

## Corporate Governance Report

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# COMMUNICATION

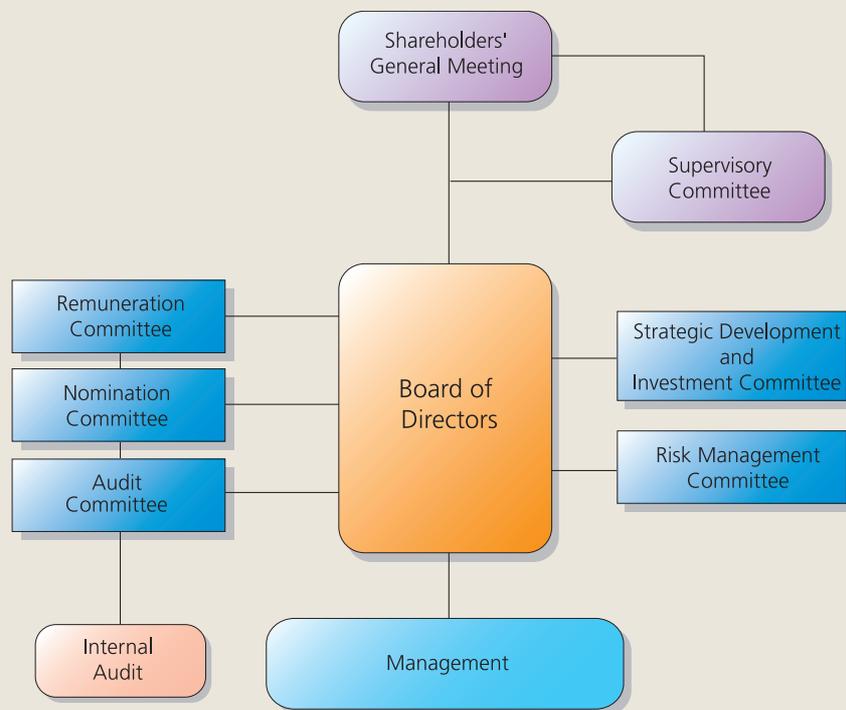
and two-way exchange with investors. A corporate culture based on respect and accountability towards investors has been initiated and developed within the Company.



# Corporate Governance Report

The Company always aims to ensure stable business development and to enhance value for shareholders through its commitment to the corporate values of integrity and diligence. It is our belief that such an aim will be achieved by persistent adherence to sound corporate governance principles, efforts to enhance transparency and independence of the Company's operations and the establishment of an effective accountability system.

**The Company's corporate governance structure is as follows:**



## CODE ON CORPORATE GOVERNANCE PRACTICES

During the Reporting Period, the Company has fully adopted the code provisions of the Code on Corporate Governance Practices (the "Code") as set out in Appendix 14 to the Listing Rules of the HKEX. As compared to 2005, during the Reporting Period, the Company arranged member(s) of the Independent Board Committee to attend shareholders' meeting for the approval of the Company's connected transactions to respond to questions raised by shareholders.

In recent years, the Company has strengthened the transparency of information disclosure regarding areas in which shareholders' concern is gradually growing, such as internal control and risk management, investor relations, remuneration of directors and senior management, and analyses of financial conditions. The codes on corporate governance and relevant practices currently adopted by the Company have gone beyond the requirements of the aforesaid Code in certain aspects, including:

- the adoption of the cumulative voting system for elections of directors;
- the stipulation on the terms of office for Independent Directors of no more than six years;
- the establishment of the Nomination Committee, the Risk Management Committee (RMC) and the Strategic Development and Investment Committee (SDIC) under the Board, in addition to the Audit Committee and the Remuneration Committee;
- disclosure of senior management remuneration on named basis in annual report;
- preparing and publishing quarterly results announcements in accordance with PRC accounting standards, and voluntarily notify major differences between the accounting statements prepared under PRC accounting standards and HKFRS;
- increasing the disclosure of shareholder information;
- enhancing communication with shareholders.

Details regarding the above are contained herebelow, whereas the content marked with the symbol<sup>④</sup> can be found on the website of the Company.

### A. BOARD OF DIRECTORS

#### Responsibilities and Division of Work

The Board is responsible for leading the Group's development, establishing the Group's strategic goals, as well as ensuring the availability of necessary financial and other resources for the Group to achieve pre-set strategic goals. The principal duties of the Board are to exercise management and decision-making authorities as conferred by the shareholders' general meeting in respect of corporate development strategies, management structures, investment and financing, planning, financial control, human resources, and so forth. The Articles and the attachments to the Articles<sup>④</sup> have already spelt out the Board's duties and authorities in respect of corporate development strategies and management as well as its duties and authorities to supervise and inspect the Company's development and operation.

The different duties and roles of the Chairman of the Board (the "Chairman") and the Chief Executive (the "General Manager") have been clearly defined which have also been spelt out in the Articles and the attachments to the Articles<sup>④</sup>. The Chairman of the Company is Mr. Yang Hai, while the General Manager is Mr. Wu Ya De. The Chairman is responsible for providing leadership in the Board to set strategies and achieve the Group's goals and his duties, including: overseeing and coordinating the operation of the Board to ensure efficient functioning of the Board; ensuring the availability of accurate, timely and clear information to induce effective contribution from the Board; monitoring the execution of the Board's resolutions; and maintaining effective communication with shareholders. The General Manager, with the support and assistance of the Board and other senior management of the Company, is responsible for coordinating and managing the Group's business and operations, implementing the strategies laid down by the Board and making day-to-day operating decisions.

