NOTES TO THE UNAUDITED INTERIM FINANCIAL REPORT

1 Basis of Preparation

This interim financial report is unaudited, but has been reviewed by KPMG in accordance with Hong Kong Standard on Review Engagements 2410, *Review of Interim Financial Information Performed by the Independent Auditor of the Entity*, issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA"). KPMG's independent review report to the Board of Directors is set out on page 56. In addition, this interim financial report has been reviewed by the Company's Audit Committee.

This interim financial report has been prepared in accordance with the applicable disclosure provisions of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited, including compliance with Hong Kong Accounting Standard ("HKAS") 34, *Interim financial reporting*, issued by the HKICPA.

The preparation of an interim financial report in conformity with HKAS 34 requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets, liabilities, income and expenses on a year-to-date basis. Actual results may differ from these estimates.

This interim financial report contains the condensed consolidated accounts and selected explanatory notes, which include an explanation of events and transactions that are significant to an understanding of the changes in financial position and performance of the Company and its subsidiaries (collectively referred to as the "Group") and the Group's interest in non-controlled subsidiaries and associates since the issuance of the 2011 annual accounts. The condensed consolidated interim accounts and notes thereon do not include all of the information required for a complete set of accounts prepared in accordance with Hong Kong Financial Reporting Standards ("HKFRSs").

The financial information relating to the financial year ended 31 December 2011 included in this interim financial report does not constitute the Company's statutory accounts for that financial year but is derived from those accounts. Statutory accounts for the year ended 31 December 2011, on which the auditors have expressed an unqualified opinion on those accounts in their report dated 8 March 2012, are available from the Company's registered office.

The accounting policies adopted for the preparation of this interim financial report are the same as those adopted in the preparation of the 2011 annual accounts except for the changes required for the first time adoption of new or revised HKFRSs as set out in the subsequent paragraphs.

The HKICPA has issued a number of amendments to HKFRSs that are first effective for the current accounting period of the Group. Of these, only Amendments to HKAS 12, *Income taxes – Deferred tax: Recovery of underlying assets*, has impact on the Group's financial statements. On adoption of the Amendments, the Group has changed its accounting policy on measuring deferred tax arising from investment property that is measured using the fair value model in HKAS 40, *Investment Property*.

As a result of the change, the Group now measures any deferred tax liability arising from investment properties in Hong Kong with reference to the tax liability that would arise if the properties are disposed of at their carrying amounts at the balance sheet date. Previously, where these properties were held under leasehold interests, deferred tax was generally measured using the tax rate that would apply as a result of recovery of the asset's value through use.

This change in policy has been adopted retrospectively by restating the opening balances at 1 January 2011 and 1 July 2011 with consequential adjustments to comparatives for the period ended 30 June 2011. This has resulted in a reduction in the amount of deferred tax provided on valuation gain as follows:

in HK$ million	As previously reported	Effect of adoption of Amendments to HKAS 12	As restated
Consolidated profit and loss account for the half year ended 30 June 2011			
Income tax	**(1,502)**	**727**	**(775)**
Profit for the period	**8,136**	**727**	**8,863**
Profit for the period attributable to equity shareholders of the Company:			
– Arising from investment property revaluation	**3,681**	**727**	**4,408**
– Total	**8,050**	**727**	**8,777**
Basic and diluted earnings per share	**HK$1.39**	**HK$0.13**	**HK$1.52**
Consolidated balance sheet as at 31 December 2011			
Deferred tax assets	**27**	**(3)**	**24**
Deferred tax liabilities	**15,105**	**(5,607)**	**9,498**
Other reserves - Retained profits	**82,458**	**5,604**	**88,062**
Consolidated balance sheet as at 1 January 2011			
Deferred tax assets	**9**	**(5)**	**4**
Deferred tax liabilities	**13,854**	**(4,769)**	**9,085**
Other reserves - Retained profits	**71,781**	**4,764**	**76,545**

2 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, Government of the Hong Kong Special Administrative Region ("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;

- 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.

