments	Total
2011							
Liabilities							
Segment liabilities	**9,080**	**988**	**1,422**	**2,987**	**928**	**3,351**	**18,756**
Obligations under service concession	**10,557**	**–**	**–**	**167**	**–**	**–**	**10,724**
Deferred income	**–**	**47**	**–**	**288**	**–**	**68**	**403**
	19,637	**1,035**	**1,422**	**3,442**	**928**	**3,419**	**29,883**
Unallocated liabilities							**38,945**
Total liabilities							**68,828**
Other Information							
Capital expenditure on:							
Operational assets	**57**	**16**	**11**	**90**	**14**	**1**	**189**
Assets under construction	**1,296**	**83**	**–**	**110**	**–**	**–**	**1,489**
Investment properties	**–**	**–**	**1,040**	**–**	**–**	**–**	**1,040**
Service concession assets	**630**	**–**	**–**	**2,122**	**–**	**–**	**2,752**
Railway construction in progress	**5,585**	**–**	**–**	**–**	**–**	**–**	**5,585**
Property development in progress	**–**	**–**	**–**	**–**	**–**	**3,045**	**3,045**
Non-cash expenses other than depreciation and amortisation	**28**	**2**	**–**	**–**	**2**	**–**	**32**

* Operational assets include property, plant and equipment and other assets employed in the operations of individual business segments.

21 Segmental Information *(continued)*

in HK$ million	Hong Kong transport operations	Hong Kong station commercial business	Property rental and manage-ment businesses	Railway subsidiaries outside of Hong Kong	Other businesses	Property develop-ments	Total
2010							
Revenue	12,635	2,853	2,961	10,144	925	–	29,518
Operating expenses before depreciation, amortisation and variable annual payment	(6,821)	(294)	(654)	(9,865)	(751)	–	(18,385)
	5,814	2,559	2,307	279	174	–	11,133
Profit on property developments	–	–	–	–	–	4,034	4,034
Operating profit before depreciation, amortisation and variable annual payment	5,814	2,559	2,307	279	174	4,034	15,167
Depreciation and amortisation	(2,901)	(109)	(9)	(38)	(63)	–	(3,120)
Variable annual payment	(36)	(9)	–	–	–	–	(45)
	2,877	2,441	2,298	241	111	4,034	12,002
Project studies and business development expenses							(216)
Operating profit before interest and finance charges							11,786
Interest and finance charges							(1,237)
Investment property revaluation			4,074				4,074
Share of profits of non-controlled subsidiaries and associates				13	126		139
Income tax							(2,590)
Profit for the year ended 31 December 2010							12,172
Assets							
Operational assets *	73,920	1,557	46,093	2,411	1,255	652	125,888
Assets under construction	2,161	10	–	26	–	–	2,197
Service concession assets	15,963	–	–	5,504	–	–	21,467
Property management rights	–	–	31	–	–	–	31
Property development in progress	–	–	–	–	–	9,128	9,128
Deferred expenditure	1,021	–	21	–	–	37	1,079
Deferred tax assets	–	1	5	3	–	–	9
Investments in securities	–	–	–	–	285	–	285
Properties held for sale	–	–	–	–	–	1,936	1,936
Loan to a property developer	–	–	–	–	–	1,975	1,975
Interests in non-controlled subsidiaries	–	–	–	–	541	–	541
Interests in associates	–	–	–	836	–	–	836
	93,065	1,568	46,150	8,780	2,081	13,728	165,372
Unallocated assets							16,293
Total assets							181,665

21 Segmental Information *(continued)*

in HK$ million	Hong Kong transport operations	Hong Kong station commercial business	Property rental and management businesses	Railway subsidiaries outside of Hong Kong	Other businesses	Property developments	Total
2010							
Liabilities							
Segment liabilities	10,578	921	1,241	2,206	745	1,357	17,048
Obligations under service concession	10,592	–	–	157	–	–	10,749
Deferred income	–	37	–	–	–	568	605
	21,170	958	1,241	2,363	745	1,925	28,402
Unallocated liabilities							35,970
Total liabilities							64,372
Other Information							
Capital expenditure on:							
Operational assets	65	3	14	95	9	1	187
Assets under construction	1,561	142	–	24	2	–	1,729
Investment properties	–	–	247	–	–	–	247
Service concession assets	566	–	–	1,757	–	–	2,323
Railway construction in progress	3,462	–	–	–	–	–	3,462
Property development in progress	–	–	–	–	–	4,372	4,372
Non-cash expenses other than depreciation and amortisation	44	2	–	4	–	–	50

* Operational assets include property, plant and equipment and other assets employed in the operations of individual business segments.

Unallocated assets and liabilities mainly comprise cash, bank balances and deposits, investments in securities, derivative financial assets and liabilities, interest-bearing loans and borrowings and deferred tax liabilities.

The following table sets out information about the geographical location of the Group's revenue from external customers and the Group's fixed assets, property management rights, railway construction in progress, property development in progress, deferred expenditure and interests in non-controlled subsidiaries and associates ("specified non-current assets"). The geographical location of customers is based on the location at which the services were provided or goods were delivered. The geographical location of the specified non-current assets is based on the physical location of the asset, in the case of property, plant and equipment, railway construction in progress and property development in progress; the location of the proposed capital project, in the case of deferred expenditure; the location of the operation to which they are related, in the case of service concession assets and property management rights; and the location of operation, in the case of interests in non-controlled subsidiaries and associates.

	Revenue from external customers		Specified non-current assets	
in HK$ million	**2011**	2010	**2011**	2010
Hong Kong (place of domicile)	**20,951**	19,177	**157,615**	149,073
Australia	**8,927**	7,239	**265**	123
Mainland of China	**328**	175	**11,065**	6,268
Sweden	**3,166**	2,858	**145**	151
Other countries	**51**	69	**80**	57
	12,472	10,341	**11,555**	6,599
	33,423	29,518	**169,170**	155,672

22 Other Comprehensive Income

A Tax effects relating to each component of other comprehensive income of the Group are shown below:

in HK$ million	2011 Before-tax amount	2011 Tax benefit/ (expense)	2011 Net-of-tax amount	2010 Before-tax amount	2010 Tax benefit/ (expense)	2010 Net-of-tax amount
Exchange differences on translation of:						
– Financial statements of overseas subsidiaries	**146**	**–**	**146**	141	–	141
– Non-controlling interests	**(1)**	**–**	**(1)**	16	–	16
	145	**–**	**145**	157	–	157
Cash flow hedges: net movement in hedging reserve	**(14)**	**2**	**(12)**	(31)	5	(26)
Self-occupied land and building: net movement in fixed assets revaluation reserve	**564**	**(93)**	**471**	341	(56)	285
Other comprehensive income	**695**	**(91)**	**604**	467	(51)	416

B The changes in each component of equity arising from transactions recognised in other comprehensive income of the Group are as follows:

in HK$ million	2011	2010
Exchange reserve		
Exchange differences on translation of financial statements of overseas subsidiaries	**146**	141
Hedging reserve		
Effective portion of changes in fair value of hedging instruments recognised during the year	**(64)**	(104)
Amounts transferred to initial carrying amount of hedged items	**(8)**	(12)
Transferred to profit or loss:		
– Interest and finance charges (note 15)	**63**	86
– Other expenses (note 10E)	**(5)**	(1)
Net deferred tax credited/(debited) to other comprehensive income resulting from:		
– Changes in fair value of hedging instruments recognised during the year	**11**	17
– Amounts transferred to initial carrying amount of hedged items	**1**	2
– Transferred to profit or loss	**(10)**	(14)
Net movement during the year recognised in other comprehensive income	**(12)**	(26)
Fixed assets revaluation reserve		
Changes in fair value recognised during the year	**564**	341
Net deferred tax debited to other comprehensive income resulting from changes in fair value recognised during the year	**(93)**	(56)
Net movement during the year recognised in other comprehensive income	**471**	285

23 Investment Properties

Movements and analysis of the Group's and the Company's investment properties, all of which being held in Hong Kong and carried at fair value, are as follows:

	The Group		The Company	
in HK$ million	**2011**	2010	**2011**	2010
Cost or Valuation				
At 1 January	**45,314**	40,993	**44,166**	39,879
Additions	**1,040**	247	**1,033**	229
Change in fair value	**5,088**	4,074	**5,077**	4,058
Transfer from deferred expenditure (note 30)	**11**	–	**11**	–
At 31 December	**51,453**	45,314	**50,287**	44,166
Long leases	**74**	1,589	**74**	1,589
Medium-term leases	**51,379**	43,725	**50,213**	42,577
	51,453	45,314	**50,287**	44,166

All investment properties of the Group were revalued at open market value at 31 December 2011 by an independent firm of surveyors, Jones Lang LaSalle Limited, who have among their staff Members of the Hong Kong Institute of Surveyors. The valuations are based on a "term and reversion basis", which capitalises the existing and reversionary net rental income having regard to market valuation checks on comparable sales and yields. The net increase in fair value of HK$5,088 million (2010: HK$4,074 million) arising from the revaluation has been credited to the consolidated profit and loss account.

The Group's future minimum lease receipts in respect of investment properties under non-cancellable operating leases are disclosed together with those in respect of other properties under note 24D.

24 Other Property, Plant and Equipment

The Group

in HK$ million	Leasehold land	Self-occupied land and buildings	Civil works	Plant and equipment	Assets under construction	Total
2011						
Cost or Valuation						
At 1 January 2011	732	2,403	46,642	61,534	2,197	113,508
Additions	–	–	3	186	1,489	1,678
Capitalisation adjustments *	–	–	(2)	(4)	–	(6)
Disposals/write-offs	–	–	(1)	(207)	(3)	(211)
Surplus on revaluation (note 22B)	–	491	–	–	–	491
Reclassification within other property, plant and equipment	–	–	5	(6)	1	–
Transfer to additional concession property (note 25)	–	–	–	(5)	(10)	(15)
Other assets commissioned	–	–	4	1,623	(1,627)	–
Exchange differences	–	–	–	(5)	1	(4)
At 31 December 2011	732	2,894	46,651	63,116	2,048	115,441
At Cost	732	–	46,651	63,116	2,048	112,547
At 31 December 2011 Valuation	–	2,894	–	–	–	2,894
Aggregate depreciation						
At 1 January 2011	191	–	5,410	30,631	–	36,232
Charge for the year	13	73	403	2,268	–	2,757
Written back on disposal	–	–	(1)	(161)	–	(162)
Written back on revaluation (note 22B)	–	(73)	–	–	–	(73)
At 31 December 2011	204	–	5,812	32,738	–	38,754
Net book value at 31 December 2011	528	2,894	40,839	30,378	2,048	76,687

24 Other Property, Plant and Equipment *(continued)*

The Group

in HK$ million	Leasehold land	Self-occupied land and buildings	Civil works	Plant and equipment	Assets under construction	Total
2010						
Cost or Valuation						
At 1 January 2010	732	2,120	46,507	61,026	1,366	111,751
Additions	–	–	–	187	1,729	1,916
Capitalisation adjustments *	–	–	(9)	(2)	–	(11)
Disposals/write-offs	–	–	(1)	(360)	(19)	(380)
Surplus on revaluation (note 22B)	–	283	–	–	–	283
Reclassification within other property, plant and equipment	–	–	12	(31)	19	–
Transfer to additional concession property (note 25)	–	–	–	(6)	(68)	(74)
Other assets commissioned	–	–	133	699	(832)	–
Exchange differences	–	–	–	21	2	23
At 31 December 2010	732	2,403	46,642	61,534	2,197	113,508
At Cost	732	–	46,642	61,534	2,197	111,105
At 31 December 2010 Valuation	–	2,403	–	–	–	2,403
Aggregate depreciation						
At 1 January 2010	178	–	5,008	28,721	–	33,907
Charge for the year	13	58	403	2,232	–	2,706
Written back on disposal	–	–	(1)	(324)	–	(325)
Written back on revaluation (note 22B)	–	(58)	–	–	–	(58)
Exchange differences	–	–	–	2	–	2
At 31 December 2010	191	–	5,410	30,631	–	36,232
Net book value at 31 December 2010	541	2,403	41,232	30,903	2,197	77,276

* Capitalisation adjustments relate to adjustments on the cost of assets to their final contract values after finalisation of contract claims with contractors.

Depreciation charge for the year ended 31 December 2011 was HK$2,757 million (2010: HK$2,706 million), comprising depreciation for the year of HK$2,757 million (2010: HK$2,707 million) less nil (2010: HK$1 million) capitalisation adjustment.

24 Other Property, Plant and Equipment *(continued)*

The Company

in HK$ million	Leasehold land	Self-occupied land and buildings	Civil works	Plant and equipment	Assets under construction	Total
2011						
Cost or Valuation						
At 1 January 2011	732	2,403	46,642	60,529	2,161	112,467
Additions	–	–	3	76	1,345	1,424
Capitalisation adjustments *	–	–	(2)	(4)	–	(6)
Disposals/write-offs	–	–	(1)	(205)	(3)	(209)
Surplus on revaluation (note 22B)	–	491	–	–	–	491
Reclassification within other property, plant and equipment	–	–	5	(6)	1	–
Transfer to additional concession property (note 25)	–	–	–	(5)	(10)	(15)
Other assets commissioned	–	–	4	1,460	(1,464)	–
At 31 December 2011	732	2,894	46,651	61,845	2,030	114,152
At Cost	732	–	46,651	61,845	2,030	111,258
At 31 December 2011 Valuation	–	2,894	–	–	–	2,894
Aggregate depreciation						
At 1 January 2011	191	–	5,410	30,021	–	35,622
Charge for the year	14	73	403	2,189	–	2,679
Written back on disposal	–	–	(1)	(161)	–	(162)
Written back on revaluation (note 22B)	–	(73)	–	–	–	(73)
At 31 December 2011	205	–	5,812	32,049	–	38,066
Net book value at 31 December 2011	527	2,894	40,839	29,796	2,030	76,086

24 Other Property, Plant and Equipment *(continued)*

The Company

in HK$ million	Leasehold land	Self-occupied land and buildings	Civil works	Plant and equipment	Assets under construction	Total
2010						
Cost or Valuation						
At 1 January 2010	732	2,120	46,507	60,177	1,350	110,886
Additions	–	–	–	89	1,678	1,767
Capitalisation adjustments *	–	–	(9)	(2)	–	(11)
Disposals/write-offs	–	–	(1)	(364)	(19)	(384)
Surplus on revaluation (note 22B)	–	283	–	–	–	283
Reclassification within other property, plant and equipment	–	–	12	(31)	19	–
Transfer to additional concession property (note 25)	–	–	–	(6)	(68)	(74)
Other assets commissioned	–	–	133	666	(799)	–
At 31 December 2010	732	2,403	46,642	60,529	2,161	112,467
At Cost	732	–	46,642	60,529	2,161	110,064
At 31 December 2010 Valuation	–	2,403	–	–	–	2,403
Aggregate depreciation						
At 1 January 2010	178	–	5,008	28,167	–	33,353
Charge for the year	13	58	403	2,177	–	2,651
Written back on disposal	–	–	(1)	(323)	–	(324)
Written back on revaluation (note 22B)	–	(58)	–	–	–	(58)
At 31 December 2010	191	–	5,410	30,021	–	35,622
Net book value at 31 December 2010	541	2,403	41,232	30,508	2,161	76,845

* Capitalisation adjustments relate to adjustments of the cost of assets to their final contract values after finalisation of contract claims with contractors.

Depreciation charge for the year ended 31 December 2011 was HK$2,679 million (2010: HK$2,651 million), comprising depreciation for the year of HK$2,679 million (2010: HK$2,652 million) less nil (2010: HK$1 million) of capitalisation adjustment.

24 Other Property, Plant and Equipment *(continued)*

A The lease term of the Group's and the Company's leasehold land is analysed as follows:

The Group and the Company

in HK$ million	2011	2010
At net book value		
– long leases	142	146
– medium-term leases	385	395
	527	541

The lease of the land on which civil works as well as plant and equipment are situated for Hong Kong transport operations was granted to the Company under a running line lease which is coterminous with the Company's franchise to operate the mass transit railway under the Operating Agreement (notes 57A, 57B and 57C).

Under the terms of the lease, the Company undertakes to keep and maintain all the leased areas, including underground and overhead structures, at its own cost. With respect to parts of the railway situated in structures where access is shared with other users, such as the Lantau Fixed Crossing, the Company's obligation for maintenance is limited to the railway only. All maintenance costs incurred under the terms of the lease have been dealt with as expenses relating to Hong Kong transport operations in the consolidated profit and loss account.

B All of the Group's self-occupied land and buildings are held in Hong Kong under medium-term leases and carried at fair value. All self-occupied land and buildings were revalued at open market value on an existing use basis at 31 December 2011 by an independent firm of surveyors, Jones Lang LaSalle Limited, who have among their staff Members of the Hong Kong Institute of Surveyors. The valuation resulted in a revaluation surplus of HK$564 million (2010: HK$341 million), which, net of deferred tax provision of HK$93 million (2010: HK$56 million) (note 22B), has been recognised in other comprehensive income and accumulated in fixed assets revaluation reserve account (note 51).

The carrying amount of the self-occupied land and buildings at 31 December 2011 would have been HK$874 million (2010: HK$899 million) had the land and buildings been stated at cost less accumulated depreciation.

C Assets under construction include capital works on operating railway.

D The Group leases out investment properties and station kiosks, including duty free shops, under operating leases. The leases typically run for an initial period of one to ten years, with an option to renew the lease after that date, at which time all terms will be renegotiated. Lease payments are usually adjusted annually to reflect market rentals. Certain leases above carry additional rental based on turnover, some of which are with reference to thresholds. Lease incentives granted are amortised in the consolidated profit and loss account as an integral part of the net lease payment receivable.

The gross carrying amounts of investment properties of the Group and the Company held for use in operating leases were HK$51,453 million (2010: HK$45,314 million) and HK$50,287 million (2010: HK$44,166 million) respectively. The gross carrying amounts of station kiosks of the Group and the Company held for use in operating leases were HK$585 million (2010: HK$551 million) and the related accumulated depreciation charges were HK$221 million (2010: HK$190 million).

Total future minimum lease receipts under non-cancellable operating leases are receivable as follows:

	The Group		The Company	
in HK$ million	2011	2010	2011	2010
Within 1 year	4,101	3,846	3,811	3,592
After 1 year but within 5 years	5,777	5,486	4,963	4,664
Later than 5 years	336	391	239	74
	10,214	9,723	9,013	8,330

24 Other Property, Plant and Equipment *(continued)*

E In March 2003, the Group entered into a series of structured transactions with unrelated third parties to lease out and lease back certain of its passenger cars ("Lease Transaction") involving a total original cost of HK$2,562 million and a total net book value of HK$1,674 million as at 31 March 2003. Under the Lease Transaction, the Group has leased the assets to institutional investors in the United States (the "Investors"), who have prepaid all the rentals in relation to the lease agreement. Simultaneously, the Group has leased the assets back from the Investors based on terms ranging from 21 to 29 years with an obligation to pay rentals in accordance with a pre-determined payment schedule. The Group has an option to purchase the Investors' leasehold interest in the assets at the expiry of the lease term for fixed amounts. Part of the rental prepayments received from the Investors has been invested in debt securities to meet the Group's rental obligations and the amount payable for exercising the purchase option under the Lease Transaction. The Group has an obligation to replace these debt securities with other debt securities in the event those securities do not meet certain credit ratings requirements. In addition, the Group has provided standby letters of credit to the Investors to cover additional amounts payable by the Group in the event the transactions are terminated prior to the expiry of the lease terms.

The Group retains legal title to the assets and there are no restrictions on the Group's ability to utilise these assets in the operation of the railway business.

As a result of the Lease Transaction, an amount of approximately HK$3,688 million was received in an investment account and was used to purchase debt securities ("Defeasance Securities") to be used to settle the long-term lease payments with an estimated net present value in March 2003 of approximately HK$3,533 million. This resulted in the Group having received in 2003 an amount of HK$141 million net of costs. As the Group is not able to control the investment account in pursuit of its own objectives and its obligations to pay the lease payments are funded by the proceeds of the above investments, those obligations and investments in the Defeasance Securities were not recognised in March 2003 as liabilities and assets of the Group. The net amount of cash received was accounted for as deferred income by the Group.

During 2008, credit ratings of some of these Defeasance Securities were downgraded and subsequently these securities were replaced by standby letters of credit issued to the relevant Investors to support the corresponding payment obligations.