## Composition of the Board

The current Board is in its fourth session since the establishment of the Company and it is composed of 12 directors. Details of the members of the Board are as follows:

Name	Position	Principal Duties in Shareholder Entity	Date First Become Director	Experience/Skills
<b>Executive Directors:</b>				
Yang Hai	Chairman	Director, XTC Company	April 2005	industry experience; road and bridge construction
Wu Ya De	General Manager	—	January 1997	industry experience; corporate management
<b>Non-executive Directors:</b>				
Li Jing Qi	Non-executive Director	Executive Director and President, Shenzhen International	April 2005	international banking experience; risk management
Wang Ji Zhong	Non-executive Director	Director and Deputy General Manager, XTC Company	April 2005	industry experience; financial management
Liu Jun	Non-executive Director	Executive Director and Vice President, Shenzhen International	January 2006	financial and foreign investment management
Lin Xiang Ke	Non-executive Director	Chairman and General Manager, SGH Company	June 1998	industry experience; financial management
Zhang Yang	Non-executive Director	Assistant to General Manager, Huajian Centre	March 2001	industry experience; investment project management
Chiu Chi Cheong, Clifton	Non-executive Director	—	December 1996	financial, securities and accounting
Li Zhi Zheng	Independent Non-executive Director	—	January 2003	technical, operations and administrative management
Zhang Zhi Xue	Independent Non-executive Director	—	January 2003	human resources management
Poon Kai Leung, James	Independent Non-executive Director	—	May 2003	investment banking experience; financial and risk management
Wong Kam Ling	Independent Non-executive Director	—	June 2005	financial management

The above-mentioned Directors were nominated by shareholders of the Company or the Board, and were elected at the extraordinary general meeting held on 28 December 2005. The terms of office of all Directors are from 1 January 2006 to 31 December 2008.

Members of the Board come from different industries, with more than one Independent Director possessing professional accounting qualifications as required by the stock exchanges or appropriate expertise in accounting or related financial management. Brief biographies of the members of the Board are set out on pages 82 to 87 of this annual report.

The Board currently has four Independent Directors, representing 1/3 of the total membership of the Board. All incumbent Independent Directors have extensive professional experience, and all have participated in the meetings of the Board and related specialised committees in a highly conscientious and responsible manner. By providing independent judgment, knowledge and experience to the matters to be resolved, they have played an important check-and-balance role to safeguard the interests of the Company and shareholders as a whole by ensuring that reporting on the Company's financial or other responsible matters would be properly conducted by the Board and by offering constructive criticisms and assistance on the Company's formulation of strategic plans. Since 2005, the Independent Directors have submitted annual work reports each year to the annual general meeting for shareholders' scrutiny.

### **Board Meetings**

Seven Board meetings were held in 2006 to discuss the Group's operational and financial performance, management structure, investment and financing proposals and so forth. Major items discussed include:

- consideration of the annual final accounts and budgets, work reports of the Board and internal control assessment reports;
- consideration of the annual, interim and quarterly reports;
- amendments to the Articles;
- election of new Chairman, formulation of a new session of the specialised committees of the Board;
- formulation of the Directors' remuneration scheme;
- determination of the Company's annual performance targets, renewals of appointments of senior management of the Company;
- re-appointment of international auditors and statutory auditors;
- consideration of the proposed issuance of Bonds With Warrants and approval of the Company's borrowing proposals;
- consideration of acquisitions or disposals of toll highway projects.

Discussions were carried out effectively and decisions were made swiftly and prudently at the Board meetings. Attendance of Directors at the Board meetings in 2006 was 100% (including attendance by appointing other Directors as proxies). Details of attendance of each Director at the Board meetings and the specialised committees' meetings are as follows:

Director	Attendance in Person / Total Number of Meetings					
	Strategic Development and Investment Committee		Audit Committee	Remuneration Committee	Nomination Committee	Risk Management Committee
	The Board					
<b>Executive Directors:</b>						
Yang Hai	7/7	1/1	5 (as observer)	4/4	5/5	—
Wu Ya De	6/7 <sup>#</sup>	1/1	4 (as observer)	3 (as observer)	3 (as observer)	—
<b>Non-executive Directors:</b>						
Li Jing Qi	7/7	—	—	—	—	3/3
Wang Ji Zhong	6/7 <sup>#</sup>	1 (as observer)	—	—	—	—
Liu Jun	6/7 <sup>#</sup>	—	—	—	—	—
Lin Xiang Ke	6/7 <sup>#</sup>	—	—	—	—	—
Zhang Yang	5/7 <sup>#</sup>	—	—	—	—	3/3
Chiu Chi Cheong, Clifton	6/7 <sup>#</sup>	1/1	6/6	—	—	—
<b>Independent Directors:</b>						
Li Zhi Zheng	5/7 <sup>#</sup>	1/1	—	4/4	5/5	—
Zhang Zhi Xue	7/7	1 (as observer)	—	4/4	5/5	—
Poon Kai Leung, James	5/7 <sup>#</sup>	—	5/6 <sup>#</sup>	—	—	3/3
Wong Kam Ling	7/7	1 (as observer)	6/6	—	—	—

<sup>#</sup> Directors who were unable to attend meetings in person had appointed other Directors as their proxies to attend and vote at the meetings on their behalf.

Whenever a transaction is considered at a Board meeting, the Directors are required to report their respective interests involved, and abstain when appropriate. According to the Company's Rules of Procedures for the Board of Directors<sup>10</sup>, a Director should abstain from a meeting and be given no voting rights in case an item considered by the Board is relevant to his/her personal economic interests. In addition, according to the Listing Rules of the SSE, a Director who also holds office in a connected company is not allowed to vote in case the Board is considering a transaction between the connected company and the listed company. During the Year, when the Company was considering the investment proposal of acquiring 5% interests in Meiguan Company, four Directors holding offices in connected companies reported their respective interests in accordance with the relevant rules and abstained from voting.

The Company's management is responsible for supplying the Board with the relevant information and data necessary for the consideration of various resolutions, as well as arranging managers to report on various businesses, in particular the progress on substantial issues of the Company, whenever Board meetings are convened. The Directors, as well as the specialised committees of the Board, may seek the services of independent professional institutions in the course of exercising their authorities, performing their duties or fulfilling any business requirements. Reasonable expenses incurred in this connection will be borne by the Company.

## B. DIRECTORS

### Appointment

Directors are elected or replaced at shareholders' general meetings. Shareholders of the Company, the Board and the Supervisory Committee are eligible to nominate candidates for directorship in writing. Directors serve for a term of three years and, upon expiry of the term, their appointment is subject to further consideration at a general meeting and they may offer themselves for re-election. Independent Directors are eligible for re-election, subject to a maximum term of six years.

The Company's Rules of Procedures for the Board of Directors<sup>10</sup> have listed the Company's requirements on the qualifications and basic qualities of Directors, the nomination format and the proposing procedures: that is, the Nomination Committee is responsible for qualification inspection and quality assessment on the candidates for directorship, as well as making proposals to the Board and providing explanations to the general meetings.

