

# Corporate governance

The Company is committed to ensuring high standards of corporate governance in the interests of shareholders and devotes considerable effort to identifying and formalising best practices.

## The Board of Directors

The overall management of the Company's business is vested in the Board. Pursuant to the Articles of Association and the Protocol adopted by the Board, the Board has delegated the day-to-day management of the Company's business to the Executive Directorate, and focuses its attention on matters affecting the Company's overall strategic policies, finances and shareholders. These include financial statements, dividend policy, significant changes in accounting policy, the annual operating budget, certain material contracts, strategies for future growth, major financing arrangements and major investments, risk management strategies, treasury policies and fare structures.

The Board comprises 11 members, consisting of one executive Director (the Chief Executive Officer) and ten non-executive Directors, of whom six are independent non-executive Directors. Following the Board's decision to split the roles of Chairman and Chief Executive Officer, Dr. Raymond Ch'ien Kuo-fung, already a member of the Board, was appointed non-executive Chairman for three years with effect from 21 July 2003, and Mr. Chow Chung-kong was appointed Chief Executive Officer and a member of the Board on 1 December 2003. Two of the other non-executive Directors (being the Secretary for the Environment, Transport and Works and the Commissioner for Transport) are appointed by the Chief Executive of the HKSAR. Another non-executive Director, Mr. Frederick Ma Si-hang, is the Secretary for Financial Services and the Treasury of the Government of the HKSAR. The Government of the HKSAR through The Financial Secretary Incorporated, holds approximately 76% of the issued share capital of the Company. Coming from diverse business and professional backgrounds, the non-executive Directors actively bring their valuable experience to the Board for promoting the best interests of the Company and its shareholders. On the other hand, independent non-executive Directors contribute to ensuring that interests of all shareholders of the Company are taken into account by the Board and that relevant issues are subjected to objective and dispassionate consideration by the Board. The Company has received confirmation from each independent non-executive Director about his/her independence under the Listing Rules, and continues to consider each of them to be independent. None of the Directors or members of the Executive Directorate is related to each other.

The posts of Chairman and Chief Executive Officer are distinct and separate. The non-executive Chairman is responsible for chairing and managing the operations of the Board, as well as monitoring the performance of the Chief Executive Officer and members of the Executive Directorate. Apart from ensuring adequate information about the Company's business is provided to the Board on a timely basis, the Chairman also facilitates effective contribution of non-executive Directors at Board meetings. As head of the Executive Directorate, the Chief Executive Officer is responsible to the Board for managing the business of the Company.

The Board meets in person regularly, and all members of the Board have full and timely access to relevant information and may take independent professional advice, if necessary. In year 2004, the Board held eight meetings, of which the possible merger between the Company and Kowloon-Canton Railway Corporation ("KCRC") was discussed at seven meetings by members of the Board who did not have conflicts of interest. In addition, two meetings solely on the possible merger were held during the year by those members who did not have conflicts of interest. The attendance record of each member of the Board is set out below:

Directors	Attendance of Board meetings in 2004	Attendance rate
<b>Non-executive Directors</b>		
Dr. Raymond Ch'ien Kuo-fung (Chairman)	9/10	90%
Commissioner for Transport (Robert Charles Law Footman)	8/8	100%
Secretary for the Environment, Transport and Works (Dr. Sarah Liao Sau-tung) * 4 meetings were attended by alternate directors	8/8*	100%
Frederick Ma Si-hang † 3 meetings were attended by alternate director	8/8†	100%
<b>Independent Non-executive Directors</b>		
Professor Cheung Yau-kai	6/10	60%
David Gordon Eldon	4/8	50%
Christine Fang Meng-sang	9/10	90%
Edward Ho Sing-tin	10/10	100%
Lo Chung-hing	10/10	100%
T. Brian Stevenson	10/10	100%
<b>Executive Director</b>		
Chow Chung-kong (Chief Executive Officer)	10/10	100%

A person may be appointed as a member of the Board at any time either by the shareholders in general meeting or by the Board upon recommendation of the Nominations Committee. Directors who are appointed by the Board must retire at the first annual general meeting after their appointment. In either case, the Directors so elected and appointed are eligible for re-election and re-appointment. At each annual general meeting of the Company, one third of the Directors (or such number as is nearest to and less than one third) are required to retire from office by rotation.

The Chief Executive of the HKSAR may, pursuant to Section 8 of the MTR Ordinance, appoint up to three persons as "additional directors". Unless the Chief Executive of the HKSAR otherwise directs, the Directors appointed in this way may not be removed from office and they are not subject to any requirement to retire by rotation stated in the preceding paragraph. In all other respects, "additional directors" are treated for all purposes in the same way as other Directors. The Chief Executive has appointed the Office for the Secretary for Environment, Transport and Works and the Office for Commissioner for Transport as "additional directors".

Each of the Directors, on appointment to the Board, is given a comprehensive induction programme on key areas of business operations and practices of the Company, as well as a Directors' Manual. Amongst other things, the Manual not only sets out general and specific duties of Directors under general law (common law and legislation) and the Listing Rules, but also the Terms of Reference of Board Committees. The Directors' Manuals are updated from time to time to reflect developments in those areas.

### Board Committees

As an integral part of good corporate governance, the Board has established the following Board Committees to oversee particular aspects of the Company's affairs. Each of these Committees comprise entirely non-executive Directors who have been invited to serve as members. The Committees are governed by their respective Terms of Reference.

#### Audit Committee

The Audit Committee consists of three non-executive Directors, two of whom are independent non-executive Directors. The members of the Committee are T. Brian Stevenson (chairman), Professor Cheung Yau-kai and the Commissioner for Transport (Robert Charles Law Footman). The Finance Director, the Head of Internal Audit Department and representatives of the external auditors of the Company are expected to attend meetings of the Committee. At the discretion of the Committee, others may also be invited to attend meetings. The Committee normally meets four times a year, and the external auditors or the Finance Director may request a meeting if they consider it necessary.

