MTR

ANNUAL REPORT 2010

GROWTH MOMENTUM

GROWTH MOMENTUM

In 2010, the Company has ridden the economic recovery to post a strong set of results, with increases in revenue and profit. Looking ahead, our growth momentum continues, with our five major expansion projects in Hong Kong on track, and further progress in our growing portfolio of businesses in the Mainland of China and overseas.

As a builder and operator of infrastructure assets, we try to ensure that our expansion plans benefit present and future generations, and our aim is to become a global leader in sustainable transportation.


22
Hong Kong Passenger Services
36
Station Commercial and Rail Related Businesses
42
Property and Other Businesses
54
Hong Kong Network Expansion
60
Mainland and Overseas Growth
66
Human Resources

CONTENTS

MTR Corporation in Numbers – 2010

CONSOLIDATED FINANCIALS

Total Revenue
HK$29.5 billion

Underlying Profit
HK$8.66 billion

Total Assets
HK$181.7billion

Net Debt-to-Equity Ratio
12.8%

HONG KONG PASSENGER SERVICES

Share of Franchised Public Transport Market
44.3%

Domestic Service Fare Revenue Per Passenger
HK$6.67

Passenger Journeys on Time
99.9%

Total Route Length
218 km

Total Patronage
1,608 million

HONG KONG NETWORK EXPANSION

5 New Rail Projects are progressing well, which will add **56 km** to our network in Hong Kong

PROPERTY AND OTHER BUSINESSES

Investment Property Portfolio in Hong Kong Includes

12 Shopping Centres

18 Floors of Two ifc

Property Development Profit

HK$4.03 billion

STATION COMMERCIAL AND RAIL RELATED BUSINESSES

Station Commercial and Rail Related Revenue

12.6%

of Total Revenue

MAINLAND AND OVERSEAS GROWTH

850 million

Passengers Carried by Our Rail Operations in

5 Cities

Outside of Hong Kong

HUMAN RESOURCES

20,501

Staff Worldwide

Hong Kong Operating Network with Future Extensions

Properties Owned / Developed / Managed by the Corporation

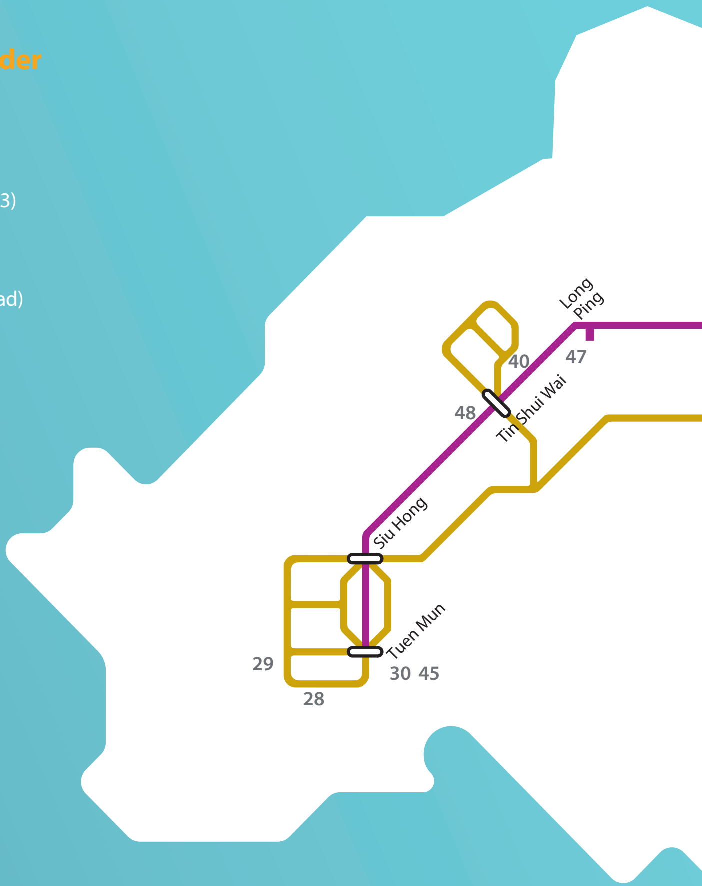
01 Telford Gardens / Telford Plaza I and II
02 World-wide House
03 Admiralty Centre
04 Argyle Centre
05 Luk Yeung Sun Chuen / Luk Yeung Galleria
06 New Kwai Fong Gardens
07 Sun Kwai Hing Gardens
08 Fairmont House
09 Kornhill / Kornhill Gardens
10 Fortress Metro Towers
11 Hongway Garden / Vicwood Plaza
12 Perfect Mount Gardens
13 New Jade Garden
14 Southorn Garden
15 Heng Fa Chuen / Heng Fa Villa / Paradise Mall
16 Park Towers
17 Felicity Garden
18 Tierra Verde / Maritime Square
19 Tung Chung Crescent / Citygate / Novotel Citygate / Seaview Crescent / Coastal Skyline / Caribbean Coast
20 Central Park / Island Harbourview / Park Avenue / Harbour Green / Bank of China Centre / HSBC Centre / Olympian City One / Olympian City Two
21 The Waterfront / Sorrento / The Harbourside / The Arch / Elements / The Cullinan / The Harbourview Place / W Hong Kong / International Commerce Centre
22 One International Finance Centre / Two International Finance Centre / IFC Mall / Four Seasons Hotel / Four Seasons Place
23 Central Heights / The Grandiose / The Edge
24 Residence Oasis / The Lane
25 No.8 Clear Water Bay Road / Choi Hung Park & Ride
26 Metro Town
27 Royal Ascot / Plaza Ascot
28 Pierhead Garden / Ocean Walk
29 Sun Tuen Mun Centre / Sun Tuen Mun Shopping Centre
30 Hanford Garden / Hanford Plaza
31 Citylink Plaza
32 MTR Hung Hom Building / Hung Hom Station Carpark
33 Trackside Villas
34 The Capitol / Le Prestige
35 The Palazzo
36 Lake Silver
37 Festival City (Phases 1 & 2)

Property Developments under Construction / Planning

23 Tseung Kwan O Station Area 56
34 LOHAS Park Package 2-10
37 Tai Wai Maintenance Centre (Phase 3)
38 Che Kung Temple Station
39 Tai Wai Station
40 Tin Shui Wai Light Rail (Tin Wing Road)
41 Austin Station Site C
42 Austin Station Site D

West Rail Line Property Development (As Government Agent)

43 Nam Cheong Station
44 Yuen Long Station
45 Tuen Mun Station
46 Tsuen Wan West Station
47 Long Ping Station
48 Tin Shui Wai Station
49 Kam Sheung Road Station
50 Pat Heung Maintenance Centre
51 Kwai Fong Site



Legend

- Station
- Interchange Station
- Proposed Station
- Proposed Interchange Station
- Shenzhen Metro Network
- * Racing days only

Projects in Progress

- Guangzhou-Shenzhen-Hong Kong Express Rail Link
- West Island Line

Extensions under Study

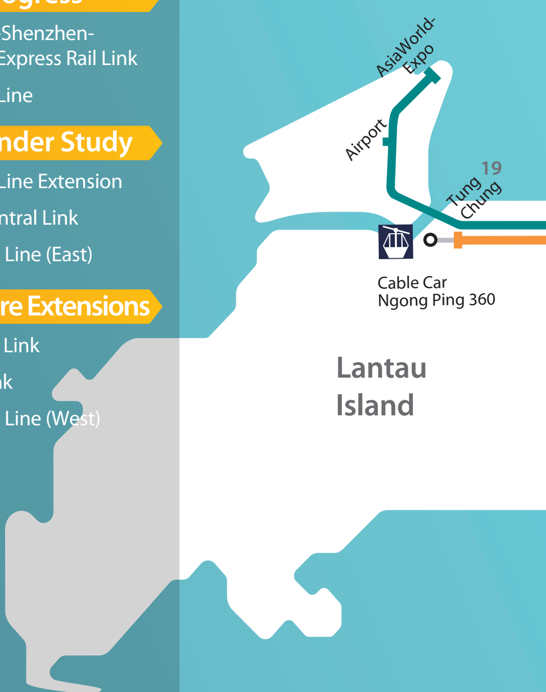
- Kwun Tong Line Extension
- Shatin to Central Link
- South Island Line (East)

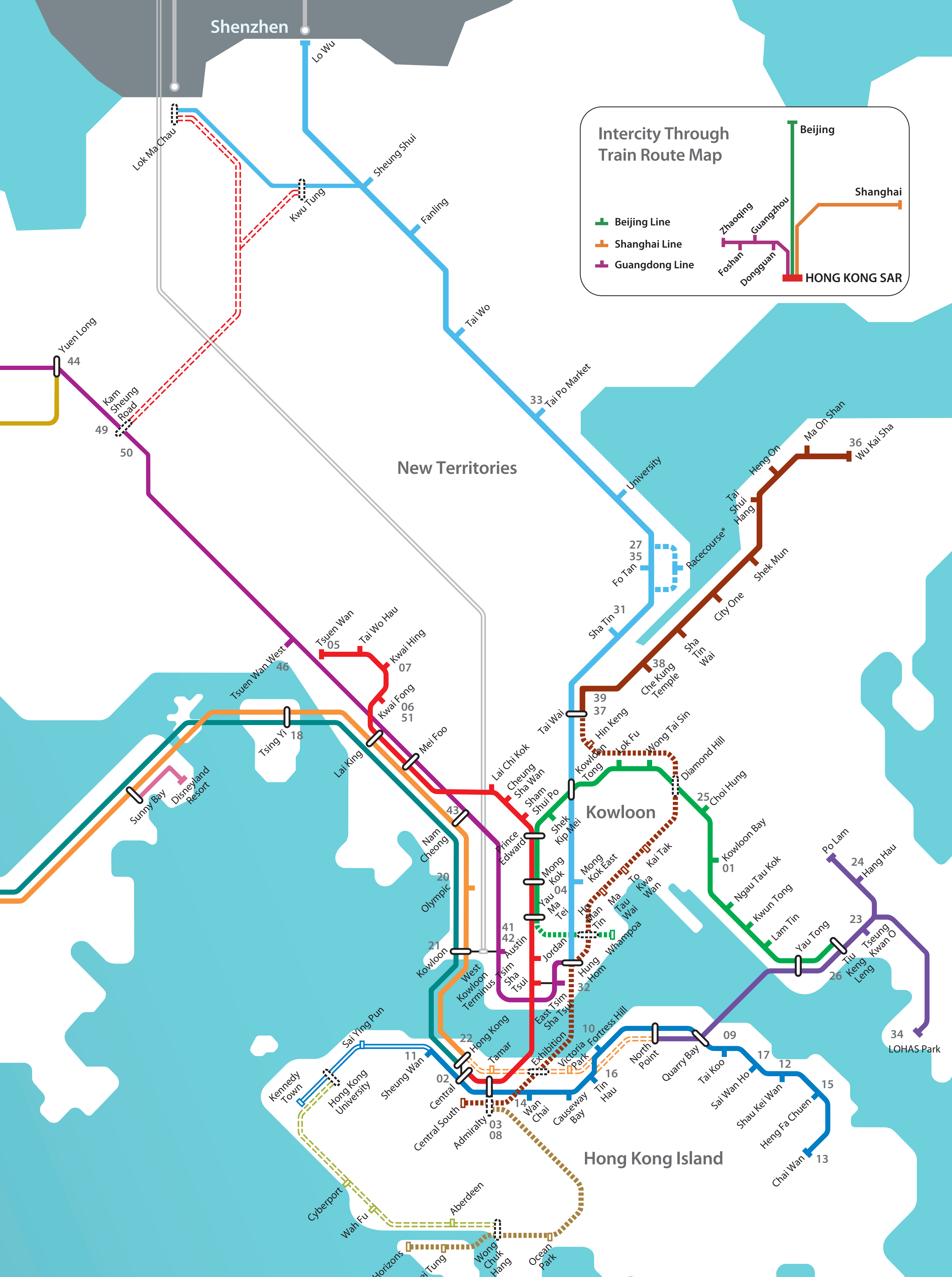
Existing Network

- Airport Express
- Disneyland Resort Line
- East Rail Line
- Island Line
- Kwun Tong Line
- Light Rail
- Ma On Shan Line
- Tseung Kwan O Line
- Tsuen Wan Line
- Tung Chung Line
- West Rail Line

Potential Future Extensions

- North Island Link
- Northern Link
- South Island Line (West)





Shenzhen
Lo Wu
Lok Ma Chau
Sheung Shui
Kwu Tung
Fanling
Tai Wo
33 Tai Po Market
University
New Territories
Intercity Through Train Route Map
Beijing
Shanghai
Beijing Line
Shanghai Line
Guangdong Line
Zhaoqing
Guangzhou
Foshan
Dongguan
HONG KONG SAR
Yuen Long
44
Kam Sheung Road
49
50
Ma On Shan
36 Wu Kai Sha
Heng On
Tai Shui Hang
Racecourse*
27
35
Fo Tan
Shek Mun
City One
Sha Tin Wai
Sha Tin 31
38 Che Kung Temple
Tsuen Wan 05
Tai Wo Hau
Kwai Hing 07
Kwai Fong 06 51
Tsuen Wan West 46
Mei Foo
Lai King
Tsing Yi 18
Sunny Bay
Disneyland Resort
Tai Wai
39
37
Hin Keng
Kowloon Tong
Lok Fu
Wong Tai Sin
Diamond Hill
25 Choi Hung
Kowloon Bay 01
Ngau Tau Kok
Kwun Tong
Lam Tin
Yau Tong
Lai Chi Kok
Cheung Sha Wan
Sham Shui Po
Shek Kip Mei
Prince Edward
Mong Kok
Mong Kok East
Kowloon
Kai Tak
To Kwa Wan
Ma Tau Wai
Ho Man Tin
Whampoa
Hung Hom 32
Yau Ma Tei 04
Jordan
Tsim Sha Tsui
East Tsim Sha Tsui
Austin 41 42
West Kowloon Terminus
Nam Cheong
43
Olympic 20
Kowloon 21
Po Lam
24 Hang Hau
23 Tseung Kwan O
Tiu Keng Leng 26
34 LOHAS Park
Sai Ying Pun
Kennedy Town
Hong Kong University
Sheung Wan 11
Hong Kong 22
Tamar
Central 02
Central South
Admiralty 03 08
Wan Chai 14
Exhibition
Causeway Bay
Victoria Park
10 Fortress Hill
Tin Hau 16
North Point
Quarry Bay
Tai Koo 09
Sai Wan Ho 17
Shau Kei Wan 12
Heng Fa Chuen 15
Chai Wan 13
Hong Kong Island
Cyberport
Wah Fu
Aberdeen
South Horizons
Lei Tung
Wong Chuk Hang
Ocean Park

MTR Corporation at a Glance

The Company is regarded as one of the world's leading railway operators, with proven success in our integrated approach of rail and property. Since opening our first railway line in Hong Kong over 30 years ago, our activities have increased in size, scale, geographic coverage and diversity. Our strategy for future growth is firmly on track. We are actively engaged in a significant expansion of our network in Hong Kong, while building a growing portfolio of businesses in the Mainland of China and overseas.

Hong Kong Passenger Services

Business Description

We operate a predominantly rail based transportation system in Hong Kong, comprising Domestic and Cross-boundary services, a dedicated high-speed Airport Express railway and a light rail system. The entire system stretches 218.2 km and has 84 stations and 68 stops. Our network is one of the most intensively used in the world, and its reliability, safety and efficiency are held in high regard. We also provide intercity services to the Mainland of China as well as a small bus operation in Hong Kong offering convenient feeder services.

2010 Highlights

- Modifications to trains and stations enhanced accessibility further
- The high standards attained by our service performance again earned a large number of awards
- Construction has made good progress on the West Island Line and Express Rail Link projects
- The detailed design for the South Island Line (East) and Kwun Tong Line Extension projects has been substantially completed
- The preliminary designs for the E&M systems for the Shatin to Central Link have been completed

Station Commercial and Rail Related Businesses

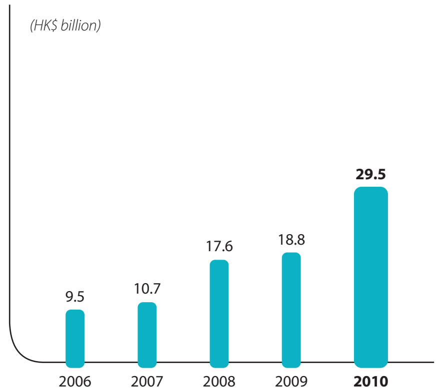
Business Description

We leverage our railway assets and expertise into additional businesses, including rental of station retail space, advertising in trains and stations, telecommunications, and rail consultancy.

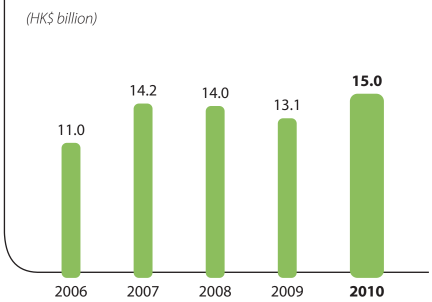
2010 Highlights

- 38 new trades and brands were added to our Hong Kong network giving passengers more choices
- Platform TVs were enlarged to 103 inches giving better impact
- 3G data usage by passengers saw strong growth

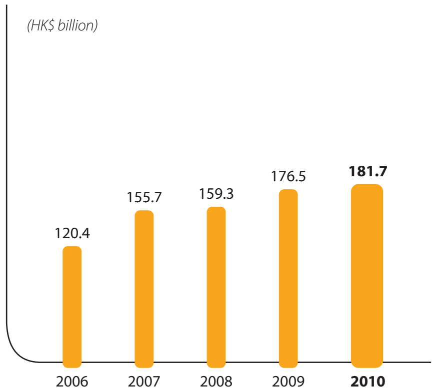
Turnover



Operating Profit before Depreciation, Amortisation and Variable Annual Payment Arising from the Rail Merger



Total Assets



Property and Other Businesses

Business Description

We develop mainly residential properties in conjunction with property developers. We own investment properties, principally shopping malls and offices, and manage our properties and those of others. Our investment portfolio primarily includes 12 shopping malls in Hong Kong, one shopping mall in Beijing and 18 floors of the Two International Finance Centre (Two ifc) office tower in Hong Kong.

2010 Highlights

- Pre-sales for Phase 1 of Festival City at Tai Wai Maintenance Centre in March saw a good market response, and pre-sales of Phase 2 were launched in November
- Austin Station Sites C and D were awarded in March to Fast New Limited, a consortium formed by New World Development Company Limited and Wheelock Properties Limited
- Our shopping malls and our 18 floors of Two ifc in Hong Kong were close to 100% let

Mainland and Overseas Growth

Business Description

We continue our strategy to grow outside of Hong Kong by investing in urban rail networks in the Mainland of China, and pursuing "asset-light" operating concessions in overseas markets.

2010 Highlights

- Beijing Metro Line 4 (BJL4) celebrated its first anniversary on 28 September, achieving high levels of service and ridership in its first year
- Daxing Line, an extension to BJL4, commenced operations on 30 December
- In July, we took over operation of Phase 1 of Shenzhen Metro Line 4
- Service performance has shown encouraging improvement at our rail concessions in London and Stockholm whilst, after a difficult period, operational performance is improving in Melbourne

Chairman's Letter

"...a successful rail line must nurture local communities and consider local aspirations during design, construction and in operation."

Dear Shareholders and other Stakeholders,

I am pleased to report that MTR Corporation achieved a strong set of results for the year ended 31 December 2010 by leveraging off the recovery in the Hong Kong economy. Our recurrent businesses in Hong Kong experienced good patronage growth, augmented by gains at our station retail and property rental businesses, as well as a pick-up in our advertising business. We recorded strong property development profits, relating mainly to Le Prestige at LOHAS Park. The year 2010 also saw the first full year results of a number of our rail businesses outside of Hong Kong, as well as the introduction of Phase 1 of Shenzhen Metro Line 4 (SZL4). The financial results of these rail businesses outside of Hong Kong were either in line with or better than expectation in their initial year of operations, except for our Stockholm franchise.

For the year, revenue rose by 57.0% to HK$29,518 million, on the back of strong Hong Kong recurrent businesses as well as the full year revenue contribution from rail franchises outside of Hong Kong. Operating profit from railway and related businesses before depreciation, amortisation and variable annual payment increased by 14.7% to HK$10,917 million and property development profit for the year was 13.5% higher at HK$4,034 million. Excluding investment properties revaluation and the related deferred tax, net profit from underlying businesses attributable to equity shareholders increased by 18.5% to HK$8,657 million. Including pre-tax gain in revaluation of investment properties of HK$4,074 million, the net profit attributable to equity shareholders was HK$12,059 million and earnings per share were HK$2.10. Your Board has proposed a final dividend of HK$0.45 per share, giving a full year dividend of HK$0.59 per share, which is an increase of 13.5% compared to the previous year.

Growth Strategy

Our growth strategy of expanding our rail network in Hong Kong and participating in rail businesses outside of Hong Kong remains on track.

In Hong Kong, we have five railway projects at various stages of development which, when completed, will increase our route network by 56-km. Construction of the West Island Line and the Hong Kong section of the Guangzhou-Shenzhen-Hong Kong Express Rail Link is progressing well. We have also steadily advanced the South Island Line (East), Kwun Tong Line Extension and Shatin to Central Link projects through work on their detailed design, planning and approval processes.

In the Mainland of China, the Daxing Line extension of Beijing Metro Line 4 commenced operations on 30 December 2010. Our wholly owned subsidiary MTR Corporation (Shenzhen) Limited took over Phase 1 of SZL4 in July 2010, with Phase 2 nearing completion and services expected to commence in mid 2011. The Company signed a Memorandum of Understanding with Shenzhen Line 3 Investment Company to participate in the feasibility, land and planning study, and the investment study for Shenzhen Metro Line 6. The project for the investment in, construction and operation of the Hangzhou Metro Line 1, in which we plan to hold a 49% shareholding, is awaiting regulatory approval from the Central Government.

Sustainability and Corporate Responsibility

The Company aims to be a globally recognised leader in meeting the transportation needs of present and future generations, connecting and growing communities with caring service. We see a railway system not merely as a physical infrastructure, but an asset with social, environmental and economic implications. Properly designed and integrated with property development, a railway enables more effective utilisation of land, contributing towards sustainable urban development and benefiting the environment.

As such, a successful rail line must nurture local communities and consider local aspirations during design, construction and in operation. We have developed ongoing relationships with local communities to maximise the benefit of our long-term infrastructure, drawing on stakeholder views throughout

> "...we will continue to pursue our strategy to achieve sustainable growth, while carefully managing risk through the application of sound principles of corporate governance."

the planning, design and construction stages. We also use a Sustainable Competitive Advantage model, which combines and balances risk management, operator requirements and stakeholder views and aspirations, thus embedding sustainability into management decisions.

Our concern to bring sustainability into the heart of our business has led us to the publication since 2000 of our Sustainability Report, using a well respected framework which follows the Global Reporting Initiative.

We continue to make progress in reducing energy consumption, to address our responsibilities in relation to the local environment and global warming. While constrained by the relatively carbon intensive power generation in Hong Kong, continuous improvements in operational efficiency have supported a downward trend in power usage from 5.94 kWh per revenue car-km in 2005 to 4.83 kWh in 2010. In February 2010, we launched a programme to install LED lighting in 136 trains. Once installation is completed in 2014, starting from 2015, these changes will result in a measurable reduction of 2,519 MWh each year in electric power consumption. This is one of many energy saving initiatives during the year targeting rolling stock, tunnels and stations.

We also apply the same approach of sustainable development to our network expansion projects. In addition to community engagement on the planning and design, we make every effort to achieve high quality, safety and environmental standards during construction, through award schemes and other incentives. On the West Island Line, new technology using electronic detonators with water ballast rather than sand bags to absorb the pressure from blasting has enabled us to excavate the construction shaft at the King George V Memorial Park at Sai Ying Pun with barely noticeable levels of noise and dust.

Community Care

A key objective of our Corporate Responsibility Policy is to enhance the quality of life and actively engage in the communities where we operate. These efforts fall under our Community Care Action programme, which targets four broad categories, namely Youth, Community Outreach, Art & Culture and Green & Healthy Living.

Our recent initiative "'Friend' for life's journeys", targets secondary school students. It aims to broaden their horizons and equip them with useful life skills through a variety of activities. Launched in December 2009 and continuing into 2011, the programme initially paired 100 secondary school students with 100 young staff volunteers to act as mentors, sharing insights and bringing the students a new perspective. The other youth initiative is "'Train' for life's journeys", which provided 100 Form Five students with personal development and hands-on experience of working in our operations.

More broadly, our "More Time Reaching Community" scheme encouraged 198 volunteering community service projects during 2010 involving about 4,400 volunteers. Furthermore, in May 2010, in support of the Employee Volunteer Week organised by Community Business, our staff volunteers organised seven projects for the elderly, chronically ill, underprivileged families and mentally challenged people across Hong Kong.

We maintained our support for local art and culture through the "art in mtr" programme, including a 90 metre long corridor in Tsuen Wan Station featuring 132 works of mosaic art called "Urban Flow".