The Company's election of Directors adopts the cumulative voting system whereby, on election of Directors, the number of votes that each shareholder is entitled to cast is equal to the number of shares that he/she holds multiplied by the number of Directors whom he/she has the right to elect. Each shareholder may elect a Director by using all the votes held or may allocate the votes to all the candidates whom he/she has the right to elect at discretion. The candidate with more votes will be elected. The voting on the election of Independent Directors shall be conducted separately from that of non-independent Directors.

### **Information Support and Professional Development**

Upon appointment, new Directors are provided with a comprehensive set of introductory materials by the Company, including a brief introduction to the Group's operations, the responsibilities of Directors, and other statutory requirements. The Company will also arrange for them specialised training organised by external or internal parties. In addition, through the Company Secretary, all the Directors, during their terms of appointment, are able to obtain timely information and updates relating to the statutory, regulatory and other ongoing obligations that the Directors of a listed company must comply with. In 2006, the Company compiled 10 issues of reference document reports or market news summaries for the Directors, providing them with the most updated compliance policy documents and related reports and analyses of the securities market and the news media. During the Year, the Company also held an annual work progress meeting and an investment and financing work progress meeting, and organised a trip for the Directors to inspect Qinglian Project. During the Year, six Non-executive Directors took part in training courses for directors organised by regulatory bodies, while two Executive Directors and two Non-executive Directors participated in the professional training sessions held internally by the Company.

Through various approaches ranging from provision of information, progress reports and field trips to professional training, all Directors, particularly the Non-executive Directors, may obtain timely updates on the Company's business development, competition and regulatory environment and other information which may affect the Group and the industry, thus ensuring a good understanding of their duties, facilitating themselves to exercise correct decision-making and effective monitoring, and a thorough implementation of the procedures of the Board and due compliance with applicable laws and regulations.

### **Remuneration of Directors**

The Company has been disclosing the remunerations of Directors and Supervisors on named basis since 2004 and the same policy has been adopted for senior management since 2005. Details of the Company's remuneration policies, Directors' and senior management's remunerations, and the appraisals and incentive regimes for senior management are set out on page 46 and pages 72 to 73 of this annual report.

### **Independence of Directors**

The Company has appointed a sufficient number of Independent Directors. The Board has obtained written confirmations from all Independent Directors concerning their independence in accordance with rule 3.13 of the Listing Rules of HKEX. The Company believes that the incumbent Independent Directors have all complied with the relevant guidelines as stipulated in such rule and are still regarded as independent.

### **Securities Transactions by Directors**

The Securities Transaction Code of the Company<sup>(b)</sup> has been adopted by the Board in accordance with Appendix 10 to the Listing Rules of HKEX entitled "Model Code for Securities Transactions by Directors of Listed Issuers" and the relevant rules of the SSE in light of the Company's actual situation, as a written guide to regulate dealings in the Company's securities by the Directors, Supervisors and relevant staff. The standards set under Appendix 10 to the Listing Rules have been incorporated into the Securities Transaction Code of the Company.



After specifically inquiring with all the Directors, Supervisors and senior management, except that a Director, Mr. Liu Jun, sold his entire holding of 100,000 H Shares of the Company on 4 April 2006, the Company confirms that none of the Directors, Supervisors or senior management had held, bought or sold any securities of the Company during the Reporting Period. On 5 April 2006, the Board published an announcement in "Hong Kong Economic Times" and "The Standard" regarding the sale of the Company's shares by Mr. Liu Jun.

### C. SPECIALISED COMMITTEES OF THE BOARD

Five specialised committees have been set up under the Board, each of which has formulated its terms of reference<sup>(f)</sup> for monitoring the specific areas of the Company's business. Such terms of reference have been approved by the Board.

#### Strategic Development and Investment Committee

Established in November 2001, the SDIC is principally responsible for examining and reviewing the directions of the Company's strategic plans, formulating strategic plans, monitoring the implementation of strategies and facilitating adjustments to the Company's strategies and governance structure on a timely basis.

Members of the SDIC include:

Mr. Yang Hai (Chairman of the Committee)	<i>Executive Director</i>
Mr. Wu Ya De	<i>Executive Director</i>
Mr. Chiu Chi Cheong, Clifton	<i>Non-executive Director</i>
Mr. Li Zhi Zheng	<i>Independent Director</i>

One meeting of the SDIC was held in 2006, attended by all incumbent members as well as by invited Directors, Supervisors and senior management of the Company. The Company's "Development Strategies 2005-2009" and their implementation in the past two years were reviewed and evaluated at the meeting. The Company's strategic development directions, specific implementation strategies and corresponding management and work objectives were discussed with reference to changes in the internal and external environment. Opinions formed by the SDIC regarding the implementation approaches and planning of strategies were submitted to the Board for confirmation as guiding principles and basis for the management to ascertain the future work focus and planning.

#### Audit Committee

The Audit Committee was established in August 1999, with its terms of reference drawn from proposals set forth in "A Guide for Effective Audit Committees" issued by the Hong Kong Institute of Certified Public Accountants, the "Code on Corporate Governance Practices" in Appendix 14 to the Listing Rules of the HKEX, and the "Corporate Governance Standards for Listed Companies in China" issued by the CSRC. The Audit Committee is principally responsible for reviewing and monitoring the quality and procedures of the Group's financial reporting; evaluating whether the Company's internal control regimes are sound and effective; appointing the independent auditors, coordinating their work and reviewing the efficiency and quality of their work; and reviewing all written reports furnished by internal audit officers as well as the management's feedback to such reports.

Members of the Audit Committee include:

Mr. Wong Kam Ling (Chairman of the Committee)	<i>Independent Director</i>
Mr. Poon Kai Leung, James	<i>Independent Director</i>
Mr. Chiu Chi Cheong, Clifton	<i>Non-executive Director</i>

Six meetings of the Audit Committee were held in 2006, with the external auditors invited to five of such meetings. In order to ensure the independence of reporting, prior to each meeting, the chairman of the meeting would fully consult the external auditors, the Company's management and the internal audit department so as to confirm whether the relevant institutions would need independent meetings with the Audit Committee, and would make arrangements accordingly if applicable.