3 Revenue and Expenses from Railway Subsidiaries outside of Hong Kong

Revenue and expenses relating to railway subsidiaries outside of Hong Kong comprise:

in HK$ million	Stockholm Metro	Melbourne Train	Shenzhen Metro Longhua Line	Total
Half year ended 30 June 2012				
Revenue				
– Railway operations related	**1,562**	**3,361**	**188**	**5,111**
– Project related	**–**	**1,221**	**3**	**1,224**
	1,562	**4,582**	**191**	**6,335**
Expenses				
– Railway operations related	**1,517**	**3,166**	**171**	**4,854**
– Project related	**–**	**1,146**	**2**	**1,148**
	1,517	**4,312**	**173**	**6,002**
Half year ended 30 June 2011				
Revenue				
– Railway operations related	1,614	3,124	28	4,766
– Project related	–	1,405	–	1,405
	1,614	4,529	28	6,171
Expenses				
– Railway operations related	1,585	2,968	74	4,627
– Project related	–	1,298	–	1,298
	1,585	4,266	74	5,925

Phase 2 of Shenzhen Metro Longhua Line commenced revenue operation on 16 June 2011.

4 Profit on Property Developments

Profit on property developments comprises:

in HK$ million	**Half year ended 30 June 2012**	Half year ended 30 June 2011
Transfer from deferred income on payments received from developers	**–**	468
Share of surplus from development	**627**	402
Income recognised from sharing in kind	**–**	572
Miscellaneous income net of other overhead costs	**–**	3
	627	1,445

Within the profit attributable to equity shareholders of the Company, the amount attributable to property developments had taken into account the effect of related income tax expense of HK$103 million (2011: HK$145 million of income tax and HK$11 million of net interest income).

5 Share of Profits of Non-controlled Subsidiaries and Associates

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

in HK$ million	**Half year ended 30 June 2012**	Half year ended 30 June 2011
Share of profit before taxation of non-controlled subsidiaries	**108**	93
Share of profit before taxation of associates	**173**	78
	281	171
Share of income tax of non-controlled subsidiaries	**(13)**	(12)
Share of income tax of associates	**31**	(4)
	299	155

6 Income Tax

Income tax in the consolidated profit and loss account represents:

in HK$ million	**Half year ended 30 June 2012**	Half year ended 30 June 2011 (Restated)
Current tax		
– Provision for Hong Kong Profits Tax at 16.5% (2011: 16.5%) for the period	**666**	654
– Mainland of China and overseas tax for the period	**87**	16
	753	670
Deferred tax		
– Origination and reversal of temporary differences on:		
– tax losses	**–**	4
– depreciation allowances in excess of related depreciation	**5**	80
– provision and others	**38**	21
	43	105
	796	775

Current tax provision for Hong Kong Profits Tax for the half year ended 30 June 2012 is calculated at 16.5% (2011: 16.5%) on the estimated assessable profits for the period after deducting accumulated tax losses brought forward, if any. Current taxes for the Mainland of China and overseas subsidiaries are 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% (2011: 16.5%) while those arising in the Mainland of China and overseas are calculated at the appropriate current rates of taxation ruling in the relevant countries.

7 Dividends

Dividends paid and proposed to equity shareholders of the Company comprise:

in HK$ million	**Half year ended 30 June 2012**	Half year ended 30 June 2011
Dividends payable attributable to the period		
– Interim dividend declared after the balance sheet date of 25 cents (2011: 25 cents) per share	**1,447**	1,446
Dividends paid attributable to the previous year		
– Final dividend of 51 cents (2010: 45 cents) per share approved and paid during the period	**2,951**	2,598

8 Earnings Per Share

A Basic Earnings Per Share

The calculation of basic earnings per share is based on the profit for the half year ended 30 June 2012 attributable to equity shareholders of HK$5,861 million (2011: HK$8,777 million as restated) and the weighted average number of ordinary shares of 5,785,696,289 in issue during the period (2011: 5,775,572,284), calculated as follows:

	Half year ended 30 June 2012	Half year ended 30 June 2011
Issued ordinary shares at 1 January	**5,784,871,250**	5,772,563,031
Effect of scrip dividends issued	**–**	2,514,447
Effect of share options exercised	**825,039**	494,806
Weighted average number of ordinary shares at 30 June	**5,785,696,289**	5,775,572,284

B Diluted Earnings Per Share

The calculation of diluted earnings per share is based on the profit for the half year ended 30 June 2012 attributable to equity shareholders of HK$5,861 million (2011: HK$8,777 million as restated) and the weighted average number of ordinary shares of 5,788,779,216 in issue during the period (2011: 5,780,254,276) after adjusting for the number of dilutive potential ordinary shares under the employee share option schemes, calculated as follows:

	Half year ended 30 June 2012	Half year ended 30 June 2011
Weighted average number of ordinary shares at 30 June	**5,785,696,289**	5,775,572,284
Effect of dilutive potential shares under the Company's share option schemes	**3,082,927**	4,681,992
Weighted average number of ordinary shares (diluted) at 30 June	**5,788,779,216**	5,780,254,276

C Both basic and diluted earnings per share would have been HK$0.71 (2011: HK$0.76) if the calculation is based on profit attributable to equity shareholders of the Company arising from underlying businesses of HK$4,121 million (2011: HK$4,369 million).

9 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 the 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.

9 Segmental Information *(continued)*

(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 at locations near 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". For the half year ended 30 June 2011, HK$440 million of revenue and HK$395 million of expenses were re-categorised under "Other Businesses". Accordingly, the comparatives of the consolidated profit and loss account and segmental information are reclassified.

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 management businesses	Railway subsidiaries outside of Hong Kong	Other businesses	Property developments	Total
Half year ended 30 June 2012							
Revenue	**6,914**	**1,699**	**1,730**	**6,335**	**476**	**–**	**17,154**
Operating expenses before depreciation, amortisation and variable annual payment	**(3,534)**	**(188)**	**(335)**	**(6,002)**	**(476)**	**–**	**(10,535)**
	3,380	**1,511**	**1,395**	**333**	**–**	**–**	**6,619**
Profit on property developments	**–**	**–**	**–**	**–**	**–**	**627**	**627**
Operating profit before depreciation, amortisation and variable annual payment	**3,380**	**1,511**	**1,395**	**333**	**–**	**627**	**7,246**
Depreciation and amortisation	**(1,470)**	**(70)**	**(7)**	**(36)**	**(30)**	**–**	**(1,613)**
Variable annual payment	**(321)**	**(81)**	**–**	**–**	**–**	**–**	**(402)**
	1,589	**1,360**	**1,388**	**297**	**(30)**	**627**	**5,231**
Project study and business development expenses							**(100)**
Operating profit before interest and finance charges							**5,131**
Interest and finance charges							**(432)**
Investment property revaluation			**1,740**				**1,740**
Share of profits of non-controlled subsidiaries and associates				**204**	**95**		**299**
Income tax							**(796)**
Profit for the half year ended 30 June 2012							**5,942**
Half year ended 30 June 2011 (Restated)							
Revenue	6,471	1,527	1,560	6,171	440	–	16,169
Operating expenses before depreciation, amortisation and variable annual payment	(3,302)	(159)	(336)	(5,925)	(395)	–	(10,117)
	3,169	1,368	1,224	246	45	–	6,052
Profit on property developments	–	–	–	–	–	1,445	1,445
Operating profit before depreciation, amortisation and variable annual payment	3,169	1,368	1,224	246	45	1,445	7,497
Depreciation and amortisation	(1,461)	(70)	(6)	(43)	(31)	–	(1,611)
Variable annual payment	(241)	(60)	–	–	–	–	(301)
	1,467	1,238	1,218	203	14	1,445	5,585
Project study and business development expenses							(51)
Operating profit before interest and finance charges							5,534
Interest and finance charges							(459)
Investment property revaluation			4,408				4,408
Share of profits of non-controlled subsidiaries and associates				74	81		155
Income tax							(775)
Profit for the half year ended 30 June 2011							8,863

9 Segmental Information *(continued)*

The following table sets out information about the geographical location of the Group's revenue from external customers. The geographical location of customers is based on the location at which the services were provided or goods were delivered.

in HK$ million	**Half year ended 30 June 2012**	Half year ended 30 June 2011
Hong Kong (place of domicile)	**10,732**	9,902
Australia	**4,582**	4,530
Mainland of China	**260**	97
Sweden	**1,562**	1,614
Other countries	**18**	26
	6,422	6,267
	17,154	16,169