25 Service Concession Assets

Movements and analysis of the Group and the Company's service concession assets are as follows:

The Group

	KCRC Rail Merger				
in HK$ million	Initial concession property	Additional concession property	Shenzhen Longhua Line	Stockholm Metro	Total
2011					
Cost					
At 1 January 2011	**15,226**	**1,818**	**5,429**	**91**	**22,564**
Net additions during the year	**–**	**630**	**2,122**	**–**	**2,752**
Disposal	**–**	**(5)**	**–**	**–**	**(5)**
Transfer from other property, plant and equipment (note 24)	**–**	**15**	**–**	**–**	**15**
Exchange differences	**–**	**–**	**304**	**(3)**	**301**
At 31 December 2011	**15,226**	**2,458**	**7,855**	**88**	**25,627**
Accumulated amortisation					
At 1 January 2011	**939**	**142**	**2**	**14**	**1,097**
Charge for the year	**304**	**130**	**156**	**13**	**603**
Written-off on disposal	**–**	**–**	**–**	**–**	**–**
Exchange differences	**–**	**–**	**1**	**(2)**	**(1)**
At 31 December 2011	**1,243**	**272**	**159**	**25**	**1,699**
Net book value at 31 December 2011	**13,983**	**2,186**	**7,696**	**63**	**23,928**

25 Service Concession Assets *(continued)*

The Group

in HK$ million	KCRC Rail Merger Initial concession property	KCRC Rail Merger Additional concession property	Shenzhen Longhua Line	Stockholm Metro	Total
2010					
Cost					
At 1 January 2010	15,226	1,183	3,539	88	20,036
Net additions during the year	–	566	1,757	–	2,323
Disposal	–	(5)	–	–	(5)
Transfer from other property, plant and equipment (note 24)	–	74	–	–	74
Exchange differences	–	–	133	3	136
At 31 December 2010	15,226	1,818	5,429	91	22,564
Accumulated amortisation					
At 1 January 2010	634	50	–	1	685
Charge for the year	305	95	2	12	414
Written-off on disposal	–	(3)	–	–	(3)
Exchange differences	–	–	–	1	1
At 31 December 2010	939	142	2	14	1,097
Net book value at 31 December 2010	14,287	1,676	5,427	77	21,467

The Company

in HK$ million	Initial concession property	Additional concession property	Total
2011			
Cost			
At 1 January 2011	**15,226**	**1,818**	**17,044**
Net additions during the year	**–**	**630**	**630**
Disposal	**–**	**(5)**	**(5)**
Transfer from other property, plant and equipment (note 24)	**–**	**15**	**15**
At 31 December 2011	**15,226**	**2,458**	**17,684**
Accumulated amortisation			
At 1 January 2011	**939**	**142**	**1,081**
Charge for the year	**304**	**130**	**434**
Written-off on disposal	**–**	**–**	**–**
At 31 December 2011	**1,243**	**272**	**1,515**
Net book value at 31 December 2011	**13,983**	**2,186**	**16,169**

25 Service Concession Assets *(continued)*

The Company

in HK$ million	Initial concession property	Additional concession property	Total
2010			
Cost			
At 1 January 2010	15,226	1,183	16,409
Net additions during the year	–	566	566
Disposal	–	(5)	(5)
Transfer from other property, plant and equipment (note 24)	–	74	74
At 31 December 2010	15,226	1,818	17,044
Accumulated amortisation			
At 1 January 2010	634	50	684
Charge for the year	305	95	400
Written-off on disposal	–	(3)	(3)
At 31 December 2010	939	142	1,081
Net book value at 31 December 2010	14,287	1,676	15,963

Initial concession property relates to the payments recognised at inception of the Rail Merger with KCRC while additional concession property relates to the expenditures for the replacement and/or upgrade of the initial concession property after inception of the Rail Merger.

26 Property Management Rights

Property management rights relate to the rights acquired by the Company from KCRC in the Rail Merger in respect of existing and future managed properties on the Appointed Day.

The Group and The Company

in HK$ million	**2011**	2010
Cost at 1 January and 31 December	**40**	40
Accumulated amortisation at 1 January and 31 December	**9**	9
Net book value at 31 December	**31**	31

27 Railway Construction in Progress

The Group and The Company

in HK$ million	Balance at 1 January	Transfer from deferred expenditure (note 30)	Expenditure	Balance at 31 December
2011				
West Island Line Project				
Construction costs	**3,955**	**–**	**2,682**	**6,637**
Consultancy fees	**430**	**–**	**50**	**480**
Staff costs and other expenses	**750**	**–**	**308**	**1,058**
Interest income	**(58)**	**–**	**(78)**	**(136)**
Utilisation of government grant	**(5,077)**	**–**	**(2,962)**	**(8,039)**
	–	**–**	**–**	**–**
South Island Line (East) Project				
Construction costs	**–**	**41**	**1,653**	**1,694**
Consultancy fees	**–**	**394**	**37**	**431**
Staff costs and other expenses	**–**	**277**	**165**	**442**
Finance costs	**–**	**23**	**22**	**45**
	–	**735**	**1,877**	**2,612**
Kwun Tong Line Extension Project				
Construction costs	**–**	**18**	**500**	**518**
Consultancy fees	**–**	**137**	**39**	**176**
Staff costs and other expenses	**–**	**123**	**121**	**244**
Finance costs	**–**	**8**	**8**	**16**
	–	**286**	**668**	**954**
Total	**–**	**1,021**	**2,545**	**3,566**
2010				
West Island Line Project				
Construction costs	891	–	3,064	3,955
Consultancy fees	364	–	66	430
Staff costs and other expenses	418	–	332	750
Finance costs/(interest income)	12	–	(70)	(58)
Utilisation of government grant	(1,685)	–	(3,392)	(5,077)
Total	–	–	–	–

A West Island Line ("WIL") Project

On 13 July 2009, the Company entered into a Project Agreement with HKSAR Government for the financing, design, construction and operation of the WIL and related services and facilities.

Pursuant to the agreement, HKSAR Government provided a grant of HK$12,252 million to the Company in March 2010 (having already made HK$400 million available in February 2008 under a preliminary project agreement). This grant is subject to a repayment mechanism whereby, within 24 months of commercial operations commencing on the WIL, the Company will pay to HKSAR Government amounts to reflect the excess of the original estimation over actual costs incurred on certain capital expenditure, price escalation costs, land costs and the amount of contingency in relation to the railway and related works (together with interest).

27 Railway Construction in Progress *(continued)*

A West Island Line ("WIL") Project *(continued)*

The project is targeted to complete in 2014. Total capital cost for the project based on the defined scope of works and programme is estimated at HK$17,117 million. As at 31 December 2011, the Company has incurred cumulative expenditure of HK$8,039 million (2010: HK$5,077 million), which was wholly offset by the government grant, and has authorised outstanding commitments on contracts totalling HK$5,324 million (2010: HK$7,042 million) and estimated future project costs of HK$3,754 million in relation to the project (note 58).

B South Island Line (East) ("SIL(E)") Project

On 17 May 2011, the Company entered into a Project Agreement with HKSAR Government for the financing, design, construction and operation of the SIL(E).

The project is targeted to complete in 2015. Total capital cost for the project based on the defined scope of works and programme is estimated at HK$15,273 million. As at 31 December 2011, the Company has incurred cumulative expenditure of HK$2,612 million and has authorised outstanding commitments on contracts totalling HK$5,326 million and estimated future project costs of HK$7,335 million in relation to the project (note 58).

C Kwun Tong Line Extension ("KTE") Project

On 17 May 2011, the Company entered into a Project Agreement with HKSAR Government for the financing, design, construction and operation of the KTE.

The project is targeted to complete in 2015. Total capital cost for the project based on the defined scope of works and programme is estimated at HK$6,511 million. As at 31 December 2011, the Company has incurred cumulative expenditure of HK$954 million and has authorised outstanding commitments on contracts totalling HK$2,449 million and estimated future project costs of HK$3,108 million in relation to the project (note 58).

28 Other Railway Construction in Progress under Entrustment by Kowloon-Canton Railway Corporation or HKSAR Government

A Kowloon Southern Link ("KSL") Project

Pursuant to the KSL Project Management Agreement, which was the one of the principal agreements of the Rail Merger, the Company acted as a project management agent to KCRC in respect of the construction of the KSL, which was completed and commenced operation on 16 August 2009. During the year ended 31 December 2011, HK$3 million of project management fee (2010: HK$52 million of project management fee and HK$55 million of incentive payment) was recognised as income in the consolidated profit and loss account.

B Hong Kong Section of the Guangzhou-Shenzhen-Hong Kong Express Rail Link ("XRL") Project

On 24 November 2008, HKSAR Government and the Company entered into an entrustment agreement for the design of and site investigation and procurement activities in relation to the XRL ("Preliminary Entrustment Agreement"). Pursuant to the Preliminary Entrustment Agreement, the Company shall carry out or procure the carrying out of the design, site investigation and procurement activities and HKSAR Government shall fund directly the total cost of such activities and pay to the Company a maximum amount of HK$1.5 billion in respect of certain costs incurred by the Company, including the Company's in-house design costs and certain on-costs and preliminary costs.

On 26 January 2010, HKSAR Government and the Company entered into another entrustment agreement for the construction, testing and commissioning of the XRL ("Entrustment Agreement"). Pursuant to the Entrustment Agreement, the Company shall be responsible for the construction, testing and commissioning of the XRL and HKSAR Government is responsible as the owner of XRL to fund directly the total cost of such activities and pay to the Company HK$4,590 million in respect of the Company's management of the project. Such sum may be varied in accordance with the terms of the Entrustment Agreement but is subject to a maximum annual limit of HK$2,000 million and a total limit of HK$10 billion. In addition, HKSAR Government has agreed that the Company will be invited to undertake the operation of the XRL under the service concession approach.

During the year ended 31 December 2011, project management revenue of HK$585 million (2010: HK$433 million) was recognised in the consolidated profit and loss account.

C Shatin to Central Link ("SCL") Project

On 24 November 2008, HKSAR Government and the Company entered into an entrustment agreement for the design of and site investigation and procurement activities in relation to the SCL ("Preliminary Entrustment Agreement"). Pursuant to the Preliminary Entrustment Agreement, the Company shall carry out or procure the carrying out of the design, site investigation and procurement activities and HKSAR Government shall fund directly the total cost of such activities and pay to the Company a maximum amount of HK$1.5 billion in respect of certain costs incurred by the Company, including the Company's in-house design costs and certain on-costs and preliminary costs.

On 17 May 2011, the Company entered into another entrustment agreement with HKSAR Government for the financing, construction, procurement of services and equipment and other matters associated with 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 ancillary works in relation to the SCL ("Entrustment Agreement"). Pursuant to the Entrustment Agreement, the Company shall carry out or procure the carrying out of the agreed works and receive from HKSAR Government a project management fee while HKSAR Government shall bear and pay to the Company all the work costs. The maximum aggregate amount payable by HKSAR Government to the Company is limited to HK$3,000 million per annum and HK$15 billion in total.

29 Property Development in Progress

Pursuant to the project agreements in respect of the construction of railway extensions and the Property Package Agreements in respect of the Rail Merger, HKSAR Government has granted the Company development rights on the lands over the stations along railway lines. As at 31 December 2011, the outstanding property developments include the Tseung Kwan O Extension Property Projects at depot sites along the Tsueng Kwan O Line, the East Rail Line/Kowloon Southern Link/Light Rail Property Projects at five development sites along the East Rail Line, Kowloon Southern Link and Light Rail, South Island Line (East) Property Project at a site in Wong Chuk Hang and Kwun Tong Line Extension Property Project at a site in Ho Man Tin.

Costs incurred by the Company for the acquisition of property development rights and preparation of the sites for development including land premium are capitalised as property development in progress and offset by payments received from developers in respect of the same development. In cases where payments received from developers exceed the related expenditure incurred by the Company, such excess is recorded as deferred income (note 29B). In these cases, any subsequent expenditure incurred by the Company in respect of that development will be charged against deferred income. The remaining deferred income is to be recognised as profits of the Company at the appropriate time after taking into account the outstanding risks and obligations retained by the Company relating to each development. Until such time as deferred income is recognised as profit, it is recorded as a liability of the Company in recognition of the Company's obligations under the grant of the development rights.

During the year ended 31 December 2011, the Company's two wholly owned subsidiaries, MTR Corporation (Shenzhen) Limited and MTR Property (Shenzhen) Company Limited, won the bid for Lot 1 of the Shenzhen Metro Longhua Line Depot Site. The two subsidiaries will incorporate a project company in the Mainland of China to undertake residential and commercial development of the site ("Shenzhen Property Project"). Part of the net profits generated from this property development will be shared with the Shenzhen Municipal Government.

A Property Development in Progress

The Group

in HK$ million	Balance at 1 January	Transfer from deferred expenditure (note 30)	Expenditure	Offset against payments received from developers	Transfer out on project completion	Balance at 31 December
2011						
Airport Railway Property Projects	**–**	**–**	**4**	**(4)**	**–**	**–**
Tseung Kwan O Extension Property Projects	**1,151**	**–**	**159**	**(9)**	**(213)**	**1,088**
East Rail Line/Kowloon Southern Link/ Light Rail Property Projects	**7,977**	**–**	**123**	**(19)**	**–**	**8,081**
South Island Line (East) Property Project	**–**	**32**	**253**	**–**	**–**	**285**
Kwun Tong Line Extension Property Project	**–**	**4**	**61**	**–**	**–**	**65**
Shenzhen Property Project	**–**	**–**	**2,445**	**–**	**–**	**2,445**
	9,128	**36**	**3,045**	**(32)**	**(213)**	**11,964**
2010						
Airport Railway Property Projects	–	–	14	(14)	–	–
Tseung Kwan O Extension Property Projects	2,245	–	331	(12)	(1,413)	1,151
East Rail Line/Kowloon Southern Link/ Light Rail Property Projects	4,473	–	4,027	(523)	–	7,977
	6,718	–	4,372	(549)	(1,413)	9,128

29 Property Development in Progress *(continued)*

A Property Development in Progress *(continued)*

The Company

in HK$ million	Balance at 1 January	Transfer from deferred expenditure (note 30)	Expenditure	Offset against payments received from developers	Transfer out on project completion	Balance at 31 December
2011						
Airport Railway Property Projects	**–**	**–**	**4**	**(4)**	**–**	**–**
Tseung Kwan O Extension Property Projects	**1,151**	**–**	**159**	**(9)**	**(213)**	**1,088**
East Rail Line/Kowloon Southern Link/ Light Rail Property Projects	**7,977**	**–**	**123**	**(19)**	**–**	**8,081**
South Island Line (East) Property Project	**–**	**32**	**253**	**–**	**–**	**285**
Kwun Tong Line Extension Property Project	**–**	**4**	**61**	**–**	**–**	**65**
Shenzhen Property Project	**–**	**–**	**2**	**–**	**–**	**2**
	9,128	**36**	**602**	**(32)**	**(213)**	**9,521**
2010						
Airport Railway Property Projects	–	–	14	(14)	–	–
Tseung Kwan O Extension Property Projects	2,245	–	331	(12)	(1,413)	1,151
East Rail Line/Kowloon Southern Link/ Light Rail Property Projects	4,473	–	4,027	(523)	–	7,977
	6,718	–	4,372	(549)	(1,413)	9,128

East Rail Line/Kowloon Southern Link/Light Rail Property Projects include the acquisition cost for the property development rights on the development sites from KCRC and mandatory payments in respect of enabling works carried out by KCRC for such sites. As at 31 December 2011, outstanding mandatory payments including interest accrued amounted to HK$720 million (2010: HK$699 million). Expenditure during the year ended 31 December 2010 included HK$3,900 million of land premium in respect of the property development of Austin Station Sites C and D.

Shenzhen Property Project includes the price for Lot 1 of the Shenzhen Metro Longhua Line Depot Site of RMB1,977 million (HK$2,438 million). In this regard, HK$493 million, representing an equivalent amount of RMB400 million, has been deposited into the foreign currency bank account of the Shenzhen Land Exchange Centre.

B Deferred Income on Property Development

The Group and The Company

in HK$ million	Balance at 1 January	Payments received from developers	Offset against development in progress (note 29A)	Amount recognised as profit (note 12)	Balance at 31 December
2011					
Airport Railway Property Projects	**38**	**–**	**(4)**	**–**	**34**
Tseung Kwan O Extension Property Projects	**43**	**–**	**(9)**	**–**	**34**
East Rail Line/Kowloon Southern Link/ Light Rail Property Projects	**487**	**–**	**(19)**	**(468)**	**–**
	568	**–**	**(32)**	**(468)**	**68**
2010					
Airport Railway Property Projects	69	–	(14)	(17)	38
Tseung Kwan O Extension Property Projects	55	–	(12)	–	43
East Rail Line/Kowloon Southern Link/ Light Rail Property Projects	–	1,010	(523)	–	487
	124	1,010	(549)	(17)	568

29 Property Development in Progress *(continued)*

C Stakeholding Funds

Being the stakeholder under certain Airport Railway, Tseung Kwan O Extension and East Rail Line Property Projects, the Company receives and manages deposit monies and sales proceeds in respect of sales of properties under those developments. These monies are placed in separate designated bank accounts and, together with any interest earned, are to be released to the developers for the reimbursement of costs of the respective developments in accordance with the terms and conditions of the Government Consent Schemes and development agreements. Any balance remaining is to be released for distribution only after all obligations relating to the developments have been met. Accordingly, the balances of the stakeholding funds and the corresponding bank balances have not been included in the Group's and the Company's balance sheets. Movements in stakeholding funds during the year are as follows:

The Group and The Company

in HK$ million	2011	2010
Balance as at 1 January	**3,708**	6,455
Stakeholding funds received	**25,039**	43,110
Add: Interest earned thereon	**15**	18
	28,762	49,583
Disbursements during the year	**(23,926)**	(45,875)
Balance as at 31 December	**4,836**	3,708
Represented by :		
Balances in designated bank accounts as at 31 December	**4,834**	3,706
Retention receivable	**2**	2
	4,836	3,708

In addition to the above, there are certain deposit monies and sales proceeds in respect of an East Rail Line property development site, amounting to HK$2,410 million at 31 December 2011 (2010: HK$1,225 million) that are under the custody of the solicitors and managed by the Company on behalf of KCRC as KCRC's agent.

D West Rail Property Developments

As part of the Rail Merger, the Company was appointed to act as the agent of KCRC and certain KCRC subsidiary companies ("West Rail Subsidiaries") in the development of specified development sites along the West Rail. The Company will receive an agency fee of 0.75% of the gross sale proceeds in respect of the developments except for the Tuen Mun development on which the Company will receive 10% of the net profits accrued under the development agreement. The Company will also recover from the West Rail Subsidiaries all the costs incurred in respect of the West Rail development sites plus 16.5% on-cost, together with interest accrued thereon. During the year ended 31 December 2011, the reimbursable costs incurred by the Company including on-cost and interest accrued were HK$96 million (2010: HK$60 million).

30 Deferred Expenditure

The Group and The Company

in HK$ million	2011	2010
Balance at 1 January	**1,079**	558
Expenditure during the year	**3**	521
Transfer to investment properties (note 23)	**(11)**	–
Transfer to railway construction in progress (note 27)	**(1,021)**	–
Transfer to property development in progress (note 29)	**(36)**	–
Balance at 31 December	**14**	1,079

Upon signing of the Project Agreements in relation to the South Island Line (East) ("SIL(E)") and Kwun Tong Line Extension ("KTE") on 17 May 2011, expenditures previously incurred for the SIL(E) (HK$735 million on railway construction and HK$32 million on property development) and KTE (HK$286 million on railway construction and HK$4 million on property development) were transferred to railway construction in progress (note 27) and property development in progress (note 29). Deferred expenditure as at 31 December 2011 mainly related to property development project studies.

31 Interests in Non-controlled Subsidiaries

in HK$ million	The Group 2011	The Group 2010	The Company 2011	The Company 2010
Unlisted shares, at cost	**–**	–	**24**	24
Share of net assets	**579**	541	**–**	–
	579	541	**24**	24

The following list contains the particulars of all major non-controlled subsidiaries of the Group:

		Proportion of ownership interest				
Name of company	Issued and paid up ordinary share capital	Group's effective interest	Held by the Company	Held by subsidiary	Place of incorporation and operation	Principal activities
Octopus Holdings Limited	HK$42,000,000	57.4%	57.4%	–	Hong Kong	Investment holding
Octopus Cards Limited	HK$42,000,000	57.4%	–	100%	Hong Kong	Operate a contactless smartcard common payment system in Hong Kong
Octopus China Investments Limited	HK$1	57.4%	–	100%	Hong Kong	Investment holding
Octopus Connect Limited	HK$2	57.4%	–	100%	Hong Kong	Dormant
Octopus International Projects Limited	HK$1	57.4%	–	100%	Hong Kong	Investment holding
Octopus Investments Limited	HK$2	57.4%	–	100%	Hong Kong	Investment holding
Octopus Knowledge Limited	HK$2	57.4%	–	100%	Hong Kong	Consultancy services on introducing a smartcard system in Dubai
Octopus Netherlands Limited	HK$1	57.4%	–	100%	Hong Kong	Consultancy services on introducing a smartcard system in the Netherlands
Octopus Payments Limited	HK$2	57.4%	–	100%	Hong Kong	Project management
Octopus Rewards Limited	HK$1	57.4%	–	100%	Hong Kong	Develop and operate a common loyalty scheme
Octopus Solutions Limited	HK$2	57.4%	–	100%	Hong Kong	Consultancy services in Auckland
Octopus Systems Limited	HK$2	57.4%	–	100%	Hong Kong	Consultancy services in Hong Kong
Octopus Transactions Limited	HK$2	57.4%	–	100%	Hong Kong	Project management
Octopus Cards Macau Limited	MOP25,000	57.4%	–	100%	Macau	Promote the contactless smartcard common payment system in Macau

Octopus Cards Limited ("OCL") was formed in 1994 by the Company and four other local transport companies to undertake the development and operation of the "Octopus" contactless smart card ticketing system. In 2000, the Hong Kong Monetary Authority ("HKMA") approved OCL to become a deposit-taking company ("DTC") and extend the use of Octopus cards to non-transport related services. In 2001, the Company disposed 10.4% of the shareholding interest of OCL to certain other shareholders of OCL for a consideration of HK$16 million, together with a deferred consideration to be received in the event of OCL subsequently becoming a stock exchange listed company. In 2005, OCL undertook a company re-structuring to separate OCL's regulated payment businesses and non-payment businesses by setting up a new holding company, Octopus Holdings Limited ("OHL"), to hold the entire issued share capital of OCL as well as other companies established for the non-payment businesses. The Company's effective interest in OHL and OHL's subsidiaries remains unchanged at 57.4% and the Company's appointees to the OHL's Board of Directors are limited to 49% of the voting rights at board meetings.