### Report of the Audit Committee

The Audit Committee is principally responsible for reviewing and monitoring the quality and procedures of the Group's financial reporting. Pursuant to the relevant procedures, the management is responsible for the preparation of the Group's financial statements, including the selection of the appropriate accounting policies therefor; the external auditors are responsible for auditing and verifying the Group's financial statements and evaluating the Group's internal control regimes; while the Audit Committee supervises the work of the management and the external auditors and approves the procedures and protective measures adopted by the management and the external auditors.

The unaudited financial statements for the first and third quarters of 2006 (prepared under PRC Accounting Standards) and the unaudited financial statements for the first six months of 2006 have been reviewed by the Audit Committee and submitted to the Board for approval prior to their publication.

The Audit Committee has discussed with the management and the external auditors the consolidated financial statements contained in the 2006 Annual Report, and conducted studies and communications regarding the adoption of accounting policies and substantial accounting treatment matters, and the impact of the new PRC Accounting Standards scheduled to be adopted on 1 January 2007. The Audit Committee has obtained a report from the external auditors and met with them to discuss the scope of their audit and their evaluation on the Group's internal control regimes. On the basis of the aforesaid reviews and discussions as well as the report of the external auditors, the Audit Committee proposed the Board to approve the consolidated financial report for the year ended 31 December 2006 and the auditors' report in relation thereto.

The Audit Committee also carried out an independent evaluation on whether the Group's internal control regimes were efficient; monitored and appraised the Company's internal audit; and furnished the management with professional advice on the enhancement of internal control and corporate governance standards on an ongoing basis. In addition, the Audit Committee also furnished the management promptly with professional advice on the Company's significant matters or reminded the Company of any risks associated with such matters.

In 2006, the Audit Committee provided the Company with a basic framework of risk management, and assisted the Company to develop and implement a thorough risk management regime. In addition, the Audit Committee also discussed the issue of preventing fraud within the Company and set up a separate reporting mail box<sup>☎</sup> to obtain fraud-related information in a timely manner.

The Audit Committee will, after each meeting, submit a report to the Board on major items discussed and brief the Board at least every six months on its work and progress.

Members of the Audit Committee

Wong Kam Ling, Poon Kai Leung, James, Chiu Chi Cheong, Clifton

2 March 2007



Established in November 2001 as the Human Resources and Remuneration Committee and subsequently renamed as the Human Resources and Nomination Committee (collectively referred to as "HRNC") in January 2003, HRNC is responsible for the remunerations of, and nominations to, the Board. Its principal duties include: examining and devising the Company's human resources development strategies and planning; examining and reviewing the Company's human resources policies, remuneration policies and incentive regimes; and making proposals in respect of appraisals, appointments/removals and nominations of Directors and members of the senior management. Pursuant to a resolution of the Board, HRNC was split into the Remuneration Committee and the Nomination Committee in June 2005 to perform their respective duties.

### Remuneration Committee

The Remuneration Committee is principally responsible for studying and examining the Company's remuneration policies and incentive regimes, devising the appraisal standards for the Company's Directors and members of the senior management, and conducting appraisals thereof.

Members of the Remuneration Committee include:

Mr. Li Zhi Zheng (Chairman of the Committee)	<i>Independent Director</i>
Mr. Zhang Zhi Xue	<i>Independent Director</i>
Mr. Yang Hai (Ceased to be a member of the Committee from 8 December 2006)	<i>Executive Director</i>
Ms. Zhang Yang (Appointed to the Committee on 8 December 2006)	<i>Non-executive Director</i>

To further enhance the governance quality of the Company and accelerate the establishment of the Company's stock option incentive regime, the Board appointed Ms. Zhang Yang, a Non-executive Director, as a member of the Remuneration Committee, while Executive Director Mr. Yang Hai ceased to be a member of the committee.

Four meetings of the Remuneration Committee were held in 2006, attended by all incumbent members. Major tasks accomplished by the Remuneration Committee during the Year include:

- Reviewing the execution of the Company's operating performance for 2005 and the management's performance targets for 2006;
- Reviewing the Company's proposals on enterprise annuity adjustment, management remuneration disclosure, and annual distribution of the special incentive fund under the share appreciation rights scheme;
- Drafting the remuneration proposal for the Directors of the fourth session of the Board;
- Providing guidance on the review and improvement work on the Company's remuneration system and the implementation of the Company's performance management and incentive schemes.

### Nomination Committee

The Nomination Committee is principally responsible for examining and devising the Company's human resources development strategies and planning; and conducting studies and making proposals in respect of nominees, nomination criteria and nomination procedures for the Directors and members of the senior management.

Members of the Nomination Committee include:

Mr. Li Zhi Zheng (Chairman of the Committee)	<i>Independent Director</i>
Mr. Zhang Zhi Xue	<i>Independent Director</i>
Mr. Yang Hai	<i>Executive Director</i>

Five meetings of the Nomination Committee were held in 2006, attended by all incumbent members. Major tasks accomplished by the Nomination Committee during the Year include:

- Providing guidance on the institutional reform and organisational improvement work of the Company, and reviewing the proposal on the adjustment of the operations centre's organisation;
- Guiding and monitoring the work arrangement and appraisal procedures for the term appraisals on the members of the senior management, as well as reviewing the results of the term appraisal on the Administrative Controller;
- Reviewing the Company's proposals on appointing representatives to invested enterprises;
- Making proposals to the Board regarding membership changes of the Remuneration Committee;
- Providing guidance on the training work for the Company's management.

### **Risk Management Committee**

Established in August 2004, currently the RMC is principally responsible for improving and enhancing the Company's procedures and systems for managing its investment activities, and providing support to the Company's business decision-making and operations by performing risk analysis and controls in relation to individual investment projects.

Members of the RMC include:

Mr. Poon Kai Leung, James (Chairman of the Committee)	<i>Independent Director</i>
Ms. Zhang Yang	<i>Non-executive Director</i>
Mr. Li Jing Qi	<i>Non-executive Director</i>

Three meetings of the RMC were held in 2006, attended by all incumbent members. During the Year, the RMC reviewed and discussed the Company's risk management handbook on investment projects, setting preliminary drafts of standardised investment proposals and financial analysis model for investment projects, as well as providing relevant requirements for post-investment follow-up reporting and risk evaluation analysis. In addition, the RMC also considered two proposals on toll highway asset acquisition or disposal and offered constructive opinions to the Board.