10 Other Comprehensive Income

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

in HK$ million	**Half year ended 30 June 2012**	Half year ended 30 June 2011
Exchange reserve		
Exchange differences on translation of financial statements of overseas subsidiaries and non-controlled subsidiaries	**(49)**	94
Hedging reserve		
Effective portion of changes in fair value of hedging instruments recognised during the period	**(32)**	(19)
Amounts transferred to initial carrying amount of hedged items	**(2)**	(5)
Transferred to profit or loss	**33**	27
Net deferred tax credited/(debited) to other comprehensive income resulting from:		
– Changes in fair value of hedging instruments recognised during the period	**5**	4
– Amounts transferred to initial carrying amount of hedged items	**–**	1
– Transferred to profit or loss	**(5)**	(4)
Net movement during the period recognised in other comprehensive income	**(1)**	4
Fixed assets revaluation reserve		
Changes in fair value recognised during the period	**142**	492
Net deferred tax debited to other comprehensive income resulting from changes in fair value recognised during the period	**(23)**	(81)
Net movement during the period recognised in other comprehensive income	**119**	411

11 Investment Properties

All investment properties of the Group were revalued at open market value at 30 June 2011 and 2012 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 sale and yields. The net increase in fair value of HK$1,740 million (2011: HK$4,408 million) arising from the revaluation has been credited to the consolidated profit and loss account.

12 Other Property, Plant and Equipment

A Acquisitions and Disposals

During the half year ended 30 June 2012, the Group acquired or commissioned assets at a total cost of HK$723 million (2011: HK$688 million). Items of civil works and plant and equipment with a net book value of HK$21 million (2011: HK$14 million) were disposed of during the same period, resulting in a net loss on disposal of HK$10 million (2011: HK$11 million).

B Valuation

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 an open market value on an existing use basis at 30 June 2011 and 2012 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$142 million (2011: HK$492 million), which, net of deferred tax provision of HK$23 million (2011: HK$81 million), has been recognised in other comprehensive income and accumulated in the fixed assets revaluation reserve account (note 10).

13 Service Concession Assets

Service concession assets include the right to access, use and operate the KCRC system ("Initial Concession Property"), the expenditures incurred in relation to the replacement and upgrade of the KCRC system ("Additional Concession Property"), the value of construction services provided in respect of the construction of Shenzhen Metro Longhua Line Phase 2, the capitalised present value of the total annual lease payments for the operation of Shenzhen Metro Longhua Line Phase 1, as well as the costs incurred to prepare for the operation and maintenance of the Stockholm Metro in Sweden.

During the half year ended 30 June 2012, the Group had net additions of Additional Concession Property of HK$278 million (2011: HK$224 million) and additions of service concession assets in respect of Shenzhen Metro Longhua Line of HK$242 million (2011: HK$2,717 million). Amortisation charges during the same period amounted to HK$230 million (2011: HK$211 million) for Initial Concession Property and Additional Concession Property, HK$150 million (2011: HK$16 million) for Shenzhen Metro Longhua Line and HK$6 million (2011: HK$6 million) for Stockholm Metro.

14 Railway Construction in Progress

A Railway Projects Owned by the Group

Movements of railway construction in progress for projects owned by the Group are as follows:

in HK$ million	Balance at 1 January	Transfer from deferred expenditure	Expenditure	Utilisation of government grant	Balance at 30 June/ 31 December
At 30 June 2012 (Unaudited)					
West Island Line Project	**–**	**–**	**1,410**	**(1,410)**	**–**
South Island Line (East) Project	**2,612**	**–**	**1,242**	**–**	**3,854**
Kwun Tong Line Extension Project	**954**	**–**	**565**	**–**	**1,519**
	3,566	**–**	**3,217**	**(1,410)**	**5,373**
At 31 December 2011 (Audited)					
West Island Line Project	–	–	2,962	(2,962)	–
South Island Line (East) Project	–	735	1,877	–	2,612
Kwun Tong Line Extension Project	–	286	668	–	954
	–	1,021	5,507	(2,962)	3,566

B Railway Construction Activities Managed by the Group

On 29 May 2012, the Company and HKSAR Government entered into the third entrustment agreement in respect of the Shatin to Central Link ("SCL"). Pursuant to the third entrustment agreement for the construction and commissioning of the SCL, the Company shall carry out or procure to the carrying out of the works specified in the agreement (and the first and second entrustment agreements) for a project management fee of HK$7,893 million. The Government shall bear all the work costs specified in the third entrustment agreement except for approximately HK$7 billion (in 2011 prices), which will be contributed by the Company for the works involving the modification, upgrade or expansions of certain assets for which the Company is responsible under the existing service concession agreement with KCRC.