During the year ended 31 December 2011, the Company incurred HK$116 million (2010: HK$109 million) of expenses for the central clearing services provided by OCL. OCL incurred HK$29 million (2010: HK$48 million) of expenses for the load agent and Octopus card issuance and refund services, computer equipment and relating services, staff secondment, project administration services as well as warehouse storage space provided by the Company. During the year, OHL distributed dividends of HK$144 million (2010: HK$75 million) to the Company.

31 Interests in Non-controlled Subsidiaries *(continued)*

The condensed consolidated profit and loss account and the balance sheet for OHL are shown below:

Consolidated Profit and Loss Account

Year ended 31 December in HK$ million	2011 (Audited)	2010 (Audited)
Turnover	**704**	662
Other operating income	**8**	6
	712	668
Staff costs	**(126)**	(119)
Load agent fees and bank charges for add value services	**(88)**	(80)
Other expenses	**(148)**	(222)
Operating profit before depreciation	**350**	247
Depreciation	**(38)**	(43)
Operating profit before interest and finance charges	**312**	204
Net interest income	**54**	56
Share of loss from a jointly controlled entity	**(4)**	(2)
Profit before taxation	**362**	258
Income tax	**(45)**	(39)
Profit for the year	**317**	219
Group's share of profit before taxation (note 16)	**208**	148
Group's share of income tax (note 16)	**(26)**	(22)

Consolidated Balance Sheet

at 31 December in HK$ million	2011 (Audited)	2010 (Audited)
Assets		
Fixed assets	**216**	189
Investments	**2,641**	2,195
Other assets	**358**	277
Cash at banks and on hand	**517**	671
	3,732	3,332
Liabilities		
Card floats and card deposits due to cardholders	**(2,244)**	(2,004)
Amounts due to related parties	**(55)**	(24)
Other liabilities	**(423)**	(362)
	(2,722)	(2,390)
Net assets	**1,010**	942
Equity		
Share capital	**42**	42
Exchange reserve	**1**	–
Retained profits	**967**	900
	1,010	942
Group's share of net assets	**579**	541

32 Investments in Subsidiaries

The Company

in HK$ million	2011	2010
Unlisted shares, at cost	**1,260**	1,256

Investments in subsidiaries include HK$24 million (2010: HK$24 million) in respect of investments in non-controlled subsidiaries, the relevant details of which are disclosed in note 31. The following list contains details of controlled subsidiaries as defined under note 2C as at 31 December 2011, which have been consolidated into the Group's accounts.

		Proportion of ownership interest				
Name of company	Issued and paid up ordinary/registered share capital	Group's effective interest	Held by the Company	Held by subsidiary	Place of incorporation and operation	Principal activities
Subsidiaries held throughout 2011						
Glory Goal Limited	HK$10,000	100%	100%	–	Hong Kong	Investment holding
Hanford Garden Property Management Company Limited	HK$10,000	100%	100%	–	Hong Kong	Property management
MTR (Estates Management) Limited	HK$1,000	100%	100%	–	Hong Kong	Investment holding and property management
MTR (Shanghai Project Management) Limited	HK$1,000	100%	100%	–	Hong Kong	Railway consultancy services, property investment and development
MTR Beijing Line 4 Investment Company Limited	HK$1	100%	100%	–	Hong Kong	Investment holding
MTR Building Works Company Limited (previously Rail Sourcing Solutions (International) Limited)	HK$2	100%	100%	–	Hong Kong	General building, maintenance and engineering works
MTR China Commercial Management No. 1 Holdings Limited	HK$1,000	100%	100%	–	Hong Kong	Investment holding
MTR China Consultancy Company Limited	HK$1,000	100%	100%	–	Hong Kong	Railway consultancy services
MTR China Property Holdings Limited (previously Extensive Growth Limited)	HK$1	100%	100%	–	Hong Kong	Investment holding
MTR China Property Limited	HK$1,000	100%	100%	–	Hong Kong	Property management
MTR Engineering Services Limited	HK$1,000	100%	100%	–	Hong Kong	Engineering services
MTR Hangzhou Line 1 Investment Company Limited	HK$1,000	100%	100%	–	Hong Kong	Investment holding
MTR Information Solutions Company Limited	HK$1,000	100%	100%	–	Hong Kong	License MTR software to MTR's subsidiaries and associates
MTR Property Agency Co. Limited	HK$2	100%	100%	–	Hong Kong	Property agency
MTR Property (Beijing) No. 1 Company Limited	HK$1	100%	–	100%	Hong Kong	Property development, investment and management
MTR Property (Shenzhen) Company Limited	HK$1	100%	100%	–	Hong Kong	Property development, investment and management
MTR Rail Transport Training (International) Company Limited	HK$2,800,000	100%	100%	–	Hong Kong	Provide rail transport training in Mainland China

32 Investments in Subsidiaries *(continued)*

Name of company	Issued and paid up ordinary/registered share capital	Proportion of ownership interest: Group's effective interest	Proportion of ownership interest: Held by the Company	Proportion of ownership interest: Held by subsidiary	Place of incorporation and operation	Principal activities
MTR Shenyang Holdings Limited	HK$1,000	100%	100%	–	Hong Kong	Investment holding
MTR Shenyang Investment Holdings Limited	HK$1	100%	100%	–	Hong Kong	Investment holding
MTR Shenyang Property No.1 Limited	HK$1	100%	–	100%	Hong Kong	Property development, investment and management
MTR Shenzhen Investment Holding Limited	HK$400,000	100%	100%	–	Hong Kong	Investment holding
MTR Telecommunication Company Limited	HK$100,000,000	100%	100%	–	Hong Kong	Mobile telecommunication services
MTR Travel Limited	HK$2,500,000	100%	100%	–	Hong Kong	Travel services
Ngong Ping 360 Limited	HK$2	100%	100%	–	Hong Kong	Operate the Tung Chung to Ngong Ping cable car system and Theme Village in Ngong Ping
Pierhead Garden Management Company Limited	HK$50,000	100%	100%	–	Hong Kong	Property management
Royal Ascot Management Company Limited	HK$50,000	100%	100%	–	Hong Kong	Property management
Sun Tuen Mun Centre Management Company Limited	HK$50,000	100%	100%	–	Hong Kong	Property management
TraxComm Limited	HK$15,000,000	100%	100%	–	Hong Kong	Fixed telecommunication network services
V-Connect Limited	HK$1,000	100%	100%	–	Hong Kong	Mobile telecommunication network services
360 Holidays Limited	HK$500,000	100%	–	100%	Hong Kong	Guided tour services
Metro Trains Melbourne Pty. Ltd. *	AUD16,250,000	60% on ordinary shares; 30% on Class A shares	60% on ordinary shares; 30% on Class A shares	–	Australia	Railway operations and maintenance
Fasttrack Insurance Ltd.	HK$77,500,000	100%	100%	–	Bermuda	Insurance underwriting
Candiman Limited *	US$1	100%	100%	–	British Virgin Islands	Investment holding
MTR Corporation (C.I.) Limited	US$1,000	100%	100%	–	Cayman Islands/ Hong Kong	Finance
MTR Finance Lease (001) Limited	US$1	100%	100%	–	Cayman Islands/ Hong Kong	Finance
MTR Stockholm AB	SEK40,000,000	100%	–	100%	Sweden	Railway operations and maintenance

32 Investments in Subsidiaries *(continued)*

Name of company	Issued and paid up ordinary/registered share capital	Proportion of ownership interest: Group's effective interest	Held by the Company	Held by subsidiary	Place of incorporation and operation	Principal activities
Chongqing Premier Property Management Company Limited *	US$150,000	70%	–	70%	The People's Republic of China	Property management
MTR (Beijing) Commercial Facilities Management Co., Ltd.	HK$93,000,000	100%	–	100%	The People's Republic of China	Property leasing and management
MTR (Beijing) Property Services Company Limited *	RMB3,000,000	100%	100%	–	The People's Republic of China	Property management
MTR Commercial Management (Beijing) Company Limited *	HK$120,000	100%	–	100%	The People's Republic of China	Business management, business consultancy, commercial facilities strategy and consultancy services, and corporate training management
MTR Consultancy (Beijing) Co. Limited (Incorporated)	HK$4,200,000	100%	100%	–	The People's Republic of China	Railway consultancy services, marketing and promotion
MTR Consulting (Shenzhen) Co. Ltd. (Incorporated)	HK$1,000,000	100%	100%	–	The People's Republic of China	Railway consultancy services
MTR Corporation (Shenzhen) Limited (Incorporated)	HK$2,636,000,000	100%	–	100%	The People's Republic of China	Railway construction, operation and management
MTR Corporation (Shenzhen) Training Centre * (Incorporated)	RMB2,000,000	100%	–	100%	The People's Republic of China	Provide rail transport training
Shanghai Hong Kong Metro Construction Management Co. Ltd. (Incorporated)	HK$15,000,000	60%	–	60%	The People's Republic of China	Railway construction management and development
MTR Corporation (Silverlink) Limited	GBP1	100%	–	100%	United Kingdom	Investment holding
MTR Corporation (UK) Limited	GBP29	100%	100%	–	United Kingdom	Investment holding
<u>Subsidiaries established during 2011</u>						
MTR Property (Tianjin) No. 1 Company Limited	HK$1	100%	–	100%	Hong Kong	Property development, investment and management
MTR Property (Tianjin) No. 2 Company Limited	HK$1	100%	–	100%	Hong Kong	Property development, investment and management

* Subsidiaries not audited by KPMG

During the year ended 31 December 2011, MTR (Macau) Property Management Company Limited was wound up and resolution was passed to dissolve Shanghai Hong Kong Metro Construction Management Co. Ltd..

33 Interests in Associates

The Group

in HK$ million	2011	2010
Share of net assets	**948**	836

The Group and the Company had interests in the following associates as at 31 December 2011:

Name of company	Issued and paid up ordinary/registered share capital	Proportion of ownership interest: Group's effective interest	Proportion of ownership interest: Held by subsidiary	Place of incorporation and operation	Principal activities
Beijing MTR Corporation Limited (Incorporated)	RMB1,380,000,000	49%	49%	The People's Republic of China	Railway construction, operation, management and development
Shenyang MTR Corporation Limited	RMB100,000,000	49%	49%	The People's Republic of China	Railway operation and management
Tunnelbanan Teknik Stockholm AB	SEK30,000,000	50%	50%	Sweden	Railway maintenance
London Overground Rail Operations Ltd ("LOROL") *	GBP2	50%	50%	United Kingdom	Railway management

* Companies not audited by KPMG

The Company has reached agreement with the other parent company of Shenyang MTR Corporation Limited ("Shenyang MTR") to wind up Shenyang MTR. The request for approval has been submitted to the Shenyang Municipal Government and the process for liquidation has started.

During the year ended 31 December 2011, Tunnelbanan Teknik Stockholm AB provided rolling stock maintenance and other supporting services to MTR Stockholm AB at an amount of SEK520 million (HK$629 million) (2010: SEK511 million or HK$550 million). MTR Stockholm AB leased depots, depot equipment and provided other supporting services to Tunnelbanan Teknik Stockholm AB at a total amount of SEK108 million (HK$131 million) (2010: SEK114 million or HK$122 million).

During the same year, the Company provided staff secondment, information technology and other support services to Beijing MTR Corporation Limited at a total amount of HK$19 million (2010: HK$32 million). During the year ended 31 December 2010, the Company provided staff secondment and consultancy service to LOROL at an amount of HK$1 million.

The summary financial information of the Group's effective interests in associates is as follows:

in HK$ million	2011	2010
Non-current assets	**2,319**	2,435
Current assets	**793**	747
Non-current liabilities	**(860)**	(972)
Current liabilities	**(1,304)**	(1,374)
Net assets	**948**	836
Income	**1,760**	1,612
Expenses	**(1,608)**	(1,590)
Profit before taxation	**152**	22
Income tax	**(37)**	(9)
Net profit for the year	**115**	13

34 Investments in Securities

Investments in securities, representing bank medium term notes held by the Company and debt securities held by the overseas insurance underwriting subsidiary, comprise:

The Group

in HK$ million	2011	2010
Held-to-maturity securities, at amortised cost		
– maturing within 1 year	**2,626**	1,000
– maturing after 1 year	**–**	2,627
	2,626	3,627
Trading securities listed overseas, at fair value (Level 1, see note 36 for definition)		
– maturing within 1 year	**126**	67
– maturing after 1 year	**222**	218
	348	285
	2,974	3,912

The Company

in HK$ million	2011	2010
Held-to-maturity securities, at amortised cost		
– maturing within 1 year	**2,626**	1,000
– maturing after 1 year	**–**	2,627
	2,626	3,627

35 Properties Held for Sale

The Group and The Company

in HK$ million	2011	2010
Properties held for sale		
– at cost	**3,718**	1,829
– at net realisable value	**39**	107
	3,757	1,936

Properties held for sale at 31 December 2011 comprised mainly residential units and car parking spaces at Festival City at Tai Wai Maintenance Centre and The Palazzo at Fo Tan Station along the East Rail Line and Lake Silver at Wu Kai Sha Station along the Ma On Shan Line. They represent either properties received by the Company as sharing in kind or as part of the profit distribution upon completion of the development. The properties are stated on the balance sheet at the lower of cost, which is deemed to be their fair value upon initial recognition as determined by reference to an independent open market valuation at the date of receipt (notes 2K(iv) and (v)), and their net realisable value at the balance sheet date. Net realisable value represents the estimated selling price less costs to be incurred in selling the properties. The net realisable values as at 31 December 2011 and 2010 were determined by reference to an open market valuation of the properties as at those dates, undertaken by an independent firm of surveyors, Jones Lang LaSalle Limited, who have among their staff Members of the Hong Kong Institute of Surveyors.

Properties held for sale at net realisable value are stated net of provision of HK$18 million (2010: HK$12 million), made in order to state these properties at the lower of their cost and estimated net realisable value.

36 Derivative Financial Assets and Liabilities

A Fair Value

The contracted notional amounts, fair values and maturities based on contractual undiscounted cash flows of derivative financial instruments outstanding are as follows:

The Group and The Company

in HK$ million	Notional amount	Fair value	Level*	Contractual undiscounted cash flow maturing in Less than 1 year	1-2 years	2-5 years	Over 5 years	Total
2011								
Derivative Financial Assets								
Gross settled:								
Foreign exchange forwards								
– cash flow hedges :	86	3	2					
– inflow				29	26	34	–	89
– outflow				(27)	(26)	(33)	–	(86)
– not qualified for hedge accounting :	6	–	2					
– inflow				5	–	–	–	5
– outflow				(5)	–	–	–	(5)
Cross currency swaps								
– fair value hedges :	1,245	54	2					
– inflow				37	811	6	470	1,324
– outflow				(6)	(785)	–	(465)	(1,256)
Net settled:								
Interest rate swaps								
– fair value hedges	2,833	287	2	134	95	78	34	341
– cash flow hedges	300	–	2	(1)	(1)	2	–	–
– not qualified for hedge accounting	388	–	2	–	–	–	–	–
	4,858	344		166	120	87	39	412
Derivative Financial Liabilities								
Gross settled:								
Foreign exchange forwards								
– cash flow hedges :	83	4	2					
– inflow				59	16	4	–	79
– outflow				(62)	(17)	(4)	–	(83)
– not qualified for hedge accounting :	174	7	2					
– inflow				132	27	7	–	166
– outflow				(138)	(28)	(7)	–	(173)
Cross currency swaps								
– fair value hedges :	4,663	28	2					
– inflow				12	13	6,593	–	6,618
– outflow				(18)	(21)	(6,609)	–	(6,648)
Net settled:								
Interest rate swaps								
– cash flow hedges	1,912	112	2	(59)	(48)	(16)	(3)	(126)
	6,832	151		(74)	(58)	(32)	(3)	(167)
Total	11,690							

36 Derivative Financial Assets and Liabilities *(continued)*

A Fair Value *(continued)*

The Group and The Company

in HK$ million	Notional amount	Fair value	Level*	Contractual undiscounted cash flow maturing in Less than 1 year	1-2 years	2-5 years	Over 5 years	Total
2010								
Derivative Financial Assets								
Gross settled:								
Foreign exchange forwards								
– cash flow hedges :	147	11	2					
– inflow				121	27	12	–	160
– outflow				(112)	(25)	(12)	–	(149)
– not qualified for hedge accounting :	11	2	2					
– inflow				13	–	–	–	13
– outflow				(11)	–	–	–	(11)
Cross currency swaps								
– fair value hedges :	1,255	75	2					
– inflow				46	37	817	467	1,367
– outflow				(15)	(10)	(792)	(464)	(1,281)
Net settled:								
Interest rate swaps								
– fair value hedges	2,834	280	2	102	123	91	18	334
– cash flow hedges	350	7	2	(7)	(5)	5	11	4
	4,597	375		137	147	121	32	437
Derivative Financial Liabilities								
Gross settled:								
Foreign exchange forwards								
– cash flow hedges :	82	4	2					
– inflow				49	19	8	–	76
– outflow				(52)	(20)	(8)	–	(80)
– not qualified for hedge accounting :	129	–	2					
– inflow				108	17	4	–	129
– outflow				(108)	(17)	(4)	–	(129)
Cross currency swaps								
– fair value hedges :	4,663	32	2					
– inflow				9	15	5,092	–	5,116
– outflow				(15)	(26)	(5,106)	–	(5,147)
Net settled:								
Interest rate swaps								
– fair value hedges	–	–	2	–	–	–	–	–
– cash flow hedges	1,312	112	2	(49)	(42)	(29)	–	(120)
	6,186	148		(58)	(54)	(43)	–	(155)
Total	10,783							

* The levels are defined in HKFRS 7 as follows:

Level 1: Fair values measured using quoted prices (unadjusted) in active markets for identical financial instruments

Level 2: Fair values measured using quoted prices in active markets for similar financial instruments, or using valuation techniques in which all significant inputs are directly or indirectly based on observable market data

Level 3: Fair values measured using valuation techniques in which any significant input is not based on observable market data

36 Derivative Financial Assets and Liabilities *(continued)*

A Fair Value *(continued)*

The discounted cash flow method, which discounts the future contractual cash flows at the current market interest and foreign exchange rates that are available to the Group for similar financial instruments, is the main valuation technique used to determine the fair value of the Group's borrowings and derivative financial instruments such as interest rate swaps and cross currency swaps. The fair value of forward foreign exchange contracts is determined using forward exchange market rates at the balance sheet date.

The Group's derivative financial instruments consist predominantly of interest rate and cross currency swaps, and the relevant interest rate swap curves as of 31 December 2011 and 2010 were used to discount the cash flows of financial instruments. Interest rates used ranged from 0.250% to 1.877% (2010: 0.045% to 3.407%) for Hong Kong dollars, 0.208% to 2.027% (2010: 0.392% to 3.509%) for US dollars and 0.677% to 2.381% (2010: 0.379% to 3.393%) for Euro.

The table above details the remaining contractual maturities at the balance sheet date of the Group's and the Company's derivative financial liabilities and assets, which are based on contractual undiscounted cash flows (including interest payments computed using contractual rates or, if floating, based on rates current at the balance sheet date) and the earliest date the Group and the Company can be required to pay.

B Financial Risks

The Group's operating activities and financing activities expose it to four main types of financial risks, namely liquidity risk, interest rate risk, foreign exchange risk and credit risk. The Group's overall risk management policy focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects of these financial risks on the Group's financial performance.

The Board of Directors provides principles for overall risk management and approves policies covering specific areas, such as liquidity risk, interest rate risk, foreign exchange risk, credit risk, concentration risk, use of derivative financial instruments and non-derivative financial instruments, and investment of excess liquidity. The Group's Preferred Financing Model (the "Model") is an integral part of its risk management policies. The Model specifies, amongst other things, the preferred mix of fixed and floating rate debts, the permitted level of foreign currency debts and an adequate length of financing horizon for coverage of forward funding requirements, against which the Group's financing related liquidity, interest rate and currency risk exposures are measured, monitored and controlled. The Board regularly reviews its risk management polices and authorises changes if necessary based on operating and market conditions and other relevant factors. The Board also reviews on an annual basis as part of the budgeting process and authorises changes if necessary to the Model in accordance with changes in market conditions and practical requirements.