Finally, during the year the Company took part in a number of events relating to the environment and health. The sixth MTR HONG KONG Race Walking, held in Central in April 2010, raised over HK$1.13 million for the Hospital Authority's Health InfoWorld. We also supported Community Business' Work-Life Balance Day, Earth Hour, organised by the World Wide Fund for Nature, and World Car Free Day.

Conclusion

Although we have seen a global recovery from the recent financial crisis, it remains fragile. In this environment, we will continue to pursue our strategy to achieve sustainable growth, while carefully managing risk through the application of sound principles of corporate governance. I wish to thank my fellow directors, our staff and all our stakeholders for their support as we journey forward. I would also like to welcome Mr Alasdair George Morrison, who joined the Board in July 2010 as an independent non-executive Director of the Company, and thank Mr Andrew McCusker, who retired in December 2010 as Operations Director. I further welcome Dr Jacob Kam, who became Operations Director on Andrew's retirement.

Dr. Raymond Ch'ien Kuo-fung, *Chairman*
Hong Kong, 3 March 2011

CEO's Review of Operations and Outlook

"...all of our businesses posted solid gains in 2010, taking full advantage of the active economies in Hong Kong and abroad."

Dear Shareholders and other Stakeholders,

I am pleased to report that all of our businesses posted solid gains in 2010, taking full advantage of the active economies in Hong Kong and abroad.

Growth in our recurrent businesses in Hong Kong was strong. Our Hong Kong rail business benefited from good patronage growth and an upward adjustment in fares, in accordance with the Fare Adjustment Mechanism. Higher rental reversions, as well as an increase in retail space positively impacted our property rental and station retail businesses. Our advertising business also saw a strong rebound. In property development, profit booking came mainly from Le Prestige in LOHAS Park.

Our businesses outside of Hong Kong also made good progress. Beijing Metro Line 4 (BJL4) celebrated its first anniversary in September 2010, with ridership exceeding 250 million passenger trips whilst achieving high service levels. The Daxing Line, an extension of BJL4, commenced service on 30 December 2010. In Shenzhen, our wholly owned subsidiary MTR Corporation (Shenzhen) Limited (SZMTR) took over the operations of the five-station 4.5-km Phase 1 of Shenzhen Metro Line 4 (SZL4) in July 2010. Our operations in the UK, Sweden and Australia, also made progress.

In Hong Kong construction is under way on the West Island Line and the Hong Kong section of the Guangzhou-Shenzhen-Hong Kong Express Rail Link (Express Rail Link). The planning, design and approval processes for the South Island Line (East), Kwun Tong Line Extension and Shatin to Central Link projects have all been advanced during the year.

Total revenue in 2010 rose by 57.0% to HK$29,518 million. Operating profit from railway and related businesses before depreciation, amortisation and variable annual payment increased by 14.7% to HK$10,917 million. Excluding our overseas railway subsidiaries, revenue was 9.1% higher and operating profit was 11.9% higher, while operating margin improved by 1.4 percentage points to 54.9%. Property development profit for the year was HK$4,034 million compared to HK$3,554 million in 2009. Excluding investment properties revaluation and the related deferred tax, net profit from underlying businesses attributable to equity shareholders increased by 18.5% to HK$8,657 million, representing earnings per share of HK$1.51. Gain on revaluation of investment properties was HK$4,074 million pre-tax (HK$3,402 million post-tax) as compared with HK$2,798 million pre-tax for 2009. Therefore net profit attributable to equity shareholders increased by 25.1% to HK$12,059 million, equivalent to earnings per share of HK$2.10 after such revaluation. Your Board has recommended a final dividend of HK$0.45 per share, resulting in a total dividend for the year of HK$0.59 per share as compared with HK$0.52 per share in 2009.

Hong Kong Passenger Services

Hong Kong fare revenue, which comprises our rail, light rail and bus services, reached HK$12,459 million in 2010, 8.4% higher than for 2009.

Patronage

Total patronage in Hong Kong increased by 6.8% over the previous year to 1,608.5 million.

Patronage on the Domestic Service rose by 6.6% over 2009 to 1,298.7 million. This growth was due to a combination of the full year effect of the opening of the Kowloon Southern Link and the LOHAS Park Station, both in the second half of 2009, strong tourist arrivals in Hong Kong as well as the economic recovery. Average weekday patronage was 3.8 million, an increase of 6.4% over the previous year.

The Cross-boundary Service at Lo Wu and Lok Ma Chau reported a 6.3% rise in patronage over 2009 to 100.0 million in 2010, due to the economic recovery and an increase in tourists from the Mainland of China.

Passenger traffic on the Airport Express in 2010 increased by 12.9% over 2009 to 11.1 million journeys, boosted by the revival in air travel as the global economy improved as well as the one-off "River of Wisdom – Animated Version of the Riverside Scene at Qingming Festival" exhibition at the AsiaWorld-Expo in November.

Passenger volume on Light Rail, Bus and Intercity services totalled 198.7 million in 2010, an increase of 8.0 % over 2009.

Market Share

The Company's overall share of the franchised public transport market in Hong Kong rose from 42.6% in 2009 to 44.3% in 2010. Within this total, our share of the cross-harbour traffic increased from 64% to 65.3%. Our Cross-boundary business market share was 55.0% in 2010.

CEO's Review of Operations and Outlook

Fare Revenue

Domestic Service fare revenue increased by 8.5% in 2010 to HK$8,668 million, accounting for 69.6% of the total Hong Kong fare revenue of HK$12,459 million. Average fare per passenger on our Domestic Service increased by 1.9% to HK$6.67, mainly due to an adjustment to fares in June 2010 as well as longer passenger trips after the opening of the Kowloon Southern Link, which connected the East Rail Line and West Rail Line.

Fare revenue from the Cross-boundary Service in 2010 was HK$2,487 million, an increase of 6.9% over 2009. Airport Express fare revenue reached HK$694 million in 2010, a rise of 12.5% as compared with 2009. Fare revenue from Light Rail, Bus and Intercity services was HK$610 million in 2010, a rise of 7.4% over 2009.

Service and Performance

As in previous years, we exceeded all our performance standards, including both those stipulated in the Operating Agreement and our own more demanding Customer Service Pledges.

The Company's service performance was widely recognised in Hong Kong, including the Hong Kong Service Awards in the Public Transportation Category presented by East Week magazine and as the category award winner in the Public Transportation Category of the Sing Tao Excellent Services Brand Award 2009 organised by Sing Tao Daily.

To seek continuous service improvement, we continue to upgrade our stations and rolling stock. During 2010, renovations were completed in five stations, with work under way in three more. Installation of automatic platform gates at eight above ground stations on the Island, Kwun Tong and Tsuen Wan lines have commenced. Platform queuing tiles have been installed at ten West Rail Line stations. A new noise enclosure was constructed for the tracks at Wo Liu Hang in Fo Tan in March 2010.

Eight new light rail vehicles were put into operation in 2010. Ten new underground trains are targeted for delivery in 2011. We have also modified train compartments to make them more accessible for the disabled and added more ramps and wide gates at stations.

Station Commercial and Rail Related Businesses

Revenue from our station commercial and rail related businesses rose by 11.6% over 2009 to HK$3,715 million. The increase was mainly due to a strong recovery in the advertising business, good rental reversion and an increase in the rental area of station shops. Project management on behalf of Government in relation to the Express Rail Link also added to revenue and, in similar amount, to expenses.

Station retail revenue in 2010 was HK$1,716 million, an increase of 6.9% as compared with 2009. The rise in revenue reflects the increased rental rates resulting from a refinement of trade mix and an active economy, as well as an increase in the number of shops.

The total number of station shops increased from 1,228 at the end of 2009 to 1,254 at the end of 2010, and the total area of station retail space increased from 52,788 square metres at the end of 2009 to 53,880 square metres.

Advertising revenue in 2010 increased by 22.9% over 2009 to HK$734 million, reflecting an improving economy, and the timely launch of new advertising packages.

Revenue from our telecommunications business in 2010 was 6.2% higher than in 2009 at HK$290 million. The increase was due to incremental income from mobile phone networks at new stations, the strong growth of 3G data transmission as well as rentals from new rooftop sites as mobile phone operators expanded their outdoor network coverage.

Revenue from external consultancy in 2010 was HK$113 million. This decline of 28.9% over 2009 reflects completion of the Airport Authority Hong Kong Automatic People Mover Modification Works project in June 2009.

The small and unprofitable freight business was wound down in June 2010.

Property and Other Businesses

The Hong Kong property market was buoyant throughout most of 2010, due to a combination of low interest rates, the economic recovery and increased purchases by Mainland Chinese buyers.

To increase transparency in the sales process of primary residential units, Government introduced a number of measures, such as more detailed listing of the composition of saleable floor area, and the disclosure of price lists three days in advance of sale, all of which we welcome and support. To promote sustainable development, Government also announced measures which made conditions to obtain additional developable floor area for environmental features more restrictive. We are taking steps to comply with these new requirements while mitigating any potential impact on the Company.

In November, Government introduced special stamp duty on properties sold within two years of purchase, with the aim of discouraging speculative purchases. This action led to a reduction in sales volumes, although prices remained relatively firm. Sales volume in the secondary market saw a recovery starting in early 2011.

Property Development

Profit from property development in 2010 was HK$4,034 million, with the major contribution from Le Prestige at LOHAS Park. The sale of units in inventory at The Palazzo in Fo Tan and Lake Silver in Wu Kai Sha also added to this result.

Pre-sales commenced for Phase 1 and Phase 2 of Festival City at Tai Wai Maintenance Centre in March and November 2010 respectively. By the end of 2010, approximately 47% of the 2,728 units in the two phases had been sold.

Occupation Permits were issued for Le Prestige, Phase 2a of LOHAS Park in January 2010 and Festival City Phase 1 and Phase 2 at Tai Wai Maintenance Centre in February 2010 and November 2010 respectively.

In our property tendering activity, we awarded Austin Station Sites C and D to Fast New Limited, a consortium of New World Development Company Limited and Wheelock Properties Limited, in March 2010. We contributed HK$3.9 billion to this development as part of the land premium payments for the sites.

In the second half of 2010, Government introduced a number of new measures relating to property development as discussed above, which has resulted in some adjustments to our property development plans.

Property Rental, Property Management and Other Businesses

The combined revenue of our property rental, property management and other businesses increased by 9.3% in 2010, as compared with 2009, to HK$3,200 million.

Total property rental income from Hong Kong and the Mainland of China rose by 8.2%, to HK$2,758 million. Our shopping mall portfolio in Hong Kong reported an average rental reversion of 14% for the year. At 31 December 2010, our 12 shopping malls in Hong Kong and the Company's 18 floors at Two International Finance Centre remained close to 100% let. Our shopping malls in Hong Kong continued to receive recognition, winning over ten international and local awards.

In Hong Kong, at the end December 2010, the Company's attributable share of investment properties comprised of 225,650 square metres of lettable floor area of retail properties and 41,090 square metres of lettable floor area of offices.

Property management revenue in 2010 was 1.9% lower, as compared with 2009, at HK$203 million. The number of residential units under our management in Hong Kong rose from 79,449 to 81,962 units.

Ngong Ping 360

The Ngong Ping cable car and associated theme village on Lantau Island saw revenue increase by 38.2% to HK$239 million in 2010, as visitor numbers rose from about 1.4 million in 2009 to 1.7 million in 2010. The improved performance was the result of smooth operations, increased sales of the premium "crystal cabin ride", active promotional programmes and the success of our new travel agency, "360 Holidays" in promoting Lantau as a tourist destination.

Octopus

Octopus continued its expansion in the retail sector by recruiting more small to medium-sized retail merchants and introducing new applications to provide greater convenience to consumers and businesses. By the end of December, there were over 3,000 Octopus service providers in Hong Kong, including those served by Octopus-appointed acquirers. Cards in circulation were 23.1 million and average daily transaction volume and value were 11.5 million and HK$106.6 million respectively. The Company's share of Octopus' net profit for 2010 was HK$126 million, a decrease of 15.4% from 2009 mainly due to one-off expenses incurred by Octopus relating to the data privacy incident.

Mainland of China and Overseas Businesses

The Company's operating railway franchises outside of Hong Kong in 2010 comprised of our 49% interest in Beijing MTR Corporation Limited (BJMTR), which operates the BJL4 and our 100% interest in SZMTR, which operates the SZL4, both in the Mainland of China, our 60% interest in Metro Trains Melbourne

Pty. Ltd. (MTM) in Australia, our 100% interest in MTR Stockholm AB (MTRS) in Sweden, our 50% interest in Tunnelbanan Teknik Stockholm AB (TBT), which maintains rolling stock for MTRS, and our 50% interest in London Overground Rail Operations Limited (LOROL) in the UK.

Revenue from railway subsidiaries outside of Hong Kong, MTM, MTRS and SZMTR, was HK$10,144 million. Operating costs were HK$9,865 million, yielding an operating profit of HK$279 million and an operating profit margin of 2.8%. As operation and maintenance franchises, MTM and MTRS require modest capital investment and hence operating margins will typically be much lower than for more capital intensive projects. SZMTR, which commenced operations on 1 July 2010, made a small operating loss, as expected, in 2010. Although the financial performance for MTM has been encouraging, MTRS has not met expectations financially and measures have been implemented to enhance operating efficiency. BJMTR, LOROL and TBT are accounted for as associates, and contributed a total of HK$22 million in post-tax profit in 2010, better than expectations.

Total passengers carried by our rail subsidiaries and associates outside of Hong Kong was close to 850 million in 2010.

BJL4's total ridership in 2010 exceeded 250 million passenger trips, with a daily average of 750,000 trips. On 1 May 2010, the line reported a record ridership of 1 million passenger trips. Performance in terms of average train service availability and punctuality have exceeded targets. On 30 December 2010, the 22-km Daxing Line extension of BJL4 opened for passenger service. BJMTR has an operation and maintenance contract only for the Daxing Line.

In Shenzhen, SZMTR took over the operations of the five-station 4.5-km Phase 1 SZL4 on 1 July 2010. Performance has been good, with average train service delivery and punctuality both exceeding targets. Work progresses well on the ten-station 16-km Phase 2 of SZL4, which is expected to open in the middle of 2011.

With key personnel changes at major stakeholders in Shenyang, including its municipal Government, our 49% owned Shenyang operation and maintenance joint venture has been presented with serious obstacles and is prevented from delivering on the proposed scope of its contract. We are in discussions with the relevant Shenyang parties to resolve this matter, which will lead to our withdrawal from Shenyang. Our investment relating to the joint venture comprises mainly staff costs employed by or supporting the joint venture company and is written off in the 2010 accounts.

In the UK, the introduction of new trains during the year contributed to further service improvements by LOROL. In May 2010, LOROL started full passenger services on the refurbished and extended East London Line, increasing the overall route length from 85 km to 110 km.

In Stockholm, MTRS has returned satisfactory operational performance since the start of operations in November 2009. Performance in terms of average train service punctuality exceeded target.

In Melbourne, MTM encountered a number of operational issues in the first half of the year. Remedial measures were introduced, resulting in improved performance in the second half of the year. MTM has continued to implement asset reliability and operational initiatives aimed at improving performance.

Future Growth

Growth in Hong Kong

We made good progress during the year on the five major projects now under way to extend the railway network in Hong Kong, namely the West Island Line, South Island Line (East), Kwun Tong Line Extension, Express Rail Link and Shatin to Central Link.

All of the Government financial grants for the 3-km West Island Line have been received and construction work is progressing on schedule. All civil works contracts for this project were awarded by April 2010. The civil infrastructure works for the Kennedy Town Swimming Pool (Phase 1) and the David Trench Rehabilitation Centre were substantially completed by the end of 2010. This project has carefully integrated community aspirations to preserve local heritage and create opportunities for urban renewal.

The Government published the gazette amendment for the 7-km South Island Line (East) railway scheme on 4 June 2010 and the project was authorised by the Executive Council on 30 November 2010. The detailed design for the project has been substantially completed. The proposal to zone the Wong Chuk Hang site, which will be used for the depot, into a Comprehensive Development Area for integrated property development, was agreed by the Town Planning Board in June

2010. Formal approval under the Town Planning Ordinance is expected later in 2011. Financial viability for the South Island Line (East) is expected to be achieved using the "Rail plus Property" model.

The 3-km Kwun Tong Line Extension scheme was authorised by the Executive Council on 30 November 2010. The detailed design has been substantially completed. It is proposed to use property development rights above Ho Man Tin Station to achieve financial viability for this line under the "Rail plus Property" model.

The Hong Kong Government will fund the costs for construction of the 26-km Express Rail Link, but has entrusted the design and construction of the line to the Company and has agreed to invite the Company to operate the service on a concession basis upon completion. The Entrustment Agreement for construction was signed on 26 January 2010. Construction started in January 2010 and is making good progress.

Station designs and construction planning for the 17-km Shatin to Central Link are being progressed in parallel with further consultation with local communities and other stakeholders. The scheme was gazetted on 26 November 2010. On 18 February 2011, the advanced funding for the construction of the Shatin to Central Link's share of Admiralty Station and Ho Man Tin Station was approved by the Finance Committee of Legislative Council. This will facilitate further progress for the South Island Line (East) and Kwun Tong Line Extension in the first half of 2011.

Growth in Mainland of China and Overseas

Construction work on SZL4 Phase 2 has made good progress with rolling stock manufacturing well advanced. Full line operation, encompassing Phase 1 and Phase 2, is expected to commence in the middle of 2011.

The Public-Private-Partnership project for the investment in, construction and operation of the 48-km Hangzhou Metro Line 1, for which we entered into a Concession Agreement in March 2010, is awaiting regulatory approval from the Central Government.

Financial Review

Total turnover of the Group in 2010 increased by 57.0% from 2009 to HK$29,518 million as a result of the strong economic rebound in Hong Kong as well as the full-year operation of the international railway subsidiaries. Hong Kong fare revenue grew by 8.4% to HK$12,459 million while non-fare revenue increased by 10.5% to HK$6,915 million. With the full year of operating results from our subsidiaries in Stockholm and Melbourne as well as six months of results from SZL4 Phase 1, which we took over in mid-2010, revenue of HK$10,144 million was generated from these subsidiaries. Including railway subsidiaries outside of Hong Kong, total operating costs in 2010 increased by 100.4% to HK$18,601 million. Excluding these subsidiaries, operating costs grew by 5.9% compared with a 9.1% increase in revenues. The resulting operating profit before depreciation, amortisation and variable annual payment to KCRC for the service concession increased by 14.7% to HK$10,917 million, with operating profit margin decreasing by 13.6 percentage points to 37.0%. Excluding the railway subsidiaries outside of Hong Kong, operating profit margin would have increased by 1.4 percentage points to 54.9% with operating profit increasing by 11.9% to HK$10,638 million. Property development profits in 2010 were HK$4,034 million, mainly from Le Prestige. The one-month provision of variable annual payment to KCRC in 2010 was HK$45 million. After accounting for depreciation and amortisation of HK$3,120 million, interest and finance charges of HK$1,237 million, investment property revaluation gains of HK$4,074 million, share of profits of non-controlled subsidiaries and associates of HK$139 million and income tax of HK$2,590 million, net profit attributable to equity shareholders of the Company in 2010 increased by 25.1% to HK$12,059 million, or HK$2.10 per share. Excluding investment property revaluation, net profit attributable to shareholders increased by 18.5% to HK$8,657 million, or HK$1.51 per share.

As at 31 December 2010, the Group's net assets increased by 10.2% to HK$117,293 million with a 2.9% increase in total assets and a 8.1% decrease in total liabilities. The increase in assets was mainly due to investment property revaluation gains, construction progress of SZL4 and land premium payment for Austin Station Sites C and D. The receipt of West Island Line Government funding support of HK$12,252 million in 2010 led to the decrease in the amounts due from Government and other related parties while this receipt, together with strong cash flow, increased the investments in securities and cash balance. The reductions in liabilities were mainly attributable to the utilisation of West Island Line Government funding support and repayment of debts from surplus cash. With the share capital, share premium and capital reserves increasing by HK$1,237 million and retained earnings and other reserves increasing by

HK$9,526 million, total equity attributable to shareholders of the Company grew by 10.1% to HK$117,150 million. The net debt-to-equity ratio decreased from 25.8% at 2009 year end to 12.8% at 2010 year end.

During the year, the Group generated net cash inflow from operating activities after tax payments of HK$10,907 million, an increase of 34.5%. Cash receipts from property developments were HK$5,249 million, while other cash receipts amounted to HK$166 million. After netting off total cash outflows of HK$15,711 million, mainly for capital projects, property developments, fixed annual payment as well as interest and dividend payments, net cash inflow of HK$611 million was generated. Including the West Island Line Government funding support of HK$12,252 million, total net cash inflow of the Group in 2010 was HK$12,863 million, of which HK$3,015 million was used to reduce debt while HK$3,624 million was invested in bank medium term notes.

Following our progressive dividend policy, the Board has recommended a final dividend of HK$0.45 per share, which, when added to the interim dividend of HK$0.14 per share, gives a total dividend of HK$0.59 per share for the year, an increase of HK$0.07 per share or 13.5% from last year.

Human Resources

The Company has expanded its businesses rapidly in recent years and now employs some 13,829 people in Hong Kong and 6,672 outside of Hong Kong, including those employed by our subsidiaries.

Proactive recruitment planning, appropriate training and open communication have helped the Company to attract and retain the people we need and have underpinned harmonious staff relations. In Hong Kong, over 1,000 vacancies for operating railway staff were filled and 430 new recruits were hired in the Projects Division during the year. Recruitment for our graduate and apprentice schemes was also increased to support our business expansion. Staff retention continues to be effective through reinforcing career advancement for high calibre staff, competitive employment terms and conditions, and staff consultation programmes and motivational schemes.

We strive to develop our colleagues to ensure that they are fully equipped to meet the challenges and opportunities ahead and align their personal goals with the Company’s goals. We have also put in place effective programmes to groom future leaders for the Company.

Outlook

In spite of some uncertainties, global economic recovery should continue in 2011.

In this environment our rail business should see continued patronage growth whilst any fare adjustment will be implemented in June 2011 in accordance with the Fare Adjustment Mechanism. Our station commercial and property rental businesses will benefit from a more promising market whilst we expect further recovery in our advertising business.

The year 2011 will see the first full year of variable annual payment to KCRC in line with the Rail Merger.

In our railway franchises outside of Hong Kong, we expect to open Phase 2 of SZL4 in the middle of 2011.

In our property development business, recognition of profit from Festival City in Tai Wai is based on the later of the date when Occupation Permit for the third Phase is issued or the date when sales proceeds exceed the cost of development. Currently, Occupation Permit for Phase 3 is expected by December 2011. At Area 56 in Tseung Kwan O where we have a share in the 20,000 square metre shopping mall, Occupation Permit was issued in January 2011. Hence we will book profits on this mall in the first half of 2011 based on the assessed value of our share of the mall. The mall will open for business in early 2012. Apart from our share of the mall, we have no further financial interest in the Area 56 development.

In our property tendering activities, from now until the end of 2011, we may tender out the Tai Wai Station and the smaller Tin Shui Wai sites, subject to market conditions. The Tai Wai Station site is above East Rail Line Tai Wai Station, whilst our Tin Shui Wai site is above a Light Rail stop. For West Rail development sites, where we only act as agent for Government, we may tender out the Nam Cheong Station site and the Tsuen Wan West (TW5) site in the second half of 2011.

Finally, I take this opportunity to thank my fellow directors and all of my over 20,000 colleagues for their dedication and hard work. They are the heroes of MTR.

C K Chow, *Chief Executive Officer*
Hong Kong, 3 March 2011

Key Figures

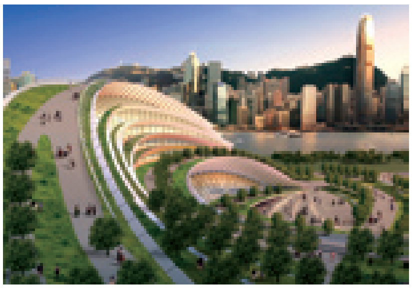
	2010	2009	% Increase/ (Decrease)
Financial highlights *(HK$ million)*			
Revenue			
– Hong Kong Fare	**12,459**	11,498	8.4
– Non-fare	**6,915**	6,256	10.5
– Railway subsidiaries outside of Hong Kong	**10,144**	1,043	872.6
Operating profit from railway and related businesses before depreciation, amortisation and variable annual payment arising from the Rail Merger	**10,917**	9,515	14.7
Profit on property developments	**4,034**	3,554	13.5
Operating profit before depreciation, amortisation and variable annual payment arising from the Rail Merger	**14,951**	13,069	14.4
Profit attributable to equity shareholders	**12,059**	9,639	25.1
Profit attributable to equity shareholders (excluding change in fair value of investment properties and related deferred tax)	**8,657**	7,303	18.5
Total assets	**181,665**	176,494	2.9
Loans, other obligations and bank overdrafts	**21,057**	23,868	(11.8)
Obligations under service concession	**10,749**	10,625	1.2
Total equity attributable to equity shareholders	**117,150**	106,387	10.1
Financial ratios			
Operating margin *(%)*	**37.0**	50.6	(13.6)% pts.
Operating margin (excluding railway subsidiaries outside of Hong Kong) *(%)*	**54.9**	53.5	1.4% pts.
Net debt-to-equity ratio* *(%)*	**12.8**	25.8	(13.0)% pts.
Return on average equity attributable to equity shareholders *(%)*	**10.8**	9.4	1.4% pts.
Return on average equity attributable to equity shareholders (excluding change in fair value of investment properties and related deferred tax) *(%)*	**7.7**	7.2	0.5% pt.
Interest cover *(times)*	**10.5**	7.1	3.4 times
Share information			
Basic earnings per share *(HK$)*	**2.10**	1.69	24.3
Basic earnings per share (excluding change in fair value of investment properties and related deferred tax) *(HK$)*	**1.51**	1.28	18.0
Dividend per share *(HK$)*	**0.59**	0.52	13.5
Share price at 31 December *(HK$)*	**28.30**	26.80	5.6
Market capitalisation at 31 December *(HK$ million)*	**163,364**	153,506	6.4
Operations highlights			
Total passenger boardings			
– Domestic Service *(million)*	**1,298.7**	1,218.8	6.6
– Cross-boundary Service *(thousand)*	**99,954**	94,016	6.3
– Airport Express *(thousand)*	**11,145**	9,869	12.9
– Light Rail *(thousand)*	**154,522**	143,489	7.7
Average number of passengers *(thousand)*			
– Domestic Service *(weekday)*	**3,770**	3,544	6.4
– Cross-boundary Service *(daily)*	**273.8**	257.6	6.3
– Airport Express *(daily)*	**30.5**	27.0	12.9
– Light Rail *(weekday)*	**433.0**	402.1	7.7
Fare revenue per passenger *(HK$)*			
– Domestic Service	**6.67**	6.55	1.9
– Cross-boundary Service	**24.89**	24.75	0.5
– Airport Express	**62.28**	62.48	(0.3)
– Light Rail	**2.65**	2.68	(1.0)
Proportion of franchised public transport boardings *(%)*	**44.3**	42.6	1.7% pts.