### **STATEMENT OF RESPONSIBILITY BY THE BOARD FOR THE FINANCIAL STATEMENTS**

This statement intends to clarify for our shareholders the responsibilities to be assumed respectively by the Directors and the auditors of the Company for the financial statements. It should be read together with the statement of responsibility by the auditors set out in the Independent Auditor's Report on page 90.

It is the Board's opinion that the financial statements were prepared on the basis of ongoing operations given that the resources available to the Company are sufficient enough for carrying out ongoing business operations in the foreseeable future. Appropriate accounting policies have been adopted in preparing the financial statements on pages 90 to 146. These policies have been applied throughout the preparation of the financial statements and supported by reasonable and prudent judgments and estimates, and in accordance with all accounting standards which the Board deems appropriate.

It is the responsibility of the Board to ensure that the account records prepared by the Company can reflect a reasonable and accurate view of the Company's financial position and that the financial statements are in compliance with the requirements of relevant accounting standards of Hong Kong.



## D. CONTROL MECHANISMS

### Supervisory Committee

The Supervisory Committee exercises independently the power of supervision upon the Company in accordance with the law to ensure that the lawful rights of the shareholders, the Company and its staff are not infringed.

The Supervisory Committee of the Company is composed of three supervisors, including Mr. Zhong Shan Qun (Chairman of the Supervisory Committee), Mr. Zhang Yi Ping and Mr. Yi Ai Guo. The Supervisory Committee is in its fourth session since the establishment of the Company. The term of office of the Supervisors commenced from 1 January 2006 to 31 December 2008.

The size and composition of the Company's Supervisory Committee are in compliance with the requirements of the relevant laws and regulations. Seven meetings of the Supervisory Committee were held during 2006 to supervise, on behalf of the shareholders, on the Company's financial matters and on whether the discharge of duties by the Directors and senior management was lawful and regulated. The Supervisory Committee's members attended all Board meetings and general meetings, and diligently performed their supervisory duties. Details relating to the work of the Supervisory Committee are set out in the Report of the Supervisory Committee on pages 80 to 81 of this annual report.

### Internal Control

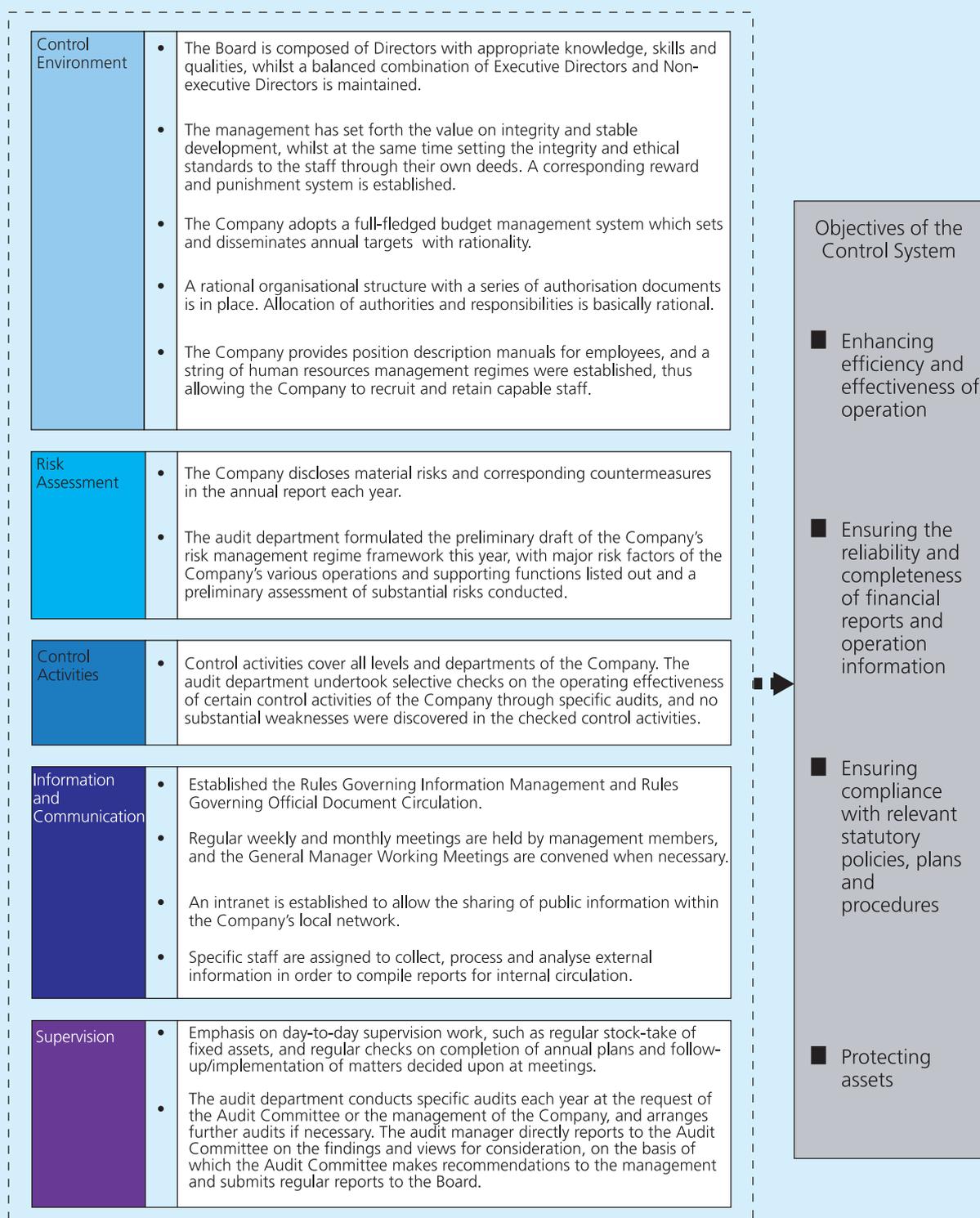
The Board is responsible for developing and maintaining an internal control system of the Company to protect shareholders' interest and to safeguard the Group's assets by reviewing the effectiveness of major control procedures for financial, operational, compliance and risk management matters. In December 2004, the Company's "Internal Control System Manual", which was based on the COSO (the Committee of Sponsoring Organisations of the Treadway Commission) framework, was considered and approved by the Board. This manual contains a comprehensive overview and description of the objectives, content, methods and duties of the Company's internal controls, and will facilitate the ongoing examination and evaluation conducted by the Board in respect of the effectiveness of the internal controls. The internal control system is implemented by the management upon the authorisation of the Board and the effectiveness of the system is reviewed by the Board through the Audit Committee.