15 Property Development in Progress

Property development in progress comprises foundation, site enabling works and land costs incurred by the Group for property development projects as well as considerations paid and mandatory payments payable to KCRC for the property development rights acquired in the Rail Merger, net of payments received from developers. Movements of property development in progress during the half year ended 30 June 2012 and the year ended 31 December 2011 are as follows:

in HK$ million	Balance at 1 January	Transfer from deferred expenditure	Expenditure	Offset against payments received from developers	Transfer out on project completion	Exchange difference	Balance at 30 June/ 31 December
At 30 June 2012 (Unaudited)							
Airport Railway Property Projects	**–**	**–**	**1**	**(1)**	**–**	**–**	**–**
Tseung Kwan O Extension Property Projects	**1,088**	**–**	**42**	**(4)**	**–**	**–**	**1,126**
East Rail Line/Kowloon Southern Link/ Light Rail Property Projects	**8,081**	**–**	**57**	**–**	**–**	**–**	**8,138**
South Island Line (East) Property Project	**285**	**–**	**183**	**–**	**–**	**–**	**468**
Kwun Tong Line Extension Property Project	**65**	**–**	**67**	**–**	**–**	**–**	**132**
Shenzhen Property Project	**2,445**	**–**	**9**	**–**	**–**	**(25)**	**2,429**
	11,964	**–**	**359**	**(5)**	**–**	**(25)**	**12,293**
At 31 December 2011 (Audited)							
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

16 Investments in Securities

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

in HK$ million	**At 30 June 2012 (Unaudited)**	At 31 December 2011 (Audited)
Held-to-maturity securities, at amortised cost		
– maturing within 1 year	**1,702**	2,626
– maturing after 1 year	**–**	–
	1,702	2,626
Trading securities listed overseas, at fair value		
– maturing within 1 year	**93**	126
– maturing after 1 year	**316**	222
	409	348
	2,111	2,974

17 Properties Held for Sale

in HK$ million	At 30 June 2012 (Unaudited)	At 31 December 2011 (Audited)
Properties held for sale		
– at cost	**1,199**	3,718
– at net realisable value	**41**	39
	1,240	3,757

Properties held for sale at net realisable value are stated net of cost provision of HK$16 million (31 December 2011: HK$18 million) in order to state these properties at the lower of their costs and estimated net realisable values.

18 Derivative Financial Assets and Liabilities

The notional amounts and fair values of derivative financial assets and liabilities are as follows:

	At 30 June 2012 (Unaudited)		At 31 December 2011 (Audited)	
in HK$ million	Notional amount	Fair value	Notional amount	Fair value
Derivative Financial Assets				
Foreign exchange forwards				
– cash flow hedges	**73**	**3**	86	3
– not qualified for hedge accounting	**15**	**–**	6	–
Cross currency swaps				
– fair value hedges	**2,021**	**43**	1,245	54
Interest rate swaps				
– fair value hedges	**3,633**	**276**	2,833	287
– cash flow hedges	**–**	**–**	300	–
– not qualified for hedge accounting	**388**	**–**	388	–
	6,130	**322**	4,858	344
Derivative Financial Liabilities				
Foreign exchange forwards				
– cash flow hedges	**128**	**5**	83	4
– not qualified for hedge accounting	**165**	**6**	174	7
Cross currency swaps				
– fair value hedges	**5,080**	**40**	4,663	28
Interest rate swaps				
– cash flow hedges	**2,212**	**110**	1,912	112
	7,585	**161**	6,832	151
Total	**13,715**		11,690	

19 Debtors, Deposits and Payments in Advance

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 operations 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 it is collected through pre-sale agents which settle the amounts due within 21 days.

(ii) Fare revenue from Shenzhen Metro 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 the revenue 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 telecommunication 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 terms of the respective agreements.

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

(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 the relevant development agreements or sale and purchase agreements.

The ageing of debtors is analysed as follows:

in HK$ million	**At 30 June 2012 (Unaudited)**	At 31 December 2011 (Audited)
Amounts not yet due	**3,622**	2,612
Overdue by 30 days	**59**	428
Overdue by 60 days	**49**	21
Overdue by 90 days	**13**	8
Overdue by more than 90 days	**29**	20
Total debtors	**3,772**	3,089
Deposits and payments in advance	**678**	677
Prepaid pension costs	**197**	198
	4,647	3,964

Included in the balance as at 30 June 2012 was HK$1,809 million (31 December 2011: HK$1,203 million) in respect of property development projects.