* Including obligations under service concession and loan from holders of non-controlling interests as components of debts and investments in bank medium term notes as a component of cash.

Key Events in 2010

JANUARY

The Company commenceds construction works for the Express Rail Link.



FEBRUARY

The Company was named a Sustainability Leader within the global travel and tourism industry sector, and won a Gold Class award from Sustainable Asset Management. The Company was also the only Hong Kong company included in the Global 100 list of the world's 100 most sustainable companies.

The Middle Road Subway Extension connecting Tsim Sha Tsui Station and East Tsim Sha Tsui Station with the Canton Road area opened for service.

MARCH

The Company introduced new multi-purpose smart tickets equipped with memory chips for the Airport Express to replace the magnetic tickets.

Tender for Austin Station Sites C and D was awarded to Fast New Limited, a consortium formed by New World Development Company Limited and Wheelock Properties Limited on 2 Mar 2010.

Pre-sales of the 1,360 units of Phase 1 of Festival City at Tai Wai Maintenance Centre were launched on 26 Mar 2010 with good results.

MTR's Tourist Ambassador Programme started its trial in March 2010 at selected MTR stations that have a large number of tourists. The Programme aims to render assistance to tourist passengers and to provide participating ambassadors who are tertiary education students an internship opportunity to earn study credits.

APRIL

The Company launched a new TV Campaign "MTR – Connecting You to Your Future Destinations" to highlight the convenience of rail transport. The Company also joined hands with the Central and Western District Council to organise "Our Memories of the Western District Photographic Competition", to encourage public support and involvement for the West Island Line project.

MTR HONG KONG Race Walking 2010 attracted over 1,400 participants to promote healthy living and raised over HK$1.13 million for the Hospital Authority Health InfoWorld to support its work on disease prevention and health education.

MAY

The "MTR Mobile" iPhone app was launched as a free download, enabling users to browse routes, make travel plans and check station information across the MTR network.

Elderly Ambassadors aged between 55 and 65 were recruited from the local community to provide assistance and show care to passengers, especially elderly passengers.

The Company was awarded five top honours by *FinanceAsia* Magazine, including Hong Kong's "Best Managed Company", "Best Corporate Governance", "Best CEO", "Best CFO" and "Best Investor Relations".

JUNE

The Company adjusted individual MTR, Light Rail and MTR Bus fares in accordance with the Fare Adjustment Mechanism – the first such adjustment in 13 years.

An amendment to the South Island Line (East) project was gazetted under the Railways Ordinance.

JULY

Wholly owned subsidiary MTR Corporation (Shenzhen) Limited, took over operation of the five-station, 4.5-km Shenzhen Metro Longhua Line Phase 1, preparing for the integrated full line services in mid 2011.

The Company was included as one of 30 Hong Kong-listed companies in the new Hang Seng Corporate Sustainability Index, recognising its achievement in corporate governance, environmental, social and workplace practices.

AUGUST

The Company commenced major modification works including installation of new tracks, overhead lines, signalling and other railway operation systems at Sheung Wan Station as part of the West Island Line project.

The Company organised roving exhibitions to gauge public views on the Shatin to Central Link. A new website www.mtr-shatincentrallink.hk was launched to provide information on the project.

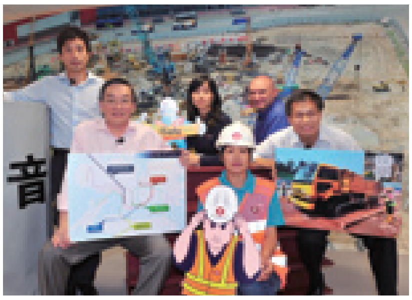
SEPTEMBER

The Company's two teams of six talented young people won the Grand Award and First Runner-up Award at the International Association of Public Transport's (UITP) "Solutions for Our Future Award" competition, beating entries from Canada, the Netherlands, India, the Mainland of China, Taiwan and other countries.

The Company launched a limited edition "Railway 100th Anniversary Commemorative Ticket Set" to celebrate the centenary of railway operation in Hong Kong.

OCTOBER

The Company launched the "Please excuse us" advertising campaign to thank the communities, who will be affected by construction of the new rail lines, for their patience and understanding.



Cheung Lai Street Pedestrian Subway was opened, with new entrances to Lai Chi Kok Station.

As part of a trial scheme, staff in ten stations received specialised training on the use of automated external defibrillators to help passengers suffering from cardiac arrest.

NOVEMBER

The Shatin-to-Central Link was gazetted under the Railways Ordinance.

The Chief Executive in Council authorised the schemes for the South Island Line (East) and Kwun Tong Line Extension projects under the Railways Ordinance.

Pre-sales of the 1,368 units of Festival City II, Phase 2 of Festival City, was launched in mid November.

DECEMBER

The Daxing Line, a 22-km extension of Beijing Metro Line 4, commenced service. The new line is operated by Beijing MTR Corporation Limited, the joint venture company comprising MTR Corporation, Beijing Infrastructure Investment Co. Ltd. and Beijing Capital Group.

The "MTR Mobile" iPhone app won international recognition for its excellence in mobile marketing and digital creativity, receiving the "Best Use of Mobile Marketing Award" in the relationship building category of the 2010 Mobile Marketing Association Global Awards (MMA Awards) and the Leisure/Travel sector "Bronze Award" at the 2010 Digital Media Awards (DMA).

A record 5 million passengers rode on the MTR network during the overnight service on Christmas Eve. This is the highest number of passenger trips the railway has recorded on a 24-hour service day.

Escalator Safety Ambassadors helped reduce accidents at top ten escalators with highest accident rates by

55%

MTR Opinion Zone collected over

1,200 useful customer comments

Energy saving

initiatives have reduced traction power usage by 18.7% over past 5 years

MOVING FORWARD

CARING FOR LIFE'S JOURNEYS

Hong Kong Passenger Services

40 integrated entrances in 32 stations have enhanced connectivity, convenience and accessibility for passengers

29 fare saver machines offer discounts to passengers

Busy Tai Wai Station connects the eastern New Territories to other parts of Hong Kong

Our Hong Kong fare revenue, which comprises our rail, light rail and bus services, reached HK$12,459 million in 2010. This was 8.4% higher than for 2009 and reflected a combination of an improving economy, the full year effect of the opening of Kowloon Southern Link and LOHAS Park Station and the application of the Fare Adjustment Mechanism in June 2010.

Patronage

Total patronage from all of our rail, light rail and bus services in Hong Kong increased by 6.8% as compared to last year to 1,608.5 million in 2010.

On the back of an economic rebound, our Domestic Service saw total patronage rise by 6.6% over 2009 to 1,298.7 million. Average weekday patronage from our Domestic Service in 2010 was 3.8 million, an increase of 6.4% over last year.

Cross-boundary Service at Lo Wu and Lok Ma Chau reported a 6.3% rise in patronage over 2009 to 100.0 million in 2010, reflecting the growth in travellers from Mainland of China and the economic recovery.

WORLD-CLASS CITY
WORLD-CLASS SERVICE

Passenger traffic on the Airport Express in 2010 increased by 12.9% over 2009 to 11.1 million journeys, boosted by the revival in air travel as the global economy recovered as well as a number of well-attended events at the Asia World Expo, particularly the "River of Wisdom" event in November 2010.

Passenger volume on Light Rail, Bus and Intercity services totalled 198.7 million in 2010, an increase of 8.0 % over 2009.

The Company's overall share of the franchised public transport market in Hong Kong rose from 42.6% in 2009 to 44.3% in 2010. Within this total, our share of the cross-harbour traffic increased from 64% to 65.3%. Our Cross-boundary business again faced strong competition during the year, as a result of which our market share fell slightly to 55.0% in 2010 from 55.3% in 2009.

Fare Revenue

Hong Kong fare revenue from our rail, light rail and bus services increased by 8.4% to HK$12,459 million in 2010.

Domestic Service fare revenue increased by 8.5% in 2010 to HK$8,668 million, accounting for 69.6% of the total Hong Kong fare revenue. Average fare per passenger on our Domestic Service increased by 1.9% to HK$6.67 mainly due to the application of the Fare Adjustment Mechanism as well as slightly longer journeys taken by some passengers as a result of the opening of Kowloon Southern Link, which connected the East Rail Line and West Rail Line in 2009.

Fare revenue from the Cross-Boundary Service in 2010 was HK$2,487 million, an increase of 6.9% over 2009 while the fare revenue from the Airport Express reached HK$694 million in 2010, a rise of 12.5% as compared with 2009.


Our services are renowned for efficiency, comfort and convenience

"Our Hong Kong fare revenue, which comprises our rail, light rail and bus services, reached HK$12,459 million in 2010."

Fare revenue from Light Rail, Bus and Intercity services was HK$610 million in 2010, a rise of 7.4% over 2009.

An adjustment to a number of fares was made on 13 June 2010, which was in accordance with the Fare Adjustment Mechanism adopted as part of the Rail Merger in 2007. The weighted average adjustment of all applicable fares, predominately fares for our Domestic Service, Cross-boundary Service, Bus and Light Rail, was +2.05%. In accordance with the agreed methodology, this figure was calculated according to the year-on-year change in the Composite Consumer Price Index and Transport Wage Index for December 2009, plus the adjustment rate, of 0.7%, which was not implemented in 2009 but carried forward to 2010. The adjustment was 20 Hong Kong cents or less for an estimated 83% of all passenger trips subject to the adjustment, including an estimated 10% of passenger trips that experienced no fare change.

Service Promotions

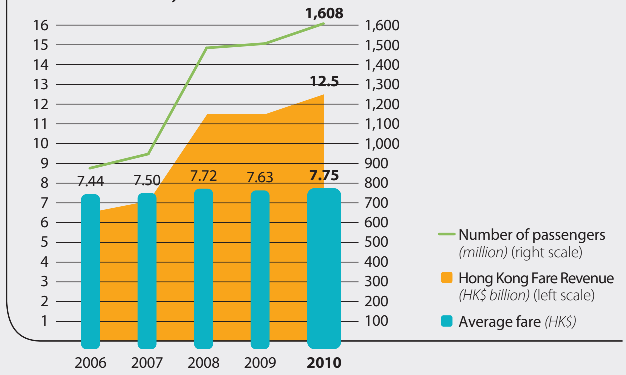
A number of innovative marketing campaigns plus a variety of carefully designed service promotions helped increase passenger traffic on our Hong Kong network during 2010.

Promotions during the year included a Valentine Promotion to promote leisure travel, and MTR shop coupons for Octopus users who accumulated fares of HK$100 on weekdays. In May, we launched an iPhone application providing users with information for journey planning and facilities in our stations, which soon ranked as number one amongst free applications in the Apple App Store (Hong Kong). We launched an iPad application in December to build on the success of the iPhone application. Furthermore, our enhanced fare promotions for the elderly were extended into 2011.

"...we exceeded all our performance standards, both those stipulated in the Operating Agreement as well as our own more demanding Customer Service Pledges."

Passengers and Fares (Hong Kong Passenger Services)

The increase in fare revenue and patronage was helped by the economic recovery.



A Tourist Ticket Value Pack was launched from April to December 2010, providing tourists buying our tourist tickets with special discount offers from major local attractions and sightseeing services. A joint promotion with Asia Miles was launched in March to promote the online purchase of Airport Express tickets and tourists passes. In addition, we supported Government in the "River of Wisdom – Animated Version of the Riverside Scene at Qingming Festival" exhibition held at AsiaWorld-Expo from 9 – 29 November 2010. The event attracted more than 900,000 visitors, who enjoyed fare discounts and additional train services. We also organised themed tours on our Intercity Through Trains together with local travel agencies and revamped our Intercity website. "Ktt", the Intercity train managed by the Company that runs between Hong Kong and Guangzhou, was appointed an official carrier for the Asian Games which took place in Guangzhou in November 2010.

Our friendly staff are available to help people on the network

Service Connectivity

We continued our work on improving service connectivity and inter-modal operations, through creating more convenient entrances, walkways, subways and pedestrian links.

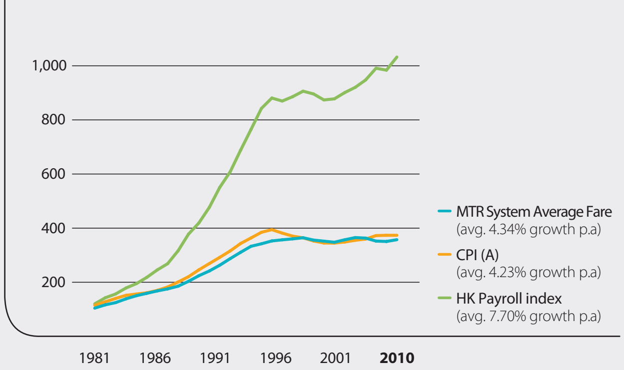
At Lai Chi Kok Station a new air-conditioned subway was completed and a wider stairway was made permanent at Tin Shui Wai Station. Tuen Mun Station benefited from the completion of a fully air-conditioned integrated entrance equipped with escalators and a passenger lift connected to the new public transport interchange. At Tsim Sha Tsui Station, the opening of the Middle Road Subway Extension and two new exits enhanced connectivity to shops, businesses and points of interest in the area, allowing passengers comfortable all-weather access. Work to upgrade the footbridges at Po Lam Station was completed in February 2010. Site works on a new entrance connecting to the footbridge of the Sun Hung Kai redevelopment at Kwai Hing Station made good progress and is targeted for opening in the first quarter of 2011. Furthermore, we had 58 feeder routes offering intermodal discounts across the network by the end of 2010.

Service Performance and Market Recognition

As in previous years, we exceeded all our performance standards, both those stipulated in the Operating Agreement as well as our own more demanding Customer Service Pledges. Train service delivery, passenger journeys on time and train punctuality were all at 99.7% or above.

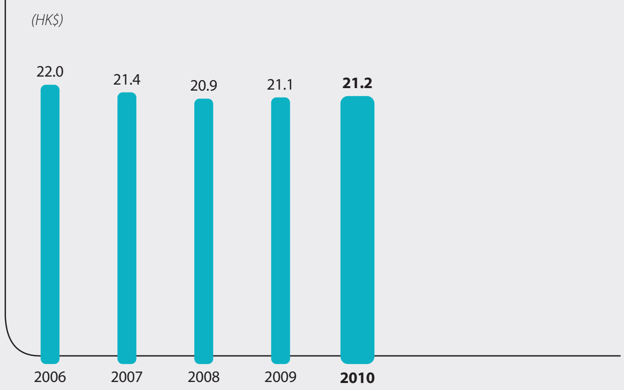
Fare Trend

In past years, MTR fares have consistently lagged behind the growth in Hong Kong payroll but were in line with the long-term changes in consumer prices in Hong Kong.



Operation Costs Per Car-km Operated for Hong Kong Passenger Services

Operating costs per car-km were maintained at a low level.



The excellent service levels which the Company achieved again secured wide recognition in Hong Kong, including the Hong Kong Service Awards in the Public Transportation Category presented by East Week magazine and the category award winner in the Public Transportation Category of the Sing Tao Excellent Services Brand Award 2009 organised by Sing Tao Daily.

Customer satisfaction recorded by our regular surveys remained high during 2010. The Service Quality Index for Domestic and Cross-Boundary services and for the Airport Express rose to 73 and 83 respectively, from 70 and 82 in 2009. The Fare Index for the two segments, which measures the level of customer satisfaction with fares, increased to 65 and 67 from 61 and 63 over the twelve months.

Service Improvement

To ensure continuous service improvement, we continued to enhance stations and rolling stock through modifications and upgrades. During 2010, various levels of renovations were completed at Mei Foo, Jordan, Sheung Shui and Mong Kok East stations and renovations are underway at Fanling Station. The concourses at Kam Sheung Road and Tin Shui Wai stations were also revamped.

Installation of automatic platform gates at eight aboveground stations on the Island, Kwun Tong and Tsuen Wan lines has commenced. Platform queuing tiles have been installed at ten West Rail Line stations. A new noise enclosure was constructed for the tracks at Wo Liu Hang in Fo Tan in March 2010.

Following the opening of the Kowloon Southern Link last year, 22 light rail vehicles procured for the Light Rail network have been progressively put into service, while ten new underground trains are targeted for delivery starting from the second quarter of 2011.

Environmentally friendly architecture and art in our stations help enhance the travelling experience

Access to the Network for the Disabled

As a company noted for its commitment to the community, we make every effort to ensure our services are available to everyone, including people who are disabled and those with reduced mobility.

During 2010, we continued to offer special fares for those with disabilities and increased the number of station assistants to help disabled people.

New ramps for the disabled were added at Kwai Fong and Kwai Hing stations, and new external lifts at Wong Tai Sin, Sham Shui Po and Jordan stations were under construction.

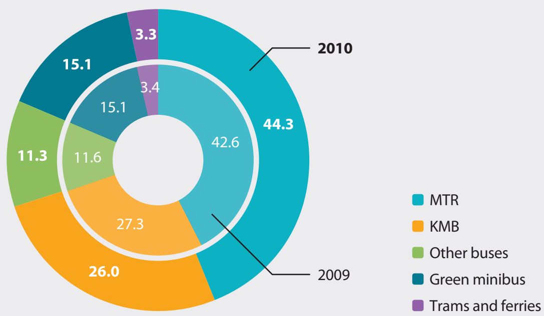
A rigorous maintenance programme underpins our high service performance

"The excellent service levels which the Company achieved again secured wide recognition in Hong Kong..."

Market Shares of Major Transport Operators in Hong Kong

The Company's overall market share increased from 42.6% in 2009 to 44.3% in 2010.

(Percentage)



Additional wide gates were installed during 2010 at Kwai Fong, Kwai Hing and Tsuen Wan West stations.

We have also modified train compartments to make them more accessible to the disabled, through a scheme to modify certain train cars to provide more multi-purpose spaces. This project is about 30% complete. All new Light Rail vehicles will feature multi-purpose and wheelchair space.

Toilets at the Hong Kong Station arrival hall level, with an improved design that make them easier to use for disabled people, were opened to the public in October 2010, followed by those at the mezzanine level in December 2010, and with those at the in-town check-in level to be completed in the first half of 2011.

To assist the visually impaired, during the year, full length tactile guide paths were installed on the East Rail Line platforms in Kowloon Tong Station. The tactile guide path for all other platforms on East Rail Line stations will be modified to cover full platform length during 2011 and 2012. Braille maps and handrail Braille plates were installed at Tai Wo Hau, Mong Kok, Shek Kip Mei, Diamond Hill, and Sunny Bay stations.

Productivity

During the year, we made further improvements in productivity and efficiency, including energy efficiency. Efficiency enhancement came from smart-metering for station kiosks and improvements to tunnel ventilation at Tseung Kwan O Station and depot, which generated considerable savings. Additional savings came from electronic ballast replacement at East Rail Line stations and optimisation of station lighting. The installation of static inverters on certain East Rail Line trains, in addition to saving energy, also reduced noise. LED lighting for 136 trains is currently under product design and type testing in the factory, with installation targeted for completion in mid 2014. In addition to the initiatives in energy saving, we continue to identify opportunities to enhance productivity such as alternative sourcing, and streamlining work processes for station maintenance work.

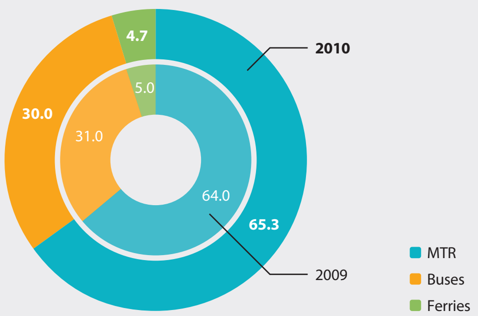
Overall our cost per car-km was HK$21.2 in 2010, a below inflation increase of 0.47% from 2009. Operating margin for our Hong Kong transport business improved to 46.0% from 43.1%.

Improving services and accessibility to sustain high customer satisfaction

Market Shares of Major Transport Operators Crossing the Harbour

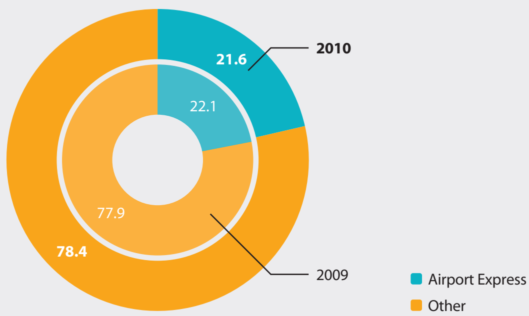
The Company's market share of cross-harbour traffic rose to 65.3%.

(Percentage)



Market Shares of Airport Express

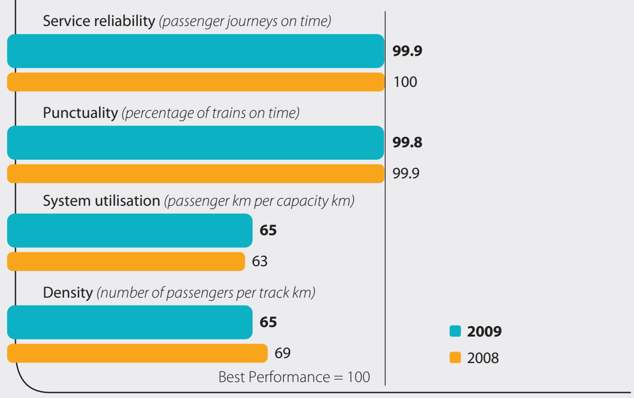
The proportion of air passengers using the Airport Express decreased.



Benchmarking Comparisons

MTR Corporation maintained its strong position, particularly in service reliability, against international benchmarks.

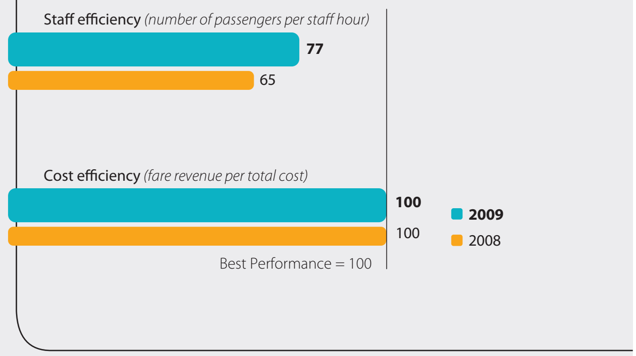
MTR performance vs. Best Performance



Staff Efficiency and Cost Efficiency

New initiatives continue to be introcuced to enhance operating efficiency.