The use of derivative financial instruments to control and hedge against interest rate and foreign exchange risk exposures is an integral part of the Group's risk management strategy. In accordance with Board policy, these instruments shall only be used for controlling or hedging risk exposures, and cannot be used for speculation purposes. All of the derivative instruments used by the Group are over-the-counter derivatives comprising principally interest rate swaps, cross currency swaps and foreign exchange forward contracts.

(i) Liquidity Risk

Liquidity risk refers to the risk that funds are not available to meet liabilities as they fall due, and it may result from timing and amount mismatches of cash inflow and outflow.

The Group employs projected cash flow analysis to manage liquidity risk by forecasting the amount of cash required, including working capital, debt repayments, dividend payments, capital expenditures and new investments, and by maintaining sufficient cash balance and/or undrawn committed banking facilities to ensure these requirements are met. It adopts a prudent approach and will maintain sufficient cash balance and committed banking facilities to provide forward coverage of at least 6 to 15 months of projected cash requirements as specified in the Model. The Group also conducts stress testing of its projected cash flow to analyse liquidity risk, and would arrange additional banking facilities or debt issuance or otherwise take appropriate actions if such stress tests reveal significant risk of material cash flow shortfall.

The following table details the remaining contractual maturities at the balance sheet date of the Group's and the Company's non-derivative financial liabilities, which are based on contractual undiscounted cash flows (including interest payments computed using contractual rates or, if floating, based on rates current at the balance sheet date) and the earliest date the Group and the Company can be required to pay:

The Group

	2011				2010			
in HK$ million	Capital market instruments	Bank loans and overdrafts	Others	Total	Capital market instruments	Bank loans and overdrafts	Others	Total
Loans and other obligations								
Amounts repayable beyond 5 years	**2,876**	**4,305**	**592**	**7,773**	3,218	2,315	598	6,131
Amounts repayable within a period of between 2 and 5 years	**7,498**	**840**	**1**	**8,339**	8,717	1,318	1	10,036
Amounts repayable within a period of between 1 and 2 years	**3,883**	**387**	**2**	**4,272**	603	6,569	1	7,173
Amounts repayable within 1 year	**632**	**6,426**	**2**	**7,060**	1,013	480	1	1,494
	14,889	**11,958**	**597**	**27,444**	13,551	10,682	601	24,834

36 Derivative Financial Assets and Liabilities *(continued)*

B Financial Risks *(continued)*

The Company

in HK$ million	2011 Capital market instruments	2011 Bank loans and overdrafts	2011 Others	2011 Total	2010 Capital market instruments	2010 Bank loans and overdrafts	2010 Others	2010 Total
Loans and other obligations								
Amounts repayable beyond 5 years	**543**	**–**	**592**	**1,135**	577	–	598	1,175
Amounts repayable within a period of between 2 and 5 years	**117**	**326**	**–**	**443**	117	531	–	648
Amounts repayable within a period of between 1 and 2 years	**39**	**194**	**–**	**233**	39	6,457	–	6,496
Amounts repayable within 1 year	**39**	**6,229**	**–**	**6,268**	39	376	–	415
	738	**6,749**	**592**	**8,079**	772	7,364	598	8,734

Others represent obligations under lease out/lease back transaction (note 24E).

(ii) Interest Rate Risk

The Group's interest rate risk arises principally from its borrowing activities. Borrowings based on fixed and floating rates expose the Group to fair value and cash flow interest rate risk respectively due to fluctuations in market interest rates. The Group manages and controls its interest rate risk exposure by maintaining a level of fixed rate debt between 40% and 70% of total debt outstanding as specified by the Model. Should the actual fixed rate debt level deviate substantially from the Model, derivative financial instruments such as interest rate swaps would be procured to align the fixed and floating mix with the Model. As at 31 December 2011, 51% of the Group's total debt outstanding was denominated either in or converted to fixed interest rate after taking into account outstanding cross currency and interest rate swaps.

The Group's exposure due to its floating rate borrowings is offset by the floating rate interest income it earns from its cash balances, bank deposits and other investment instruments. As at 31 December 2011, the Group had total cash balances and bank deposits of HK$7,156 million from which it derived floating rate interest income, compared with total floating rate borrowings of HK$11,031 million.

As at 31 December 2011, it is estimated that a 100 basis points increase/25 basis points decrease in interest rates, with all other variables held constant, would increase/decrease the Group's profit after tax and retained profits by approximately HK$31/HK$8 million. Other components of consolidated equity would increase/decrease by approximately HK$46/HK$16 million.

The sensitivity analysis above has been determined assuming that the change in interest rates had occurred at the balance sheet date and had been applied to the exposure to interest rate risk for both derivative and non-derivative financial instruments in existence at that date. The interest rate assumptions represent management's assessment of a reasonable possible change in interest rates over the period until the next annual balance sheet date in the light of the current low absolute levels of interest rates and the greater scope for rate increase than decrease in the future.

In 2010, a similar analysis was performed based on the assumption of a general increase/decrease of 100/50 basis points in interest rates, which would increase/decrease the Group's profit after tax and retained profits by approximately HK$85/HK$24 million. Other components of consolidated equity would increase/decrease by approximately HK$49/HK$26 million.

(iii) Foreign Exchange Risk

Foreign exchange risk arises when recognised assets and liabilities are denominated in a currency that is not the Group's functional currency. For the Group, it arises principally from its borrowing and overseas procurement activities.

The Group manages and controls its foreign exchange risk exposure by maintaining a modest level of unhedged non-Hong Kong dollar debt as specified by the Model, and minimal foreign exchange open positions created by its procurements overseas. Where the currency of a borrowing is not matched with that of the expected cash flows for servicing the debt, the Group would convert its foreign currency exposure resulting from the borrowing to Hong Kong dollar exposure through cross currency swaps. For procurement in foreign currencies, the Group would enter into foreign exchange forward contracts to secure the necessary foreign currencies at pre-determined exchange rates for settlement.

The Group's exposure to US dollars due to its foreign currency borrowings is also offset by the amount of US dollar cash balances, bank deposits and investments that it maintains.

As most of the Group's receivables and payables are denominated in the respective Group companies' functional currencies (Hong Kong dollars, Renminbi, Australian dollars or Swedish krona) or United States dollars (with which Hong Kong dollars are pegged) and most of its payment commitments denominated in foreign currencies are covered by foreign exchange forward contracts, management does not expect that there will be any significant currency risk associated with them.

36 Derivative Financial Assets and Liabilities *(continued)*

B Financial Risks *(continued)*

(iv) Credit Risk

Credit risk refers to the risk that a counterparty will be unable to pay amounts in full when due. For the Group, this arises mainly from the deposits it maintains and the derivative financial instruments that it has entered into with various banks and counterparties as well as from the Defeasance Securities it procured under the lease out/lease back transaction (note 24E). The Group limits its exposure to credit risk by placing deposits and transacting derivative financial instruments only with financial institutions with acceptable investment grade credit ratings or guarantee, and diversifying its exposure to various counterparties.

All derivative financial instruments are subject to a maximum counterparty limit based on the respective counterparty's credit ratings in accordance with policy approved by the Board. Credit exposure in terms of estimated fair market value of and largest potential loss arising from these instruments based on the "value-at-risk" concept is measured, monitored and controlled against their respective counterparty limits. To further reduce counterparty risk exposure, the Group also applies set-off and netting arrangements across all derivative financial instruments and other financial transactions with the same counterparty.

All deposits and investments are similarly subject to a separate maximum counterparty/issuer limit based on the respective counterparty/issuer's credit ratings and/or status as Hong Kong's note-issuing banks. There is also a limit on the length of time that the Group can maintain a deposit with a counterparty or investment from an issuer based upon the counterparty/issuer's credit ratings. Deposit/investment outstanding and maturity profile are monitored regularly to ensure they are within the limits established for the counterparties/issuers. In addition, the Group actively monitors the credit default swap levels of counterparties/issuers and their daily changes, and may on the basis of the observed levels and other considerations adjust its exposure and/or maximum counterparty/issuer limit to the relevant counterparty.

As at balance sheet date, the maximum exposure to credit risk of the Group with respect to derivative financial assets and bank deposits is represented respectively by the carrying amount of the derivative financial assets and the aggregate amount of deposits on its balance sheet. As at balance sheet date, there was no significant concentration risk to a single counterparty.

In addition, the Company also manages and controls its exposure to credit risks in respect of receivables as stated in note 38.

37 Stores and Spares

	The Group		The Company	
in HK$ million	**2011**	2010	**2011**	2010
Stores and spares expected to be consumed:				
– within 1 year	**695**	643	**570**	519
– after 1 year	**446**	426	**368**	363
	1,141	1,069	**938**	882
Less: Provision for obsolete stock	**(6)**	(8)	**(6)**	(8)
	1,135	1,061	**932**	874

Stores and spares expected to be consumed after 1 year comprise mainly contingency spares and stocks kept to meet cyclical maintenance requirements.

38 Debtors, Deposits and Payments in Advance

	The Group		The Company	
in HK$ million	**2011**	2010	**2011**	2010
Debtors, deposits and payments in advance relate to:				
– Property development projects	**1,203**	636	**1,203**	636
– Railway subsidiaries outside of Hong Kong	**1,204**	1,203	**–**	–
– Hong Kong operations and others	**1,557**	1,222	**1,426**	1,143
	3,964	3,061	**2,629**	1,779

38 Debtors, Deposits and Payments in Advance *(continued)*

The Group's credit policies in respect of receivables arising from its principal activities are as follows:

(i) The majority of fare revenue from Hong Kong transport operation is collected either through Octopus Cards with daily settlement on the next working day or in cash for other ticket types. A small portion of fare revenue from Hong Kong transport operation collected through pre-sale agents is due within 21 days.

(ii) Fare revenue from Shenzhen Longhua Line is collected either through Shenzhen Tong Cards with daily settlement on the next working day or in cash for other ticket types.

(iii) Franchise revenue in Melbourne is collected either weekly or monthly depending on its nature. The majority of the franchise revenue in Stockholm is collected in the transaction month with the remainder being collected in the following month.

(iv) Rentals, advertising and telecommunications service fees are billed monthly with due dates ranging from immediately due to 50 days. Tenants of the Group's investment properties and station kiosks are required to pay three months' rental deposit upon the signing of lease agreements.

(v) Amounts receivable under interest rate and currency swap agreements with financial institutions are due in accordance with the respective terms of the agreements.

(vi) Consultancy service incomes are billed monthly, upon work completion or on other basis stipulated in the consultancy contracts and are due within 30 days.

(vii) Debtors in relation to contracts and capital works entrusted to the Group, subject to any agreed retentions, are due within 30 days upon the certification of work in progress.

(viii) Amounts receivable in respect of property development are due in accordance with the terms of relevant development agreements or sale and purchase agreements.

The ageing of debtors is analysed as follows:

	The Group		The Company	
in HK$ million	**2011**	2010	**2011**	2010
Amounts not yet due	**2,612**	1,904	**1,831**	1,092
Overdue by 30 days	**428**	157	**242**	61
Overdue by 60 days	**21**	27	**5**	21
Overdue by 90 days	**8**	8	**6**	3
Overdue by more than 90 days	**20**	11	**2**	6
Total debtors	**3,089**	2,107	**2,086**	1,183
Deposits and payments in advance	**677**	785	**345**	427
Prepaid pension costs	**198**	169	**198**	169
	3,964	3,061	**2,629**	1,779

Included in amounts not yet due as at 31 December 2011 was HK$1,203 million (2010: HK$634 million) in respect of property development, comprising receivable on profits distributable based on the terms of the development agreements and sales and purchase agreements, receivable from certain stakeholding funds (note 29C) awaiting finalisation of the respective development accounts as well as other receivables on miscellaneous recoverable expenses.

As at 31 December 2011, all debtors, deposits and payments in advance were expected to be recovered within one year except for amounts relating to deposits and receivables of HK$279 million (2010: HK$153 million) included in Hong Kong operations and others, which were expected to be recovered between one to three years. The nominal values less impairment losses for bad and doubtful debts are not discounted as it is considered that the effect of discounting would not be significant.

Included in debtors, deposits and payments in advance are the following amounts denominated in a currency other than the functional currency of the entity to which they relate:

	The Group		The Company	
	2011	2010	**2011**	2010
New Taiwan dollars (in million)	**–**	2	**–**	2
Pound sterling (in million)	**1**	–	**1**	–
United States dollars (in million)	**9**	9	**9**	8

39 Loan to a Property Developer

The Group and The Company

in HK$ million	2011 Nominal amount	2011 Carrying amount	2010 Nominal amount	2010 Carrying amount
Interest-free loan to a property developer	–	–	2,000	1,975

The outstanding loan provided to the developer of Tseung Kwan O Area 86 Package 2 ("LOHAS Park") property development project under the terms of the development agreement was fully repaid during the year ended 31 December 2011.

40 Amounts Due from Related Parties

	The Group		The Company	
in HK$ million	**2011**	2010	**2011**	2010
Amounts due from:				
– HKSAR Government	**248**	156	**248**	156
– KCRC	**20**	25	**20**	25
– non-controlled subsidiaries	**23**	17	**23**	17
– associates	**111**	132	**63**	71
– other subsidiaries of the Company (net of impairment losses)	**–**	–	**4,681**	4,096
	402	330	**5,035**	4,365

The amount due from HKSAR Government includes outstanding receivables in relation to the Shatin to Central Link, South Island Line (East) and Kwun Tong Line Extension projects.

The amount due from KCRC related to payments to the Company in respect of the Outsourcing Agreement and costs on certain capital works recoverable from KCRC in accordance with the Merger Framework Agreement.

The amount due from non-controlled subsidiaries related to receivables from Octopus Cards Limited.

The amounts due from associates of the Group as at 31 December 2011 included the outstanding balances of loan to Tunnelbanan Teknik Stockholm AB ("TBT"), amounting to HK$56 million (SEK50 million) (2010: HK$75 million or SEK65 million), which bears an interest rate of 3% per annum above the 3-month Stockholm Inter Bank Offer Rate published by the Riksbank with repayment due by 31 December 2013. The amounts due from associates of the Group as at 31 December 2010 included a loan to London Overground Rail Operations Ltd ("LOROL") amounting to HK$12 million or GBP 1 million, which was fully repaid during the year ended 31 December 2011.

All contract retentions on the above entrusted works were due for release within one year. All other amounts due from HKSAR Government and other related parties were expected to be received within 12 months.

The nominal values of amounts due from HKSAR Government and other related parties are considered not significantly different from their fair values as the amounts due are expected to be substantially settled within 24 months.

41 Cash, Bank Balances and Deposits

	The Group		The Company	
in HK$ million	**2011**	2010	**2011**	2010
Deposits with banks and other financial institutions	**14,009**	12,337	**13,728**	12,065
Cash at banks and on hand	**2,091**	997	**243**	208
Cash, bank balances and deposits	**16,100**	13,334	**13,971**	12,273
Less: Bank deposits with more than three months to maturity when placed	**(12,673)**	(9,610)	**(12,396)**	(9,355)
Less: Bank overdrafts (note 42A)	**–**	(16)	**–**	(16)
Cash and cash equivalents in the cash flow statement	**3,427**	3,708	**1,575**	2,902

Included in cash, bank balance and deposits in the balance sheet are the following amounts denominated in a currency other than the functional currency of the entity to which they relate:

	The Group		The Company	
	2011	2010	**2011**	2010
Australian dollars (in million)	**5**	11	**5**	11
Euros (in million)	**6**	5	**6**	5
Japanese Yen (in million)	**42**	100	**42**	100
New Taiwan dollars (in million)	**8**	10	**8**	10
Pound sterling (in million)	**2**	–	**2**	–
Renminbi (in million)	**3**	–	**–**	–
Swedish krona (in million)	**–**	2	**–**	2
United States dollars (in million)	**603**	679	**601**	676

42 Loans and Other Obligations

A By Type

The Group

	2011			2010		
in HK$ million	Carrying amount	Fair value	Repayable amount	Carrying amount	Fair value	Repayable amount
Capital market instruments						
Listed or publicly traded:						
Debt issuance programme (Eurobond due 2014)	**4,734**	**5,038**	**4,663**	4,759	5,144	4,663
	4,734	**5,038**	**4,663**	4,759	5,144	4,663
Unlisted:						
Debt issuance programme notes due 2012 to 2020 (2010: due 2011 to 2020)	**8,421**	**9,130**	**8,180**	6,679	7,202	6,447
	8,421	**9,130**	**8,180**	6,679	7,202	6,447
Total capital market instruments	**13,155**	**14,168**	**12,843**	11,438	12,346	11,110
Bank loans	**9,663**	**9,665**	**9,665**	8,971	8,973	8,972
Others	**350**	**469**	**350**	332	370	332
Loans and others	**23,168**	**24,302**	**22,858**	20,741	21,689	20,414
Bank overdrafts	**–**	**–**	**–**	16	16	16
Short-term loans	**–**	**–**	**–**	300	300	300
Total	**23,168**	**24,302**	**22,858**	21,057	22,005	20,730

42 Loans and Other Obligations *(continued)*

A By Type *(continued)*

The Company

in HK$ million	2011 Carrying amount	2011 Fair value	2011 Repayable amount	2010 Carrying amount	2010 Fair value	2010 Repayable amount
Capital market instruments						
Unlisted:						
Debt issuance programme notes due 2018	**461**	**673**	**465**	457	646	466
Bank loans	**6,698**	**6,700**	**6,700**	6,915	6,918	6,916
Others	**343**	**464**	**343**	328	366	328
Loans and others	**7,502**	**7,837**	**7,508**	7,700	7,930	7,710
Bank overdrafts	**–**	**–**	**–**	16	16	16
Short-term loans	**–**	**–**	**–**	300	300	300
Total	**7,502**	**7,837**	**7,508**	8,016	8,246	8,026

Others include non-defeased obligations under lease out/lease back transaction (note 24E).

As at 31 December 2011, the Group had a number of uncommitted facilities with undrawn amounts totalling HK$14,135 million (2010: HK$15,028 million), comprising a debt issuance programme and short-term bank loan facilities.

The fair values are based on the discounted cash flows method which discounts the future contractual cash flows at the current market interest and foreign exchange rates that is available to the Group for similar financial instruments.

The carrying amounts of short-term loans and bank overdrafts approximated their fair values.

The amounts of borrowings, denominated in a currency other than the functional currency of the entity to which they relate, before and after currency hedging activities are as follows:

The Group

	Before hedging activities		After hedging activities	
	2011	2010	**2011**	2010
Euros (in million)	**–**	1	**–**	–
Renminbi (in million)	**1,000**	–	**–**	–
United States dollars (in million)	**760**	761	**–**	1

The Company

	Before hedging activities		After hedging activities	
	2011	2010	**2011**	2010
Euros (in million)	**–**	1	**–**	–
United States dollars (in million)	**60**	61	**–**	1

42 Loans and Other Obligations *(continued)*

B By Repayment Terms

The Group

in HK$ million	2011 Capital market instruments	2011 Bank loans and overdrafts	2011 Others	2011 Total	2010 Capital market instruments	2010 Bank loans and overdrafts	2010 Others	2010 Total
Long-term loans and others								
Amounts repayable beyond 5 years	**2,515**	**2,862**	**343**	**5,720**	2,715	1,471	328	4,514
Amounts repayable within a period of between 2 and 5 years	**6,863**	**364**	**2**	**7,229**	7,793	1,084	2	8,879
Amounts repayable within a period of between 1 and 2 years	**3,363**	**221**	**3**	**3,587**	102	6,400	1	6,503
Amounts repayable within 1 year	**102**	**6,218**	**2**	**6,322**	500	17	1	518
	12,843	**9,665**	**350**	**22,858**	11,110	8,972	332	20,414
Bank overdrafts	**–**	**–**	**–**	**–**	–	16	–	16
Short-term loans	**–**	**–**	**–**	**–**	–	300	–	300
	12,843	**9,665**	**350**	**22,858**	11,110	9,288	332	20,730
Less: Unamortised discount/premium/ finance charges outstanding	**(35)**	**(2)**	**–**	**(37)**	(38)	(5)	–	(43)
Adjustment due to fair value change of financial instruments	**347**	**–**	**–**	**347**	366	4	–	370
Total carrying amount of debt	**13,155**	**9,663**	**350**	**23,168**	11,438	9,287	332	21,057

The Company

in HK$ million	2011 Capital market instruments	2011 Bank loans and overdrafts	2011 Others	2011 Total	2010 Capital market instruments	2010 Bank loans and overdrafts	2010 Others	2010 Total
Long-term loans and others								
Amounts repayable beyond 5 years	**465**	**–**	**343**	**808**	465	–	328	793
Amounts repayable within a period of between 2 and 5 years	**–**	**322**	**–**	**322**	1	511	–	512
Amounts repayable within a period of between 1 and 2 years	**–**	**189**	**–**	**189**	–	6,389	–	6,389
Amounts repayable within 1 year	**–**	**6,189**	**–**	**6,189**	–	16	–	16
	465	**6,700**	**343**	**7,508**	466	6,916	328	7,710
Bank overdrafts	**–**	**–**	**–**	**–**	–	16	–	16
Short-term loans	**–**	**–**	**–**	**–**	–	300	–	300
	465	**6,700**	**343**	**7,508**	466	7,232	328	8,026
Less: Unamortised discount/premium/ finance charges outstanding	**(5)**	**(2)**	**–**	**(7)**	(5)	(5)	–	(10)
Adjustment due to fair value change of financial instruments	**1**	**–**	**–**	**1**	(4)	4	–	–
Total carrying amount of debt	**461**	**6,698**	**343**	**7,502**	457	7,231	328	8,016

The amounts repayable within 1 year in respect of capital market instruments and bank loans are included in long-term loans as these amounts are intended to be refinanced on a long-term basis.