The Board considers that internal controls may help the Company to realise its operating results and objectives, as well as making significant contributions to an effective use of resources. It can also provide reasonable assurance over the reliability and statutory compliance of the Company's financial statements, preventing damage to the public image or other undesirable consequences, and ultimately safeguarding the tangible and intangible assets of the Company. During this stage of business development, the Company's business and internal administration institutions are under an ongoing process of restructuring and adjustment, and in an ever-changing environment, staying alert to any matters having implications on internal controls and detecting and managing such matters in a timely manner are key to the success of the Company's business.

The Company's internal control system is operated through personnel management, segregation of duties, authorisation and limitation of authorities, cross-checking, asset protection, file safe-keeping, budget management, electronic information control, accounting system control and so forth. The Board has been dedicating itself to reviewing the effectiveness of the Group's financial and non-financial control systems, which include operation and compliance controls, risk management and the Group's internal control procedures. Review work includes an evaluation of internal controls by the Company's audit department, and the submission of reports by the external auditors regarding issues discovered in statutory auditing work.

During the Year, the Board has thoroughly reviewed the effectiveness of the Company's internal control system for the year ended 31 December 2006 through the Audit Committee and its subordinate audit department, with reference to the five crucial elements of internal control: the control environment, risk assessment, control activities, information and communication, and supervision. Based on the reviews in previous years and an assessment of the internal control system for the Year, the Board is of the view that during the Year and as at the date of this annual report, the Company has continuously maintained a comprehensive internal control system covering the areas of corporate governance, operation, construction, finance, administration and personnel management, and that such an internal control system is effective.

## Basic Evaluation of the Internal Control System, 2006



Given the limitations inherent to any internal control system, the Company's internal control system has been established for the purpose of managing potential risks. It is impossible for the system to eliminate all risks. Thus the system can only offer a reasonable, rather than absolute, assurance for the achievement of the Company's operating objectives. Accordingly, it is impossible for the system to eliminate all false representations or losses.

## Internal Audit

The Company's internal audit department has been established since August 2000 for the purpose of reviewing the effectiveness of the Company's operating management activities and the internal control system in a more effective manner, and for the purpose of assuring the Company's transparency as well as its compliance with the regulations when disclosing information to the public. Depending on the materiality and the potential risks existing in the internal control systems of various businesses and processes of the Company, the internal audit department carries out inspection, monitoring and evaluation of the Company's financial information disclosures and internal control activities on a regular or as-needed basis. It furnishes independent and objective evaluations and recommendations in the form of an audit report. Internal audit staff are authorised to access any information relating to the Company and to make enquiries to staff concerned, and the audit manager will directly report to the Audit Committee on the findings and views, on the basis of which the Audit Committee will make recommendations to the management and submit regular reports to the Board.

In 2006, the audit department has reviewed the Company's domestic and foreign annual and interim reports, as well as the domestic quarterly reports; examined the preliminary drafts of such reports in terms of compliance with statutory disclosure rules, thoroughness and accuracy of disclosed items; and submitted internal audit reports and improvement proposals to the Audit Committee.

Moreover, the audit department conducts specific audits each year on the basis of risk assessment. In the past three years, the specific audits conducted by the audit department covered key business aspects including operation, construction, investment, corporate governance and financial management, providing continuous monitoring and evaluation of the Company's internal control system and management efficiency:

Year	Contents of the Specific Audit				
	Operation	Construction	Investment	Corporate	Financial
2004		1	1		
2005	1		2	1	1
2006	1	1 (in progress)	1		2

The four specific audits completed by the audit department in 2006 include: the specific audit on the operations centre's reform results, the specific audit on the Wuhuang project, the specific audit on capital management and the specific audit on toll highway tariff income. The respective audit reports were submitted to the Audit Committee for consideration and the major contents of such reports were furnished to the Board in the form of committee meeting memoranda. By the end of the Year, the audit department had also compiled a summary of audit proposals and a report on the follow-up of such proposals for review by the Board.

## Auditors

The financial statements contained in the Company's 2006 annual report were prepared in accordance with the PRC accounting standards and HKFRS respectively, and have been audited by PricewaterhouseCoopers Zhong Tian CPAs Co., Ltd. ("PwC Zhong Tian") and PricewaterhouseCoopers (Certified Public Accountants, Hong Kong) ("PwC"), respectively.

The Audit Committee is responsible for reviewing the appointment, resignation or replacement of independent auditors, as well as assessing the quality of the auditors' services and whether their audit fees are reasonable and making recommendations to the Board in this regard. The appointment and replacement of auditors as well as the audit fees are proposed by the Board to the general meetings for approval.

PwC as the Company's international auditors has been providing audit services to the Company for 11 consecutive years since 1996. Its partners in charge of the Company's audit were changed in 2003. PwC Zhong Tian was appointed as statutory auditors since 2004, and it has been providing audit services to the Company for three consecutive years.

The remuneration of the auditors in the year 2006 is set out as follows:

(RMB'000)	2006		2005	
	Audit fees <sup>Note 1</sup>	Other fees <sup>Note 1</sup>	Audit fees <sup>Note 1</sup>	Other fees <sup>Note 1</sup>
PwC	1,650	—	1,650	1,265
PwC Zhong Tian	1,800 <sup>Note 2</sup>	—	800	—

As other fees are all about specific audit fees and evaluation service fees for due diligence reviews on the Company's investment projects provided by the auditors, the Board believes that this would not affect the independence of the auditors. However, from the perspective of improving governance quality, the Audit Committee has clarified its principles on the issue. The Company has ceased appointing the Company's auditors to conduct other non-audit services.

*Note 1:* Audit fees are fees paid by a listed company for appointing auditors to conduct audit, verification and review services for financial reports or other matters in accordance with the requirements of laws, administrative rules and regulatory documents; other fees represent fees, other than those mentioned above, paid by a listed company for asset evaluation or appointing auditors for consultation services, and so forth. The "Other fees" mentioned in the table above are specific audit fees and evaluation service fees for due diligence reviews on the Company's proposed investments provided by the auditors. The Company was not required to pay for travel expenses of the auditors incurred for providing audit and review services, but should pay for travel expenses incurred for providing specific audit and evaluation services for due diligence reviews.