MTR performance vs. Best Performance



Airport Express provides convenient and reliable services to air travellers

System and Market Information

Railway operation data	2010		2009	
Total route length *(km)*		**218.2**		218.2
Number of rail cars		**1,941**		1,921
Number of stations (Island Line, Tsuen Wan Line, Kwun Tong Line, Tseung Kwan O Line, Tung Chung Line, Disneyland Resort Line, West Rail Line, Airport Express, East Rail Line and Ma On Shan Line)		**84**		84
Number of Light Rail stops		**68**		68
Number of e-instant Bonus machines in stations		**44**		36
Number of station kiosks and mini-banks in stations		**1,254**		1,228
Number of advertising points in stations		**21,021**		20,742
Number of advertising points in trains		**23,817**		26,823
Daily hours of operation				
Island Line, Tsuen Wan Line, Kwun Tong Line, Tseung Kwan O Line, Tung Chung Line, Disneyland Resort Line, West Rail Line, Airport Express and Light Rail		**19.0**		19.0
East Rail Line and Ma On Shan Line		**19.5**		19.5
Minimum train headway *(second)*	**Morning Peak**	**Evening Peak**	Morning Peak	Evening Peak
– Tsuen Wan Line	**128**	**130**	128	130
– Kwun Tong Line	**128**	**144**	128	144
– Island Line	**120**	**150**	120	150
– East Rail Line				
Hung Hom to Sheung Shui	**212**	**212**	212	212
Hung Hom to Lo Wu	**327**	**327**	327	327
Hung Hom to Lok Ma Chau	**600**	**600**	600	600
– Ma On Shan Line	**180**	**240**	180	240
– Tseung Kwan O Line	**150**	**150**	160	180
– Tung Chung Line				
Hong Kong to Tung Chung	**360**	**480**	360	480
Hong Kong to Tsing Yi	**240**	**240**	240	240
– Airport Express	**720**	**720**	720	720
– West Rail Line	**180**	**270**	180	270
– Disneyland Resort Line	**270**	**270**	270	270
– Light Rail	**270**	**300**	270	300

International Performance Comparisons: The 13-member Community of Metros (CoMET)

Metro system network data (2009)	MTR *	Metro A	Metro B	Metro C	Metro D	Metro E	Metro F	Metro G	Metro H	Metro I	Metro J	Metro K	Metro L
Passenger journeys *(million)*	**1,313**	809	532	1,078	1,415	648	2,392	1,598	1,542	461	611	878	706
Car kilometres *(million)*	**248**	177	119	472	348	201	722	567	246	98	106	169	112
Route length *(km)*	**175**	200	146	439	201	275	298	480	215	115	86	241	61
Number of stations	**82**	106	173	270	147	241	164	424	300	66	86	156	55

* The lines included in the CoMET metro benchmarking programme are Kwun Tong Line, Tsuen Wan Line, Island Line, Tung Chung Line, Tseung Kwan O Line and Disneyland Resort Line, East Rail Line, Ma On Shan Line and West Rail Line. The Airport Express is excluded from the benchmarking.

Note: The other metros in the comparison are Berliner Verkehrsbetriebe, London Underground Limited, New York City Transit, Sistema de Transporte Colectivo, Régie Autonome des Transports Parisiens Metro, Régie Autonome des Transports Parisiens Réseau Express Régional, Metropolitano de São Paulo, Moscow Metro, Metro de Madrid, Metro de Santiago, Shanghai Metro Operation Corporation and Beijing Mass Transit Railway Operation Corporation. The benchmarking agreement prohibits specifically identifying the data by metro system.

Operations Performance in 2010

Service performance item	Performance Requirement	Customer Service Pledge Target	**Actual Performance**
Train service delivery			
– Kwun Tong Line, Tsuen Wan Line, Island Line, Tseung Kwan O Line, Tung Chung Line, Disneyland Resort Line and Airport Express	98.5%	99.5%	**99.8%**
– East Rail Line (including Ma On Shan Line)	98.5%	99.5%	**99.9%**
– West Rail Line	98.5%	99.5%	**99.9%**
– Light Rail	98.5%	99.5%	**99.9%**
Passenger journeys on time			
– Kwun Tong Line, Tsuen Wan Line, Island Line, Tseung Kwan O Line, Tung Chung Line and Disneyland Resort Line	98.5%	99.5%	**99.9%**
– Airport Express	98.5%	99.0%	**99.9%**
– East Rail Line (including Ma On Shan Line)	98.5%	99.0%	**99.9%**
– West Rail Line	98.5%	99.0%	**99.9%**
Train punctuality			
– Kwun Tong Line, Tsuen Wan Line, Island Line, Tseung Kwan O Line, Tung Chung Line and Disneyland Resort Line	98.0%	99.0%	**99.7%**
– Airport Express	98.0%	99.0%	**99.9%**
– East Rail Line (including Ma On Shan Line)	98.0%	99.0%	**99.9%**
– West Rail Line	98.0%	99.0%	**99.8%**
– Light Rail	98.0%	99.0%	**99.9%**
Train reliability: train car-km per train failure causing delays ≥ 5 minutes			
– Kwun Tong Line, Tsuen Wan Line, Island Line, Tseung Kwan O Line, Tung Chung Line, Disneyland Resort Line and Airport Express	N/A	500,000	**2,459,083**
– East Rail Line (including Ma On Shan Line) and West Rail Line	N/A	500,000	**3,813,015**
Ticket reliability: magnetic ticket transactions per ticket failure			
– Kwun Tong Line, Tsuen Wan Line, Island Line, Tseung Kwan O Line, Tung Chung Line, Disneyland Resort Line, Airport Express, East Rail Line (including Ma On Shan Line) and West Rail Line	N/A	8,000	**26,955**
Add value machine reliability			
– Kwun Tong Line, Tsuen Wan Line, Island Line, Tseung Kwan O Line, Tung Chung Line, Disneyland Resort Line and Airport Express	98.0%	99.0%	**99.5%**
– East Rail Line (including Ma On Shan Line)	98.0%	99.0%	**99.8%**
– West Rail Line	98.0%	99.0%	**99.7%**
– Light Rail	N/A	99.0%	**99.5%**
Ticket machine reliability			
– Kwun Tong Line, Tsuen Wan Line, Island Line, Tseung Kwan O Line, Tung Chung Line, Disneyland Resort Line and Airport Express	97.0%	99.0%	**99.6%**
– East Rail Line (including Ma On Shan Line)	97.0%	99.0%	**99.7%**
– West Rail Line	97.0%	99.0%	**99.6%**
– Light Rail	N/A	99.0%	**99.8%**

Operations Performance in 2010 *(continued)*

Service performance item	Performance Requirement	Customer Service Pledge Target	**Actual Performance**
Ticket gate reliability			
– Kwun Tong Line, Tsuen Wan Line, Island Line, Tseung Kwan O Line, Tung Chung Line, Disneyland Resort Line and Airport Express	97.0%	99.0%	**99.8%**
– East Rail Line (including Ma On Shan Line)	97.0%	99.0%	**99.9%**
– West Rail Line	97.0%	99.0%	**99.9%**
Light Rail platform Octopus processor reliability	N/A	99.0%	**99.9%**
Escalator reliability			
– Kwun Tong Line, Tsuen Wan Line, Island Line, Tseung Kwan O Line, Tung Chung Line, Disneyland Resort Line and Airport Express	98.0%	99.0%	**99.9%**
– East Rail Line (including Ma On Shan Line)	98.0%	99.0%	**99.8%**
– West Rail Line	98.0%	99.0%	**99.9%**
Passenger lift reliability			
– Kwun Tong Line, Tsuen Wan Line, Island Line, Tseung Kwan O Line, Tung Chung Line, Disneyland Resort Line and Airport Express	98.5%	99.5%	**99.7%**
– East Rail Line (including Ma On Shan Line)	98.5%	99.5%	**99.9%**
– West Rail Line	98.5%	99.5%	**99.9%**
Temperature and ventilation			
– Trains, except Light Rail: to maintain a cool, pleasant and comfortable train environment generally at or below 26°C	N/A	97.0%	**99.9%**
– Light Rail: on-train air-conditioning failures per month	N/A	<3	**0**
– Stations: to maintain a cool, pleasant and comfortable environment generally at or below 27°C for platforms and 29°C for station concourses, except on very hot days	N/A	90.0%	**99.8%**
Cleanliness			
– Train compartment: cleaned daily	N/A	98.5%	**99.9%**
– Train exterior: washed every 2 days (on average)	N/A	99.0%	**100.0%**
Northwest Transit Service Area Bus Service			
– Service Delivery	N/A	99.0%	**99.8%**
– Cleanliness: washed daily	N/A	99.0%	**100.0%**
Passenger enquiry response time within 6 working days	N/A	99.0%	**99.9%**


Refurbished
station
shops
make travelling
by MTR a pleasant
journey

SPREADING OUT
TO TOUCH EVERYONE

3G
in all stations brings mobile internet access everywhere

Over
200 brands
offering shopping convenience to passengers

Station Commercial and Rail Related Businesses

1,254 stations shops
to meet different passenger needs

MTR Mobile
enables
iPhone
users to plan their journeys

Revenue from our station commercial and rail related businesses rose by 11.6% over 2009 to HK$3,715 million. The increase was mainly due to a strong recovery in the advertising business as well as good rental reversion and an increase in floor area in our portfolio of station shops. Project management on behalf of Government in relation to the Hong Kong section of Guangzhou-Shenzhen-Hong Kong Express Rail Link (Express Rail Link) also added to revenue and, in similar amount, to expenses.

Station Retail

The Company's portfolio of retail outlets in stations had a good year, with station retail revenue in 2010 rising by 6.9% over 2009 to HK$1,716 million. The rise in revenue reflects the increase in both the area and number of shops, as well as increased rental rates resulting from a refinement of the trade mix and favourable renewal rates due to the stronger economy.

Following renovations at Tsing Yi, Tsim Sha Tsui, Sheung Shui, Kowloon Tong, Central, Cheung Sha Wan, Hong Kong, Fanling

TOTAL CUSTOMER EXPERIENCE

and Shatin stations, the total number of station shops increased to 1,254 at the end of 2010 compared to 1,228 at the end of 2009. A total of 38 new trades and brands were added. Total station retail space increased by 1,092 square metres to 53,880 square metres, mainly due to increases at Tsing Yi, Cheung Sha Wan and Hong Kong stations.

To enhance the attraction of our shops and support our tenants, a number of strategic marketing programmes were held throughout the year, including "10 Coolest MTR Shops Products Voting Campaign", "MTR Club Bonus Points Scheme Joint Promotion" and "Thankful Fest".

Advertising

Advertising revenue in 2010 increased by 22.9% over 2009 to HK$734 million, reflecting an improving economy and the timely launch of new advertising packages. Our trains and stations in Hong Kong provided a total of 44,838 advertising points during the year.

Mobile internet access in all stations enables iPad users to fully utilise the MTR iPad App

New formats are helping advertisers to target their marketing

To strengthen the visual impact of our TV networks, during 2010 all concourse TVs were replaced and trackside TV units enlarged from 63 inches to 103 inches. Three "Innovative Panels" were installed to allow advertisers to collect passengers' opinions, distribute samples or coupons and display products. Two shopping guide maps were modified to create a "Multi-media Panel" for advertisers to showcase their entertainment and digital products. The number of "Digital Escalator Crown Banks" installed increased from ten to 12.

Telecommunications

Revenue from our telecommunications business in 2010 was 6.2% higher than in 2009 at HK$290 million. The increase was due to incremental income from mobile phone networks at new stations, the strong growth of 3G data transmission as well as rentals from eight new rooftop sites as mobile phone operators expanded their outdoor network coverage.

In May 2010, the Company concluded an agreement with two telecom operators to participate in a 3G Capacity Enhancement Project to double their 3G capacity at 15 stations in prime locations. Work began in September 2010 and is on schedule for completion in mid 2011. To improve mobile phone services further, the Company signed agreements during 2010 with three telecom operators to facilitate upgrading of their mobile phone equipment along the railway.

External Consultancy

Revenue from external consultancy in 2010 was HK$113 million. This represented a decline of 28.9% over 2009 reflecting completion of the Airport Authority Hong Kong Automatic People Mover Modification Works project in June 2009. Our consultancy projects in Thailand, Brazil and India all progressed satisfactorily.

Other Rail Related Businesses

Project management income from KCRC and Government in 2010 was HK$557 million, representing a 40.7% increase compared to 2009, mainly due to the project management fees received starting in January 2010 relating to the Entrustment Agreement for the Express Rail Link.

The Company wound down its freight business in June 2010 to utilise train paths better and provide greater flexibility for passenger train services. Members of staff working in the freight business were given job placements within the Company. Retraining, change management workshops and site visits facilitated a smooth transition to their new posts.

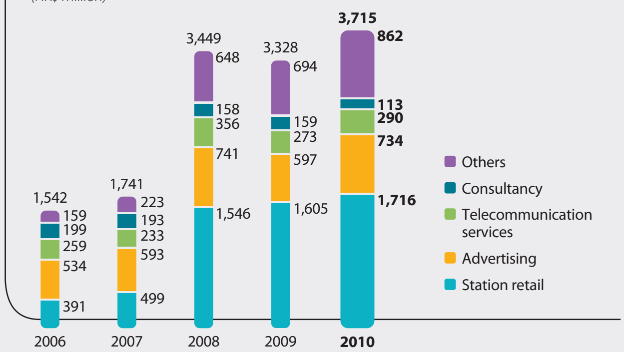
Themed advertising helps drive sales during major promotion campaigns

"To enhance the attraction of our shops and support our tenants, a number of strategic marketing programmes were held throughout the year..."

Revenue from Station Commercial and Rail Related Businesses

Revenue increased for 2010 due to a strong recovery in the advertising business, good rental reversion as well as an increase in floor area in our portfolio of station shops, and project management revenue from Government.

(HK$ million)



UP-LIFTING
THE QUALITY OF LIFE

81,962

households enjoy quality living in our managed properties

Bringing a **green** living concept to our 36 managed residential developments

Property and Other Businesses

Building
self-sufficient communities
with seamless rail connections for maximum convenience

225,650 sq.m.
(Lettable Floor Area) of MTR shopping malls to enhance customers' shopping experience

The Hong Kong property market was robust throughout most of 2010, due to a combination of low interest rates, the economic recovery as well as increased interest in property purchases from Mainland Chinese buyers. The number of residential transactions and sales proceeds were the highest since the previous property boom in 1997.

During the year, in response to public concern over rising prices, Government enacted various policy initiatives relating to the development and sale of residential properties. In February, it raised the stamp duty to 4.25% for property transactions valued at or over HK$20 million. In April and August, to increase transparency in the sale process of primary residential units, Government introduced a number of measures including more detailed listing of the composition of saleable floor area, publicising transactions within five days of sale, disclosing transactions involving Board members and their families, and the disclosure of price lists three days in advance of sale, all of which we welcome.

BUILDING COMMUNITIES

In order to support sustainable development, from April 2011, the concession area allowed to a development to provide environmental features is expected to be reduced and conditions to obtain such areas made more onerous. We are taking steps to reduce the impact of these newly proposed regulations on our developments, particularly as some of the new requirements, such as those regarding building separation and underground car parking space, pose challenges to the planning of our property developments where approvals have been obtained based on the existing statutory requirements.

Towards the end of the year, Government also announced measures to moderate speculative activity in the property market. In November 2010, Government introduced special stamp duty on residential properties sold within two years of acquisition, and reduced the loan-to-value ratio for more expensive residential properties and investment properties. This proposal immediately led to a reduction in sales volumes, although prices remained relatively firm. Sales volume in the secondary market saw a recovery starting in early 2011.

West Rail Line Property Development Plan

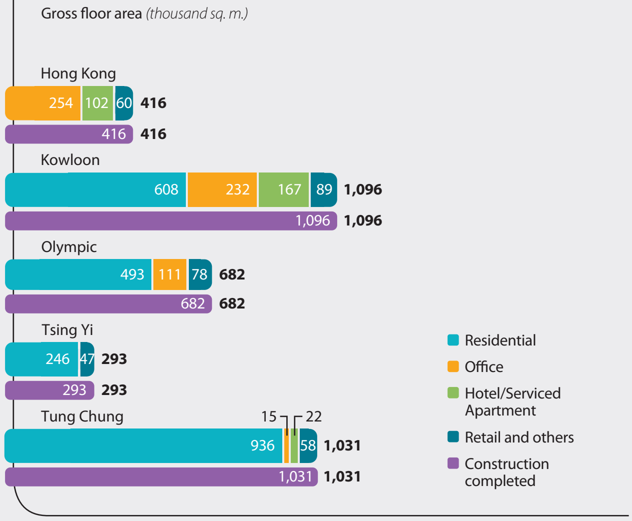
The Company acts as agent for the West Rail property projects.

Station	Site Area *(hectares)*	Period of package tenders	Expected completion date
Tuen Mun	2.65	Aug 2006	By phases from 2012 – 2013
Nam Cheong	6.20	2011	2017
Tsuen Wan West (TW5)	5.60	2011	2017
Tsuen Wan West (TW6)	1.39	Under review	Under review
Tsuen Wan West (TW7)	2.37	Sep 2008	2013
Yuen Long	3.47	Under review	Under review
Long Ping (North)	1.12	Under review	Under review
Long Ping (South)	1.49	Under review	Under review
Tin Shui Wai	3.48	Under review	Under review
Kam Sheung Road	9.85	Under review	Under review
Pat Heung Maintenance Centre	24.00	Under review	Under review
Kwai Fong	1.92	Under review	Under review
Total	**63.54**		

"The Hong Kong property market was robust throughout most of 2010, due to a combination of low interest rates, the economic recovery as well as increased interest in property purchases from Mainland Chinese buyers."

Airport Railway Property Development Plan and Progress

Along the Airport Railway, all 56 units of La Mer, the town house development which is the last phase of Caribbean Coast, were sold by August 2010.



Excellent property management services are provided to residents

Property Development

Profit from property development in 2010 was HK$4,034 million, with the major contribution coming from Le Prestige at LOHAS Park as well as the sale of units in inventory at The Palazzo in Fo Tan and Lake Silver in Wu Kai Sha.

Pre-sales commenced for Phase 1 and Phase 2 of Festival City at Tai Wai Maintenance Centre in March and November 2010 respectively. By the end of 2010, approximately 47% of the 2,728 units in the two phases had been sold. Pre-sales were also launched for the 56 units of La Mer in Tung Chung with all units sold. We have no financial interest in La Mer.

Occupation Permits were issued for Le Prestige, Phase 2a of LOHAS Park, in January 2010 and Festival City Phase 1 and Phase 2 at Tai Wai Maintenance Centre in February and November 2010 respectively. In addition, Occupation Permits were issued during the first half of the year for the remaining projects at Kowloon Station, namely the International Commerce Centre (ICC), Ritz Carlton Hotel, the Observation Deck on level 100 of ICC and the final phase of Elements.

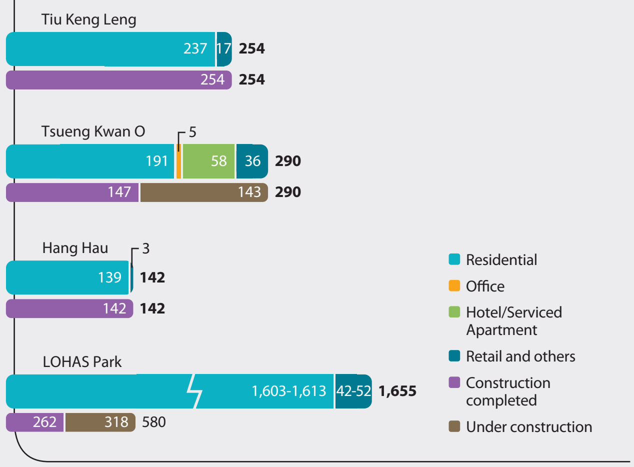
In our property tendering activity, we awarded Austin Station Sites C and D to Fast New Limited, a consortium of New World Development Company Limited and Wheelock Properties Limited, in March 2010. We contributed HK$3.9 billion to this development as part of the land premium payments for the sites.

In the second half of 2010, the Government introduced a number of new measures relating to property development as discussed above, which has resulted in some adjustments to our property development plans.

Tseung Kwan O Line Property Development Plan and Progress

Occupation Permits were issued for Le Prestige, Phase 2a of LOHAS Park, in January 2010.

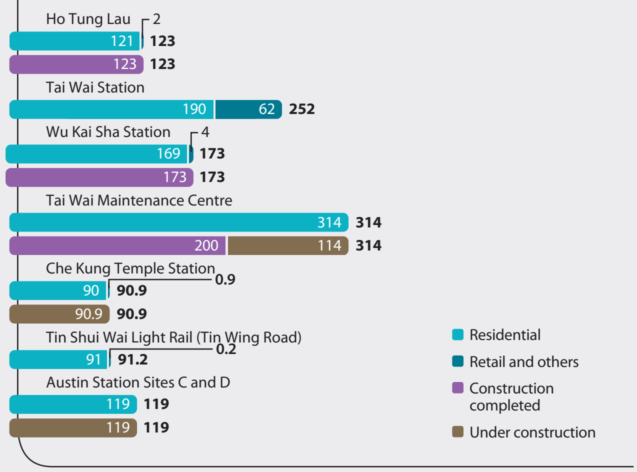
Gross floor area *(thousand sq. m.)*



East Rail Line, Ma On Shan Line, Light Rail and Austin Station Property Development Plan and Progress

Pre-sales commenced for Phase 1 and Phase 2 of Festival City at Tai Wai Maintenance Centre in March and November 2010. We awarded Austin Station Sites C and D to Fast New Limited, a consortium of New World Development Company Limited and Wheelock Properties Limited, in March 2010.

Gross floor area *(thousand sq. m.)*



In planning for the future Kwun Tong Line Extension and South Island Line (East), which will use the "Rail plus Property" model, we are currently in discussion with Government on property development rights relating to a site at the former Valley Road Estate in Ho Man Tin and a site at the former Wong Chuk Hang Estate respectively.

Property Rental, Property Management and Other Businesses

The combined revenue of our property rental, property management and other businesses increased by 9.3% in 2010, as compared with 2009, to HK$3,200 million.

Property Rental

Total property rental income from Hong Kong and the Mainland of China rose by 8.2%, to HK$2,758 million. Our shopping mall portfolio in Hong Kong reported an average 14 % increase in rental reversion for the year. At 31 December 2010, our 12 shopping malls in Hong Kong and the Company's 18 floors at Two International Finance Centre remained close to 100% let. Our shopping malls in Hong Kong continued to receive recognition, winning over ten local and international awards, including Elements, which was listed in the Top 30 in the Gunn Report. Our shopping malls also received the Gold Prime Award for Eco-Business 2010 issued by Prime Magazine and the Business Environment Council in Hong Kong.

The quality residential towers, The Cullinan, above Kowloon Station

In Hong Kong, at the end of December 2010, the Company's attributable share of investment properties amounted to a lettable floor area of 225,650 square metres of retail properties, 41,090 square metres of offices and 11,202 square metres of real estate for other use.

In the Mainland of China, the Company's attributable share of investment properties stood at a lettable floor area of 18,351 square meters at the end of December 2010, comprising the Ginza Mall in Beijing, which was 97% let at year end. The mall achieved an average increase on rental reversion of 3.5% during 2010.

We have made vigorous efforts to promote energy conservation and environmental awareness in our shopping malls, which has resulted in certification by many Government Departments in areas ranging from indoor air quality, water quality, air conditioning, lighting and lifts.

Property Management

Property management revenue in 2010 was 1.9% lower, as compared to 2009, at HK$203 million. As at 31 December 2010, commercial space under management in Hong Kong was virtually unchanged at 744,214 square metres. The number of residential units under our management in Hong Kong rose to 81,962 units, and our managed property portfolio in the Mainland of China totalled 776,402 square metres.

The Company's managed properties gained wide recognition from various government bodies during 2010 in areas covering safety, environmental protection and landscaping. One of our managed properties, the LOHAS Park development, has led the way in environmental protection, including the introduction of electric vehicle for security patrol, and the provision of electric vehicle charging facilities for residents.

The active promotional programmes enhanced the travel experience of guests at Ngong Ping 360

Elements offers a variety of high quality shopping and dining

Other Businesses

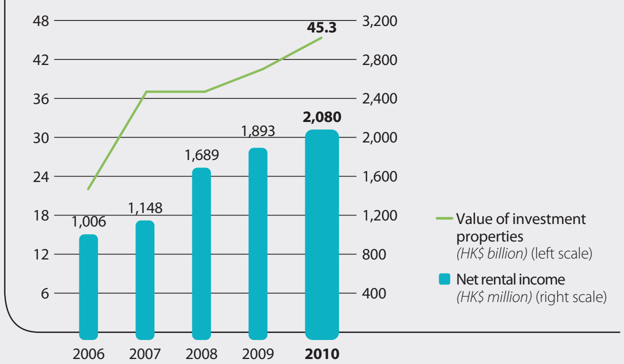
Ngong Ping 360

The Ngong Ping cable car and associated theme village on Lantau Island saw revenue increase by 38.2% to HK$239 million in 2010, as visitor numbers rose from about 1.4 million in 2009 to 1.7 million in 2010. The good performance was the result of smooth operations, increased sales of the premium "crystal cabin ride" and the launch of active promotional programmes throughout the year designed to penetrate different markets and enrich the travel experience of visitors.

The number of overseas tourists visiting Ngong Ping 360 increased by 35% during 2010, with growth coming mainly from visitors from the Mainland of China, India and South East Asia. In April 2010, Ngong Ping 360 Limited received ISO 9001:2008 certification and for the year, the cable car system achieved a reliability rate of over 99%. The service won a large number of awards, including The Pacific Asia Travel Association (PATA) Gold Award 2010 in the "Corporate Environment Programme", and the "Certificate of Quality Tourism Service Scheme" from the Hong Kong Tourism Board.