20 Material Related Party Transactions

The Financial Secretary Incorporated, which holds approximately 76.6% 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 this interim financial report.

As at 30 June 2012, amounts due from/to HKSAR Government and other related parties in respect of material related party transactions with the Group are stated below:

in HK$ million	**At 30 June 2012 (Unaudited)**	At 31 December 2011 (Audited)
Amounts due from:		
– HKSAR Government	**428**	248
– KCRC	**19**	20
– non-controlled subsidiaries	**22**	23
– associates	**69**	111
	538	402
Amounts due to:		
– HKSAR Government	**11**	31
– KCRC	**1,572**	1,432
– an associate	**9**	18
	1,592	1,481

As at 30 June 2012, the amount due from HKSAR Government related to the costs recoverable for the Shatin to Central Link and Express Rail Link projects, reimbursable costs for the essential public infrastructure works for the South Island Line (East) and Kwun Tong Line Extension projects, as well as receivables and retention for other entrustment and maintenance works. The amount due to HKSAR Government related to land administrative fees for railway extensions.

The amount due from KCRC related to the costs recoverable for certain capital works and property enabling works in accordance with the Rail Merger agreements. The amount due to KCRC related to mandatory payments and the 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 fixed and variable annual payments arising from the Rail Merger.

The amount due from associates related to the outstanding balances of a loan to Tunnelbanan Teknik Stockholm AB ("TBT") as well as staff secondment and other service fees receivable from Beijing (MTR) Corporation Limited. The amount due to an associate related to rolling stock maintenance service fees payable to TBT.

During the half year ended 30 June 2012, cash dividends of HK$2,262 million (2011: HK$1,996 million) were paid to HKSAR Government.

Details of major related party transactions entered into by the Group with HKSAR Government in prior years which are still relevant for the current period and with KCRC in respect of the Rail Merger were described in the Company's audited accounts for the year ended 31 December 2011.

20 Material Related Party Transactions *(continued)*

During the half year ended 30 June 2012, the Group had the following transactions with its non-controlled subsidiaries, Octopus Holdings Limited and its subsidiaries ("Octopus Group"), and associates, TBT, Beijing (MTR) Corporation Limited ("Beijing MTR") and London Overground Rail Operations Ltd ("LOROL"):

in HK$ million	**Half year ended 30 June 2012**	Half year ended 30 June 2011
Octopus Group		
– Expenses paid or payable in respect of central clearing services provided by Octopus Group	**60**	56
– Fees received or receivable in respect of load agent, Octopus card issuance and refund services, computer equipment and relating services and warehouse storage space provided to Octopus Group	**14**	13
– Dividend paid by Octopus Group	**149**	63
TBT		
– Expenses paid or payable in respect of rolling stock maintenance and other supporting services provided by TBT for the Stockholm Metro operation	**302**	310
– Fees received or receivable in respect of staff secondment, depots and depot equipment rental and other support services provided to TBT	**71**	72
Beijing MTR		
– Fees received or receivable in respect of staff secondment and other support services provided to Beijing MTR	**7**	10
LOROL		
– Dividend paid by LOROL	**52**	–

21 Creditors and Accrued Charges

As at 30 June 2012, creditors and accrued charges included HK$3,202 million (31 December 2011: HK$4,613 million) of Government grant not yet utilised for the construction of the West Island Line and HK$1,924 million (31 December 2011: HK$1,950 million) of payables in relation to the property development of Lot 1 of Shenzhen Metro Longhua Line Depot. Other creditors and accrued charges mainly related to capital projects to be settled upon certification of work in progress. The Group has no significant balances of trade creditors resulting from its provision of transportation services.