42 Loans and Other Obligations *(continued)*

C Bonds and Notes Issued and Redeemed

Notes issued during the year ended 31 December 2011 and 2010 comprise:

The Group

in HK$ million	2011 Principal amount	2011 Net consideration received	2010 Principal amount	2010 Net consideration received
Debt issuance programme notes	**2,206**	**2,198**	–	–

The above notes were issued in Hong Kong by a subsidiary, MTR Corporation (C.I.) Limited. The notes issued are unconditionally and irrevocably guaranteed by the Company, and are direct, unsecured, unconditional and unsubordinated to other unsecured and unsubordinated obligations of MTR Corporation (C.I.) Limited. The obligations of the Company under the guarantee are direct, unsecured, unconditional, and unsubordinated to other unsecured and unsubordinated obligations of the Company.

During the year ended 31 December 2011, the Group redeemed HK$500 million of its unlisted debt securities (2010: HK$1,100 million). During the year ended 31 December 2011, the Group did not redeem any of its listed securities (2010: redeemed US$600 million).

D Guarantees and Pledges

(i) There were no guarantees given by HKSAR Government in respect of the loan facilities of the Group as at 31 December 2011 and 2010.

(ii) As at 31 December 2011, certain assets held by MTR Corporation (Shenzhen) Limited, an indirect wholly owned subsidiary of the Company in the Mainland of China, were pledged as security for a RMB4,000 million (2010: RMB4,000 million) bank loan facility granted to it.

(iii) As at 31 December 2011, certain assets held by Metro Trains Melbourne Pty. Ltd., a 60% owned subsidiary of the Company in Australia, were pledged as security for an AUD13 million (2010: AUD13 million) bank loan facility granted to it.

Apart from the above, none of the other assets of the Group was charged or subject to any encumbrance as at 31 December 2011.

43 Creditors and Accrued Charges

in HK$ million	The Group 2011	The Group 2010	The Company 2011	The Company 2010
Creditors and accrued charges				
– West Island Line Project	**417**	512	**417**	512
– South Island Line (East) Project	**479**	27	**479**	27
– Kwun Tong Line Extension Project	**188**	14	**188**	14
– Shenzhen Metro Longhua Line Project	**1,183**	535	**–**	–
– Hong Kong property development projects	**681**	657	**681**	657
– Mainland property development project	**1,950**	–	**–**	–
– Railway subsidiaries outside of Hong Kong	**1,337**	1,163	**–**	–
– Hong Kong operations and others	**5,539**	4,993	**5,025**	4,508
Gross amount due to customers for contract work	**15**	15	**15**	15
Government grant on West Island Line Project un-utilised	**4,613**	7,575	**4,613**	7,575
	16,402	15,491	**11,418**	13,308

As at 31 December 2011, the aggregate amount of contract costs incurred plus recognised profits less recognised losses included in the gross amount due to customers for contract works was HK$294 million (2010: HK$294 million). All of the gross amount due to customers for contract work as at 31 December 2011 and 2010 is expected to be settled after more than one year.

43 Creditors and Accrued Charges *(continued)*

The analysis of creditors by due dates is as follows:

	The Group		The Company	
in HK$ million	**2011**	2010	**2011**	2010
Due within 30 days or on demand	**2,765**	2,331	**1,267**	1,025
Due after 30 days but within 60 days	**2,379**	1,603	**1,612**	1,077
Due after 60 days but within 90 days	**537**	341	**335**	331
Due after 90 days	**3,950**	1,725	**1,627**	1,530
	9,631	6,000	**4,841**	3,963
Rental and other refundable deposits	**1,704**	1,517	**1,618**	1,472
Accrued employee benefits	**454**	399	**346**	298
Government grant on West Island Line Project un-utilised	**4,613**	7,575	**4,613**	7,575
	16,402	15,491	**11,418**	13,308

Creditors and accrued charges were expected to be settled within one year except for HK$1,540 million (2010: HK$1,544 million) included in Hong Kong operations and others and HK$29 million (2010: nil) included in railway subsidiaries outside of Hong Kong, which were expected to be settled after one year. The amounts due after one year are mainly rental deposits received from investment property and station kiosk tenants and advance income received from telecommunication service operators, majority of which are due to be repaid within three years. The Group considers the effect of discounting these deposits would be immaterial.

The nominal values of creditors and accrued charges are not significantly different from their fair values.

Included in creditors and accrued charges are the following amounts denominated in a currency other than the functional currency of the entity to which they relate:

	The Group		The Company	
	2011	2010	**2011**	2010
Australian dollars (in million)	**2**	1	**2**	1
Euros (in million)	**3**	6	**3**	6
Japanese Yen (in million)	**83**	31	**83**	31
Pound sterling (in million)	**1**	1	**1**	1
Renminbi (in million)	**1,577**	–	**–**	–
United States dollars (in million)	**17**	17	**2**	2

44 Contract Retentions

The Group

in HK$ million	Due for release within 12 months	Due for release after 12 months	Total
2011			
Railway extension projects	**2**	**300**	**302**
Transport operations and others	**120**	**221**	**341**
	122	**521**	**643**
2010			
Railway extension projects	3	123	126
Transport operations and others	105	173	278
	108	296	404

44 Contract Retentions *(continued)*

The Company

in HK$ million	Due for release within 12 months	Due for release after 12 months	Total
2011			
Railway extension projects	**2**	**300**	**302**
Transport operations and others	**60**	**61**	**121**
	62	**361**	**423**
2010			
Railway extension projects	3	123	126
Transport operations and others	46	49	95
	49	172	221

The effect of discounting these contract retentions is considered immaterial as these amounts are substantially due to be released within 24 months.

45 Amounts Due to Related Parties

	The Group		The Company	
in HK$ million	**2011**	2010	**2011**	2010
Amounts due to:				
– HKSAR Government	**31**	27	**31**	27
– KCRC	**1,432**	809	**1,432**	809
– an associate	**18**	56	**–**	–
– subsidiaries	**–**	–	**11,781**	11,243
	1,481	892	**13,244**	12,079

The amount due to HKSAR Government related to land administrative costs in respect of the West Island Line, South Island Line (East) and Kwun Tong Line Extension projects.

The amount due to KCRC relates to mandatory payments and related interest payable to KCRC upon tender award in respect of the property development sites along the East Rail Line and Light Rail as well as the accrued portion of the fixed annual payment and variable annual payment.

The amount due to an associate as at 31 December 2010 included the outstanding balance of a loan from Tunnelbanan Teknik Stockholm AB to MTR Stockholm AB amounting to HK$29 million (SEK25 million), which was fully repaid during the year ended 31 December 2011. The loan is unsecured, bears an interest rate of 3% per annum above the 3-month Stockholm Inter Bank Offer Rate and has no fixed terms of repayment.

The amount due to the Company's subsidiaries included HK$11,641 million (2010: HK$11,162 million) due to MTR Corporation (C.I.) Limited in respect of proceeds from bonds and notes issued by the subsidiary, which were on-lent to the Company for its general corporate purposes with specified repayment dates and interest rates (note 42C), and accrued interest. These amounts are stated at their fair values. The remaining balances due to subsidiaries are non-interest bearing and have not been discounted as they do not have any fixed repayment terms and the amount is not material. Out of the total amount due to subsidiaries as at 31 December 2011, HK$11,328 million (2010: HK$10,481 million) is expected to be settled after one year.

46 Obligations under Service Concession

Movements of the Group's and the Company's obligations under service concessions are as follows:

in HK$ million	The Group 2011	The Group 2010	The Company 2011	The Company 2010
Balance as at 1 January	**10,749**	10,625	**10,592**	10,625
Add: Total annual lease payments capitalised at inception	**–**	151	**–**	–
Add: Net increase in interest payable	**3**	4	**–**	–
Less: Amount repaid/payable during the year	**(35)**	(36)	**(35)**	(33)
Exchange difference	**7**	5	**–**	–
Balance as at 31 December	**10,724**	10,749	**10,557**	10,592

During the year ended 31 December 2010, the Group recognised HK$151 million of the obligation under service concession for the annual lease payment in respect of Shenzhen Longhua Line Phase 1.

The outstanding balances as at 31 December 2011 and 2010 are repayable as follows:

The Group

in HK$ million	2011 Present value of fixed annual payments	2011 Interest expense relating to future periods	2011 Total fixed annual payments	2010 Present value of fixed annual payments	2010 Interest expense relating to future periods	2010 Total fixed annual payments
Amounts repayable beyond 5 years	**10,510**	**20,531**	**31,041**	10,549	21,232	31,781
Amounts repayable within a period of between 2 and 5 years	**137**	**2,132**	**2,269**	128	2,140	2,268
Amounts repayable within a period of between 1 and 2 years	**40**	**716**	**756**	37	719	756
Amounts repayable within 1 year	**37**	**718**	**755**	35	721	756
	10,724	**24,097**	**34,821**	10,749	24,812	35,561

The Company

in HK$ million	2011 Present value of fixed annual payments	2011 Interest expense relating to future periods	2011 Total fixed annual payments	2010 Present value of fixed annual payments	2010 Interest expense relating to future periods	2010 Total fixed annual payments
Amounts repayable beyond 5 years	**10,343**	**20,344**	**30,687**	10,392	21,045	31,437
Amounts repayable within a period of between 2 and 5 years	**137**	**2,113**	**2,250**	128	2,122	2,250
Amounts repayable within a period of between 1 and 2 years	**40**	**710**	**750**	37	713	750
Amounts repayable within 1 year	**37**	**713**	**750**	35	715	750
	10,557	**23,880**	**34,437**	10,592	24,595	35,187

47 Loan from Holders of Non-controlling Interests

Loan from holders of non-controlling interests represents that portion of total shareholder loan of AUD48.75 million (HK$384 million) granted to Metro Trains Melbourne Pty. Ltd. ("MTM") by the holders of its non-controlling interests. The loan carries an interest rate of 7.5% per annum and is repayable at the discretion of MTM or on the expiry of the operation and maintenance franchise on 29 November 2017, whichever is earlier.

48 Deferred Income

Movements of deferred income are as follows:

The Group

in HK$ million	Balance at 1 January	Amount received during the year	Offset against development in progress	Amount recognised in profit and loss account	Exchange difference	Balance at 31 December
2011						
Deferred income on property development (note 29B)	**568**	**–**	**(32)**	**(468)**	**–**	**68**
Deferred income on transfer of assets from customers	**37**	**19**	**–**	**(9)**	**–**	**47**
Deferred income on government grant	**–**	**638**	**–**	**(349)**	**(1)**	**288**
	605	**657**	**(32)**	**(826)**	**(1)**	**403**
2010						
Deferred income on property development (note 29B)	124	1,010	(549)	(17)	–	568
Deferred income on transfer of assets from customers	43	–	–	(6)	–	37
	167	1,010	(549)	(23)	–	605

The Company

in HK$ million	Balance at 1 January	Amount received during the year	Offset against development in progress	Amount recognised in profit and loss account	Exchange difference	Balance at 31 December
2011						
Deferred income on property development (note 29B)	**568**	**–**	**(32)**	**(468)**	**–**	**68**
2010						
Deferred income on property development (note 29B)	124	1,010	(549)	(17)	–	568

Deferred income on government grant relates to government subsidy for the operation of Shenzhen Metro Longhua Line.

49 Income Tax in the Balance Sheet

A Current taxation in the consolidated balance sheet comprised provision for Hong Kong Profits Tax for the Company and certain subsidiaries for the year ended 31 December 2011, chargeable at Hong Kong Profits Tax Rate at 16.5% (2010: 16.5%) and after netting off provisional tax paid, and overseas tax chargeable at the appropriate current rates of taxation ruling in the relevant countries.

	The Group		The Company	
in HK$ million	**2011**	2010	**2011**	2010
Provision for Hong Kong Profits Tax for the year (note 17)	**1,619**	1,495	**1,604**	1,484
Hong Kong Provisional Profits Tax paid	**(1,035)**	(581)	**(1,022)**	(574)
	584	914	**582**	910
Balance relating to overseas tax	**13**	104	**–**	–
	597	1,018	**582**	910

49 Income Tax in the Balance Sheet *(continued)*

B Deferred Tax Assets and Liabilities Recognised

The components of deferred tax assets and liabilities recognised in the balance sheet and the movements during the year are as follows:

The Group

	Deferred tax arising from					
in HK$ million	Depreciation allowances in excess of related depreciation	Revaluation of properties	Provision and other temporary differences	Cash flow hedges	Tax losses	Total
2011						
At 1 January 2011	**8,669**	**5,044**	**154**	**(15)**	**(7)**	**13,845**
Charged/(credited) to consolidated profit and loss account	**316**	**840**	**(1)**	**–**	**(9)**	**1,146**
Charged/(credited) to reserves	**–**	**93**	**–**	**(2)**	**–**	**91**
Exchange difference	**(4)**	**–**	**–**	**–**	**–**	**(4)**
At 31 December 2011	**8,981**	**5,977**	**153**	**(17)**	**(16)**	**15,078**
2010						
At 1 January 2010	8,382	4,316	121	(10)	(17)	12,792
Charged to consolidated profit and loss account	287	672	33	–	10	1,002
Charged/(credited) to reserves	–	56	–	(5)	–	51
At 31 December 2010	8,669	5,044	154	(15)	(7)	13,845

The Company

	Deferred tax arising from					
in HK$ million	Depreciation allowances in excess of related depreciation	Revaluation of properties	Provision and other temporary differences	Cash flow hedges	Tax losses	Total
2011						
At 1 January 2011	**8,651**	**5,051**	**153**	**(15)**	**–**	**13,840**
Charged/(credited) to profit and loss account	**274**	**838**	**(12)**	**–**	**–**	**1,100**
Charged/(credited) to reserves	**–**	**93**	**–**	**(2)**	**–**	**91**
At 31 December 2011	**8,925**	**5,982**	**141**	**(17)**	**–**	**15,031**
2010						
At 1 January 2010	8,362	4,325	121	(10)	–	12,798
Charged to profit and loss account	289	670	32	–	–	991
Charged/(credited) to reserves	–	56	–	(5)	–	51
At 31 December 2010	8,651	5,051	153	(15)	–	13,840

	The Group		The Company	
in HK$ million	**2011**	2010	**2011**	2010
Net deferred tax assets recognised on the balance sheet	**(27)**	(9)	**–**	–
Net deferred tax liabilities recognised on the balance sheet	**15,105**	13,854	**15,031**	13,840
	15,078	13,845	**15,031**	13,840

C The Group has not recognised deferred tax assets in respect of some of its subsidiaries' cumulative tax losses of HK$281 million (2010: HK$395 million) as it is not probable that future taxable profits against which the losses can be utilised will be available in the relevant tax jurisdictions and entities.

50 Share Capital and Capital Management

A Share Capital, Share Premium and Capital Reserve

in HK$ million	2011	2010
Authorised:		
6,500,000,000 shares of HK$1.00 each	**6,500**	6,500
Issued and fully paid:		
5,784,871,250 shares (2010: 5,772,563,031 shares) of HK$1.00 each	**5,785**	5,773
Share premium	**11,089**	10,773
Capital reserve	**27,188**	27,188
	44,062	43,734

Pursuant to the Articles of Association of the Company, the capital reserve can only be applied in paying up in full unissued shares to be allotted and distributed as fully paid bonus shares to the shareholders of the Company.

Share premium represents the amount by which the issue price of shares exceeds the par value of those shares. The application of the share premium account is governed by section 48B of the Hong Kong Companies Ordinance.

New shares issued and fully paid up during the year comprise:

	Number of shares	Option/ scrip price HK$	Proceeds received/Transfer from employee share-based capital reserve: Share capital account HK$ million	Share premium account HK$ million	Total HK$ million
Employee share options exercised					
– New Joiners Share Option Scheme	**525,700**	**9.75**	**1**	**6**	**7**
	266,500	**20.66**	**–**	**6**	**6**
– 2007 Share Option Scheme	**932,500**	**18.30**	**1**	**19**	**20**
	31,000	**26.52**	**–**	**1**	**1**
	74,000	**26.85**	**–**	**2**	**2**
	135,000	**27.60**	**–**	**4**	**4**
Issued as 2010 final scrip dividends	**10,343,519**	**27.87**	**10**	**278**	**288**
	12,308,219		**12**	**316**	**328**

An analysis of the Company's outstanding share options as at 31 December 2011 are disclosed in note 53.

B Capital Management

The Group's primary objectives in managing capital are to safeguard its ability to continue as a going concern, and to generate sufficient profit to maintain growth and provide an adequate return to its shareholders.

The Group manages the amount of capital in proportion to risk, and makes adjustments to its capital structure through the amount of dividend payment to shareholders, issuance of scrip and new shares, and managing its debt portfolio in conjunction with projected financing requirement. The Financial Secretary Incorporated of HKSAR Government is the majority shareholder of the Company holding 4,434,552,207 shares as at 31 December 2011, representing 76.7% of total equity interest in the Company.

The Group monitors capital on the basis of the net debt-to-equity ratio, which is calculated on net borrowings as a percentage of the total equity attributable to shareholders of the Company, where net borrowings are represented by the aggregate of loans and other obligations, bank overdrafts, obligations under service concession and loan from holders of non-controlling interests net of cash and cash equivalents and bank medium term notes. The Group's net debt-to-equity ratios over the past years have been trending downward since the Rail Merger from 48.5% at 31 December 2007 to 12.8% at 31 December 2010 and 11.9% at 31 December 2011.

Octopus Cards Limited is subject to a prescribed ratio of total capital to total risk-weighted assets as required by the Hong Kong Monetary Authority. Fasttrack Insurance Ltd. is required to maintain a minimum level of shareholders' fund based on the Bermuda Insurance Act. MTR Corporation (Shenzhen) Limited is subject to minimum capital requirement at 40% of the total investment for the Shenzhen Longhua Line project in accordance with the concession agreement. Metro Trains Melbourne Pty. Ltd. is required to maintain total shareholders' funds at a specified amount in accordance with the franchise agreement. MTR Stockholm AB is required to maintain total shareholders' fund at or above 50% of its registered share capital based on the Swedish Companies Act. As at 31 December 2011, all these capital requirements were met. Apart from these, neither the Company nor any of its other subsidiaries are subject to externally imposed capital requirements.

51 Other Reserves

The reconciliation between the opening and closing balances of each component of the Group's consolidated equity is set out in the consolidated statement of changes in equity. Details of the changes in the Company's individual components of equity between the beginning and the end of the year are set out below:

in HK$ million	Fixed assets revaluation reserve	Hedging reserve	Employee share-based capital reserve	Retained profits	Total other reserves
2011					
Balance as at 1 January 2011	**1,417**	**(78)**	**102**	**70,815**	**72,256**
2010 final dividend	**–**	**–**	**–**	**(2,598)**	**(2,598)**
2011 interim dividend	**–**	**–**	**–**	**(1,446)**	**(1,446)**
Employee share-based payments	**–**	**–**	**110**	**–**	**110**
Employee share options exercised	**–**	**–**	**(6)**	**–**	**(6)**
Employee share options forfeited	**–**	**–**	**(5)**	**5**	**–**
Total comprehensive income for the year	**471**	**(12)**	**–**	**14,415**	**14,874**
Balance as at 31 December 2011	**1,888**	**(90)**	**201**	**81,191**	**83,190**
2010					
Balance as at 1 January 2010	1,132	(52)	52	61,920	63,052
2009 final dividend	–	–	–	(2,177)	(2,177)
2010 interim dividend	–	–	–	(807)	(807)
Employee share-based payments	–	–	57	–	57
Employee share options exercised	–	–	(6)	–	(6)
Employee share options forfeited	–	–	(1)	1	–
Total comprehensive income for the year	285	(26)	–	11,878	12,137
Balance as at 31 December 2010	1,417	(78)	102	70,815	72,256

The fixed assets revaluation reserve was set up to deal with the surpluses or deficits arising from the revaluation of self-occupied land and buildings (note 2F(ii)).

The hedging reserve comprises the effective portion of the cumulative net change in the fair value of hedging instruments used in cash flow hedges pending subsequent recognition of the hedged cash flow in accordance with the accounting policy adopted for cash flow hedges as explained in note 2T(ii).

The employee share-based capital reserve comprises the fair value of share options granted which are yet to be exercised, as explained in accounting policy under note 2U(iii). The amount will either be transferred to the share premium account when the option is exercised, or be released directly to retained profits if the option is expired or forfeited.