Investment Properties

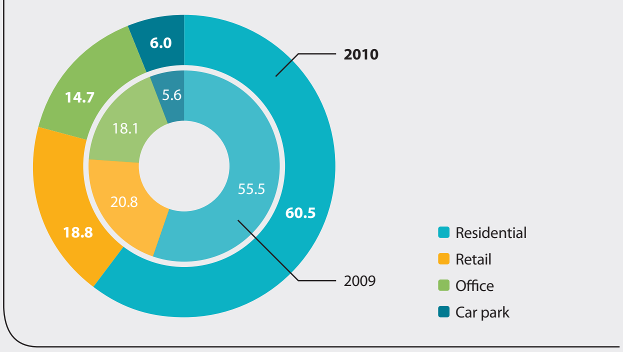
Rental income continued to grow with good rental reversion in shopping malls and increasing retail and office space in Hong Kong.



Distribution of Property Management Income

At the end of the year, the Company had 81,962 residential units and 744,214 sq.m. of commercial properties under management in Hong Kong, and 776,402 sq.m. of managed GFA in Mainland china.

(Percentage)



Facilities such as the Clubhouse at Lake Silver are big attractions to residents

Octopus

Octopus continued its expansion in the retail sector by recruiting more small to medium-sized retail merchants and introducing new applications to provide greater convenience to consumers and businesses. By the end of December, there were over 3,000 Octopus service providers in Hong Kong, including those served by Octopus-appointed acquirers. Cards in circulation were 23.1 million and average daily transaction volume and value were 11.5 million and HK$106.6 million respectively. The Company's share of Octopus' net profit for 2010 was HK$126 million, a decrease of 15.4% from 2009 which was mainly the result of one-off expenses incurred by Octopus relating to the data privacy incident.

Property Development Packages Awarded and to be Completed

Location	Developers	Type	Gross floor area *(sq. m.)*	No. of parking spaces	Period of package tenders	Expected completion date
Kowloon Station						
Package Five, Six and Seven (Elements, International Commerce Centre, The Cullinan, W Hong Kong, The Harbourview Place)	Sun Hung Kai Properties Ltd.	Retail Office Service apartment Hotel Residential Kindergarten Car park	82,750 231,778 72,472 95,000 21,300 1,045	1,683	Awarded in September 2000	Completed By phases from 2006-2010
Tseung Kwan O Station						
Area 56	Sun Hung Kai Properties Ltd.	Residential Hotel Retail Office Car park	80,000 58,130 20,000 5,000	360	Awarded in February 2007	By phases from 2011-2012
LOHAS Park Station						
Package Two (Le Prestige)	Cheung Kong (Holdings) Ltd.	Residential Kindergarten Car park	309,696 800	905	Awarded in January 2006	By phases from 2010-2012
Package Three	Cheung Kong (Holdings) Ltd.	Residential Kindergarten Car park	128,544 1,000	350	Awarded in November 2007	2013
Tai Wai Maintenance Centre						
Festival City	Cheung Kong (Holdings) Ltd.	Residential Car park	313,955	745	Awarded in April 2006	By phases from 2010-2011
Che Kung Temple Station	New World Development Co. Ltd.	Residential Retail Kindergarten Car park	89,792 193 670	232	Awarded in April 2008	2012
Austin Station						
Sites C and D	New World Development Co. Ltd. Wheelock Properties Limited	Residential Car park	119,116	592	Awarded in March 2010	2014
Tuen Mun Station#	Sun Hung Kai Properties Ltd.	Residential Retail Car park	119,512 25,000	340	Awarded in August 2006	By phases from 2012-2013
Tsuen Wan West Station TW7#	Cheung Kong (Holdings) Ltd.	Residential Car park	113,064	444	Awarded in September 2008	2013

as agent for the Government of HKSAR

Property Development Packages to be Awarded Notes 1 and 2

Location	No. of packages envisaged	Type	Gross floor area *(sq. m.)*	Expected no. of parking spaces	Period of package tenders	Expected completion date
LOHAS Park Station	6 – 10	Residential	1,025,220 – 1,035,220		2012-2016	2020
		Retail	39,500 – 49,500			
		Car park		3,303 (max)		
Tai Wai Station	1 – 2	Residential	190,480		2011	2016
		Retail	62,000			
		Car park		801		
Tin Shui Wai Light Rail (Tin Wing Road)	1	Residential	91,051		2011	2016
		Retail	205			
		Car park		267		

Notes:

1. Property development packages for which we are acting as agent for the Government of HKSAR are not included.
2. These property development packages are subject to review in accordance with planning approval, land grant conditions and completion of statutory processes.

Pre-sales of Phase 1 and Phase 2 of Festival City were launched in 2010

Investment Property Portfolio in Hong Kong (as at 31 December 2010)

Location	Type	Lettable floor area *(sq. m)*	No. of parking spaces	Company's ownership interest
Telford Plaza I, Kowloon Bay, Kowloon	Shopping centre	39,510	–	100%
	Car park	–	993	100%
Telford Plaza II, Kowloon Bay, Kowloon	Shopping centre	19,285	–	50%
	Car park	–	136	50%
Luk Yeung Galleria, Tsuen Wan, New Territories	Shopping centre	11,224	–	100%
	Car park	–	651	100%
Paradise Mall, Heng Fa Chuen, Hong Kong	Shopping centre	18,772	–	100%
	Wet market	1,216	–	100%
	Car park	–	415	100%
Maritime Square, Tsing Yi	Shopping centre	28,843	–	100%
	Kindergarten	920	–	100%
	Car park	–	220	100%
	Motorcycle park	–	50	100%
The Lane, Hang Hau	Shopping centre	2,629	–	100%
	Car park	–	16	100%
	Motorcycle park	–	1	100%
The Edge, Tseung Kwan O	Shopping centre	7,621	–	70%
	Car park	–	50	70%
G/F, No. 308 Nathan Road, Kowloon	Shop unit	70	–	100%
G/F, No. 783 Nathan Road, Kowloon	Shop unit	36	–	100%
New Kwai Fong Gardens, Kwai Chung, New Territories	Kindergarten	540	–	100%
	Car park	–	126	100%
International Finance Centre (IFC), Central, Hong Kong				
– Two IFC	Office	39,404	–	100%
– One and Two IFC	Car park	–	1,308	51%
Phase I, Carpark Building, Kornhill, Quarry Bay, Hong Kong	Car park	–	292	100%
Roof Advertising Signboard, Admiralty Centre, No. 18 Harcourt Road, Hong Kong	Advertising signboard	–	–	100%
Ten Shop Units, First Floor Podium, Admiralty Centre, No. 18 Harcourt Road, Hong Kong	Shop unit	286	–	50%
Olympian City One, Tai Kok Tsui, Kowloon	Indoor sports hall	13,219	–	100%
Olympian City Two, Tai Kok Tsui, Kowloon	Shop unit	1,252	–	100%
Choi Hung Park & Ride Public Car Park, No. 8 Clear Water Bay Road, Choi Hung, Kowloon	Car park	–	54	51%
	Motorcycle park	–	10	51%
	Park & ride	–	450	51%
Elements, No. 1 Austin Road West, Kowloon	Shopping centre	44,745	–	81%
	Car park	–	898	81%
Cross Border Coach Terminus, No. 1 Austin Road West, Kowloon	Coach terminus	5,113	–	100%
Kindergarten, No. 1 Austin Road West, Kowloon	Kindergarten	1,045	–	81%
Plaza Ascot, Fo Tan	Shopping centre	7,551	–	100%
Royal Ascot, Fo Tan	Residential	2,784	–	100%
	Car park	–	20	100%
Ocean Walk, Tuen Mun	Shopping centre	6,111	–	100%
	Car park	–	32	100%
Sun Tuen Mun Shopping Centre, Tuen Mun	Shopping centre	8,985	–	100%
	Car park	–	421	100%
Hanford Plaza, Tuen Mun	Shopping centre	1,950	–	100%
	Car park	–	22	100%
Retail Floor and 1-6/F., Citylink Plaza, Sha Tin	Shopping centre	11,954	–	100%
Portion of G/F and portion of 1/F, MTR Hung Hom Building, Hung Hom	Office	1,686	–	100%
The Capitol, LOHAS Park*	Shop Unit	391	–	100%
Le Prestige, LOHAS Park	Kindergarten	800	2	100%

* At The Capitol, there is also a Residential Care Home for the Elderly having a gross floor area of 3,100 square metres.

Investment Property Portfolio in Hong Kong (as at 31 December 2010) *(continued)*

All Properties are held by the Company and its subsidiaries under Government Leases for over 50 years except for:

- Telford Plaza I and II, Luk Yeung Galleria, Maritime Square, New Kwai Fong Gardens, IFC, Olympian City, Elements, Cross Border Coach Terminus and Kindergarten at No. 1 Austin Road West, Plaza Ascot, Royal Ascot, Ocean Walk, Sun Tuen Mun Shopping Centre and Hanford Plaza where the Government Leases expire on 30 June 2047
- Choi Hung Park & Ride where the Government Lease expires on 11 November 2051
- The Lane where the Government Lease expires on 21 October 2052
- The Edge where the Government Lease expires on 27 March 2052
- Citylink Plaza and MTR Hung Hom Building where the Government Leases exprie on 1 December 2057
- LOHAS Park where the Government Lease expires on 16 May 2052

Properties held for sale (as at 31 December 2010)

Location	Type	Gross floor area *(sq.m.)*	No.of parking spaces	Company's ownership interest
Island Harbourview, No. 11 Hoi Fai Road, Kowloon	Car park	–	579	40%
Olympian City One, No. 11 Hoi Fai Road, Kowloon	Shopping centre	6,042*	–	40%
	Car park	–	330	40%
Bank of China Centre, No. 11 Hoi Fai Road, Kowloon	Car park	–	117	40%
The Arch, No. 1 Austin Road West, Kowloon	Residential	857	–	38.5%
	Car park	–	15	38.5%
Residence Oasis, No. 15 Pui Shing Road, Hang Hau, Tseung Kwan O	Car park	–	144	71%
	Motorcycle park	–	18	71%
The Grandiose, No. 9 Tong Chun Street, Tseung Kwan O	Car park	–	65	70%
	Motorcycle park	–	24	70%
Harbour Green, No. 8 Sham Mong Road, Kowloon	Car park	–	47	35%
	Kindergarten	1,299	–	50%
Caribbean Coast, No. 1 Kin Tung Road, Tung Chung	Car park	–	12	20%
Coastal Skyline, No. 12 Tung Chung Waterfront Road, Tung Chung	Car park	–	146	20%
The Palazzo, No. 28 Lok King Street, Shatin	Residential	13,402	–	55%
	Retail	2,000	–	55%
	Car park	–	239	55%
	Motorcycle park	–	15	55%
Lake Silver, No. 599, Sai Sha Road, Shatin	Residential	10,871	–	93%
	Retail	3,000	–	93%
	Kindergarten	1,000	–	93%
	Car park	–	309	93%
	Motorcycle park	–	36	93%
Le Prestige, LOHAS Park, Tseung Kwan O	Car park	–	337	52.93%

* Lettable floor area

Managed properties in Hong Kong (as at 31 December 2010)

Number of managed residential flats	81,962 units
Area of managed commercial and office space	744,214 sq.m.


Hong Kong
railway network
to expand
56km
by 2020

FORGING AHEAD
INTO A BRIGHT FUTURE

New excavation techniques on West Island Line helped **minimise noise and dust**

South Island Line (East) will **cut travel time and traffic congestion**

Hong Kong Network Expansion

Shatin to Central Link will strengthen the linkage between the New Territories and Hong Kong Island

Express Rail Link will enhance connectivity with the Mainland

We made good progress during the year on the five major projects now under way to extend our railway network in Hong Kong, namely the West Island Line, South Island Line (East), Kwun Tong Line Extension, Express Rail Link and Shatin to Central Link.

West Island Line

The West Island Line is a 3-km extension of the Island Line which is targeted for completion in 2014. When complete, it will reduce travel time from Kennedy Town to Sheung Wan to eight minutes. The project team has made every effort to integrate community views in order to preserve the local heritage and create opportunities for urban renewal.

All civil works contracts for this project were awarded by April 2010 and the civil infrastructure works for the Kennedy Town Swimming Pool (Phase 1) and the David Trench Rehabilitation Centre were substantially completed by the end of 2010. A pioneering feature of the project has been the use of electronic detonators with water as ballast to absorb the pressure from blasting to excavate the construction shaft at the King George V Memorial Park at Sai Ying Pun. This not only enabled the shaft excavation to be completed two months ahead of schedule but also reduced noise and dust impacts on the area to an absolute minimum.

A substantial number of the contracts for the Electrical & Mechanical (E&M) works had also been awarded by the end of 2010 and mobilisation of contractors' resources has commenced.

South Island Line (East)

The 7-km South Island Line (East) will provide passenger service between Admiralty and South Horizons. Government published the gazette amendment for the scheme on 4 June 2010 and the project was authorised by the Executive Council on 30 November 2010. The Environmental Impact Assessment (EIA) Report was approved by the Environmental Protection Department (EPD) in October 2010, followed in December by the issue of the Environmental Permit.

The detailed design for the project has been substantially completed and procurement of four of the six major civil works contracts is in progress. Discussions with the public and other stakeholders are continuing.

Kwun Tong Line Extension

The 3-km Kwun Tong Line Extension will run from Yau Ma Tei Station on the Kwun Tong Line to the new Whampoa Station via the new Ho Man Tin Station, which will become an interchange station with the Shatin to Central Link. An amendment to the railway scheme was gazetted on 25 June 2010 and the project was authorised by the Executive Council on 30 November

SUSTAINABLE GROWTH
OF HONG KONG

2010. The EIA Report was approved by the EPD in August 2010, followed in September by the issue of the Environmental Permit. The detailed design for the project has been substantially completed and procurement of the civil construction contracts is now in progress.

Express Rail Link

The 26-km Express Rail Link will provide high speed cross-boundary rail services connecting Hong Kong to Shenzhen, Guangzhou and the Mainland of China's high speed intercity passenger rail network.

Construction started in January 2010 and has made good progress, including diaphragm walls and piling works at the West Kowloon Terminus, with 80% of foundation work having been completed by year end. By October 2010, orders for all six tunnel boring machines had been placed and all ten tunnel contracts had been awarded. In November 2010, we conducted the first tunnel blast at the Shek Yam construction adit. Project completion is expected in 2015.

The Express Rail Link will connect to the Mainland of China's high speed rail network

Shatin to Central Link

The Shatin to Central Link comprises two sections. An 11-km extension of the Ma On Shan Line from Tai Wai to Hung Hom will connect with the West Rail Line to form an East West corridor. A 6-km extension of the East Rail Line from Hung Hom to Hong Kong Island will become Hong Kong's fourth rail harbour crossing to form a North South corridor. The Shatin to Central Link scheme was gazetted on 26 November 2010.

Further consultation has been undertaken with local communities and other stakeholders, including District Councils,

Civil works on the West Island Line are well under way

The Shatin to Central Link will provide an important new cross-harbour route

with a website set up as a mass communication platform to gather views for integration into the station designs and construction planning of the project. The detailed design for the Tai Wai to Hung Hom section is well under way and the preliminary designs for the E&M systems have been completed. Detailed design for the Hung Hom to Hong Kong Island section will commence in 2011. In order to preserve the scheme alignment for the cross harbour section, protection works are being incorporated in the Wan Chai Development Phase II and Central-Wan Chai Bypass projects which are currently under construction by Government.

Project Funding Model

The funding model for our five new Hong Kong rail projects will take different forms, each carefully designed for the project in question.

The West Island Line, which will be owned by the Company, will use the capital grant model. An initial HK$400 million of this grant was received from Government in 2008 and the balance of HK$12,252 million was received in March 2010.

The South Island Line (East) and Kwun Tong Line Extension, both to be owned by the Company, will use our proven "Rail plus Property" model. Discussions continue with Government on the amount of property development rights required to ensure the viability of these two projects. For the South Island Line (East), the proposal to zone the Wong Chuk Hang site, which will be used for the depot, into a Comprehensive Development Area for integrated property development, was agreed by the Town Planning Board in June 2010. Formal approval under the Town Planning Ordinance is expected later in 2011. For the Kwun Tong Line Extension, it is proposed to use property development rights above Ho Man Tin Station to bridge the funding gap.

The "Service Concession" model will be adopted for the Express Rail Link and Shatin to Central Link. Under this model, Government will pay all the capital cost of the line, with the Company being responsible for operations, maintenance and asset renewals and replacement. The Finance Committee of the Legislative Council approved the funding of HK$66.9 billion (in money-of-the-day prices) for construction of both railway and non-railway works of the Express Rail Link on 16 January 2010.

Under the Entrustment Agreement signed with Government on 26 January 2010, we are responsible for the planning, design, construction, testing and commissioning of the Express Rail Link, for which the Company will be paid a total project management fee of HK$4,590 million. Furthermore, there is the understanding that Government will invite the Company to undertake the operations of the railway after its completion. The operational requirements and operational business model of the Express Rail Link are under active discussion with Government and Mainland entities. For the Shatin to Central Link, we continue further planning and design work funded by Government under an Entrustment Agreement signed in November 2008. On 18 February 2011, the advanced funding for the construction of the Shatin to Central Link's share of Admiralty Station and Ho Man Tin Station was approved by the Finance Committee of Legislative Council.

Hong Kong Network Expansion at a Glance

Network Extensions	Estimated Route Length	Project Funding
West Island Line	3 km	Capital Grant
South Island Line (East)	7 km	Rail plus Property
Kwun Tong Line Extension	3 km	Rail plus Property
Express Rail Link	26 km	Service Concession
Shatin to Central Link		
– Tai Wai to Hung Hom	11 km	Service Concession
– Hung Hom to Hong Kong Island	6 km	

A new 20,000 sq.m Admiralty Station will interconnect four existing and future MTR lines

AN EVER EXPANDING HORIZON

Took over
operations of Phase 1 of
Shenzhen Metro Line 4
on 1 July

644.5 km
of total route length of
railway operations
outside of Hong Kong

Mainland and Overseas Growth

Major investment to improve reliability of the

Melbourne network

Refurbished and extended

East London Line

opened in May

"Total passengers carried by our rail subsidiaries and associates outside of Hong Kong was close to 850 million in 2010."

The Company's rail businesses outside of Hong Kong represent an opportunity to enhance profits and expand operations.

In 2010, our operating railway businesses outside of Hong Kong comprised of our 49% interest in Beijing MTR Corporation Limited (BJMTR), which operates the Beijing Metro Line 4 (BJL4), and our 100% interest in MTR Corporation (Shenzhen) Limited (SZMTR) which operates the Shenzhen Metro Line 4 (SZL4), both in the Mainland of China, our 60% interest in Metro Trains Melbourne Pty. Ltd. (MTM) in Australia, our 100% interest in MTR Stockholm AB (MTRS) in Sweden, our 50% interest in Tunnelbanan Teknik Stockholm AB (TBT), which maintains rolling stock for MTRS, and our 50% interest in London Overground Rail Operations Limited (LOROL) in the UK.

Revenue from railway subsidiaries outside of Hong Kong, MTM, MTRS and SZMTR, was HK$10,144 million. Operating costs were HK$9,865 million, yielding an operating profit of HK$279 million and an operating profit margin of 2.8%. As operation and maintenance franchises, MTM and MTRS require modest capital investment and hence operating margins will typically be much lower than more capital intensive projects. SZMTR, which commenced operations of SZL4 Phase 1 on 1 July 2010 made an operating loss of HK$41 million in 2010. This was as expected, since the scale of business will be sub-optimal until the opening of Phase 2, which is expected in the middle of 2011. Although financial performance for MTM has been encouraging, with an operating profit of HK$326 million, MTRS has not met expectations financially. MTRS incurred an operating loss in the

EXPLORING NEW DESTINATIONS

year of HK$6 million, and measures have been implemented to enhance profitability. BJMTR, LOROL and TBT are accounted for as associates, and contributed a total of HK$22 million in post-tax profit in 2010, ahead of expectations. Our share of the post-tax profits from LOROL was HK$18 million, while BJMTR and TBT contributed profits of HK$1 million and HK$3 million respectively.

Total passengers carried by our rail subsidiaries and associates outside of Hong Kong was close to 850 million in 2010.

Mainland of China

BJL4's ridership in 2010 exceeded 250 million passenger trips, higher than expected. On 1 May 2010, the line reported a record ridership of 1 million passenger trips.

Performance in terms of average train service availability and punctuality has exceeded targets. In August, we were honoured by the visit of Chinese Vice President Xi Jinping, Beijing Party Secretary Liu Qi and Beijing Mayor Guo Jinlong, who joined regular commuters on the line to experience the train service.

Preparation works progressed well throughout the year on the 22-km Daxing Line, the extension of BJL4 to the district of Daxing, enabling it to open as planned on 30 December 2010. BJMTR has an operating and maintenance contract for the Daxing Line.

In November 2010, a Memorandum of Understanding (MOU) was signed with Beijing Infrastructure Investment Company Limited and Beijing Airport Express Rail Company Limited to provide a study on using wider Type A train cars and related facilities for the future Beijing Metro Line 16.

In Shenzhen, SZMTR took over the operations of the five-station 4.5-km Phase 1 of SZL4 on 1 July 2010, following finalisation of the concession agreement in March 2009. Performance in terms of average train service delivery and punctuality rates was above target. The average daily passenger trips of 65,000 was also above expectation.

Construction work on the ten-station 16-km Phase 2 of SZL4 has made good progress with rolling stock manufacturing well under way. Full line operation, encompassing Phase 1 and Phase

LOROL in London provides excellent services and enhances connectivity in the area

2, is expected to commence in the middle of 2011. In July 2010, the Company signed an MOU with Shenzhen Line 3 Investment Company to participate in the feasibility, land and planning study, and investment study for the future Shenzhen Metro Line 6.

In March 2010, our subsidiary, MTR Hangzhou Line 1 Investment Company Limited, together with a subsidiary of Hangzhou Metro Group Company Limited, signed a concession agreement with the Hangzhou Municipal Government to undertake a Public-Private-Partnership (PPP) project for the investment in, construction and operation of the 48-km Hangzhou Metro Line 1 (HZL1) for a term of 25 years. The total investment required is RMB22 billion, 37% (or RMB 8.3 billion) of which will be provided by a joint venture company in which MTR Corporation has an effective interest of 49%, with the remaining 51% owned by a subsidiary of the Hangzhou Metro Group Company Limited. The balance of the total investment will be funded by the Hangzhou Municipal Government. As the joint venture company will be leveraged, MTR Corporation's equity investment is estimated to be RMB2.2 billion. Civil construction work commenced on HZL1 in March 2007 and the line is expected to open in 2012. The agreement is currently pending regulatory approval from the Central Government.

With key personnel changes at our major stakeholders in Shenyang, including its municipal Government, our 49% owned Shenyang operation and maintenance joint venture has been presented with serious obstacles and is prevented from delivering on the proposed scope of its contract. We are in discussions with the relevant Shenyang parties to resolve this matter, which will lead to our withdrawal from Shenyang. Our

SZMTR took over the operations of the five-station 4.5-km Phase 1 of SZL4 on 1 July 2010 investment relating to the joint venture comprise mainly staff costs employed by or supporting the joint venture company and is written off in the 2010 accounts.

Overseas

In the UK, the introduction of new trains on all routes during the year contributed to further service improvements at LOROL, whilst performance remains above target. In May 2010, LOROL started full passenger services on the refurbished and extended East London Line, from Dalston Junction to West Croydon and Crystal Palace, increasing the overall route length from 85 km to 110 km. A station investment programme is under way to upgrade and renovate stations, and to counter fare evasion, ticket inspections have been stepped up, and follow-up procedures against offenders tightened. LOROL carried approximately 200,000 passengers a day in 2010.

MTRS in Stockholm has steadily improved operational performance since the start of operations in November 2009. Performance in terms of average train service punctuality and the number of service stoppages was above target. MTRS carries approximately 1.1 million passengers per day.

In Melbourne, MTM encountered a number of operational issues in the first half of the year, leading to poor operational performance. Measures were immediately taken to rectify this situation, resulting in improved performance in the second half of the year. These actions included operational changes such as the introduction of new dwell time management procedures at key locations, as well as asset related measures designed to enhance the infrastructure and train fleet reliability. MTM carried an average of 700,000 passengers a day in 2010.

In December, the Daxing Line was opened as the extension of BJL4

Also in Australia, we submitted a bid in November 2010 to operate and maintain a light rail project in Australia's Gold Coast. The bid was submitted in conjunction with a consortium comprising John Holland Pty. Ltd., ITOCHU Corporation and The Royal Bank of Scotland Group (Australia) Pty. Ltd., with the consortium being responsible for the construction of the system.