The analysis of creditors as at 30 June 2012 by due dates is as follows:

in HK$ million	**At 30 June 2012 (Unaudited)**	At 31 December 2011 (Audited)
Due within 30 days or on demand	**2,550**	2,765
Due after 30 days but within 60 days	**2,426**	2,379
Due after 60 days but within 90 days	**2,316**	537
Due after 90 days	**2,344**	3,950
	9,636	9,631
Rental and other refundable deposits	**2,646**	1,704
Accrued employee benefits	**500**	454
Government grant on West Island Line Project un-utilised	**3,202**	4,613
	15,984	16,402

22 Loans and Other Obligations

Notes issued by the Group during the half years ended 30 June 2012 and 2011 comprise:

in HK$ million	Half year ended 30 June 2012		Half year ended 30 June 2011	
	Principal amount	Net consideration received	Principal amount	Net consideration received
Debit issuance programme notes	**3,247**	**3,217**	1,206	1,206

The notes were issued 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 half years ended 30 June 2012 and 2011, the Group did not redeem any of its unlisted or listed debt securities.

23 Obligations under Service Concession

Obligations under service concession comprise the outstanding balances of the discounted total fixed annual payments for the service concession acquired in the Rail Merger and the discounted total annual lease payments for the service concession in respect of Shenzhen Metro Longhua Line Phase 1.

24 Deferred Tax Assets and Liabilities

A Movements of deferred tax assets and liabilities during the half year ended 30 June 2012 and the year ended 31 December 2011 are as follows:

	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
30 June 2012 (Unaudited)						
Balance as at 1 January 2012, as previously reported	**8,981**	**5,977**	**153**	**(17)**	**(16)**	**15,078**
Effect of adoption of the Amendments to HKAS 12	**–**	**(5,604)**	**–**	**–**	**–**	**(5,604)**
Balance as at 1 January 2012, as restated	**8,981**	**373**	**153**	**(17)**	**(16)**	**9,474**
Charged to consolidated profit and loss account	**5**	**–**	**38**	**–**	**–**	**43**
Charged to reserves	**–**	**23**	**–**	**–**	**–**	**23**
Exchange difference	**(1)**	**–**	**2**	**–**	**–**	**1**
Balance as at 30 June 2012	**8,985**	**396**	**193**	**(17)**	**(16)**	**9,541**
31 December 2011 (Audited and restated)						
Balance as at 1 January 2011, as previously reported	8,669	5,044	154	(15)	(7)	13,845
Effect of adoption of the Amendments to HKAS 12	–	(4,764)	–	–	–	(4,764)
Balance as at 1 January 2011, as restated	8,669	280	154	(15)	(7)	9,081
Charged/(credited) to consolidated profit and loss account, as restated	316	–	(1)	–	(9)	306
Charged/(credited) to reserves	–	93	–	(2)	–	91
Exchange difference	(4)	–	–	–	–	(4)
Balance as at 31 December 2011, as restated	8,981	373	153	(17)	(16)	9,474

B Deferred tax assets and liabilities recognised are as follows:

in HK$ million	At 30 June 2012 (Unaudited)	At 31 December 2011 (Audited and restated)
Net deferred tax assets recognised on the consolidated balance sheet	**(27)**	(24)
Net deferred tax liabilities recognised on the consolidated balance sheet	**9,568**	9,498
	9,541	9,474

25 Share Capital, Share Premium and Capital Reserve

in HK$ million	At 30 June 2012 (Unaudited)	At 31 December 2011 (Audited)
Authorised:		
6,500,000,000 shares of HK$1.00 each	**6,500**	6,500
Issued and fully paid:		
5,786,501,450 shares (2011: 5,784,871,250 shares) of HK$1.00 each	**5,787**	5,785
Share premium	**11,124**	11,089
Capital reserve	**27,188**	27,188
	44,099	44,062

A 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.

B New shares issued and fully paid up during the period comprise:

			Proceeds received / Transfer from employee share-based capital reserve		
	Number of shares	Option price	Share capital account	Share premium account	Total
		HK$	HK$ million	HK$ million	HK$ million
Employee share options exercised					
– 2007 Share Option Scheme	**1,445,700**	**18.30**	**2**	**30**	**32**
	48,000	**26.52**	**–**	**1**	**1**
	71,500	**26.85**	**–**	**2**	**2**
	65,000	**27.60**	**–**	**2**	**2**
	1,630,200		**2**	**35**	**37**

C Key details of the Company's share option schemes are summarised as follows:

	Half year ended 30 June 2012		Half year ended 30 June 2011	
	New Joiners Share Option Scheme	2007 Share Option Scheme	New Joiners Share Option Scheme	2007 Share Option Scheme
No. of previously vested share options exercised during the period	**–**	**1,630,200**	374,700	638,500
No. of share options granted during the period	**–**	**16,917,000**	–	–
No. of share options forfeited during the period	**–**	**533,500**	–	373,500
No. of share options vested during the period	**–**	**379,500**	–	1,025,500
No. of share options outstanding as at 30 June	**329,000**	**64,596,800**	746,500	51,556,500

Details of the movements in respect of these share option schemes are set out under the Corporate Governance and Other Information section on pages 24 to 34.