The exchange reserve comprises all foreign exchange differences arising from the translation of the accounts of foreign enterprises. The reserve is dealt with in accordance with the accounting policy set out in note 2CC.

Apart from retained profits, the other reserves are not available for distribution to shareholders because they do not constitute realised profits. In addition, the Company considers the cumulative surpluses on revaluation of investment properties net of tax of HK$28,382 million (2010: HK$24,143 million) included in retained profits are non-distributable as they also do not constitute realised profits. As at 31 December 2011, the Company considers that the total amount of reserves available for distribution to equity shareholders amounted to HK$52,719 million (2010: HK$46,594 million).

Included in the Group's retained profits as at 31 December 2011 is an amount of HK$665 million (2010: HK$512 million), being the retained profits attributable to the non-controlled subsidiaries and associates.

52 Cash Generated from Operations

Reconciliation of operating profit before property developments, depreciation, amortisation and variable annual payment to cash generated from operations is as follows:

in HK$ million	2011	2010
Operating profit before property developments, depreciation, amortisation and variable annual payment	**12,124**	10,917
Adjustments for:		
(Decrease)/increase in provision for obsolete stock	**(2)**	2
Loss on disposal of fixed assets	**32**	50
Amortisation of deferred income from government subsidy for Shenzhen Metro Longhua Line operation	**(62)**	–
Amortisation of deferred income from transfers of assets from customers	**(9)**	(6)
Decrease/(increase) in fair value of derivative instruments	**8**	(1)
Unrealised loss on revaluation of investment in securities	**4**	2
Employee share-based payment expenses	**113**	61
Exchange (gain)/loss	**(8)**	14
Operating profit from recurrent businesses before working capital changes	**12,200**	11,039
Increase in debtors, deposits and payments in advance	**(395)**	(244)
Increase in stores and spares	**(72)**	(5)
Increase in creditors and accrued charges	**756**	1,130
Cash generated from operations	**12,489**	11,920

53 Share-based Payments

A Equity-settled Share-based Payments

The Group granted equity-settled share options to its Members of the Executive Directorate and certain employees under share option schemes. As at 31 December 2011, the Company maintained two share option schemes, namely, the New Joiners Share Option Scheme and the 2007 Share Option Scheme. Details of the schemes are as follows:

(i) New Joiners Share Option Scheme

In May 2002, the New Joiners Share Option Scheme (the "New Option Scheme") was adopted at the 2002 Annual General Meeting to provide share options to new members of the top and senior management of the Company who did not participate in the Pre-IPO Option Scheme. Under the Rules of the New Option Scheme, a maximum of 5,056,431 shares, which represent 0.1% of the issued share capital of the Company as at 31 December 2011, may be issued pursuant to the exercise of options granted under the New Option Scheme. Options granted will be evenly vested in respect of their underlying shares over a period of three years from the date on which the relevant option is offered. The exercise price of any option granted under the New Option Scheme is to be determined by the Company upon the offer of grant of the option and the exercise price should not be less than the greatest of (i) the average closing price of an MTR share for the five business days immediately preceding the day of offer of such option; (ii) the closing price of an MTR share on the day of offer of such option, which must be a business day; and (iii) the nominal value of an MTR share. The New Option Scheme expired on 16 May 2007 and no options can be granted under this Scheme on or after that date.

The following table summarises the outstanding share options granted under the New Option Scheme since inception:

Date of grant	Number of share options	Exercise price HK$	Exercisable period
23 September 2005	213,000	15.97	on or prior to 9 September 2015
15 May 2006	22,000	20.66	on or prior to 25 April 2016
5 October 2006	94,000	19.732	on or prior to 29 September 2016

53 Share-based Payments *(continued)*

A Equity-settled Share-based Payments *(continued)*

Movements in the number of share options outstanding and their related weighted average exercise prices were as follows:

	2011		2010	
	Number of share options	Weighted average exercise price HK$	Number of share options	Weighted average exercise price HK$
Outstanding at 1 January	**1,121,200**	**14.581**	1,316,200	15.038
Exercised during the year	**(792,200)**	**13.420**	(195,000)	17.667
Outstanding at 31 December	**329,000**	**17.377**	1,121,200	14.581
Exercisable at 31 December	**329,000**	**17.358**	1,121,200	14.576

The weighted average closing price in respect of the share options exercised during the year was HK$27.470 (2010: HK$29.104).

Share options outstanding at 31 December 2011 had the following exercise prices and remaining contractual lives:

	2011		2010	
Exercise price	Number of share options	Remaining contractual life years	Number of share options	Remaining contractual life years
HK$9.75	–	–	525,700	2.54
HK$15.97	**213,000**	**3.69**	213,000	4.69
HK$20.66	**22,000**	**4.32**	288,500	5.32
HK$19.732	**94,000**	**4.75**	94,000	5.75
	329,000		1,121,200	

(ii) 2007 Share Option Scheme

Following the expiry of the New Option Scheme in May 2007, the 2007 Share Option Scheme (the "2007 Option Scheme") was submitted and approved at the 2007 Annual General Meeting to enhance the Company's ability to attract the best available personnel, to retain and motivate critical and key employees, to align their interest to the long-term success of the Company and to provide them with fair and market competitive remuneration. Under the Rules of the 2007 Option Scheme, a maximum of 277,461,072 shares, which represent 4.8% of the issued share capital of the Company as at 31 December 2011, may be issued pursuant to the exercise of options granted after 7 June 2007 under all share option schemes of the Company including the 2007 Option Scheme. Options granted will be vested in respect of their underlying shares not less than 1 year from the date on which the relevant option is offered. The exercise price of any option granted under the 2007 Option Scheme is to be determined by the Company upon the offer of grant of the option and the exercise price should not be less than the greatest of (i) the average closing price of an MTR share for the five business days immediately preceding the day of offer of such option; (ii) the closing price of an MTR share on the day of offer of such option, which must be a business day; and (iii) the nominal value of an MTR share.

Subject to the rules of the 2007 Option Scheme, the Company may, from time to time during the scheme period, offer to grant share options to any eligible employees at its absolute discretion. Under the 2007 Option Scheme, the date of grant is defined as the date of acceptance of the offer to grant the option.

53 Share-based Payments *(continued)*

A Equity-settled Share-based Payments *(continued)*

As at 31 December 2011, the following awards of share options were offered to Members of the Executive Directorate and selected employees of the Company under the 2007 Option Scheme:

Awards of share options	Date of offer	Number of share options offered and accepted	Date of acceptance
2008 Award	10 December 2007	8,273,000	Period between 11 December 2007 to 7 January 2008
	26 March 2008	2,749,000	Period between 28 March 2008 to 23 April 2008
2009 Award	8 December 2008	12,712,000	Period between 8 December 2008 to 30 December 2008
	12 June 2009	345,000	Period between 18 June 2009 to 9 July 2009
2010 Award	8 December 2009	15,718,000	Period between 9 December 2009 to 22 December 2009
	28 June 2010	355,000	On 21 July 2010
2011 Award	16 December 2010	15,546,500	16 December 2010 to 23 December 2010
	27 June 2011	215,000	On 7 July 2011

The following table summarises the outstanding share options as at 31 December 2011 granted under the 2007 Option Scheme since inception:

Date of grant	Number of share options	Exercise price HK$	Exercisable period
2008 Award			
11 December 2007	45,000	27.60	on or prior to 10 December 2014
12 December 2007	1,903,000	27.60	on or prior to 10 December 2014
13 December 2007	1,740,000	27.60	on or prior to 10 December 2014
14 December 2007	820,000	27.60	on or prior to 10 December 2014
15 December 2007	228,000	27.60	on or prior to 10 December 2014
17 December 2007	730,000	27.60	on or prior to 10 December 2014
18 December 2007	275,000	27.60	on or prior to 10 December 2014
19 December 2007	80,000	27.60	on or prior to 10 December 2014
20 December 2007	190,000	27.60	on or prior to 10 December 2014
22 December 2007	35,000	27.60	on or prior to 10 December 2014
24 December 2007	118,000	27.60	on or prior to 10 December 2014
28 December 2007	35,000	27.60	on or prior to 10 December 2014
31 December 2007	130,000	27.60	on or prior to 10 December 2014
2 January 2008	35,000	27.60	on or prior to 10 December 2014
3 January 2008	40,000	27.60	on or prior to 10 December 2014
7 January 2008	80,000	27.60	on or prior to 10 December 2014
28 March 2008	199,000	26.52	on or prior to 26 March 2015
31 March 2008	323,000	26.52	on or prior to 26 March 2015
1 April 2008	249,000	26.52	on or prior to 26 March 2015
2 April 2008	276,000	26.52	on or prior to 26 March 2015
3 April 2008	140,000	26.52	on or prior to 26 March 2015
4 April 2008	23,000	26.52	on or prior to 26 March 2015
5 April 2008	17,000	26.52	on or prior to 26 March 2015
7 April 2008	330,000	26.52	on or prior to 26 March 2015
8 April 2008	110,000	26.52	on or prior to 26 March 2015
9 April 2008	85,000	26.52	on or prior to 26 March 2015
10 April 2008	58,000	26.52	on or prior to 26 March 2015
11 April 2008	117,000	26.52	on or prior to 26 March 2015
12 April 2008	48,000	26.52	on or prior to 26 March 2015
14 April 2008	40,000	26.52	on or prior to 26 March 2015
15 April 2008	34,000	26.52	on or prior to 26 March 2015
16 April 2008	40,000	26.52	on or prior to 26 March 2015
17 April 2008	124,000	26.52	on or prior to 26 March 2015
18 April 2008	15,000	26.52	on or prior to 26 March 2015
19 April 2008	25,000	26.52	on or prior to 26 March 2015
21 April 2008	66,000	26.52	on or prior to 26 March 2015
23 April 2008	19,000	26.52	on or prior to 26 March 2015

53 Share-based Payments *(continued)*

A Equity-settled Share-based Payments *(continued)*

Date of grant	Number of share options	Exercise price HK$	Exercisable period
2009 Award			
8 December 2008	110,000	18.30	on or prior to 8 December 2015
9 December 2008	1,359,000	18.30	on or prior to 8 December 2015
10 December 2008	1,897,900	18.30	on or prior to 8 December 2015
11 December 2008	1,993,200	18.30	on or prior to 8 December 2015
12 December 2008	1,141,000	18.30	on or prior to 8 December 2015
13 December 2008	78,000	18.30	on or prior to 8 December 2015
14 December 2008	52,200	18.30	on or prior to 8 December 2015
15 December 2008	873,200	18.30	on or prior to 8 December 2015
16 December 2008	450,000	18.30	on or prior to 8 December 2015
17 December 2008	470,500	18.30	on or prior to 8 December 2015
18 December 2008	470,500	18.30	on or prior to 8 December 2015
19 December 2008	198,000	18.30	on or prior to 8 December 2015
20 December 2008	19,000	18.30	on or prior to 8 December 2015
22 December 2008	487,000	18.30	on or prior to 8 December 2015
23 December 2008	218,000	18.30	on or prior to 8 December 2015
24 December 2008	367,500	18.30	on or prior to 8 December 2015
25 December 2008	45,000	18.30	on or prior to 8 December 2015
29 December 2008	118,000	18.30	on or prior to 8 December 2015
30 December 2008	19,000	18.30	on or prior to 8 December 2015
18 June 2009	175,000	24.50	on or prior to 12 June 2016
6 July 2009	45,000	24.50	on or prior to 12 June 2016
9 July 2009	30,000	24.50	on or prior to 12 June 2016
2010 Award			
9 December 2009	585,000	26.85	on or prior to 8 December 2016
10 December 2009	2,646,000	26.85	on or prior to 8 December 2016
11 December 2009	2,235,000	26.85	on or prior to 8 December 2016
12 December 2009	565,500	26.85	on or prior to 8 December 2016
13 December 2009	12,500	26.85	on or prior to 8 December 2016
14 December 2009	2,437,500	26.85	on or prior to 8 December 2016
15 December 2009	2,506,000	26.85	on or prior to 8 December 2016
16 December 2009	1,414,000	26.85	on or prior to 8 December 2016
17 December 2009	975,000	26.85	on or prior to 8 December 2016
18 December 2009	380,500	26.85	on or prior to 8 December 2016
19 December 2009	70,000	26.85	on or prior to 8 December 2016
20 December 2009	75,000	26.85	on or prior to 8 December 2016
21 December 2009	501,000	26.85	on or prior to 8 December 2016
22 December 2009	215,000	26.85	on or prior to 8 December 2016
21 July 2010	330,000	27.73	on or prior to 28 June 2017
2011 Award			
16 December 2010	194,000	28.84	on or prior to 16 December 2017
17 December 2010	5,326,500	28.84	on or prior to 16 December 2017
18 December 2010	673,000	28.84	on or prior to 16 December 2017
19 December 2010	174,000	28.84	on or prior to 16 December 2017
20 December 2010	4,728,000	28.84	on or prior to 16 December 2017
21 December 2010	3,001,000	28.84	on or prior to 16 December 2017
22 December 2010	956,000	28.84	on or prior to 16 December 2017
23 December 2010	189,000	28.84	on or prior to 16 December 2017
7 July 2011	215,000	26.96	on or prior to 27 June 2018

53 Share-based Payments *(continued)*

A Equity-settled Share-based Payments *(continued)*

Movements in the number of share options outstanding and their related weighted average exercise prices were as follows:

	2011		2010	
	Number of share options	Weighted average exercise price HK$	Number of share options	Weighted average exercise price HK$
Outstanding at 1 January	**52,568,500**	**25.646**	38,929,500	24.185
Granted during the year	**215,000**	**26.960**	15,901,500	28.815
Exercised during the year	**(1,172,500)**	**20.128**	(1,573,500)	21.840
Forfeited during the year	**(1,767,500)**	**26.368**	(689,000)	24.888
Outstanding at 31 December	**49,843,500**	**25.756**	52,568,500	25.646
Exercisable at 31 December	**34,417,000**	**24.683**	21,495,500	24.095

Share options outstanding at 31 December 2011 had the following exercise prices and remaining contractual lives:

	2011		2010	
Exercise price	Number of share options	Remaining contractual life years	Number of share options	Remaining contractual life years
HK$27.60	**6,484,000**	**3**	7,208,000	4
HK$26.52	**2,338,000**	**3**	2,406,000	4
HK$18.30	**10,367,000**	**4**	11,523,000	5
HK$24.50	**250,000**	**4**	250,000	5
HK$26.85	**14,618,000**	**5**	15,280,000	6
HK$27.73	**330,000**	**5**	355,000	6
HK$28.84	**15,241,500**	**6**	15,546,500	7
HK$26.96	**215,000**	**6**	–	–
	49,843,500		52,568,500	

According to the Black-Scholes pricing model, the fair values of options granted during the year ended 31 December 2011 were as follows:

		Inputs into the Black-Scholes pricing model					
Date of grant	Fair value of options granted HK$	Share price immediately before grant date HK$	Exercise price HK$	Expected volatility	Expected life years	Risk-free interest rate %	Expected dividend per share HK$
7 July 2011	**5.01**	**27.70**	**26.96**	**0.2827**	**3.5**	**0.84**	**0.7**

When computing fair values of the options granted, expected volatility was determined by calculating the historical volatility of the Group's share price over the previous 3.5 years and the expected life adopted was assumed to be 3.5 years after granting of the options, with expected dividends based on historical dividends. In addition, vesting terms under the grants have been taken into account whilst no market conditions associated with the share option grants have been considered. Changes in the subjective input assumptions could materially affect the fair value estimate.

(iii) During the year ended 31 December 2011, the equity-settled share-based payments recognised as an expense amounted to HK$110 million (2010: HK$57 million), all relating to the 2007 Option Scheme.

The Pre-Global Offering Share Option Scheme expired on 11 September 2010. During the period from 1 January 2010 to the expiry day, a total of 2,922,500 previously vested share options were exercised, with a weighted average closing price of HK$27.993 per share. On the expiry day, a total of 25,500 options lapsed.

53 Share-based Payments *(continued)*

B Cash-settled Share-based Payments

(i) C K Chow did not participate in the Company's Pre-Global Offering Share Option Scheme and New Joiners Share Option Scheme. Pursuant to the completion of his two-year contract which expired on 31 December 2011, he was paid on 4 January 2012 an equivalent value in cash of 222,161 shares in the Company, amounting to HK$5.6 million (calculated 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). For the year ended 31 December 2011, HK$2.3 million (2010: HK$3.0 million) was recorded as share-based payment expense. The fair value of the outstanding entitlement as at 31 December 2010 was calculated based on the closing price of the Company's shares at year-end date of HK$28.30 per share.

(ii) Jay H Walder is entitled to 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). For the year ended 31 December 2011, HK$0.5 million (2010: nil) was recorded as share-based payment expense. The fair value of the outstanding entitlement is calculated based on the closing price of the Company's shares at year-end. As at 31 December 2011, the fair value of these shares was HK$25.15 per share.

(iii) Lincoln K K Leong was entitled to a derivative interest in the Company's shares and was paid on 12 April 2010 an equivalent value in cash of 160,000 shares in the Company, amounting to HK$4.6 million (calculated at a price of HK$28.785 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 9 April 2010). For the year ended 31 December 2010, HK$0.7 million was recorded as share-based payment expense, measured on the same basis as described in note 53B(i) above.

54 Retirement Schemes

The Group operates a number of retirement schemes in Hong Kong, Mainland of China, United Kingdom, Sweden and Australia. The assets of these schemes are held under the terms of separate trust arrangements so that the assets are kept separate from those of the Group. The majority of the Group's employees are covered by the retirement schemes operated by the Company.

A Retirement Schemes Operated by the Company in Hong Kong

The Company operates five retirement schemes under trust in Hong Kong, including the MTR Corporation Limited Retirement Scheme (the "MTR Retirement Scheme"), the MTR Corporation Limited Retention Bonus Scheme (the "MTR RBS"), the MTR Corporation Limited Provident Fund Scheme (the "MTR Provident Fund Scheme") and two Mandatory Provident Fund ("MPF") Schemes, the "MTR MPF Scheme" and the "KCRC MPF Scheme".

Currently, new eligible employees can choose between the MTR Provident Fund Scheme and the MTR MPF Scheme while the MTR MPF Scheme covers employees who did not opt for and who are not eligible to join the MTR Provident Fund Scheme.

(i) MTR Retirement Scheme

The MTR Retirement Scheme is a defined benefit scheme registered under the Occupational Retirement Schemes Ordinance (Chapter 426 of the Laws of Hong Kong) ("ORSO") and granted with MPF Exemption by the Mandatory Provident Fund Schemes Authority ("MPFA").

The MTR Retirement Scheme has been closed to new employees since 31 March 1999. It provides benefits based on the greater of a multiple of final salary times the number of years of service rendered and the accumulated contributions with investment returns. Members' contributions to the MTR Retirement Scheme are based on a fixed percentage of base salary. The Company's contributions are determined with reference to an actuarial valuation carried out by an independent actuarial consulting firm. As at 31 December 2011, the total membership was 4,979 (2010: 5,127). In 2011, members contributed HK$70 million (2010: HK$70 million) and the Company contributed HK$120 million (2010: HK$120 million) to the MTR Retirement Scheme. The net asset value of the MTR Retirement Scheme as at 31 December 2011 was HK$7,794 million (2010: HK$8,200 million).

Actuarial valuation as at 31 December 2011 to determine the accounting obligations in accordance with HKAS 19, *Employee benefits,* was carried out by an independent actuarial consulting firm, Towers Watson, using the Projected Unit Credit Method. The results of the valuation are shown in note 55.

Actuarial valuation as at 31 December 2011 to determine the cash funding requirements was also carried out by Towers Watson using the Attained Age Method. The principal actuarial assumptions used included a long-term rate of investment return net of salary increases of 1.3% (2010: 2.0%) per annum, together with appropriate allowances for expected rates of mortality, turnover, redundancy and retirement. Towers Watson confirmed that, as at the valuation date:

(a) the MTR Retirement Scheme was solvent, with assets more than adequate to cover the aggregate value of members' vested benefits had all members left the MTR Retirement Scheme; and

(b) on the assumption that the MTR Retirement Scheme continued in force, the value of assets was more than sufficient to cover the aggregate past service liability, with a funding level of 105.5%.

(ii) MTR RBS

The MTR RBS is a defined benefit scheme registered under the ORSO. It is a top-up scheme to supplement the MTR Retirement Scheme for employees classified by the Company as staff working on designated projects and who are not on gratuity terms. The MTR RBS provides benefits only in the event of redundancy for service accrued up to 31 December 2002, offset by any benefits payable from the MTR Retirement Scheme and other applicable schemes. As at 31 December 2011, there were 310 members (2010: 316) under the MTR RBS.

54 Retirement Schemes *(continued)*

A Retirement Schemes Operated by the Company in Hong Kong *(continued)*

The MTR RBS is non-contributory for members. The Company's contributions are determined with reference to an actuarial valuation carried out by an independent actuarial consulting firm. During 2010 and 2011, the Company was not required to make any contribution to the MTR RBS. The net asset value of the MTR RBS as at 31 December 2011 was HK$12 million (2010: HK$12 million).