Mainland of China and Overseas Railway Businesses at a Glance

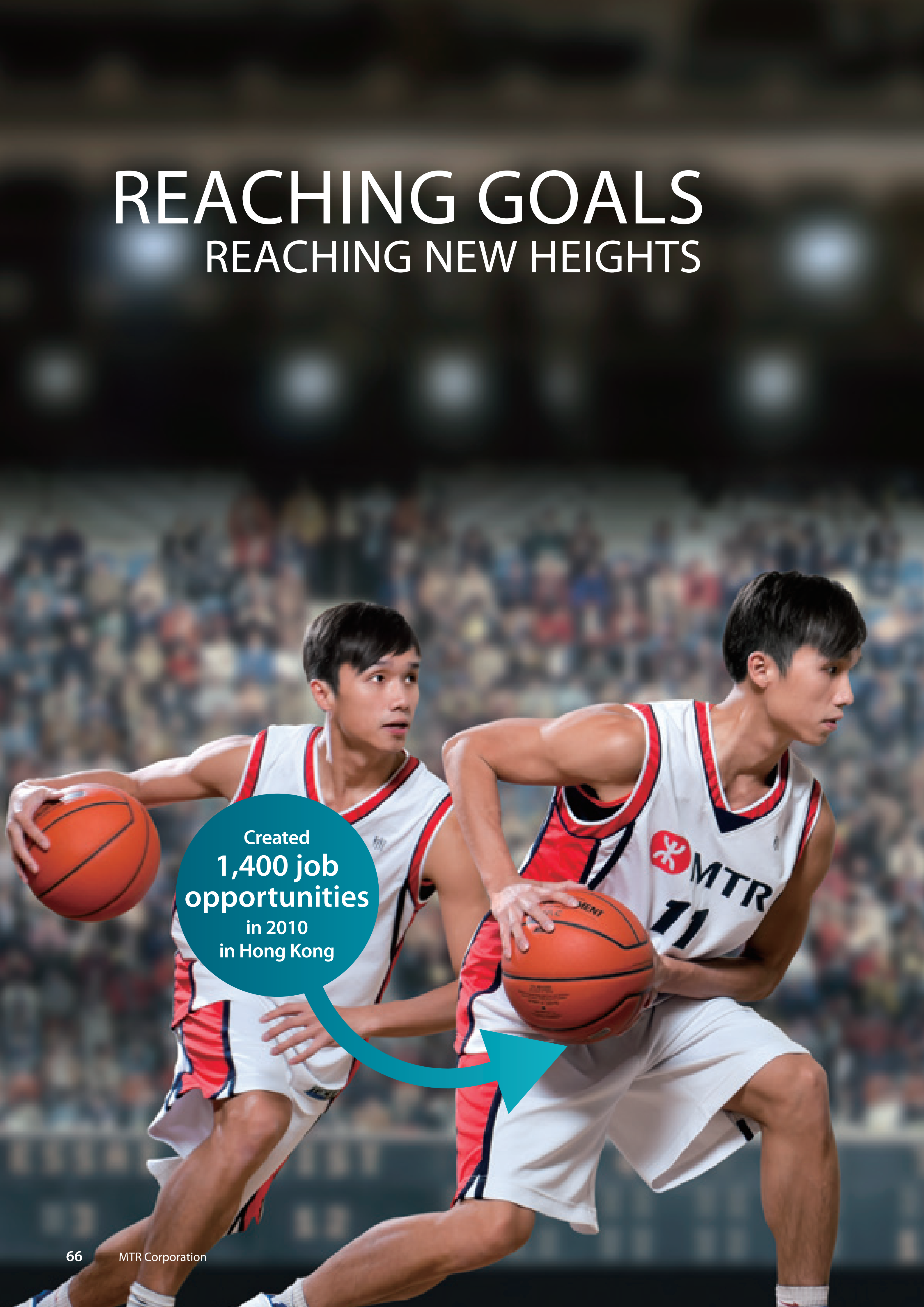
	In Operation						Pending Finalisation of Agreement
	Beijing Metro Line 4 (BJL4), Mainland of China	Daxing Line of BJL4, Mainland of China	Shenzhen Metro Line 4, Mainland of China	London Overground, United Kingdom	Stockholm Metro, Sweden	Melbourne Metro, Australia	Hangzhou Metro Line 1, Mainland of China#
MTR Corporation Shareholding	49%	49%	100%	50%	100%	60%	49%
Business Model	Public-Private-Partnership (PPP)	Operations and Maintenance (O&M) Concession	Build-Operate-Transfer (BOT)^	O&M Concession	O&M Concession*	O&M Concession	PPP
Commencement of Franchise/Expected date of commencement of operation	Sep 2009	Dec 2010	Phase 1: Jul 2010 Phase 2: Mid 2011	Nov 2007	Nov 2009	Nov 2009	2012
Franchise/Concession Period	30 Years	10 Years	30 Years	7 Years	8 Years	8 Years	25 Years
Number of Stations	24	11	Phase 1: 5 Phase 2: 10	55	100	213	31
Routh length *(km)*	28	22	Phase 1: 4.5 Phase 2: 16	110	108	372	48

* Rolling stock maintenance under a 50:50 joint venture between MTR Stockholm and Mantena AS.

The Concession Agreement with Hangzhou Municipal Government is subject to approval by relevant authorities in the Mainland of China.

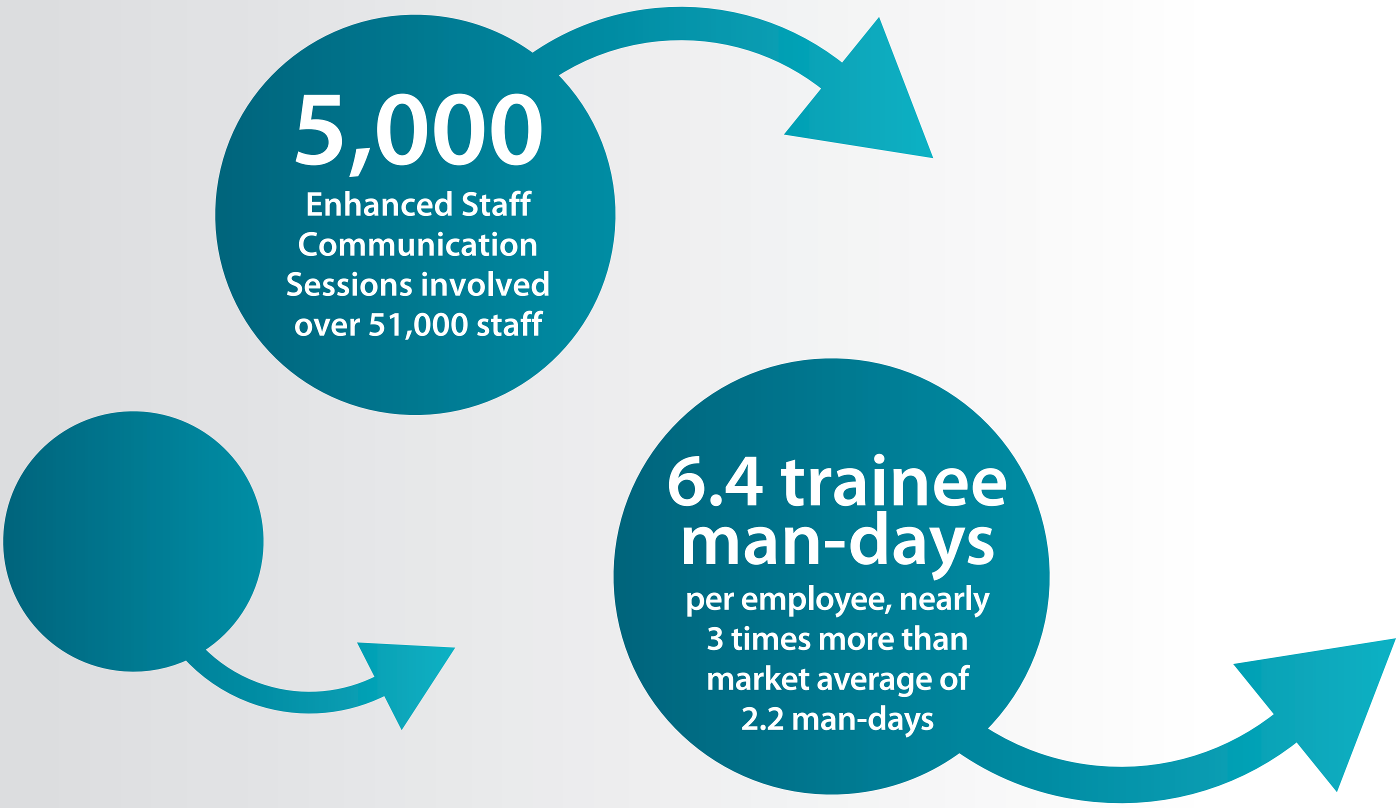
^ Shenzhen Metro Line 4 Phase 1 assets are owned by the Shenzhen Municipal Government and MTR Corporation (Shenzhen) Ltd took over the operation of Phase 1 in Jul 2010.

REACHING GOALS
REACHING NEW HEIGHTS




198
More Time Reaching Community projects with about 4,400 volunteers
Low voluntary staff turnover rate of
2.6%

Human Resources



Meeting the human resource needs of our business is a vital component of our overall success. Our staffing levels have increased significantly in recent years, keeping pace with our business expansion in both Hong Kong and other markets. As at 31 December 2010, 20,501 people were employed by the Company and our controlled subsidiaries. Meeting the staffing challenge will be one of our priorities in the years ahead. The five network expansion projects in Hong Kong alone will require over 1,000 additional Projects staff at the peak of the construction period in 2013. Proactive recruitment planning, appropriate training and open communication helps the Company to attract and retain the people we need and underpin the harmonious staff relations we enjoy.

Support for Expansion

We have formulated and put in place human resources planning and recruitment strategies to attract the right talents. Our employer branding programme has been strengthened, attracting potential professionals to register their interest in employment early.

To meet the challenge of recruiting professionals in specialised disciplines where there is a local shortage, such as geotechnical and tunnelling engineering, we have increased our focus on recruitment outside of Hong Kong.

As a result of our efforts, over 1,000 vacancies for the operating railway in Hong Kong were filled during the year, and 430 new recruits hired for the Projects Division. Recruitment for our graduate and apprentice schemes was also increased to support our business expansion. The number of graduate engineers recruited in 2010 increased to 29, and the intake of apprentices rose to 71. We also continued with our annual intake of graduate engineers and operating management associates in the Mainland of China to support business there.

Staff retention continues to be effected through various career advancement and development opportunities for high calibre staff. Competitive employment terms and conditions also contributed to high staff loyalty.

A number of schemes are in place to motivate staff through increasing their identification with the Company and our vision,

ACHIEVING SUCCESS
BUILDING A STRONG TEAM

mission and values, or "VMV". Key among these are the "Living the MTR Values Award Scheme" and "VMV Heroes", programmes that allow staff contributions to be recognised and rewarded on the spot, as well as staff motivational videos such as the five-part series "MTR People Making a Difference".

Staff Consultation

The Company's staff consultation mechanism, involving staff representatives, continues to provide an effective channel for management to listen to and address employees' concerns. The voting rate for the election of staff representatives in 2010 was 78%, indicating the high level of participation which the mechanism enjoys.

Two-way communication has been reinforced by an "Enhanced Staff Communication" programme in the Operations Division starting in January 2010. The programme allows the Company to identify and address staff concerns at an early stage through line mangers' direct communication with staff on the shop floor. Over 5,000 communication sessions involving more than 51,000 participants were conducted during the year.

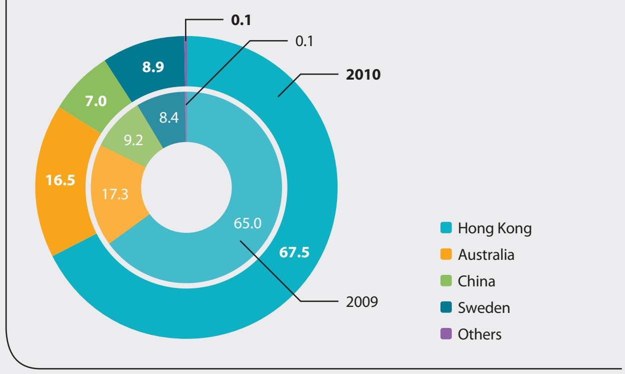
Training and Development

With a view to building and nurturing a learning culture, we strive to train and develop our people, to ensure they are well equipped to meet the business challenges ahead and that they align their personal goals with the Company's vision.

During 2010, more than 5,396 training courses were delivered across the Company covering approximately 6.4 trainee man-days per employee.

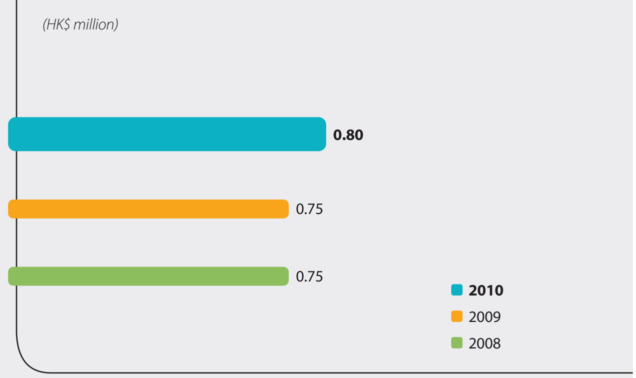
A comprehensive training programme was put in place for our intake of graduate engineers. The programme provided young engineers with all-round exposure in various engineering disciplines through job attachments, on-the-job training and project-based assignments under the guidance of senior managers acting as supervisors and mentors. In addition, the Integrated Staff Development Programme provided training for 222 employees in 2010 to enhance supervisory capability and meet the succession needs of the Company. With a strong commitment to invest in human capital, the Company continued to receive recognition in training excellence by winning both local and international awards.

Staff Distribution By Geographical Location



Staff Productivity – Earnings Per Employee*

* Hong Kong businesses excluding property development



Leadership Development

In addition to providing general, technical and competency-based training, the Company recognises the importance of identifying and grooming talented individuals for future leadership roles.

An important component of leadership development is the Executive Associate Scheme which was initiated in 2006. The first batch of 11 Executive Associates completed their three-year development programme in early 2010 and assumed higher responsibilities. Their feedback on the programme was positive and they showed great appreciation for the support they had received from the departments to which they had been assigned. During 2010, the third batch of 11 supervisors and junior managers was selected to join the programme.

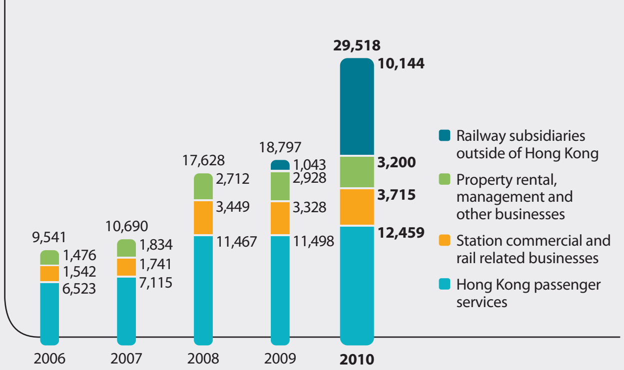
In parallel with the scheme, the first batch of Graduate Trainees recruited in 2007 completed their three years of intensive on-the-job, experiential and all-round training in 2010. This enabled their advancement to senior supervisory level positions and equipped them with both functional knowledge and managerial skills.

Various activities were launched to promote the Company's Vision, Mission and Values

Financial Review

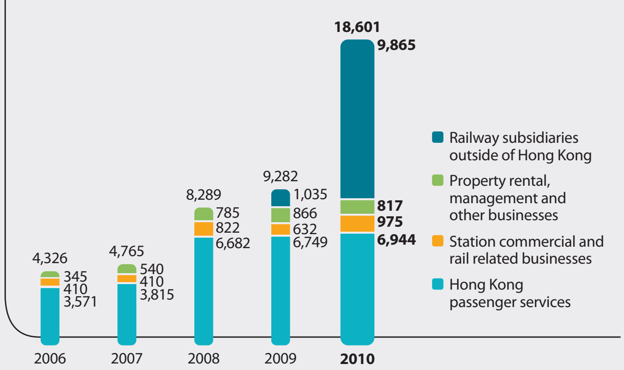
Turnover

Growth in turnover was recorded in all businesses in 2010 coupled with full-year contribution from railway subsidiaries outside of Hong Kong.



Operating Expenses

Excluding railway subsidiaries outside of Hong Kong, expense increase in 2010 was 5.9% as compared with a turnover increase of 9.1%.



Review of 2010 Financial Results

Profit and Loss

MTR leveraged off the rebound in the Hong Kong economy to record a strong financial performance in 2010.

In Hong Kong, total fare revenue in 2010 increased by 8.4% to HK$12,459 million resulting from patronage growth brought by the economic rebound and the full year impact of LOHAS Park and Austin Stations, which both opened in mid-2009, as well as a fare rise effective 13 June 2010 for those services subject to the Fare Adjustment Mechanism (FAM). Fare revenue for the Domestic Service increased by 8.5% to HK$8,668 million with patronage growth of 6.6% to 1,299 million and average fare increase of 1.9% to HK$6.67. Fare revenue for the Cross-boundary Service increased by 6.9% to HK$2,487 million with 6.3% growth in patronage to 100 million and 0.5% increase in average fare to HK$24.89. For the Airport Express, which is not subject to the FAM, fare revenue grew by 12.5% to HK$694 million with 12.9% increase in patronage to 11 million partly offset by a 0.3% decrease in average fare to HK$62.28. Light Rail, Bus and Intercity also recorded increases in fare revenue by 7.4% in total to HK$610 million.

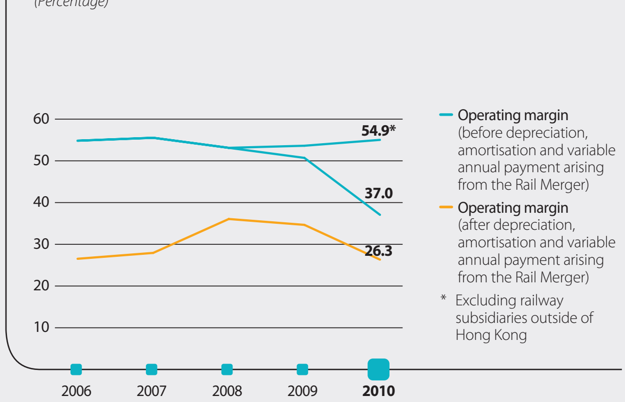
Revenue from station commercial and rail related businesses in 2010 increased by 11.6% to HK$3,715 million mainly attributable to the strong recovery of the advertising business, which reported 22.9% growth in revenue to HK$734 million, as well as favourable rate and rentable area increases in the station retail business, which recorded 6.9% increase in revenue to HK$1,716 million. Telecommunication income increased steadily by 6.2% to HK$290 million while other miscellaneous incomes, such as publications and souvenir ticket sales, grew by 4.5% to HK$278 million. These revenue increases were partially offset by decreases of consultancy and freight revenues by 28.9% and 15.6% respectively following the completion of certain consultancy works and termination of the freight business. Revenues from KCRC and the Government, mainly in respect of the entrustment works for the Express Rail Link (XRL) commencing in 2010 and project management for the Kowloon Southern Link, amounted to HK$557 million, up 40.7% from last year.

Rental, management and other revenue in 2010 increased by 9.3% to HK$3,200 million. Whilst good rental reversions for investment properties in Hong Kong contributed to the growth in property rental and management income by 7.5% to HK$2,961 million, the increases in tourists and demand for the "crystal cabin" led to a strong growth in revenue for Ngong Ping 360 with revenues increasing by 38.2% to HK$239 million.

Revenues from railway subsidiaries outside of Hong Kong in 2010 amounted to HK$10,144 million, comprising HK$2,858 million from the Stockholm Metro and HK$7,239 million from Melbourne Metropolitan Train, both of which we took over in

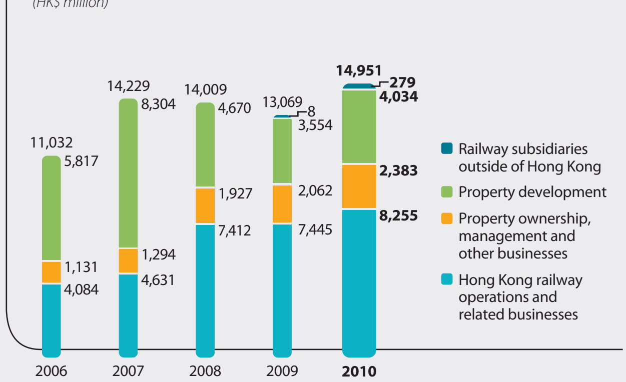
Operating Margin

Steady growth in operating margin excluding railway subsidiaries outside of Hong Kong has been achieved since the Rail Merger.



Operating Profit Contributions

While Hong Kong railway operations and related businesses continued to be the majority profit contributor, railway subsidiaries outside of Hong Kong contributed 1.9% of profit in 2010.



November 2009, and HK$47 million from Phase 1 of Shenzhen Metro Line 4 (SZL4), which MTR took over on 1 July 2010. Total revenue for the Group in 2010 including these subsidiaries therefore increased by 57.0% to HK$29,518 million. Excluding these subsidiaries outside of Hong Kong, revenue grew by 9.1%.

Total operating expenses before depreciation, amortisation and variable annual fee payable as part of the service concession payment to KCRC increased by 100.4% to HK$18,601 million mainly due to the expansion of the railway operations outside of Hong Kong. Excluding operating costs on railway subsidiaries outside of Hong Kong of HK$9,865 million, the growth in operating expenses would have been 5.9%. The major cost increases came from the Express Rail Link entrustment work costs, full-year operation of the LOHAS Park and Austin Stations as well as higher advertising agency fees, Octopus card transaction fees and operating expenses of Ngong Ping 360 in line with revenue growth.

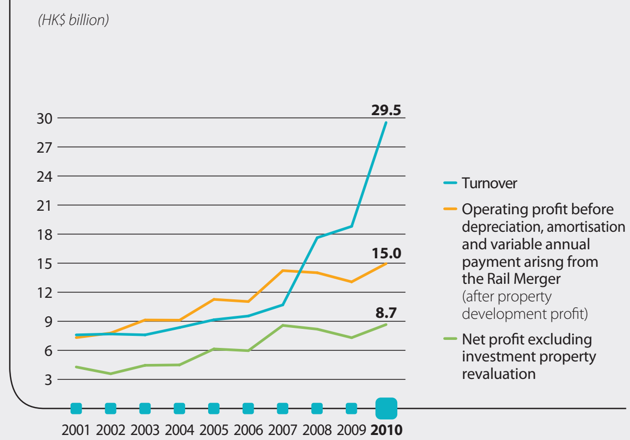
The resulting operating profit from railway and related businesses before depreciation, amortisation and variable annual payment increased by 14.7% to HK$10,917 million. Owing to the full-year operation of the asset-light and lower profit-margin railway subsidiaries in Stockholm and Melbourne, as well as the operating loss of SZL4 Phase 1 for the initial period after we took over operations in July 2010, operating profit margin in 2010 decreased from 50.6% in 2009 to 37.0%. Excluding these railway subsidiaries outside of Hong Kong, profit margin actually increased from 53.5% in 2009 to 54.9% in 2010 with operating profit increasing by 11.9% to HK$10,638 million.

Profit on property development in 2010 increased by 13.5% to HK$4,034 million mainly derived from Le Prestige at LOHAS Park and sale of units in inventory at The Palazzo in Fo Tan and Lake Silver in Wu Kai Sha. After deducting depreciation and amortisation of HK$3,120 million, which increased by 4.3% mainly due to the full-year charge for the LOHAS Park Station, and the one-month provision of variable annual payment of HK$45 million, which started at the end of 2010, being the third anniversary of the Rail Merger, operating profit before interest and finance charges increased by 17.1% to HK$11,786 million.

Interest and finance charges decreased by 17.8% to HK$1,237 million due to the scheduled debt repayment and prepayment of floating rate bank loans with surplus cash, thus resulting in lower outstanding debts. However, the weighted average cost of borrowing, at 4.3%, was higher when compared with 3.7% in 2009. Pre-tax investment property revaluation gain recognised in 2010 was HK$4,074 million. As a result of Octopus's one-off expenditures relating to the data privacy incident, the Group's

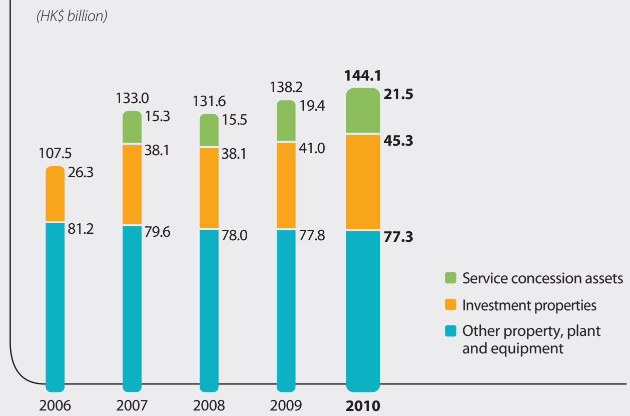
Net Results from Underlying Businesses

Underlying business profit reported a record peak in 2010.



Fixed Assets Growth

Fixed assets increased in 2010 with investment property revaluation gains and recognition of service concession assets relating to Shenzhen Line 4.



share of net profit of non-controlled subsidiaries and associates in 2010 decreased by 13.1% to HK$139 million, comprising profits of HK$126 million from Octopus Holdings Limited and HK$13 million from our rail related associated companies outside of Hong Kong.

Profit before taxation increased by 28.2% to HK$14,762 million. After deducting income tax of HK$2,590 million, profit for 2010 increased by 26.3% to HK$12,172 million, of which HK$12,059 million, an increase of 25.1% from last year, was attributable to equity shareholders of the Company. Earnings per share therefore increased from HK$1.69 in 2009 to HK$2.10 in 2010. Excluding investment property revaluation and the related deferred tax provision, the underlying profit attributable to equity shareholders increased by 18.5% to HK$8,657 million and the corresponding earnings per share increased from HK$1.28 to HK$1.51.