D During the half year ended 30 June 2012, the Company offered to grant 16,917,000 share options under the Company's 2007 Share Option Scheme to Members of the Executive Directorate and certain eligible employees of the Company (the "Grantees") on 23 March 2012 and all were accepted by the grantees on 30 March 2012.

26 Other Reserves

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 of HK$35,695 million (31 December 2011: HK$33,991 million as restated) included in retained profits are non-distributable as they also do not constitute realised profits. As at 30 June 2012, the Company considered that the total amount of reserves available for distribution to equity shareholders amounted to HK$53,633 million (31 December 2011: HK$52,719 million).

27 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	**Half year ended 30 June 2012 (Unaudited)**	Half year ended 30 June 2011 (Unaudited)
Operating profit before property developments, depreciation, amortisation and variable annual payment	**6,519**	6,001
Adjustments for:		
– Decrease in provision for obsolete stock	**(1)**	–
– Loss on disposal of fixed assets	**10**	11
– Amortisation of deferred income from transfers of assets from customers	**(5)**	(3)
– Increase in fair value of derivative instruments	**(3)**	(5)
– Unrealised gain on revaluation of investment in securities	**(6)**	(5)
– Employee share-based payment expenses	**27**	37
– Exchange (gain)/loss	**(1)**	2
Operating profit from recurrent businesses before working capital changes	**6,540**	6,038
Increase in debtors, deposits and payments in advance	**(20)**	(319)
Increase in stores and spares	**(67)**	(21)
Increase in creditors and accrued charges	**1,364**	476
Cash generated from operations	**7,817**	6,174

28 Capital Commitments

A Outstanding capital commitments as at 30 June 2012 not provided for in the accounts were as follows:

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
At 30 June 2012 (Unaudited)					
Authorised but not yet contracted for	**2,992**	**–**	**1,248**	**–**	**4,240**
Authorised and contracted for	**1,554**	**11,644**	**138**	**142**	**13,478**
	4,546	**11,644**	**1,386**	**142**	**17,718**
At 31 December 2011 (Audited)					
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

Excluded from the above table are estimated future project costs relating to the West Island Line, South Island Line (East) and Kwun Tong Line Extension of HK$3,668 million, HK$6,050 million and HK$2,717 million respectively as at 30 June 2012.

28 Capital Commitments *(continued)*

B The capital commitments under Hong Kong transport operations, Hong Kong station commercial business and other businesses comprise the following:

in HK$ million	Improvement and enhancement works	Acquisition of property, plant and equipment	Additional concession property	Total
At 30 June 2012 (Unaudited)				
Authorised but not yet contracted for	**1,507**	**239**	**1,246**	**2,992**
Authorised and contracted for	**573**	**472**	**509**	**1,554**
	2,080	**711**	**1,755**	**4,546**
At 31 December 2011 (Audited)				
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

29 Post Balance Sheet Event

On 17 July 2012, the Company's subsidiary, MTR Hangzhou Line 1 Investment Company Limited, signed a contract with a subsidiary of Hangzhou Metro Group Company Limited to set up a joint venture company to invest in and operate Hangzhou Metro Line 1 for a period of 25 years following the approval by the National Development and Reform Commission on the public-private partnership ("PPP") project for the investment, construction and operations of Hangzhou Metro Line 1. Total capital cost of Hangzhou Metro Line 1 is approximately RMB22 billion. Hangzhou Metro Group Company Limited undertakes to invest in the project's civil construction work, representing 62% of the total project cost. Under the PPP arrangement, the joint venture company is responsible for the electrical and mechanical system as well as rolling stock with a total investment of approximately RMB8.3 billion, which is approximately 38% of the total project cost. The Group has an effective interest of 49% of the joint venture company with the balance owned by Hangzhou Metro Group Company Limited.

30 Approval of Interim Financial Report

The interim financial report was approved by the Board on 13 August 2012.