Actuarial valuation as at 31 December 2010 and 2011 to determine the accounting obligations in accordance with HKAS 19, *Employee benefits,* were carried out by Towers Watson using the Projected Unit Credit Method. The results of the valuations are shown in note 55.

Actuarial valuation as at 31 December 2011 to determine the cash funding requirements was carried out by Towers Watson using the Attained Age Method. The principal actuarial assumptions used included an expected weighted rate of investment return net of salary increases, of approximately -3.5% (2010: -2.5%) per annum, together with appropriate allowance for expected rates of redundancy. Towers Watson confirmed that, as at the valuation date:

(a) due to the nature of the MTR RBS which provides for benefits only on redundancy, there was no aggregate vested liability, and thus the MTR RBS was technically solvent; and

(b) on the assumption that the MTR RBS continued in force, the value of assets was more than sufficient to cover the aggregate past service liability.

(iii) MTR Provident Fund Scheme

The MTR Provident Fund Scheme is a defined contribution scheme registered under the ORSO and granted with MPF Exemption by the MPFA. All benefits payable under the MTR Provident Fund Scheme are calculated with reference to the Company's contributions and members' own contributions, together with investment returns on these contributions. Both the Company's and members' contributions are based on fixed percentages of members' base salary.

As at 31 December 2011, the total number of employees participating in the MTR Provident Fund Scheme was 6,667 (2010: 6,276). In 2011, total members' contributions were HK$58 million (2010: HK$52 million) and total contribution from the Company was HK$171 million (2010: HK$159 million). The net asset value as at 31 December 2011 was HK$3,527 million (2010: HK$3,588 million).

(iv) MTR MPF Scheme

The MTR MPF Scheme is a defined contribution scheme covered under an MPF master trust registered with the MPFA. It covers those employees who did not opt for or who are not eligible to join the MTR Retirement Scheme or the MTR Provident Fund Scheme. Both members and the Company each contribute to the MTR MPF Scheme at the mandatory levels as required by the MPF Ordinance. The Company makes additional contributions above the mandatory level for eligible members who joined the MTR MPF Scheme before 1 April 2008, subject to individual terms of employment.

As at 31 December 2011, the total number of employees of the Company participating in the MTR MPF Scheme was 3,452 (2010: 2,540). In 2011, total members' contributions were HK$19 million (2010: HK$14 million) and total contribution from the Company was HK$21 million (2010: HK$16 million).

(v) KCRC MPF Scheme

The KCRC MPF Scheme is a defined contribution scheme covered under an MPF master trust registered with the MPFA. It covers those former KCRC employees who were previously members of the KCRC MPF Scheme and are eligible to join the MTR Provident Fund Scheme but opt to re-join the KCRC MPF Scheme. Both members and the Company each contribute to the KCRC MPF Scheme at the mandatory levels as required by the MPF Ordinance.

As at 31 December 2011, the total number of employees of the Company participating in the KCRC MPF Scheme was 856 (2010: 903). In 2011, total members' contributions were HK$6 million (2010: HK$6 million) and total contribution from the Company was HK$6 million (2010: HK$7 million).

B Retirement Schemes for Employees of Mainland and Overseas Offices and Subsidiaries

Employees not eligible for joining the retirement schemes operated by the Company in Hong Kong are covered by the retirement schemes established by their respective subsidiary companies or in accordance with respective applicable labour regulations.

(i) Defined Benefit Plan

Certain employees of the Group's Australian subsidiary are entitled to receive retirement benefits from the Emergency Services Superannuation Scheme operated in Australia. The benefit amounts are calculated based on the member's years of service and final average salary. The Group does not recognise any defined benefit liability in respect of this scheme because the Group has no legal or constructive obligation to pay future benefits relating to its employees; its only obligation is to pay contributions as they fall due. As at 31 December 2011, total number of the Group's employees participating in this scheme was 854 (2010: 894). In 2011, total members' contributions were HK$38 million (2010: HK$31 million) and total contribution from the Group was HK$53 million (2010: HK$44 million).

(ii) Defined Contribution Plans

Except for the defined benefit plan stated in note 54B(i), all other retirement schemes to cover employees in overseas offices or in subsidiaries in Hong Kong, Mainland of China or overseas are defined contribution schemes. For Hong Kong employees, these schemes are registered under the MPF Ordinance in Hong Kong. For the Mainland of China or overseas employees, these schemes are operated in accordance with the respective local laws and regulations. As at 31 December 2011, the total number of employees of the Group participating in these schemes was 7,709 (2010: 7,074). In 2011, total members' contributions were HK$104 million (2010: HK$77 million) and total contribution from the Group was HK$211 million (2010: HK$180 million).

55 Defined Benefit Retirement Plan Obligations

The Company makes contributions to and recognises defined benefit liabilities in respect of two defined benefit plans that provide benefits for employees upon retirement or termination of services for other reasons (note 54). The movements in respect of these defined benefit plans during the year are summarised as follows.

A The amounts recognised in the balance sheets are as follows:

The Group and The Company

	2011			2010		
in HK$ million	MTR Retirement Scheme	MTR RBS	Total	MTR Retirement Scheme	MTR RBS	Total
Present value of funded obligations	**(10,669)**	**–**	**(10,669)**	(9,342)	–	(9,342)
Fair value of plan assets	**7,794**	**12**	**7,806**	8,200	12	8,212
Net unrecognised actuarial losses/(gains)	**3,064**	**(3)**	**3,061**	1,302	(3)	1,299
Net asset	**189**	**9**	**198**	160	9	169

A portion of the above asset is expected to be recovered after more than one year. However, it is not practicable to segregate this amount from the amounts to be recovered in the next twelve months, as future contributions will also relate to future services rendered and future changes in actuarial assumptions and market conditions. The Company expects to pay HK$181 million in contribution to the MTR Retirement Scheme in 2012.

B Plan assets consist of the following:

The Group and The Company

	2011			2010		
in HK$ million	MTR Retirement Scheme	MTR RBS	Total	MTR Retirement Scheme	MTR RBS	Total
Equity securities	**3,761**	**–**	**3,761**	4,423	–	4,423
Bonds	**3,963**	**–**	**3,963**	3,602	–	3,602
Cash	**145**	**12**	**157**	250	12	262
	7,869	**12**	**7,881**	8,275	12	8,287
Voluntary units	**(75)**	**–**	**(75)**	(75)	–	(75)
	7,794	**12**	**7,806**	8,200	12	8,212

The plan assets include no investment in the Company's ordinary shares and the Company's debt securities in 2010 and 2011.

C Movements in the Present Value of the Defined Benefit Obligations

The Group and The Company

	2011			2010		
in HK$ million	MTR Retirement Scheme	MTR RBS	Total	MTR Retirement Scheme	MTR RBS	Total
At 1 January	**9,342**	**–**	**9,342**	8,959	–	8,959
Members' contributions paid to the Schemes	**70**	**–**	**70**	70	–	70
Benefits paid by the Schemes	**(336)**	**–**	**(336)**	(311)	–	(311)
Current service cost	**281**	**–**	**281**	293	–	293
Interest cost	**264**	**–**	**264**	227	–	227
Actuarial losses	**1,048**	**–**	**1,048**	104	–	104
At 31 December	**10,669**	**–**	**10,669**	9,342	–	9,342

55 Defined Benefit Retirement Plan Obligations *(continued)*

D Movements in Plan Assets

The Group and The Company

in HK$ million	2011 MTR Retirement Scheme	2011 MTR RBS	2011 Total	2010 MTR Retirement Scheme	2010 MTR RBS	2010 Total
At 1 January	**8,200**	**12**	**8,212**	7,542	12	7,554
Group's contributions paid to the Schemes	**120**	**–**	**120**	120	–	120
Members' contributions paid to the Schemes	**70**	**–**	**70**	70	–	70
Benefits paid by the Schemes	**(336)**	**–**	**(336)**	(311)	–	(311)
Expected return on plan assets	**486**	**–**	**486**	448	–	448
Actuarial (losses)/gains	**(746)**	**–**	**(746)**	331	–	331
At 31 December	**7,794**	**12**	**7,806**	8,200	12	8,212

E Expense recognised in the consolidated profit and loss account is as follows:

in HK$ million	2011 MTR Retirement Scheme	2011 MTR RBS	2011 Total	2010 MTR Retirement Scheme	2010 MTR RBS	2010 Total
Current service cost	**281**	**–**	**281**	293	–	293
Interest cost	**264**	**–**	**264**	227	–	227
Expected return on plan assets	**(486)**	**–**	**(486)**	(448)	–	(448)
Net actuarial losses/(gains) recognised	**32**	**–**	**32**	58	(1)	57
Expense recognised	**91**	**–**	**91**	130	(1)	129
Less: Amount capitalised	**(15)**	**–**	**(15)**	(21)	–	(21)
	76	**–**	**76**	109	(1)	108

The retirement expense is recognised under staff costs and related expenses in the consolidated profit and loss account.

F Actual Return on Plan Assets

in HK$ million	2011	2010
MTR Retirement Scheme	**(260)**	779
MTR RBS	**–**	–

55 Defined Benefit Retirement Plan Obligations *(continued)*

G The principal actuarial assumptions used as at 31 December 2011 (expressed as weighted average) are as follows:

	2011		2010	
	MTR Retirement Scheme	MTR RBS	MTR Retirement Scheme	MTR RBS
Discount rate at 31 December	**1.5%**	**0.9%**	2.9%	1.9%
Expected rate of return on plan assets	**6.0%**	**1.5%**	6.0%	1.5%
Future salary increases	**4.7%**	**5.0%**	4.0%	4.0%

The expected long-term rates of return on plan assets have been determined based on market expectations on returns over the entire life of the related obligations.

H Historical Information

The Group and The Company

	MTR Retirement Scheme				
in HK$ million	2011	2010	2009	2008	2007
Present value of funded obligations	**(10,669)**	(9,342)	(8,959)	(9,064)	(8,577)
Fair value of plan assets	**7,794**	8,200	7,542	6,162	7,929
Deficit in the Scheme	**(2,875)**	(1,142)	(1,417)	(2,902)	(648)
Experience adjustments arising on plan liabilities – gain/(loss)	**334**	(357)	(785)	1,391	(556)
Experience adjustments arising on plan assets – (loss)/gain	**(746)**	331	941	(1,997)	514

	MTR RBS				
in HK$ million	2011	2010	2009	2008	2007
Present value of funded obligations	**–**	–	–	(1)	(1)
Fair value of plan assets	**12**	12	12	12	12
Surplus in the Scheme	**12**	12	12	11	11
Experience adjustments arising on plan liabilities – gain/(loss)	**–**	–	1	–	1
Experience adjustments arising on plan assets – gain/(loss)	**–**	–	–	–	–

56 Interests in Jointly Controlled Operations

The Group has the following jointly controlled operations in respect of its awarded property development projects in Hong Kong as at 31 December 2011:

Location/Development Package	Land Use	Total Gross Floor Area (sq.m.)	Actual or Expected Date of Completion of Construction Works *
Hong Kong Station	Office/Retail/Hotel	415,894	Completed by phases from 1998–2005
Kowloon Station			
Package One	Residential	147,547	Completed in 2000
Package Two	Residential	210,319	Completed by phases from 2002–2003
Package Three	Residential/Cross Border Bus Terminus	105,113	Completed in 2005
Package Four	Residential	128,845	Completed in 2003
Package Five, Six and Seven	Residential/Office/Retail/Hotel/Service Apartment/Kindergarten	504,345	Completed by phases from 2006–2010
Olympic Station			
Package One	Residential/Office/Retail/Indoor Sports Hall	309,069	Completed in 2000
Package Two	Residential/Retail/Market	268,650	Completed in 2001
Package Three	Residential/Kindergarten	104,452	Completed in 2006
Tsing Yi Station	Residential/Retail/Kindergarten	292,795	Completed in 1999
Tung Chung Station			
Package One	Residential/Office/Retail/Hotel/Kindergarten	361,531	Completed by phases from 1999–2005
Package Two	Residential/Retail/Kindergarten	255,949	Completed by phases from 2002–2008
Package Three	Residential/Retail/Wet Market/Kindergarten	413,154	Completed by phases from 2002–2008
Hang Hau Station	Residential/Retail	142,152	Completed in 2004
Tiu Keng Leng Station	Residential/Retail	253,765	Completed by phases from 2006–2007
Tseung Kwan O Station			
Area 55b	Residential/Retail	96,797	Completed in 2006
Area 57a	Residential/Retail	29,642	Completed in 2005
Area 56	Residential/Hotel/Retail/Office	163,130	By phases from 2011–2012
Tseung Kwan O Area 86			
Package One	Residential/Retail/Residential Care Home for the Elderly	139,840	Completed in 2008
Package Two	Residential/Kindergarten	310,496	By phases from 2010–2012
Package Three	Residential/Kindergarten	129,544	2013
Choi Hung Park-and-Ride	Residential/Retail	21,538	Completed in 2005
Che Kung Temple Station	Residential/Retail/Kindergarten	90,655	2012
Austin Station			
Sites C & D	Residential	119,116	2014

* Completion based on issuance of occupation permit

The Group's assets held in relation to these joint venture operations include various site foundation works and related staff and overhead costs, land costs, acquisition cost of development rights and interest expense. These are set off against any payments received from developers in relation to that development package, and the balance is shown on the balance sheet either as property development in progress (note 29) or deferred income (note 48) as the case may be. As at 31 December 2011, total property development in progress in respect of these jointly controlled operations was HK$6,780 million (2010: HK$6,863 million) and total deferred income was HK$68 million (2010: HK$81 million).

During the year ended 31 December 2011, profits of HK$4,934 million (2010: HK$4,034 million) were recognised (note 12).

56 Interests in Jointly Controlled Operations *(continued)*

In connection with the Rail Merger, the Company entered into agreements with KCRC relating to the property development projects on the following three awarded sites:

Location/Development Package	Land Use	Total Gross Floor Area (sq.m.)	Actual or Expected Date of Completion of Construction Works *
Fo Tan Station			
Ho Tung Lau	Residential/Retail	122,900	Completed in 2008
Wu Kai Sha Station	Residential/Retail/Kindergarten	172,650	Completed in 2009
Tai Wai Maintenance Centre	Residential	313,955	Completed by phases from 2010–2011

* Completion based on issuance of occupation permit

Under these agreements, the Company was appointed as KCRC's agent to exercise the rights and to perform the obligations of KCRC as stipulated in the agreements. The Company received a right to share the net surplus from the sale of these property development projects.

57 Material Related Party Transactions

The Financial Secretary Incorporated, which holds approximately 76.7% of the Company's issued share capital on trust for HKSAR Government, is the majority shareholder of the Company. Transactions between the Group and HKSAR Government departments or agencies, or entities controlled by HKSAR Government, other than those transactions such as the payment of fees, taxes, leases and rates, etc. that arise in the normal dealings between HKSAR Government and the Group, are considered to be related party transactions pursuant to HKAS 24 (revised 2009), *Related party disclosures*, and are identified separately in these accounts.

Members of the Board and Members of the Executive Directorate and parties related to them, including their close family members, are also considered to be related parties of the Group. Transactions with these parties, except for those involving a Member of the Board or his related parties where the relevant Member abstains from voting, are separately disclosed in the accounts.

Major related party transactions entered into by the Group which are relevant for the current year include:

A On 30 June 2000, the Company was granted by HKSAR Government a franchise, for an initial period of 50 years, to operate the then existing mass transit railway, and to operate and construct any extension to the railway. On the same day, the Company and HKSAR Government entered into an Operating Agreement ("OA") which laid down the detailed provisions for the design, construction, maintenance and operation of the railway under the franchise. Pursuant to the terms of the OA, the Company's franchise will be extended for further periods of 50 years upon satisfying certain capital expenditure requirements at no payment and without any change in the terms of the franchise. The OA also provides that upon extension of the franchise and subject to HKSAR Government's prevailing land policy on the date on which the franchise is extended, certain consequential amendments will be made to agreements between HKSAR Government and the Company in relation to the mass transit railway, including the renewal of various railway running line leases and land leases at nominal cost. With the Rail Merger, the OA was replaced with effect from 2 December 2007 by a new operating agreement, details of which are set out in note 57C below.

B On 14 July 2000, the Company received a comfort letter from the Government pursuant to which HKSAR Government agreed to extend the period of certain of the Company's land interests so that they are coterminous with the Company's franchise period. To prepare for the Rail Merger, on 3 August 2007, HKSAR Government wrote to KCRC confirming that, subject to all necessary approvals being obtained, the period of certain of KCRC's land interests (which are the subject of the service concession under the Rail Merger) will be extended so that they are coterminous with the concession period of the Rail Merger.

C In connection with the Rail Merger (note 3), on 9 August 2007, the Company and HKSAR Government entered into a new operating agreement ("new OA"), which is based on the then existing OA referred to in note 57A above. On the Appointed Day, the Company's then existing franchise under the Mass Transit Railway Ordinance was expanded to cover railways other than the then existing MTR railway for an initial period of 50 years from the Appointed Day ("expanded franchise"). The new OA detailed the design, construction, maintenance and operation of the railways under the expanded franchise. Pursuant to the terms of the new OA and the MTR Ordinance, the Company's franchise may be extended for further periods of 50 years (from the date of the extension) upon satisfying certain capital expenditure requirements at no payment and without any change in the terms of the franchise. The new OA also sets out a framework for the award of new railway projects in Hong Kong and introduces a fare adjustment mechanism. A detailed description of the new OA is contained in the circular to shareholders in respect of the Extraordinary General Meeting convened to approve the Rail Merger.

D Other than the new OA described in note 57C above, the Company also entered into the following principal agreements with KCRC and HKSAR Government in connection with the Rail Merger:

(i) Merger Framework Agreement, which was entered into on 9 August 2007, contains provisions for the overall structure and certain specific aspects of the Rail Merger;

(ii) Service Concession Agreement, which was entered into on 9 August 2007, contains provisions in relation to the grant and operation of a service concession and licence granted by KCRC to the Company;

57 Material Related Party Transactions *(continued)*

D Other than the new OA described in note 57C above, the Company also entered into the following principal agreements with KCRC and HKSAR Government in connection with the Rail Merger: *(continued)*

(iii) Sale and Purchase Agreement, which was entered into on 9 August 2007, sets out the terms pursuant to which the Company acquired certain assets and contracts from KCRC;

(iv) Kowloon Southern Link ("KSL") Project Management Agreement, which was entered into on 9 August 2007, sets out the terms on which the Company was appointed by KCRC to manage the design and construction of the KSL in return for a management fee and an incentive payment if the construction of the KSL is completed ahead of time and under budget. KSL was completed for service commencement on 16 August 2009 and became part of the service concession. The final incentive payment was received in 2010;

(v) West Rail Agency Agreement, which was entered into on 9 August 2007, sets out the terms on which the Company was appointed to act as KCRC's agent to exercise certain rights and perform certain obligations relating to specified development sites along the West Rail;

(vi) Property Package Agreements, which were entered into on 9 August 2007, set out the arrangements in respect of the acquisition of the property package; and

(vii) US Cross Border Lease ("CBL") Assumption Agreements, which were entered into with KCRC on 30 November 2007, and US CBL Allocation Agreement, which was entered into with KCRC and KCRC's subsidiaries on 2 December 2007, set out the terms on which the Company has undertaken to perform, on a joint and several basis with KCRC, the obligations of KCRC under the respective CBLs, and delineate and allocate the obligations and responsibility for risks relating to the CBLs. Details of the commitment of the Company in connection with these agreements are specified in note 58E.

A detailed description of each of the above agreements is contained under the paragraph "Connected Transactions" of the Report of the Members of the Board.

E The Company entered into project agreements with HKSAR Government for the design, construction, financing and operation of new railway extensions and, where applicable, the granting of land for commercial and residential property developments along these railway extensions. Project agreements on railway extensions that are still under construction or the property developments in respect of which have not been completed in the current year include:

(i) TKE Project Agreement in respect of the Tseung Kwan O Extension, which was signed on 4 November 1998 and includes the granting of property development rights at four sites along the extension;

(ii) Preliminary Project Agreement, which was signed on 6 February 2008, and Project Agreement, which was signed on 13 July 2009 in respect of the West Island Line. Pursuant to the agreements, the Company has received from HKSAR Government a total of HK$12,652 million of government grant as funding support subject to a repayment mechanism (note 27A);

(iii) Project Agreement in respect of the SIL(E), which was signed on 17 May 2011 and includes the granting of property development rights at a site in Wong Chuk Hang (note 27B); and

(iv) Project Agreement in respect of the KTE, which was signed on 17 May 2011 and includes the granting of property development rights at a site in Ho Man Tin (note 27C).