Following our progressive dividend policy, the Board has recommended a final dividend of HK$0.45 per share, which, when added to the interim dividend of HK$0.14 per share, will bring full year dividend to HK$0.59 per share, an increase of HK$0.07 per share or 13.5% compared with last year. The final dividend, amounting to HK$2,598 million in total, offers a scrip dividend option to all shareholders except those with registered addresses in the United States of America or any of its territories or possessions.

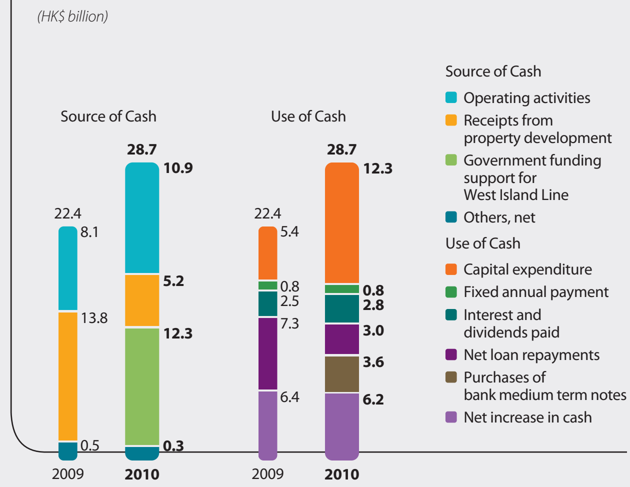
Balance Sheet

As at 31 December 2010, net assets of the Group increased by 10.2% from 2009 year end to HK$117,293 million, attributable to a 2.9% increase in total assets to HK$181,665 million and 8.1% decrease in total liabilities to HK$64,372 million.

On the asset side, total fixed assets increased by HK$5,869 million to HK$144,057 million at 31 December 2010 as a result of the revaluation gain in investment properties and the recognition of service concession assets relating to the takeover of Phase 1 and continued construction progress of Phase 2 of SZL4. Property development in progress increased from HK$6,718 million to HK$9,128 million mainly due to the contribution of land premium for Austin Station Sites C and D partly offset by profit recognition of Le Prestige. Properties held for sale decreased from HK$3,783 million to HK$1,936 million with sales mainly from The Palazzo and Lake Silver during the year. Deferred expenditure relating mainly to the South Island Line (East) and the Kwun Tong Line Extension increased from HK$558 million to HK$1,079 million.

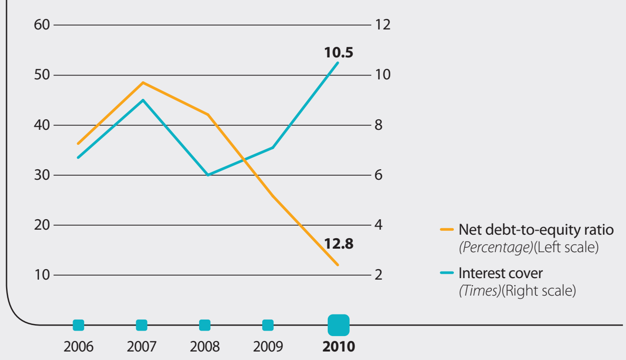
Cash Utilisation

WIL Government funding support received in 2010 was utilised to pay capital expenditures, repay borrowings and purchase bank medium term notes.



Debt Servicing Capability

Interest cover and gearing ratio were further enhanced with the growth in profit and reduction in debts.



During the year, funding support from the Government for the West Island Line (WIL) of HK$12,252 million was received, thus reducing the amounts due from Government and other related parties from HK$12,788 million to HK$330 million and contributing to the additions in investments in securities from HK$227 million to HK$3,912 million and cash, bank balances and deposits from HK$7,115 million to HK$13,334 million. As the cumulative construction costs for the WIL at HK$5,077 million was still below the Government funding support, railway construction in progress at 31 December 2010 continued to report a zero balance. With the full-year operation of overseas railway subsidiaries, debtors, deposits and payments in advance increased from HK$2,428 million to HK$3,057 million.

On the liability side, the major reduction in liabilities came from creditors and accrued charges and total loans outstanding. Creditors and accrued charges decreased from HK$20,497 million at 2009 year end to HK$15,491 million at 31 December 2010 due to the utilisation of WIL Government funding support of HK$3,392 million during the year as well as the transfer to property development profits of HK$2,963 million of pre-sales receipt from Le Prestige, received in 2009, on recognition of development profits in 2010. Total loans outstanding decreased from HK$23,868 million to HK$21,057 million as surplus cash generated were applied to repay debts. These reductions in liabilities were partially offset by an increase in current and deferred tax liabilities of HK$1,638 million to HK$14,872 million, of which HK$1,018 million related to current tax, and an increase in deferred income from HK$167 million to HK$605 million due to the receipt of guaranteed profits in respect of Festival City at Tai Wai.

Share capital, share premium and capital reserve increased by HK$1,237 million to HK$43,734 million at 31 December 2010 resulting from shares issued for scrip dividends and share options exercised. Together with the increase in retained earnings, net of dividends paid, of HK$9,076 million and increase in fixed asset revaluation reserve and other reserves of HK$450 million, total equity attributable to shareholders of the Company increased by HK$10,763 million to HK$117,150 million at 31 December 2010. Including obligations under service concession and loan from holders of non-controlling interests as components of debt and investments in bank medium term notes as component of cash, net debt-to-equity ratio decreased from 25.8% at 2009 year end to 12.8% at 2010 year end.

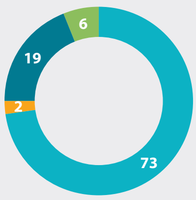
Cash Flow

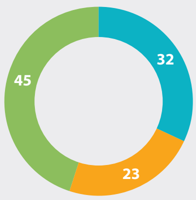
In line with the growth in operating profits, net cash inflow from operating activities of the Group, after cash tax payments, in 2010 increased by 34.5% to HK$10,907 million. During

Sources of Borrowing

Although Hong Kong is our main market, our strategy is to diversify our funding sources and maintain ready access to other important international markets.

(Percentage) (As at 31 December 2010)





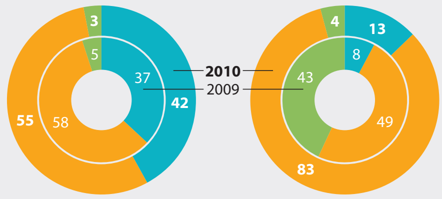
By market
- Hong Kong
- US
- Asia
- Europe

By instrument
- Medium term notes
- US$ Eurobonds
- Bank loans & export credits

Use of Interest Rate and Currency Risk Hedging Products

The Company uses derivative financial instruments for hedging purposes, and has a strict policy of limiting their usage for such purposes only.

(Percentage)* (As at 31 December 2010)



By instrument
- Interest rate swaps
- Cross currency & interest rate swaps
- Foreign exchange forwards

By maturity
- Beyond 5 years
- 2 to 5 years
- Within 2 years

* Calculated based on nominal value

the year, cash receipt in respect of property developments amounted to HK$5,249 million, mainly coming from The Palazzo, Le Prestige and Lake Silver as well as the guaranteed profit for Festival City. Including other cash receipts such as dividends from non-controlled subsidiaries and recovery of Government entrustment work costs, cash inflow in 2010 before accounting for the WIL Government funding support and financing activities was HK$16,322 million.

Cash outflows for capital projects and property developments in 2010 amounted to HK$12,336 million, comprising HK$5,766 million for railway construction projects such as WIL and SZL4, HK$1,953 million for the purchase of Hong Kong railway operational assets and HK$4,617 million for property developments including the land premium for Austin Station Sites C and D of HK$3,900 million. After settlement of the fixed annual payment for the Rail Merger of HK$750 million, net interest payment of HK$757 million, dividend payments of HK$1,872 million and other working capital adjustments, total cash outflows before loan repayment was HK$15,711 million.

Net cash inflow of HK$611 million was generated in 2010 before receipt of the WIL Government funding support. Including the WIL Government funding support of HK$12,252 million received in March 2010, total net cash inflow of the Group before financing activities was HK$12,863 million, of which HK$3,015 million was utilised to reduce debts while HK$3,624 million was invested in bank medium term notes. Cash balance of the Group therefore increased by HK$6,224 million to HK$13,318 million at 31 December 2010.

Financing Activities

Financings

For much of 2010, the US economy grew at a slow rate with all major economic indicators painting a picture of continuing slow growth and high unemployment. To stimulate growth, the US Federal Reserve in the fourth quarter embarked on a second round of quantitative easing measures and the US government extended tax cuts from the previous administration. Against this backdrop, US short-term interest rates remained low whilst longer term rates were volatile. The yield on 10-year US treasuries reached a low of 2.4% p.a. in October but closed the year at 3.3% p.a. with a significantly steepened yield curve.

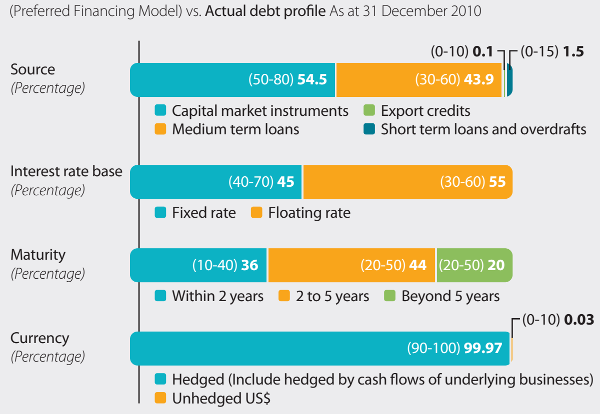
Interest rates in Hong Kong followed the US trends, with 3-month Hibor rate oscillating between 0.12% p.a. and 0.57% p.a., closing the year at 0.28% p.a.. 10-year Hong Kong Exchange Fund Notes yield reached a low of 1.9% p.a. in August and closed the year at 2.9% p.a., compared with 2.6% p.a. a year ago.

Financial Review

Throughout the year, the Group was in a very liquid position, benefiting from strong cash flows from operation and property development as well as receipt of substantial funding support from the Government for the construction of WIL. The Company did not raise any new financing as available cash and investments, combined with anticipated cash inflow and undrawn committed banking facilities, are expected to be sufficient to cover all funding requirements, including debt refinancing and capital expenditure, well into 2012.

Preferred Financing Model and Debt Profile

The Preferred Financing Model exemplifies the Company's prudent approach to debt management and helps ensure a well balanced debt portfolio.



Cost of Borrowing

Total loans outstanding declined from HK$23,868 million at the end of 2009 to HK$21,057 million at the end of 2010 due to scheduled debt repayment and prepayment of bank loans with cash surplus. The Group's weighted average borrowing cost for 2010 was 4.3% p.a., up from 3.7% p.a. in 2009 as a result of substantial prepayment of floating rate bank loans which gave rise to a higher portion of debt being denominated in higher fixed interest rates. However, net interest expense charged to the Profit and Loss Account, after interest capitalised of HK$100 million, declined to HK$1,237 million from HK$1,504 million in 2009 due to reduced borrowings.

Treasury Risk Management

The Board of Directors approves policies for overall treasury risk management. The Group's well established Preferred Financing Model (the "Model") is an integral part of these risk management policies. The Model specifies the preferred mix of fixed and floating rate debts, sources of funds from capital and loan markets, debt maturity profile, a permitted level of foreign currency debts, and an adequate length of financing horizon for coverage of forward funding requirements. During 2010, in accordance with the Model the Group maintained a well diversified debt portfolio with adequate forward coverage of funding requirements.

The use of derivative financial instruments to control and hedge against interest rate and foreign exchange risk exposures forms an integral part of the Group's risk management strategy. In accordance with Board policy, these instruments shall only be used for controlling or hedging risk exposures, and cannot be used for speculative purposes.

To control and diversify counterparty risks, the Group limits its exposure to credit risk by only placing deposits and transacting derivative financial instruments with, or investing in instruments issued by, financial institutions and companies with acceptable investment grade credit ratings.

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

All bank deposits and medium term notes investments are similarly subject to a separate counterparty limit based on the respective counterparty's credit ratings and/or status as Hong Kong's note issuing bank. There is also a limit on the length of time that the Group can maintain a deposit with or invest in an instrument issued by a counterparty based on credit ratings. Deposit outstanding and maturity profile are monitored on a frequent basis to ensure they are within the approved limits.

The Group actively monitors credit ratings and credit related changes of all its counterparties using such additional information as the counterparties' credit default swap levels, and would on the basis of all such information adjust the maximum counterparty limits of, and/or credit exposure to, its counterparties.

The Group adopts a prudent approach to managing liquidity risk, and will maintain sufficient cash balance and undrawn committed banking facilities to provide forward coverage of at least 6 to 15 months of all projected cash requirements, including debt repayments and capital expenditures, as specified by the Model. The Group also conducts stress testing of its projected cash flow to analyse liquidity risk, and would arrange additional banking facilities or debt issuance or otherwise take appropriate actions if such stress tests reveal significant risk of material cash flow shortfall.

Credit Ratings

In November, Moody's upgraded the government bond rating of the Hong Kong SAR government from "Aa2" to "Aa1", and at the same time revised the Company's issuer and senior unsecured debt ratings from "Aa2" to "Aa1", bringing them on par with the HKSAR government's sovereign rating. The rating outlook is stable.

In December, Hong Kong became one of the few countries and regions in the world that were given the highest credit rating when Standard & Poor's ("S & P's") raised the long-term issuer credit rating on Hong Kong SAR from "AA+" to "AAA". In line with the rating action, S & P's raised the Company's long-term corporate credit rating from "AA+" to "AAA" with stable outlook, the highest credit rating ever achieved in the Group's history.

Earlier, Rating & Investment Information, Inc. of Japan had also affirmed the Company's foreign currency issuer and Hong Kong dollar issuer ratings at "AA+", and Hong Kong dollar short-term credit rating at "a-1+", with a stable outlook.

Financing Capacity

The Group's capital expenditure programme consists mainly of three parts – railway projects in Hong Kong, property investment and development in Hong Kong, and overseas investments.

Capital expenditure for railway projects in Hong Kong comprises mainly investment in and expenditures relating to new railway projects, including ownership projects such as WIL, South Island Line (East) and the Kwun Tong Line Extension, as well as outlays for maintaining and upgrading the existing rail lines. Concession projects such as the Shatin to Central Link and XRL will be fully funded by the Government and therefore for funding purposes have not been included in the Group's projected capital expenditure.

Capital expenditure for property investment and development comprises mainly enabling works for property development, payment of land premium, as applicable, as well as fitting-out and refurbishment works of shopping centres. Expenditure for overseas investments consists primarily of capital expenditure for SZL4 project and equity injection for the Hangzhou Line 1 project.

Based on current programmes, total net capital expenditures for the next three years of 2011, 2012 and 2013 are estimated at HK$34.6 billion for railway projects in Hong Kong, HK$2.7 billion for property investment and development in Hong Kong, and HK$5.8 billion for overseas investments, for a total of HK$43.1 billion. Out of this total, it is estimated that HK$16.4 billion would be incurred in 2011, HK$14.8 billion in 2012, and HK$11.9 billion in 2013.

With forward financing coverage extending well into 2012, the Group's funding requirement including debt refinancing and net capital expenditure in 2011 and most of 2012 is expected to be well taken care of by the Group's existing cash and investment as well as future projected cash flow.

Credit ratings	Short-term ratings*	Long-term ratings*
Standard & Poor's	A-1+/A-1+	AAA/AAA
Moody's	-/P-1	Aa1/Aa1
Rating & Investment Information, Inc. (R&I)	a-1+	AA+

* Ratings for Hong Kong dollar/foreign currency denominated debts respectively

Ten-Year Statistics

	2010	2009	2008	2007#	2006	2005	2004	2003	2002	2001
Financial										
Profit and Loss Account *(HK$ million)*										
Turnover	**29,518**	18,797	17,628	10,690	9,541	9,153	8,351	7,594	7,686	7,592
Operating profit before depreciation, amortisation and variable annual payment arising from the Rail Merger	**14,951**	13,069	14,009	14,229	11,032	11,259	9,110	9,116	7,769	7,301
Depreciation and amortisation	**3,120**	2,992	2,944	2,752	2,688	2,695	2,512	2,402	2,470	2,178
Interest and finance charges	**1,237**	1,504	1,998	1,316	1,398	1,361	1,450	1,539	1,125	874
Change in fair value (net of deferred tax) on investment properties	**3,402**	2,336	99	6,609	1,797	2,310	2,051	–	–	–
Profit	**12,172**	9,639	8,280	15,182	7,758	8,463	6,543	4,450	3,579	4,278
Profit from underlying businesses attributable to equity shareholders †	**8,657**	7,303	8,185	8,571	5,962	6,140	4,492	4,450	3,579	4,278
Dividend proposed and declared	**3,405**	2,977	2,715	2,522	2,328	2,299	2,259	2,215	2,161	2,118
Earnings per share *(HK$)*	**2.10**	1.69	1.47	2.72	1.41	1.55	1.23	0.85	0.70	0.85
Balance Sheet *(HK$ million)*										
Total assets	**181,665**	176,494	159,338	155,668	120,421	113,666	106,674	102,366	101,119	98,126
Loans, other obligations and bank overdrafts	**21,057**	23,868	31,289	34,050	28,152	28,264	30,378	32,025	33,508	31,385
Obligations under service concession	**10,749**	10,625	10,656	10,685	–	–	–	–	–	–
Deferred income	**605**	167	156	515	1,682	3,584	4,638	5,061	6,226	8,411
Total equity attributable to equity shareholders	**117,150**	106,387	97,801	91,014	76,767	69,875	61,892	57,292	53,574	53,893
Financial Ratios										
Operating margin *(%)*	**37.0**	50.6	53.0	55.4	54.7	55.9	54.4	49.3	52.2	53.4
Operating margin (excluding railway subsidiaries outside of Hong Kong) *(%)*	**54.9**	53.5	53.0	55.4	54.7	55.9	54.4	49.3	52.2	53.4
Non-fare revenue as a percentage of turnover (excluding railway subsidiaries outside of Hong Kong) *(%)*	**35.7**	35.2	35.0	33.4	31.6	31.4	29.0	27.7	25.6	24.6
Net debt-to-equity ratio *(%)*	**12.8**	25.8	42.1	48.5	36.3	39.9	48.6	55.2	59.3	57.8
Net debt-to-equity ratio (excluding revaluation reserves) *(%)*	**13.0**	26.1	42.5	49.2	36.7	40.3	48.9	62.6	67.4	66.0
Interest cover *(times)*	**10.5**	7.1	6.0	9.0	6.7	7.6	6.1	5.6	4.5	3.8
Employees										
Corporate management and support departments	**1,362**	1,319	1,235	1,530	823	810	792	793	824	870
Station commercial and rail related businesses	**256**	294	293	305	82	82	67	61	62	60
Operations	**8,914**	8,632	8,540	8,770	4,521	4,600	4,669	4,730	4,836	4,756
Projects	**1,794**	1,365	995	942	260	242	362	398	546	973
Property and other businesses	**1,291**	1,242	1,170	1,141	832	688	660	642	618	567
China and international businesses	**212**	239	197	135	112	83	–	–	–	–
Offshore employees	**6,672**	7,059	1,646	1,311	733	486	5	5	5	5
Total	**20,501**	20,150	14,076	14,134	7,363	6,991	6,555	6,629	6,891	7,231

† Excluding change in fair value of investment properties net of related deferred tax

	2010	2009	2008	2007[#]	2006	2005	2004	2003	2002	2001
Hong Kong Passenger Services										
Revenue car km operated *(thousand)*										
Domestic and Cross-boundary	**253,067**	247,930	245,856	128,041	115,784	114,449	114,364	112,823	103,318	96,751
Airport Express	**19,833**	19,643	19,891	19,956	20,077	17,122	16,081	15,227	19,467	19,458
Light Rail	**9,586**	8,950	8,984	755	–	–	–	–	–	–
Total number of passengers *(thousand)*										
Domestic Service	**1,298,714**	1,218,796	1,205,448	915,755	866,754	857,954	833,550	770,419	777,210	758,421
Cross-boundary Service	**99,954**	94,016	93,401	8,243	–	–	–	–	–	–
Airport Express	**11,145**	9,869	10,601	10,175	9,576	8,493	8,015	6,849	8,457	9,022
Light Rail	**154,522**	143,489	137,730	11,100	–	–	–	–	–	–
Bus	**40,883**	37,522	34,736	2,757	–	–	–	–	–	–
Intercity	**3,244**	2,921	3,220	285	–	–	–	–	–	–
Average number of passengers *(thousand)*										
Domestic Service – weekday average	**3,770**	3,544	3,514	2,662[§]	2,523	2,497	2,403	2,240	2,261	2,231
Cross-boundary Service – daily average	**274**	258	255	–[@]	–	–	–	–	–	–
Airport Express – daily average	**31**	27	29	28	26	23	22	19	23	25
Light Rail – weekday average	**433**	402	385	–[@]	–	–	–	–	–	–
Bus – weekday average	**118**	107	99	–[@]	–	–	–	–	–	–
Intercity – daily average	**9**	8	9	–[@]	–	–	–	–	–	–
Average passenger km travelled										
Domestic and Cross-boundary	**10.9**	10.7	10.4	7.9	7.7	7.6	7.7	7.7	7.6	7.4
Airport Express	**29.4**	29.5	29.4	29.5	29.7	30.4	30.2	29.7	29.9	29.8
Light Rail	**2.8**	2.9	3.0	3.0	–	–	–	–	–	–
Bus	**4.5**	4.6	4.6	4.6	–	–	–	–	–	–
Average car occupancy *(number of passengers)*										
Domestic and Cross-boundary	**60**	57	55	58	58	57	56	53	57	58
Airport Express	**17**	15	16	15	14	15	15	13	13	14
Light Rail	**45**	46	46	45	–	–	–	–	–	–
Proportion of franchised public transport boardings *(%)*	**44.3**	42.6	42.0	26.7	25.0	25.2	24.8	24.3	23.5	23.5
HK$ per car km operated (all services)										
Fare revenue	**42.6**	40.2	40.3	47.6	48.0	47.7	45.5	42.9	46.6	49.3
Operating costs	**21.2**	21.1	20.9	21.4	22.0	22.7	22.2	22.5	22.8	24.6
Operating profit	**21.4**	19.1	19.4	26.2	26.0	25.0	23.3	20.4	23.8	24.7
HK$ per passenger carried (all services)										
Fare revenue	**7.75**	7.63	7.72	7.50	7.44	7.25	7.05	7.06	7.28	7.46
Operating costs	**3.85**	4.01	4.01	3.38	3.41	3.45	3.44	3.70	3.57	3.72
Operating profit	**3.90**	3.62	3.71	4.12	4.03	3.80	3.61	3.36	3.71	3.74
Safety Performance										
Domestic, Cross-boundary and Airport Express										
Number of reportable events [^]	**1,545**	1,539	1,514	989	826	748	701	641	690	686
Reportable events per million passengers carried [^]	**1.13**	1.16	1.16	1.05	0.94	0.86	0.83	0.82	0.88	0.89
Number of staff and contractors' staff accidents	**46**	60	42	26	23	31	25	33	24	39
Light Rail										
Number of reportable events [^]	**160**	146	136	6	–	–	–	–	–	–
Reportable events per million passengers carried [^]	**1.07**	1.02	0.99	0.54	–	–	–	–	–	–
Number of staff and contractors' staff accidents	**5**	11	5	–	–	–	–	–	–	–

\# After the Rail Merger on 2 December 2007, our Domestic Service comprised Kwun Tong Line, Tsuen Wan Line, Island Line, Tung Chung Line, Tseung Kwan O Line, Disneyland Resort Line, as well as East Rail Line excluding Cross-boundary Service, West Rail Line and Ma On Shan Line (which we gained after the Rail Merger). Also after the Rail Merger we gained new passenger services for Cross-boundary Service, Light Rail, Bus and Intercity.

§ The figure includes one month's post-merger passenger numbers of East Rail Line excluding Cross-boundary, West Rail Line and Ma On Shan Line. For the full year of 2007 including pre-merger operations, comparable combined passenger for Domestic Service (as adjusted for interchange passengers) would have been 3,364,000.

@ No figure is shown as there was only 1 month's post-merger passenger number. For the full year of 2007 including pre-merger KCR operations, passenger numbers of the services were 252,000 for Cross-boundary Service, 377,000 for Light Rail, 92,000 for Bus and 9,000 for Intercity.

^ Reportable events are occurrences affecting railway premises, plant and equipment, or directly affecting persons (with or without injuries), that are reportable to the Secretary for Transport and Housing, Government of the Hong Kong SAR under the Mass Transit Railway Regulations, ranging from suicides/attempted suicides, trespassing onto tracks, to accidents on escalators, lifts and moving paths.

Investor Relations

Investors and MTR Corporation

The Company is committed to maintaining good relations with its wide base of institutional and retail investors. We believe that shareholder value can be enhanced by clearly communicating the Company's corporate strategies, business development and future outlook through a continuous and active dialogue with existing and potential investors.

As a result of this commitment, for over two decades in the international capital markets the Company has demonstrated a high standard of corporate governance and disclosure, becoming recognised as a leader in investor relations practices in Asia.