*Note 2:* Apart from the fees for the annual audit, the 2006 audit fees for PwC Zhong Tian include RMB1 million of fees for the statutory engagement of PwC Zhong Tian for specific services in relation to the Company's proposed issuance of Bonds With Warrants.

The Audit Committee has discussed and assessed the professional qualities of PwC ZhongTian and PwC, the execution of audit work for 2006 and the proposed fees for 2007, and has offered opinions and improvement suggestions accordingly. The Audit Committee proposed renewing the appointments of PwC Zhong Tian as the Company's statutory auditors and PwC as the Company's international auditors. The proposal was approved by the Board and would be submitted to the 2006 annual general meeting for shareholders' approval and authorisation.

### E. SHAREHOLDERS AND OTHER STAKEHOLDERS

The Company strives to ensure that all shareholders, especially the minority shareholders, are able to fully exercise their rights on an equal basis.

#### General Meetings

The general meeting is vested with the supreme authority of the Company, where duties and powers are exercised in accordance with the law to make decisions on significant matters of the Company. The annual or extraordinary general meeting provides a channel of direct communication between the Board and the shareholders of the Company. The Company puts high regard to the general meeting. The notice on the convening of a general meeting is issued 45 days prior to the date of the meeting. All shareholders are encouraged to attend the general meeting, and all the Directors and members of the senior management are requested to make their best effort to attend. At the annual general meeting ("AGM"), all shareholders have an opportunity to raise questions to the Directors regarding issues about the Group's operation and results. The Chairman of the Company attended the AGM held in June 2006, and arranged the Chairman of the Audit Committee and the representing committee members appointed by the Chairmen of the Remuneration Committee and the Nomination Committee to attend the AGM to answer shareholders' questions. Details of the general meetings held during the Reporting Period are set out on pages 69 to 70 of this annual report.



## Substantial Shareholders

XTC Company and SGH Company are substantial shareholders of the Company. The Company and the substantial shareholders are independent from each other in terms of staffing, assets, finance, institution and business. As substantial shareholders of the Company, XTC Company and SGH Company conducted their activities in a regulated manner. They have never been involved in any acts of by-passing the general meetings in ultra vires interference, whether direct or indirect, with the Company's decision-making or operations.

Information about other shareholders as at the end of the Reporting Period, including shareholder categories, public float and shareholding details of the top ten holders of circulating shares, are set out on pages 74 to 75 of this annual report.

## Investor Relations and Communication

The Company regards effective communication as the core of investor relations, aimed at achieving a win-win situation for both the Company and its investors.

It is the Company's belief that good investor relations are underpinned by adequate disclosure of information. The Company fulfills its obligation of making statutory disclosures of information promptly and accurately and in strict compliance with relevant laws and the Listing Rules. On this basis, the Company takes the initiative in disclosing other relevant information about which investors are concerned, to enhance their understanding of the Company's business and development trends so that they have more confidence in their investment in the Company. Fair treatment towards all shareholders is the Company's primary principle in order to excel in investor relations. Accordingly, various means should be adopted to strengthen communication and two-way exchange with investors, so as to facilitate timely access to, and accurate understanding of, the Company's information by different types of investors, in particular public investors. A corporate culture based on respect and accountability towards investors should also be initiated and developed within the Company.



The Rules Governing Information Disclosure<sup>(1)</sup> and the Rules Governing Information Management of the Company have been formulated to ensure that information disclosures are open, fair and impartial. In addition, the Company has set up the corporate website <http://www.sz-expressway.com> to provide shareholders and the public with a wide range of information of investors' interest such as details of the Company's assets, traffic flow data, information disclosure, corporate governance, and so forth.

In 2006, interim and annual results announcements were made promptly pursuant to relevant regulations, and some 40 announcements and 4 circulars were released to shareholders, providing, in an objective way, statutory information on matters which might have an impact on investors' interests. The standards for making information disclosures are being continuously raised as well. Moreover, the Company continued to update investors on its latest moves and development prospects through various activities such as regular dispatches of press releases and investor newsletters in connection with the Company's operations and development, regular meetings with investors and analysts, prompt responses to investors' inquiries, participation in investor forums, results presentations, news briefings, telephone conferences, local and overseas roadshows and Online Investors Reception Days. During the Year, the Company received 92 investor visits involving about 210 visitors, and continuously held or participated in various presentation activities, of which details are as follows:

- |          |                                                                                                                                                                                                                                                                                                                      |
|----------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| January  | <ul style="list-style-type: none"> <li>Organised roadshows in Beijing, Shanghai, Hong Kong, and so forth.</li> </ul>                                                                                                                                                                                                 |
| February | <ul style="list-style-type: none"> <li>Participated in the transportation industry conference organised by BNP Paribas Peregrine in Shenzhen</li> </ul>                                                                                                                                                              |
| April    | <ul style="list-style-type: none"> <li>Held annual results presentations and press conferences in Hong Kong and Shenzhen</li> <li>Participated in the "China Conference" organised by JP Morgan Chase in Beijing</li> <li>Organised roadshows in Beijing</li> <li>Held Online Reception Day<sup>(1)</sup></li> </ul> |
| May      | <ul style="list-style-type: none"> <li>Participated in the "Chinese Investors Forum" organised by Credit Lyonnais Securities in Shanghai</li> </ul>                                                                                                                                                                  |

- |           |                                                                                                                                                                                                                                               |
|-----------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| June      | <ul style="list-style-type: none"> <li>Participated in the "Corporate Day" organised by BNP Paribas Peregrine in Hong Kong</li> </ul>                                                                                                         |
| July      | <ul style="list-style-type: none"> <li>Participated in the "Investment Forum" organised by United Securities in Guangzhou</li> <li>Participated in the "Transport Sector Day" organised by Credit Lyonnais Securities in Hong Kong</li> </ul> |
| August    | <ul style="list-style-type: none"> <li>Held interim results presentations and press conferences in Hong Kong and Shenzhen</li> </ul>                                                                                                          |
| September | <ul style="list-style-type: none"> <li>Participated in the "Investment Forum" organised by Ping An Securities in Shenzhen</li> <li>Organised roadshows in Hong Kong</li> </ul>                                                                |
| October   | <ul style="list-style-type: none"> <li>Participated in the "Greater China Conference" organised by Citigroup in Macau</li> <li>Organised reverse roadshows</li> <li>Held Online Reception Day<sup>(1)</sup></li> </ul>                        |
| November  | <ul style="list-style-type: none"> <li>Organised media relations activities</li> </ul>                                                                                                                                                        |