F The Company entered into entrustment agreements with HKSAR Government for the design, site investigation, procurement activities, construction, testing and commissioning of new railway extensions, pursuant to which HKSAR Government funds the total costs of such activities while the Company is paid a fee for its project management service. Entrustment agreements on railway extensions that are still under construction in the current year include:

(i) Preliminary Entrustment Agreement, which was signed on 24 November 2008, and Entrustment Agreement, which was signed on 26 January 2010, in respect of the Guangzhou-Shenzhen-Hong Kong Express Rail Link ("XRL"). The two agreements together entrust the Company with the project management of activities leading to the completion of XRL. Detailed description of the agreements and the amount of project management fees recognised for the year ended 31 December 2011 are provided in note 28B; and

(ii) Preliminary Entrustment Agreement, which was signed on 24 November 2008, and Entrustment Agreement, which was signed on 17 May 2011, in respect of the Shatin to Central Link ("SCL"). The two agreements together entrust the Company with the design, site investigation and procurement activities of SCL as well as construction of certain enabling works at Admiralty and Ho Man Tin Stations and other associated works. Detailed description of the agreements is provided in note 28C.

G On 19 November 2003, the Company entered into a project agreement with HKSAR Government to develop the Tung Chung Cable Car system together with a Theme Village at Ngong Ping on the Lantau Island under a franchise granted by HKSAR Government for a period of 30 years commencing 24 December 2003. The project was completed with operation commencement on 18 September 2006.

57 Material Related Party Transactions *(continued)*

H In connection with the construction of various railway projects, certain essential project works are embedded within the infrastructure works to be undertaken by HKSAR Government or certain of its related parties. These works have been entrusted to HKSAR Government and its related parties and are payable on an actual cost basis according to architectural certifications. HKSAR Government and certain of its related parties, on the other hand, have entered into entrustment agreements with the Company for the construction of various other infrastructure works that are also reimbursable according to actual costs certified. Details of the amounts receivable and the amounts paid and payable as at 31 December 2011 are provided in notes 40 and 45 respectively.

I In connection with certain property developments along the railway extensions, the Company has been granted land lots by and paid land premiums to HKSAR Government in accordance with the terms of the development agreements in respect of the following sites:

Property development site	Land grant acceptance date	Total land premium HK$ million	Land premium settlement date
Site F of Tseung Kwan O Town Lot No. 70, Area 86	24 January 2005	2,319	14 April 2005
Sha Tin Town Lot No. 519	23 April 2008	3,662	14 July 2008
Kowloon Inland Lot No. 11126 and 11129 (Sites C and D, Canton Road, Kowloon)	12 March 2010	11,708	7 June 2010

J On 16 November 2011, the Company and KCRC entered into an Outsourcing Agreement pursuant to which the Company will provide certain administrative and financial activities to KCRC. The Agreement has no specific term but can be terminated by either party giving notice period specified in the Agreement. The fee payable pursuant to the Agreement and the scope of services are to be reviewed on an annual basis and amended upon the mutual agreement of the parties.

K On 21 August 2008, the Company renewed the maintenance agreement with the Hong Kong Airport Authority in respect of the automatic people mover system serving the Hong Kong International Airport including the Sky Plaza and Sky Pier terminal buildings. The agreement covers a period of five years effective from 6 July 2008. In respect of the agreement, HK$46 million was recognised as consultancy income during the year ended 31 December 2011 (2010: HK$40 million).

L Other than those stated in notes 57A to 57J, the Company has business transactions with HKSAR Government, entities related to HKSAR Government and the Company's non-controlled subsidiaries and associates in the normal course of business operations. Details of the transactions and the amounts involved for the reporting period are disclosed in notes 31, 33, 40 and 45.

M The Group has paid remuneration to Members of the Board and the Executive Directorate. Details of these transactions are described in note 11A. In addition, Members of the Executive Directorate were granted share options under the Company's New Joiners Share Option Scheme and 2007 Share Option Scheme. Details of the terms of these options are disclosed in note 11B and the Report of the Members of the Board. Their gross remuneration charged to the profit and loss account is summarised as follows:

in HK$ million	**2011**	2010
Short-term employee benefits	**59.5**	57.1
Post-employment benefits	**2.5**	1.6
Equity compensation benefits	**14.2**	10.9
	76.2	69.6

The above remuneration is included in staff costs and related expenses disclosed in note 10A.

N During the year, the following dividends were paid to HKSAR Government:

in HK$ million	**2011**	2010
Cash dividends paid	**3,104**	1,302
Shares allotted in respect of scrip dividends	**–**	991
	3,104	2,293

58 Commitments

A Capital Commitments

(i) Outstanding capital commitments as at 31 December 2011 not provided for in the accounts were as follows:

The Group

in HK$ million	Hong Kong transport, station commercial and other businesses	Hong Kong railway extension projects	Hong Kong property rental and development	Mainland of China and overseas operations	Total
2011					
Authorised but not yet contracted for	**2,079**	**–**	**824**	**9**	**2,912**
Authorised and contracted for	**1,447**	**13,099**	**624**	**216**	**15,386**
	3,526	**13,099**	**1,448**	**225**	**18,298**
2010					
Authorised but not yet contracted for	1,575	–	142	–	1,717
Authorised and contracted for	986	7,100	326	1,340	9,752
	2,561	7,100	468	1,340	11,469

The Company

in HK$ million	Hong Kong transport, station commercial and other businesses	Hong Kong railway extension projects	Hong Kong property rental and development	Total
2011				
Authorised but not yet contracted for	**2,074**	**–**	**824**	**2,898**
Authorised and contracted for	**1,447**	**13,099**	**624**	**15,170**
	3,521	**13,099**	**1,448**	**18,068**
2010				
Authorised but not yet contracted for	1,561	–	140	1,701
Authorised and contracted for	986	7,100	315	8,401
	2,547	7,100	455	10,102

Excluded from the above tables are estimated future project costs relating to the West Island Line, South Island Line (East) and Kwun Tong Line Extension of HK$3,754 million, HK$7,335 million and HK$3,108 million respectively as at 31 December 2011.

(ii) The commitments under Hong Kong transport, station commercial and other businesses comprise the following:

The Group and The Company

in HK$ million	Improvement and enhancement works	Acquisition of property, plant and equipment	Additional concession property	Total
2011				
Authorised but not yet contracted for	**897**	**279**	**903**	**2,079**
Authorised and contracted for	**468**	**602**	**377**	**1,447**
	1,365	**881**	**1,280**	**3,526**
2010				
Authorised but not yet contracted for	795	285	495	1,575
Authorised and contracted for	344	375	267	986
	1,139	660	762	2,561

58 Commitments *(continued)*

B Operating Lease Commitments

The Group had operating leases on office buildings, staff quarters, bus depot and a shopping centre in Beijing as at 31 December 2011. The total future minimum lease payments under non-cancellable operating leases are payable as follows:

	The Group		The Company	
in HK$ million	**2011**	2010	**2011**	2010
Payable within one year	**132**	141	**6**	7
Payable after one but within five years	**3**	3	**3**	2
	135	144	**9**	9

The above includes HK$6 million (2010: HK$4 million) in respect of the office accommodation and quarters for construction project staff, majority of which are subject to rent reviews.

In addition to the above, the Group has future operating lease commitments of HK$6,061 million (2010: HK$6,747 million) in respect of railway subsidiaries outside of Hong Kong over the respective franchise periods, of which HK$1,065 million (2010: HK$1,024 million) is payable within one year, HK$4,140 million (2010: HK$3,944 million) is payable after one but within five years and HK$856 million (2010: HK$1,779 million) is payable over five years. These railway subsidiaries will generate franchise revenue receivables to the Group.

C Liabilities and Commitments in respect of Property Management Contracts

The Group has, over the years, jointly developed with outside property developers certain properties above or adjacent to railway depots and stations. Under most of the development agreements, the Group retained the right to manage these properties after their completion. The Group, as manager of these properties, enters into service contracts with outside contractors for the provision of security, cleaning, maintenance and other services on behalf of the managed properties. The Group is primarily responsible for these contracts, but any contract costs incurred will be reimbursed by the owners and tenants of the managed properties from the management funds as soon as they are paid.

As at 31 December 2011, the Group had total outstanding liabilities and contractual commitments of HK$1,599 million (2010: HK$1,314 million) in respect of these works and services. Cash funds totalling HK$1,655 million (2010: HK$1,371 million) obtained through monthly payments of management service charges from the managed properties are held by the Group on behalf of those properties for settlement of works and services provided.

D Material Financial and Performance Guarantees

In respect of the debt securities issued by MTR Corporation (C.I.) Limited (note 42C), the Company has provided guarantees to the investors of approximately HK$12,379 million (in notional amount) as at 31 December 2011. The proceeds from the debts issued are on lent to the Company and MTR Corporation (Shenzhen) Limited. As such, the primary liabilities have been recorded in the Company's balance sheet .

In respect of the lease out/lease back transaction ("Lease Transaction") (note 24E), the Group has provided standby letters of credit ("standby LC's") to the Investors to cover additional amounts payable by the Group in the event the transactions are terminated prior to the expiry of the lease terms, and such standby LC's amounted to US$110 million (HK$855 million) as at 31 December 2011. The Group has also provided standby LC's to certain of the Investors under the Lease Transaction to replace some of the Defeasance Securities previously used to support the corresponding long-term lease payments as a result of credit rating downgrades of these securities, and such standby LC's amounted to US$38 million (HK$299 million) as at 31 December 2011.

In respect of the operating lease on the shopping centre in Beijing, the Group provided a bank guarantee of RMB12.5 million and a parent company guarantee of RMB52.5 million in respect of the quarterly rental payments to the landlord.

In respect of the Melbourne Metropolitan Train Franchise, the Group and the other shareholders of the Group's 60% owned subsidiary, Metro Trains Melbourne Pty. Ltd. ("MTM"), have provided to the State of Victoria Government a joint and several parent company guarantee of AUD125 million (HK$986 million) and a performance bond of AUD75 million (HK$592 million) for MTM's performance and other obligations under the franchise agreement, with each shareholder bearing its share of liability based on its shareholdings in MTM.

In respect of the Stockholm Metro Franchise, the Group has provided to the Stockholm transport authority a guarantee of SEK1,000 million (HK$1,123 million), which can be called if the franchise is terminated early as a result of default by MTR Stockholm AB, the wholly owned subsidiary of the Group to undertake the franchise.

In respect of the London Overground Franchise, London Overground Rail Operations Ltd ("LOROL"), the Group's 50% owned associate company to undertake the franchise, has provided to Transport for London (TfL) a performance bond of GBP12.0 million (HK$144 million), which may be called by TfL if the franchise is terminated early as a result of default. The performance bond is guaranteed by Deutsche Bahn, the ultimate parent company of the other shareholder of LOROL, with the Group providing to Deutsche Bahn a counter indemnity that is further backed by a performance bond of GBP6.0 million (HK$72 million) for the Group's share of the Guarantee.

In respect of the construction of Shenzhen Longhua Line Phase 2, the Group has provided payment guarantees of RMB168 million (HK$207 million) and performance guarantees of RMB48 million (HK$59 million) to the counterparties of the construction contracts.

58 Commitments *(continued)*

E US Cross Border Lease ("CBL") Agreements

In connection with the Rail Merger, the Company entered into a number of agreements ("US CBL Assumption Agreements") with respect to the CBLs that KCRC had entered into with its CBL counterparties in relation to certain of its property and equipment ("CBL Property") between 1998 and 2003. Pursuant to the US CBL Assumption Agreements, the Company has undertaken to perform, on a joint and several basis with KCRC, the obligations of KCRC under the respective CBLs.

In addition, the Company has entered into a US CBL Allocation Agreement with KCRC, whereby the rights, obligations and responsibility for risks relating to the CBLs are delineated and allocated between the Company and KCRC. Generally, the Company is responsible for operational matters, such as repair, maintenance and insurance of the CBL Property, and KCRC is responsible for all other obligations, including payment of periodic rents and collateral related obligations. Despite this allocation of obligations, the Company is prima facie jointly and severally liable to the CBL counterparties for any failure of KCRC to perform its obligations under the CBLs.

KCRC and HKSAR Government have agreed to indemnify the Company for its reasonable costs incurred as a result of the due and proper performance by the Company of its obligations under the CBLs (unless such costs would have been incurred in any event). In addition, KCRC has agreed to indemnify the Company for losses and reasonable costs incurred arising from KCRC not complying with its obligations under the CBLs or from any breach of KCRC's representations, covenants and agreements provided for in relation to the CBLs.

The Company has agreed to indemnify each of HKSAR Government and KCRC for losses and reasonable costs incurred arising from any breach of the Company's representations, covenants and agreements provided for in relation to the CBLs.

F Service Concession in respect of the Rail Merger

Pursuant to the Rail Merger, the Company is obliged under the Service Concession Agreement ("SCA") to pay an annual fixed payment of HK$750 million to KCRC over the period of the service concession. Additionally, commencing after three years from the Appointed Day, the Company is obliged to pay a variable annual payment to KCRC based on the revenue generated from the KCRC system above certain thresholds. Furthermore, under the SCA, the Company is obliged to maintain, repair, replace and/or upgrade the KCRC system over the period of the service concession which is to be returned at the expiry of the service concession.

59 Accounting Estimates and Judgements

A Key sources of accounting estimates and estimation uncertainty include the following:

(i) Estimated Useful Life and Depreciation and Amortisation of Property, Plant and Equipment and Service Concession Assets

The Group estimates the useful lives of the various categories of property, plant and equipment and service concession assets on the basis of their design lives, planned asset maintenance programme and actual usage experience. Depreciation is calculated using the straight-line method at rates sufficient to write off their cost or valuation over their estimated useful lives (note 2I).

(ii) Impairment of Long-lived Assets

The Group reviews its long-lived assets for indications of impairment at each balance sheet date according to accounting policies set out in note 2H(ii). In analysing potential impairments identified, the Group uses projections of future cash flows from the assets based on management's assignment of a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

(iii) Pension Costs

The Group employs independent valuation professionals to conduct annual assessment of the actuarial position of the Group's retirement plans. The determination of the Group's obligation and expense for the defined benefit element of these plans is dependent on certain assumptions and factors provided by the Company, which are disclosed in notes 54A(i) and 54A(ii).

(iv) Revenue Recognition on Property Development

Recognition of property development profits requires management's estimation of the final project costs upon completion, assessment of outstanding transactions and market values of unsold units and, in the case of sharing-in-kind properties, the properties' fair value upon recognition. The Group takes into account independent qualified surveyors' reports, past experience on sales and marketing costs when estimating final project costs on completion and makes reference to professionally qualified valuers' reports in determining the estimated fair value of sharing-in-kind properties.

(v) Properties Held for Sale

The Group values unsold properties at the lower of their costs and net realisable values (note 35) at the balance sheet date. In ascertaining the properties' net realisable values, which are represented by the estimated selling prices less costs to be incurred in relation to the sales, the Group employs independent valuation professionals to assess the properties' estimated selling prices and makes estimations on further selling and property holding costs to be incurred based on past experience and with reference to general market practice.

(vi) Valuation of Investment Properties

The valuation of investment properties requires management's input of various assumptions and factors relevant to the valuation. The Group conducts semi-annual revaluation of its investment properties by independent professionally qualified valuers based on these assumptions agreed with the valuers prior to adoption.

59 Accounting Estimates and Judgements *(continued)*

A Key sources of accounting estimates and estimation uncertainty include the following: *(continued)*

(vii) Franchise in Hong Kong

The current franchise under which the Group is operating in Hong Kong allows the Group to run the mass transit railway system in Hong Kong until 1 December 2057. Pursuant to the terms stipulated in the new Operating Agreement with HKSAR Government, the Company considers that it has the legal right to extend the franchise for further periods of 50 years upon expiry of each franchise term (note 57C). The Group's depreciation policies (note 2I) in respect of certain assets' lives which extend beyond 2057 are set on this basis.

(viii) Income Tax

Certain treatments adopted by the Group in its Hong Kong Profits Tax returns in the past years are yet to be finalised with the Hong Kong Inland Revenue Department. In assessing the Group's income tax and deferred taxation in the 2011 accounts, the Company has predominantly followed the tax treatments it has adopted in these tax returns, which may be different from the final outcome in due course.

(ix) Project Provisions

The Group establishes project provisions for the settlement of estimated claims that may arise due to time delays, additional costs or other unforeseen circumstances common to major construction contracts. The claims provisions are estimated based on an assessment of the Group's liabilities under each contract by professionally qualified personnel, which may differ from the actual claims settlement.

(x) Deferred Expenditure

As disclosed in note 2J(i), the Group capitalises proposed railway and property development project costs in deferred expenditure when the projects are at a detailed study stage and having been approved in principle by the Members of the Board. Such decision involves the Board's judgement on the outcome of the proposed project.

(xi) Fair Value of Derivatives and Other Financial Instruments

In determining the fair value of financial instruments, the Group uses its judgement to select a variety of methods and make assumptions that are mainly based on market conditions existing at each balance sheet date. For financial instruments that are not traded in active markets, the fair values were derived using the discounted cash flows method which discounts the future contractual cash flows at the current market interest or foreign exchange rates, as applicable, for similar financial instruments that were available to the Group at the time.

(xii) Obligations under Service Concession

In determining the present value of the obligations under service concession, the discount rate adopted was the relevant Group company's estimated long-term incremental cost of borrowing at inception after due consideration of the relevant Group company's existing fixed rate borrowing cost, future interest rate and inflation trends.

B Critical accounting judgements in applying the group's accounting policies include the following:

(i) Provisions and Contingent Liabilities

The Group recognises provisions for liabilities of uncertain timing or amount when the Group has a legal or constructive obligation arising as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made. Where it is not probable that an outflow of economic benefits will be required, or the amount cannot be estimated reliably, the obligation is disclosed as contingent liability. As at 31 December 2011, the Group considered that it had no disclosable contingent liabilities as there were neither pending litigations nor events with potential obligation which were probable to result in material outflow of economic benefits from the Group.

(ii) Non-controlled Subsidiaries

The Group regards Octopus Holdings Limited and its subsidiaries (the "OHL Group") as non-controlled subsidiaries. In determining whether the Group has control over these subsidiaries, the Group has taken into account its voting right conferred to it under the Shareholder's Agreement of OHL and the effective influence it may exercise over the decision of OHL's Board. Throughout the year ended 31 December 2011, the Group considered that its voting right in the OHL Group has been maintained at 49% despite an equity interest of 57.4%. As such, the OHL Group was accounted for as non-controlled subsidiaries in the Group's accounts.

60 Possible Impact of Amendments, New Standards and Interpretations Issued but Not Yet Effective for the Annual Accounting Period Ended 31 December 2011

Up to the date of issue of these accounts, the HKICPA has issued the following amendments, new standards and interpretations which are not yet effective for the year ended 31 December 2011 and have not been adopted in these accounts.

	Effective for accounting periods beginning on or after
Amendments to HKFRS 1, *First-time adoption of Hong Kong Financial Reporting Standards – Severe hyperinflation and removal of fixed dates for first-time adopters*	1 July 2011
Amendments to HKFRS 7, *Financial instruments: Disclosures – Transfers of financial assets*	1 July 2011
Amendments to HKAS 12, *Income taxes – Deferred tax: Recovery of underlying assets*	1 January 2012
Amendments to HKAS 1, *Presentation of financial statements – Presentation of items of other comprehensive income*	1 July 2012
Amendments to HKFRS 7, *Financial instruments: Disclosures – Offsetting financial assets and financial liabilities*	1 January 2013
HKFRS 10, *Consolidated financial statements*	1 January 2013
HKFRS 11, *Joint arrangements*	1 January 2013
HKFRS 12, *Disclosure of interests in other entities*	1 January 2013
HKFRS 13, *Fair value measurement*	1 January 2013
HKAS 27, *Separate financial statements (2011)*	1 January 2013
HKAS 28, *Investments in associates and joint ventures*	1 January 2013
Revised HKAS 19, *Employee benefits*	1 January 2013
HK(IFRIC) 20, *Stripping costs in the production phase of a surface mine*	1 January 2013
Amendments to HKAS 32, *Financial instruments: Presentation – Offsetting financial assets and financial liabilities*	1 January 2014
HKFRS 9, *Financial instruments*	1 January 2015

The Group is in the process of making an assessment of what the impact of these amendments is expected to be in the period of initial application. At this moment, the Group considers that the adoption of Amendments to HKAS 12, Revised HKAS 19, Amendments to HKAS 1, HKFRS 12, and HKFRS 13 will have impact on the Group's accounts.

Amendments to HKAS 12 introduce a rebuttable presumption on the measurement of deferred tax on investment properties carried at fair value and the adoption of it is expected to result in the retrospective derecognition of deferred tax liabilities in relation to the change in value of investment properties upon first adoption. Such derecognition, if measured at 31 December 2011, would amount to HK$5,604 million. Revised HKAS 19 changes the accounting and disclosure requirements on defined benefit plans and therefore will affect the amounts recognised in the Group's financial statements and disclosure notes in respect of the MTRCL Retirement Scheme. Amendments to HKAS 1 will affect the presentation of items of other comprehensive income in the Statement of Comprehensive income while new HKFRS 12 and HKFRS 13 will affect the disclosures on information on non-controlling interests of subsidiaries and valuation on investment properties.

Other than the above, it has concluded so far that the adoption of other new issues or amendments is unlikely to have a material impact on the Group's results of operations and financial position.

61 Approval of Accounts

The accounts were approved by the Board on 8 March 2012.