The duties of the Audit Committee include financial and efficiency aspects. Amongst other things, the Committee reviews the truth and fairness of the Group's annual and interim financial

statements, and discusses with the external auditors the nature and scope of audit before the audit commences. It also reviews and approves non-audit services. The Audit Committee conducts an assessment, at least annually, of the effectiveness of the Company's systems of internal control. These systems allow the Board to monitor the Company's overall financial position and to protect its assets. In addition, the Committee reviews the internal audit function. The Audit Committee selects, in consultation with the Chairman and Members of Executive Directorate (or otherwise to approve) any topic to be the subject of an audit into the efficiency, effectiveness or value for money of any of the activities or operations of the Company. It then reviews reports of such audit and puts forward recommendations to the Board. The chairman of the Committee summarises activities of the Committee for the year and highlights issues arising therefrom in a report to the Board.

In year 2004, the Audit Committee held four meetings. The attendance record of each Audit Committee member is set out below. Representatives of the external auditors, the Finance Director and the Head of Internal Audit Department attended all those meetings for reporting and answering questions about their work. Further to that and by invitation, Managing Director – Operations and Business Development and Property Director had respectively provided an overview of the Company's railway operations and property business to the members at a meeting.

Directors	Attendance of Audit Committee meetings in 2004	Attendance rate
T. Brian Stevenson (chairman)	4/4	100%
Professor Cheung Yau-kai	4/4	100%
Commissioner for Transport (Robert Charles Law Footman)	4/4	100%

#### Remuneration Committee

The Remuneration Committee consists of three non-executive Directors, two of whom are independent non-executive Directors. The members of the Remuneration Committee are Edward Ho Sing-tin (chairman), T. Brian Stevenson and Frederick Ma Si-hang. The Remuneration Committee makes recommendation to the Board on executive Directors' remuneration packages and terms of employment. The Committee also determines relevant remuneration policy for executive Directors and their participation in incentive schemes operated by the Company. In 2004, the Remuneration Committee held two meetings. The attendance record of each Remuneration Committee member is set out below:

Directors	Attendance of Remuneration Committee meetings in 2004	Attendance rate
Edward Ho Sing-tin (chairman)	2/2	100%
T. Brian Stevenson	1/2	50%
Frederick Ma Si-hang	2/2	100%

### Nominations Committee

The Nominations Committee consists of three non-executive Directors, two of whom are independent non-executive Directors. The members of the Nominations Committee are David Gordon Eldon (chairman), Lo Chung-hing and the Secretary for the Environment, Transport and Works (Dr. Sarah Liao Sau-tung). The Nominations Committee nominates and recommends to the Board candidates for filling vacancies on the Board. The Committee held no meeting in 2004.

### Independent Committee

The Board is committed to looking after the interests of independent shareholders of the Company, and for this purpose, an independent committee of the Board (the "Independent Committee"), chaired by Edward Ho Sing-tin, together with Professor Cheung Yau-kai, Christine Fang Meng-sang, Lo Chung-hing and T. Brian Stevenson, has been established to consider and review terms of any possible merger between the Company and KCRC, and advise independent shareholders whether they are fair and reasonable. All members of the Independent Committee are independent non-executive Directors of the Company.

### Internal Audit

The Internal Audit Department plays a major role in support of and in collaboration with the Company's management, in monitoring the internal governance of the Company. The Department has unrestricted access to information that allows it to review all aspects of the Company's network of risk management, control and governance processes. On a regular basis, it conducts audits of the practices, procedures, expenditure and internal controls of all business and support units and subsidiaries. As the need arises, it also conducts ad-hoc reviews or investigations. The Internal Auditor reports directly to the Chief Executive Officer and has direct access to the Audit Committee.

### Code of Best Practice

The Company has complied throughout the year with the Code of Best Practice set out in Appendix 14 to the Listing Rules except that 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 MTR Ordinance) to retirement by rotation and re-election at the Company's annual general meetings in accordance with Articles 87 and 88 of the Articles of Association. Dr. Raymond Ch'ien Kuo-fung, a member of the Board, was appointed as the non-executive Chairman of the Company with effect from 21 July 2003 for a term of three years.

### Model Code for Securities Transactions by Directors of Listed Issuers (the "Model Code")

The Company, having made specific enquiry, confirms that members of the Board and the Executive Directorate complied throughout the year with the Model Code set out in Appendix 10 to the Listing Rules. Senior managers who, because of their office in the Company, are likely to be in possession of unpublished price sensitive information, have been requested to comply with the provisions of the Model Code.

### Business Ethics

The Company is committed to a high standard of business ethics and integrity.

The 2002 Code of Conduct on the ethical and behavioural framework for all staff was reviewed and reissued to all staff in June 2004 to align it with the latest developments in corporate governance standards, including corporate governance standards under the Sarbanes-Oxley Act of 2002. A new "Corporate Guidebook for All Staff on Code of Conduct" was issued to all staff at the same time. The Guidebook provides specific guidelines for employees in respect of behaviour within and outside the workplace. Communication sessions were held to brief employees on the changes in the Code of Conduct and the contents of the new Corporate Guidebook.

### US Sarbanes-Oxley Act 2002

This legislation, which seeks to enhance the transparency and accountability of companies in the areas of corporate governance and financial reporting, was signed into law by the President of the United States on 30 July 2002.

As the Company is a SEC reporting company, it is generally bound by this legislation.

The Company has been, and will continue its process of, reviewing its internal systems and practices and implementing new requirements under this legislation in line with applicable compliance dates.