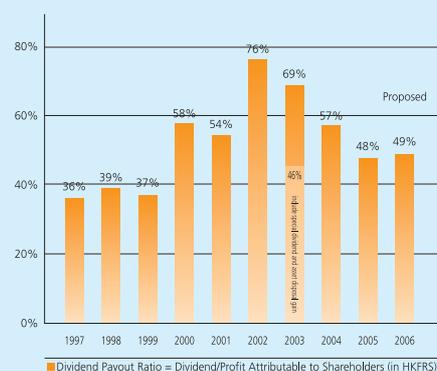
Through the participation in the above activities, the Company was able to convey its message to investors, to collect information from them and to sincerely listen to their feedback, thereby creating a constructive interaction between investors and the Company for mutual benefits.

### Shareholder Return

The Company has consistently maintained a high return for its shareholders ever since its flotation, underpinned by the payment of cash dividends for nine consecutive years with an aggregate dividend payment of approximately RMB1.9 billion.

A substantial increase in capital expenditures has been incurred to the Company due to increased investments and acquisitions of quality projects in recent years for the purpose of achieving the Company's development objectives and a higher-than-average return for its shareholders as its ultimate goal. However, the Board will still maintain a consistent dividend payout policy in the years ahead in the long-term interest of the Company's investors and for their benefit of current gains. In 2006, the Board recommended the payment of a cash dividend of RMB0.13 per share, representing 51% of the net profit in the PRC statutory financial statements or 49% of adjusted profit attributable to shareholders under the HKFRS for the Year.

**Historical Dividend Payout Ratio**



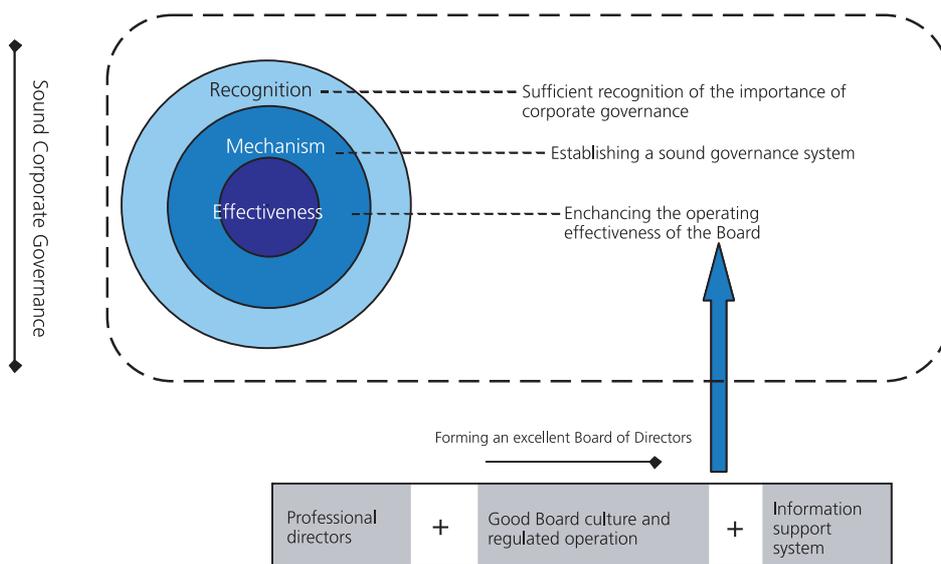
## Other Stakeholders

While dedicated to seeking satisfactory rewards for shareholders, the Company is also committed to its customers, in terms of provision of quality services, and to its employees, by making available opportunities for career development. With strong commitment to shareholders, investors, staff, customers, suppliers and the community at large and always acting with integrity and in good faith, the Company pledges to contribute to the society while pursuing profit growth: by managing and growing its business within the bounds of the law and environmental regulations, improving its standard of corporate governance and actively participating in social charities and environmental protection. It is our belief that the sustainable development of a company cannot be achieved in isolation from a healthy social environment. Noble corporate conduct is also instrumental for enhancing a company's competitiveness, and it is our duty and obligation to help improve the society and the environment on which our very existence depends.

As for our employees, apart from procuring social medical insurance under statutory requirements, the Company also voluntarily procured commercial insurance on personal accidents for our frontline employees. On this basis, the Company initiated the "Employee Mutual Aid Fund for Severe Illnesses and Personal Accidents" (the "Mutual Aid Fund") in 2002, with funds raised through voluntary employee contribution, donations from invested enterprises and the Company's donations and sponsorships, to further enhance our employees' ability to weather the risks of illnesses and injuries. In recent years, the Mutual Aid Fund has raised RMB1.87 million in aggregate, with a total of RMB530,000 distributed and 27 employees being direct beneficiaries, thus eliminating worries among our employees.

## F. CONCLUSION

The Company completed the drafting and editing of "Rules for Corporate Governance" in 2001, with amendments and improvements made continuously with reference to the relevant regulations issued by domestic and foreign regulatory bodies from time to time and the Company's actual situation. According to the requirements set out by "Notice on Convening General Meetings for Amendments to the Articles of Association" (「關於召開股東大會修改公司章程有關問題的通知」) issued by the SSE in March 2006, the Company amended certain provisions on the Articles with reference to its own actual situation and such amendments were approved by shareholders at the annual general meeting held in June 2006. For details of the amendments to the Articles, please refer to the announcement published in designated domestic and foreign newspapers and the circular to shareholders posted on the stock exchanges and the Company's websites dated 28 April 2006.



Sound corporate governance contributes to the healthy development of a company and enhances investors' confidence in the company, and the effectiveness of the Board is the core of sound corporate governance. Accordingly, in the next two years, the current session of the Board will continue to dedicate itself to advancing the efficiency and quality of decision-making and will start working on the development of a formal system of Board performance evaluation system. Meanwhile, the Board puts an emphasis on enhancing the professional qualities of the Directors and on nurturing an active and sound Board culture, so as to elevate the overall quality and performance of the Board, ensuring a stable development of the Company as well as raising shareholder value.