

AUDIT COMMITTEE REPORT

As at the date of this Report, the Audit Committee of the Company (referred to as the “Committee” in this Report) consists of six Non-executive Directors, five of whom are Independent Non-executive Directors of the Company. Details of the Committee’s membership and their attendance records during 2020 are set out on pages 112 to 113 of this Annual Report. None of the Committee members is a partner or former partner of KPMG, the Company’s external auditor.

The Finance Director (the “FD”), the Head of Internal Audit (the “Head of IA”) and representatives of the external auditor attend all 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 Chairman of the Committee, the external auditor or the FD may request additional meetings if they consider necessary. The Committee may, upon request, approve the appointment of the Company’s external auditor for undertaking non-audit work.

TERMS OF REFERENCE OF THE COMMITTEE

The Terms of Reference of the Committee (the “ToR”) is available on the respective websites of the Company (www.mtr.com.hk) and the Stock Exchange.

DUTIES OF THE COMMITTEE

Under the ToR, the duties of the Committee primarily comprise the following:

- Oversight of the relationship with the Company’s external auditor, including making recommendations to the Board on the appointment of and any change to the Company’s external auditor and communicating with the external auditor on financial matters of the Company;
- Review of the financial information of the Company, including monitoring the integrity of financial statements;

- Oversight of the Company’s financial reporting and internal control systems, including overseeing the adequacy of the resources and competence of the Company’s accounting and financial reporting functions; and
- Overseeing the Company’s Internal Audit function, including liaison with the Head of IA, approval of the annual internal audit plan of the Company and receiving periodic reports from the Head of IA.

More details on the duties of the Committee are set out in the ToR and further information can be found in the “Risk Management and Internal Control Systems” section of the Corporate Governance Report on pages 115 to 119 of this Annual Report.

Reporting to the Board

The Chairman of the Committee summarises the activities of the Committee and highlights issues arising therefrom in a report to the Board after each Committee meeting.

The minutes of Committee meetings are prepared by the secretary of the meetings with details of the matters considered by Committee members and decisions reached, including any concerns raised by Committee members, dissenting views expressed and suggestions for enhancing the governance and internal control systems of the Company. The draft minutes are circulated to Committee members for comment after each meeting. The Committee formally adopts the draft minutes at the next subsequent meeting, after taking into account any comments that Committee members may have made. Minutes of Committee meetings are open for inspection by Committee members at the Company’s registered office.

In advance of the first regular Committee meeting each year, the secretary of the meetings pre-agrees key agenda items for the year with the Chairman of the Committee who makes a final determination on the agenda for the Committee meetings.

WORK PERFORMED BY THE COMMITTEE IN 2020

In 2020, the Committee held four regular meetings. Representatives of the external auditor, the FD and the Head of IA attended all four regular meetings to report and answer questions about their work. In addition, relevant Members of the Executive Directorate were invited to join certain presentations to the Committee. The Committee also held private sessions with the external auditors without the presence of Management during the year.

The Committee devoted its attention to the review of the Company's annual and interim results announcement/accounts at the February and July meetings respectively, allowing more time to review and discuss the Company's internal controls, internal audit and other activities at the May and November regular meetings.

Acting through the Risk Committee and the Committee, the Board has mandated a review of the internal control and risk management systems for the Company's Hong Kong operations. In 2020, an external consultant was appointed to conduct a deep-dive assessment of the Company's existing Three Lines of Defence framework, with a view to identifying any gaps in the framework and making recommendations for improvement. The results of this assessment were presented to and endorsed by the Risk Committee and the Committee in late 2020. The next phase of the project will be to strengthen the Company's Second Line of Defence (in particular) in certain key risk areas through the establishment of new technical and engineering Centres of Excellence and the adoption of a new assurance framework. A further update on progress will be presented to both Committees in mid-2021.

The following key matters were reviewed/considered/endorsed (as relevant) by the Committee in 2020:

Financial

- The draft 2019 Annual Report and Accounts and 2020 Interim Report and Accounts, including the financial impact of the Company's railway construction projects under entrustment by the HKSAR Government, and the relevant disclosure notes in the said Accounts and recommendation of the same for the Board's approval;
- Updates on the carrying value of the Group's properties and rail fixed assets;
- Updates on the latest positions of the Company's railway construction projects under entrustment by the HKSAR Government;
- Update relating to Service Concession Payments and tax matters;
- 2020 cost savings analysis; and
- Preview of the 2020 interim and annual accounting and financial reporting issues.

Internal Audit and Internal Control

- Risk Management and Internal Control Systems Effectiveness for 2019 for submission to the Board (focused on the internal control system, as the risk management system effectiveness was separately reviewed and endorsed by the Risk Committee of the Company);
- Report on Evaluation of Effectiveness of Internal Audit Department for 2019;
- Continuing Connected Transactions for 2019;
- Internal Audit Department's Reports;
- Whistle-blowing Progress Reports; and
- Approval of the 2021 Internal Audit Plan.

External Auditor

- KPMG's reports on the salient features of the 2019 Annual Accounts and 2020 Interim Accounts respectively;
- 2019 Auditor's Report;
- KPMG's independence and other relevant factors when approving the appointment of KPMG in providing non-audit services; pre-approval of the engagement of KPMG to provide non-audit services; and KPMG's confirmation of independence in its audit report in respect of the 2019 Annual Accounts and 2020 Interim Accounts respectively;
- Summary of KPMG services provided to the Company and fees received by them;
- Approval of KPMG's fee proposal for the 2020 annual audit and the 2021 interim review, as well as other audit related and tax services; and
- KPMG's audit plan and strategy for the year ended 31 December 2020.

Governance

- Report on compliance with statutes and regulations, Operating Agreement and Rail Merger Related Agreements in 2019 and outstanding litigation/potential litigation;
- Updates on the Three Lines of Defence of the Company; and
- Summaries on the salient features of the Audit/Risk/Governance Committee Minutes of various subsidiaries of the Company.

RE-APPOINTMENT OF EXTERNAL AUDITOR

The Committee was satisfied with KPMG's work, its independence and objectivity, and therefore recommended the re-appointment of KPMG (which has indicated its willingness to continue in office) as the Group's external auditor for 2021 for approval by the Company's Shareholders at the 2021 Annual General Meeting.

Dr Eddy Fong Ching
Audit Committee Chairman
Hong Kong, 11 March 2021

The Audit Committee Report has been reviewed and endorsed by the Committee.