Communicating with Institutional Investors

Our proactive approach to investor relations has made the Company one of the most widely covered companies in Hong Kong. A number of local and international brokers currently publish reports on the Company on a regular basis and we are also followed by a wide range of institutional investors.

Management remains dedicated to maintaining an open dialogue with the investment community to ensure a thorough understanding of the Company and its business strategies. During the year, the Company participated in a number of investor conferences and organised roadshows both locally and internationally. In total, over 300 meetings were held with institutional investors and research analysts in 2010.

Retail Shareholder Programmes

The Company greatly values the long-standing shareholder support from our many individual shareholders. Two retail shareholder programmes were organised in 2010 allowing shareholders to enjoy various exclusive benefits, such as promotions for rides on Airport Express and on Ngong Ping 360, and MTR shopping mall promotions.

Access to Information

To ensure all shareholders have equal and timely access to important company information, the Company makes extensive use of the company website to deliver up-to-date information. During the year, the Investor's Information section of the website was regularly reviewed to enhance navigation and the level of information disclosure. Financial reports, patronage figures, together with other company news and stock exchange filings, are easily accessible on the corporate website.

In addition to the shareholder services offered by Computershare, there is also the Company's dedicated hotline to answer individual shareholders' enquiries. In 2010, the hotline handled more than 62,000 such calls.

Index Recognition

The Company's position in the Hong Kong market as a blue chip stock is affirmed through the continued inclusion of our stock in some of the most important indices. The Company is currently a constituent member of the Hang Seng Index, MSCI Index and FTSE Index Series. Since 2002, our achievements in the areas of sustainability and corporate responsibility have been recognised by both the Dow Jones Sustainability Indexes and the FTSE4Good Index Series. In 2010, the Company was also included in the newly launched Hang Seng Corporate Sustainability Index, while the Dow Jones Sustainability World Index (DJSI World) continued to rank MTR Corporation number one in Corporate Sustainability within the global travel and tourism industry sector.

Market Recognition

The Company's 2009 Annual Report won ten awards at the 2010 International Annual Report Competition (ARC) Awards, including the Grand Award for Financial Data from more than 1,900 entries from 27 countries. For the 22nd consecutive year, our Annual Report also achieved recognition in the Hong Kong Management Association (HKMA) Annual Report Awards, with the 2009 report winning the Silver Award under the "General Category" in the 2009 Best Annual Reports Awards Competition. During the year, the Company was awarded "Best Investor Relations" by FinanceAsia, for the third consecutive year. The Company was also awarded "Highly commended - Best investor relations website / webcasting (Hong Kong)" by the IR Magazine Greater China Awards 2010.

Key Shareholder Information

Financial Calendar 2011

Announcement of 2010 annual results	3 March
Last day to register for 2010 final dividend	17 March
Book closure period	18 March to 24 March (both dates inclusive)
Annual General Meeting	6 May
2010 final dividend payment date	On or about 18 May
Announcement of 2011 interim results	August
2011 interim dividend payment date	October
Financial year end	31 December

Principal Place of Business and Registered Office

MTR Corporation Limited, incorporated and domiciled in Hong Kong MTR Headquarters Building, Telford Plaza, Kowloon Bay, Kowloon, Hong Kong

Telephone: (852) 2993 2111

Facsimile: (852) 2798 8822

Share Information

Listing

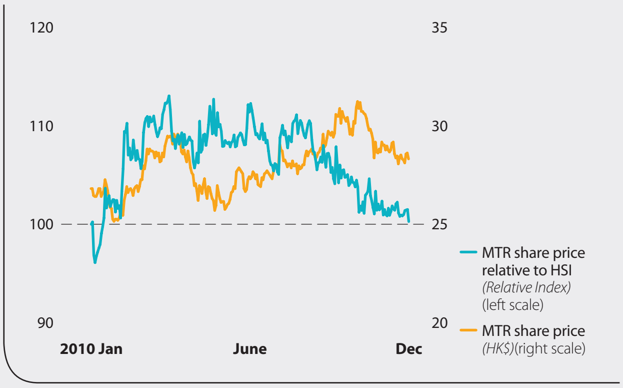
MTR Corporation Limited's shares are listed on the Stock Exchange of Hong Kong. In addition, shares are traded in the United States through an American Depositary Receipt (ADR) Level 1 Programme sponsored by J.P. Morgan Chase Bank, N.A.

Ordinary Shares *(as at 31 December 2010)*

Shares outstanding	5,772,563,031 shares
Hong Kong SAR Government Shareholding	4,434,552,207 shares (76.8%)
Free float	1,338,010,824 shares (23.2%)

Nominal Value	HK$1 per share
Market Capitalisation *(as at 31 December 2010)*	HK$163,364 million

Share Price Performance



Dividend Policy

Subject to the financial performance of the Company, the Company intends to follow a progressive dividend policy. We also expect to pay two dividends each financial year with interim and final dividends payable around October and May respectively.

Dividend per Share

	(in HK$)
2009 Total Dividend	0.52
2010 Interim Dividend	0.14
2010 Final Dividend	0.45

ADR Level 1 Programme

ADR to Ordinary Shares Ratio	1:10
Depositary Bank	J.P. Morgan Depositary Receipts, 1 Chase Manhattan Plaza, Floor 58, New York, NY 10005, USA

Stock Codes

Ordinary Shares

The Stock Exchange of Hong Kong	66
Reuters	0066.HK
Bloomberg	66 HK
ADR Level 1 Programme	MTRJY

Annual Report 2010

Shareholders can obtain copies of our annual report by writing to:

Computershare Hong Kong Investor Services Limited,
17M Floor, Hopewell Centre,
183 Queen's Road East, Wan Chai, Hong Kong

If you are not a shareholder, please write to:

Corporate Relations Department, MTR Corporation Limited
MTR Headquarters Building, Telford Plaza, Kowloon Bay,
Kowloon, Hong Kong

Our annual/interim reports and accounts are also available online at our corporate website at http://www.mtr.com.hk

Shareholder Services

Any matters relating to your shareholding, such as transfer of shares, change of name or address, and loss of share certificates should be addressed in writing to the Registrar:

Computershare Hong Kong Investor Services Limited
Shops 1712-1716, 17th Floor, Hopewell Centre
183 Queen's Road East, Wan Chai, Hong Kong

Telephone: (852) 2862 8628

Facsimile: (852) 2529 6087

Shareholder Enquiries

Our enquiry hotline is operational during normal office hours:

Telephone: (852) 2881 8888

Investor Relations

For enquiries from institutional investors and securities analysts, please contact:

Investor Relations Department, MTR Corporation Limited
MTR Headquarters Building, Telford Plaza, Kowloon Bay,
Kowloon, Hong Kong
Email: investor@mtr.com.hk

Sustainability

Our Corporate Sustainability Policy commits us to stewardship of our organisation in a way that seeks intergenerational development through meeting the needs of the present without compromising the ability of future generations to meet their needs.

Within this framework of social, economic and environmental stewardship, sustainability is our organisational goal, while corporate responsibility serves as the path that guides how we work towards development and create the resilience needed for market competitiveness.

Sustainable Development

The Company's integrated "Rail plus Property" model creates the capacity to be a self-sustaining urban transport system. Through the ownership of land assets and linked air rights we advance new land uses through high density living centres linked by rail. This vision of transit-oriented development leverages the economic opportunity derived from enhanced residential and commercial properties and activities in and around rail stations. MTR Corporation is a recognised leader in pioneering this model for 21st Century urban planning.

The high density environments fostered by our model work under a development approach in which properties adjacent to our rail lines are developed under a master plan that incorporates current social aspirations and environmental excellence. LOHAS Park brings this idea to life. Residents enjoy spacious, green community living supported by environmental programmes such as waste water recycling, road and pedestrian separation and energy efficient buildings.

During the year's C40 Hong Kong Workshop in November 2010, which was jointly hosted by the Environmental Campaign Committee of the Hong Kong SAR Government and the C40, the Company shared with mayors from major cities from around the world the merits of the "rail plus property" model. City representatives experienced our world class travel services and discussed the success of the rail and property model with Company management. C40 is a partnership between the Clinton Climate Initiative and the Large Cities Climate Leadership Group formed in August 2006.

As we grow, operate and maintain our business we focus on ensuring the resilience of assets and services. We achieve this through the continual improvement of our services, assets and supply chain, taking into consideration society's changing aspirations and the need to protect our natural environment.

We accommodate these social and environmental aspects in our operations by engaging stakeholders and understanding their expectations, including those of our customers, supply chain and business partners. Balancing their aspirations with the risks of operating as a commercial enterprise is our means of achieving sustainable development.

Transparency and Leadership

The Company reports its economic, social and environmental performance in the Annual Report and Sustainability Report. We adopt recognised global and industry standards or best practices for measuring performance, including GRI G3 Sustainability Reporting Guidelines, CoMET benchmarking programme and the Carbon Disclosure Project.

Our achievements in incorporating sustainable best practices into all our business decisions continue to attract international recognition. In 2010, we were again named as a Sustainability Leader within the global travel and tourism industry sector, and won a Gold Class award from Sustainable Asset Management (SAM). The Company is listed in the Dow Jones Sustainability Indexes, FTSE4Good Index and Hong Kong's Hang Seng Corporate Sustainability Index. We are also included as the only Hong Kong company in the 2010 Global 100 Most Sustainable Corporations in the World (the Global 100).

Corporate Responsibility

MTR HONG KONG Race Walking 2010

Corporate responsibility guides the actions by which we achieve balance and resilience. The Corporate Responsibility Policy, monitored at the Board of Directors level, identifies six areas of focus in stewardship, each aiming to pursue best sustainable practices.

Environmental Protection

We set ourselves new standards in protecting the environment through innovation and continuous improvement.

While constrained by the relatively carbon-intensive fossil fuel-based power generation in Hong Kong, the Company focuses energy management through its demand-side actions. Under the designated Energy Management Committee, opportunities are continually explored for better energy use and efficiency. Electricity consumption on the urban rail lines has shown a strong downward trend over the last five years, demonstrating a significant 18.7% reduction in kWh per revenue car-km from 5.94 in 2005 to 4.83 in 2010.

Furthermore, a new initiative on energy efficiency is being added to minimise energy use in built structures and electrical and mechanical systems. Measures include increasing the use of natural light and improving the thermal efficiency of stations. Environmental mitigation in areas such as noise, water and air quality and waste management for the construction of rail lines is being drawn from independent environmental impact assessments carried out at the preliminary and detailed design stages.

The award-winning LOHAS Park, with its facilities for food waste composting, water and waste recycling, electric vehicles, and the "Central Park" open space has obtained the BEAM Platinum certification, one of the highest environmental certifications available in Hong Kong. Several other awards of outstanding merit in environmental excellence have been received by our shopping malls, private estates and commercial properties.

In building the West Island Line, water was used for blast ballast in works, pioneering an environmental construction method that reduces noise and dust. We also built a fully enclosed conveyor belt system to transport spoil from the excavation works in Kennedy Town to reduce traffic and dust.

The growing global dialogue on climate change may imply future regulatory risk in relation to monitoring, reporting and verifying carbon emissions. Anticipating the risks that impact our future in terms of compliance, energy costs and environmental damage, we have already initiated several programmes aimed at greenhouse gas emissions management covering our supply chain, future projects and ongoing operations. The Green Procurement Policy, Supplier Code of Practice and Green Purchasing Charter demonstrate our proactive leadership in managing the life-cycle impacts of our carbon footprint.

The Company has embarked on a project to predict and track the carbon emissions involved in the development and operation of new railways. We are in the process of developing tools that will allow us to estimate the amount of embedded carbon in our railway infrastructure, which when combined with estimates of electrical power use over many years of operations, will yield an estimate for life-cycle carbon emissions. Once completed, these tools will allow us to improve our railway design, track carbon intensive elements in construction and test the accuracy of our predictions. Our initial goal is 85% accuracy in the first assessment. A completed cycle of rail construction and operation will allow that accuracy to improve over a 50-year economic evaluation.

Engaging and Building Communities

"Community Care Action" and numerous programmes organised under it targeting Youth, Community Outreach, Arts & Culture and Healthy & Green Living were launched during the year. By engaging with local communities, these programmes gain us a better understanding of community needs and help build relationships.

"'Friend' for life's journeys"

Corporate Responsibility

Caring for our youth at different life stages, we have a series of programmes designed for them. The "'Friend' for life's journeys" and "'Train' for life's journeys" programmes have each guided more than a 100 students in setting and maintaining life goals. The MTR Budding Station Master programme allows primary school students experience the job of a station master. Our CS4School Programme, jointly organised with Business Environmental Council, arranges visits for students from secondary schools to our operations introducing youth to our environmental initiatives in action.

A record 198 volunteering community service projects involving about 4,400 volunteers under our "More Time Reaching Community" scheme took place in 2010. In May 2010, our staff volunteers organised seven projects for the elderly, chronically ill, underprivileged families and mentally challenged people across Hong Kong. We also arranged visits to the elderly as part of our "Silver Network" initiative, as well as seminars and depot visits by NGOs through our "NGO Bond" and "Society Link" programmes.

Our "art in mtr" programme has brought art to numerous communities. During the year, the Company also took part in many health related events, including sponsoring the sixth MTR HONG KONG Race Walking, which raised over HK$1.13 million for the Hospital Authority's Health InfoWorld.

Ensuring Services of Value to Customers

We improve and upgrade our service and products continuously to meet the needs of our customers.

Engaging with our customers is the key to understanding their needs. MTR Facebook is the latest of our communication channels designed to capture the up-and-coming younger generation of users, alongside MTR Opinion Zone, Phone-in Radio Programme, MTR Club and the MTR Hotline.

We also work with groups representing passengers with disabilities to identify locations for retrofitting passenger lifts at stations. In 2010, we obtained statutory approvals for such projects at Sham Shui Po, Shek Kip Mei, Wong Tai Sin, Prince Edward and Cheung Sha Wan stations, in the latter case collaborating with the Housing Authority.

Developing People

Our people are the most valuable asset of the Company and we foster a company culture in which our staff can learn, grow and take pride.

To develop our people and ensure sustained management expertise, we have established the Executive Continuous Learning and Integrated Staff Development programmes to enhance the learning culture that keeps the Company at the leading edge in its various operations. To encourage work-life balance, we have worked with the Hong Kong organisation Community Business to study the issue, subsequently introducing a Healthy Living Programme.

Further details on our people initiatives are set out under the "Executive Management's Report – Human Resources" on pages 66 to 70.

Providing Reasonable Returns to Investors

We promote sustainable development of the Company by growing in Hong Kong, the Mainland of China, and capturing opportunities in Europe and other parts of the world by extending our core competencies.

Expanding the network in Hong Kong and growing our operations in the Mainland of China and overseas markets are significant milestones in business growth. Our expansion is supported by the Enterprise Risk Management framework used to identify, register, mitigate and monitor attendant risks. The actions taken under this framework reflect the application of our core competencies and values to fit external market conditions and needs. Our improving performance in these markets demonstrates the resilience of our organisation and people when operating outside of Hong Kong.

Further details on our commitment in maintaining good relations with our wide base of institutional and retail investors are set out under the "Investor Relations" on pages 80 to 81.

"art in mtr" – "Urban flow" in Tsuen Wan Station

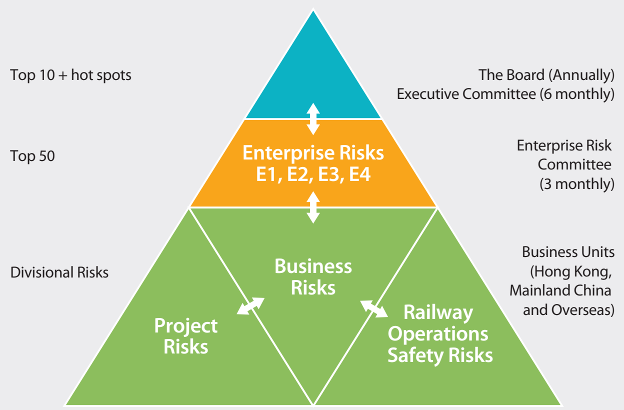
Promoting Safe and Ethical Business Practices

We uphold safety as an absolute pre-requisite for all stakeholders, observe ethical business practices, maintain ongoing stakeholder communications as well as build relations that seek to achieve common objectives.

The Corporate Safety Management Committee, supported by four divisional committees, implements policy and guides safety management across operations and business functions. Processes are in place to ensure safe and ethical business practices including PAS 55-1 for asset management, OHSAS 18001 for health and safety, Code of Conduct, Supplier Code of Practice, Competition Law Compliance Manual and the Safety Manual.

Risk Management

The Company's Enterprise Risk Management (ERM) framework is now embedded and dynamically applied across the organisation to prioritise and proactively manage the risks from our existing and growth businesses and from the ever changing external business environment. The ERM framework provides a clear and holistic view of the significant safety, business, finance, legal/regulatory and reputation/political risks facing the Company. It forges sound governance and business practices through identifying the responsible owner and action parties for each risk and ensures that risks are reviewed every six months and that adequate risk control plans are in place. The Enterprise Risk Committee (ERC), which is chaired by the Legal Director & Secretary and comprises management representatives from key business functions, is central to the process. ERC steers the implementation and improvement of the framework and reviews the Top 50 and emerging risks every quarter and reports the key risks to the Executive Committee every six months. Every year, the Audit Committee reviews the risk management process and the Board maintains an oversight of the Top Ten risks and hot spots.



The ERM Framework

The Company's simple and practical ERM framework is now applied to over 20 key business areas and we have given our staff a suite of supporting tools. Our simple and consistent risk rating language for all kinds of risks is fundamental to our strong risk culture. The Top Ten and Top 50 risk maps are instrumental in providing our Board and management a sharpened focus on our dynamic risk profile.

Risk Management Excellence to Sustain Business Success

The ERM framework has been in operation since early 2006. We maintain a strong impetus to improve our systems and tools through annual reviews with users and cross-industry benchmarking and experience sharing. The key activities undertaken during the year were:-

- Shared and learnt from the third UK ERM roundtable and the second HK ERM roundtable events the best practices for governance of subsidiaries and for establishing a structured ERM training programme for the diverse needs of over 20,000 staff.
- Participated in an industry benchmarking on risk management with global railway companies and contributed our risk management knowledge to a best practice risk management handbook.
- Developed in-house an integrated risk management information system which captures over 5,000 multi-disciplinary risks and embeds our decade of good practices and knowledge into one platform.
- Invigorating ERM and heightening staff members' risk awareness through sharing of lessons learnt, risk management training and on-line discussion forum.
- Capturing business opportunities with confidence and risk intelligence through robust business case reviews and thorough assessment of risks during bidding, project, take-over and operational phases.
- Striving for optimal risk financing and total cost of risk by integrating ERM and insurance review processes.

International Recognition

The Company's collective efforts in ERM are recognised by a world-leading risk management professional body, the Institute of Risk Management. Not only did the Company win top honours as "Risk Management Team of the Year – Commercial" and "ERM Strategy of the Year" but we were also given the "Overall Winner for Outstanding Contribution to the Industry Award". The judges commended that our strategy is "capturing the hearts and minds of employees, establishing a simple and practical framework, demonstrating best practice in many areas and truly embedding ERM within the organisation. In addition, the Board has clearly bought into the ERM process and demonstrated its willingness to invest in its development."

Corporate Governance Report

Corporate Governance Practices

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. This Report describes how the Company has applied the principles of the Code on Corporate Governance Practices (the "Code") contained in Appendix 14 of the Listing Rules.

The Company has fully complied with the Code provisions throughout the year ended 31 December 2010.

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 Committee, 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, 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 12 Members, consisting of one executive Director (the Chief Executive Officer) and 11 non-executive Directors, of whom seven are independent non-executive Directors. In this regard, the Company *well exceeds* the requirement of the Listing Rules which requires every board of directors of a listed issuer to have at least three independent non-executive directors.

Dr. Raymond Ch'ien Kuo-fung, a Member of the Board and the non-executive Chairman of the Company since 1998 and 2003 respectively, was re-appointed by the Government in November 2009 as the non-executive Chairman with effect from December 2009 until December 2012.

As announced by the Company on 29 December 2010, Mr. Chow Chung-kong, a Member of the Board and the Chief Executive Officer of the Company since 2003, will retire from the position of Chief Executive Officer and cease to be a Member of the Board when his current contract as the Chief Executive Officer expires on 31 December 2011. The Company is proceeding with a worldwide search including internal candidates to identify the right candidate for the post of the Chief Executive Officer.

Two of the non-executive Directors (being the office of the Secretary for Transport and Housing ("S for T&H") and the office of the Commissioner for Transport ("C for T")) are appointed by the Chief Executive of the HKSAR under Section 8 of the MTR Ordinance. During the year, Ms. Eva Cheng held the post of the S for T&H and Mr. Joseph Lai Yee-tak was the C for T. Another non-executive Director, Professor Chan Ka-keung, Ceajer, is the Secretary for Financial Services and the Treasury of the Government. The Government through the FSI, holds approximately 76.8% of the issued share capital of the Company.

At the 2010 Annual General Meeting on 27 May 2010 (the "2010 AGM"), Mr. Vincent Cheng Hoi-chuen retired from office pursuant to Article 85 of the Articles of Association and was elected as a Member of the Board. In addition, Mr. Chow Chung-kong and Ms. Christine Fang Meng-sang retired from office by rotation pursuant to Articles 87 and 88, and were re-elected as Members of the Board at the 2010 AGM.

Mr. Allister George Morrison (also known as Alasdair George Morrison), a businessman with international exposure through his holding of a number of senior executive positions in leading multinational enterprises particularly in Asia (Mr. Morrison's biography is set out on page 106), has been appointed as an independent non-executive Director with effect from 9 July 2010, thus increasing the number of independent non-executive Director of the Company to seven. Also, with effect from the same date, Mr. Morrison has been appointed as a Member of both the Audit Committee and the Remuneration Committee of the Board.

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, the independent non-executive Directors contribute to ensuring that the 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.

During the year, 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.

Each Director ensures that he/she can give sufficient time and attention to the affairs of the Company. They are requested to disclose the number and nature of offices held in public companies or organisations and other significant commitments as well as their identity to the Company twice a year. At the July 2010 and January 2011 Board Meetings, Directors had been advised of the increased level of continuous disclosure of information about and by them, together with other matters relating to Directors, in the light of their duties under general law (common law and legislation) and the Listing Rules.

Biographies of the Members of the Board are set out on pages 104 to 107. Save as disclosed in this Annual Report, none of the Members of the Board and the Executive Directorate has any relationship (including financial, business, family or other material or relevant relationships) between each other, although the office of the S for T&H (Ms. Eva Cheng) and the office of the C for T (Mr. Joseph Lai Yee-tak) were both appointed by the Chief Executive of the HKSAR, and Professor Chan Ka-keung, Ceajer is the Secretary for Financial Services and the Treasury of the Government, and Ms. Christine Fang Meng-sang sits on various government advisory committees.

As permitted under its Articles of Association, the Company has arranged Directors' and Officers' Liability Insurance for which Members of the Board and officers of the Company do not have to bear any excess.

Chairman and Chief Executive Officer

The posts of Chairman and Chief Executive Officer are distinct and separate (please refer to The Board of Directors section regarding their appointments on page 86). 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 making sure that adequate information about the Company's business is provided to the Board on a timely basis, the Chairman provides leadership for the Board, and ensures views on all principal and appropriate issues are exchanged by all Directors (including the non-executive Directors) in a timely manner, by encouraging them to make a full and effective contribution to the discussion. Under the Chairman's guidance, all decisions have reflected the consensus of the Board. As head of the Executive Directorate and chairman of the Executive Committee (which comprises six other Members of the Executive Directorate, General Manager – Corporate Relations, and General Manager – Marketing & Station Commercial), the Chief Executive Officer is responsible to the Board for managing the business of the Company. Biographies of the Members of the Executive Directorate and the other Members of the Executive Committee are set out on pages 107 to 109.

Board Proceedings

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 at the Company's expense, if necessary, in accordance with the approved procedures. The draft agenda for regular Board Meetings is prepared by the Legal Director & Secretary and approved by the Chairman of the Company. Members of the Board are advised to inform the Chairman or the Legal Director & Secretary not less than one week before the relevant Board Meeting if they wish to include a matter in the agenda of the Meeting. The Board Meeting dates for the following year are usually fixed by the Legal Director & Secretary and agreed by the Chairman some time in the third quarter of each year.

At each regular Board Meeting, Members of the Executive Directorate together with senior managers report to the Board on their respective areas of business, including the operations, progress of projects, property and other businesses, financial performance, legal issues, risk management, corporate governance, human resources and outlook. The Chief Executive Officer also submits his Executive Summary, which focuses on the overall strategies and principal issues of the Company, to the Board. These reports, together with the discussions at Board Meetings, provide information to enable all Members of the Board to make informed decisions for the benefit of the Company. The agenda together with Board papers are sent in full at least three days before the intended date of the Board Meeting.

All Members of the Board have access to the advice and services of the Legal Director & Secretary, who is responsible for ensuring that the correct Board procedures are followed and advises the Board on all corporate governance matters. The Members of the Board also have full access to all Members of the Executive Directorate as and when they consider necessary.

Corporate Governance Report

Unless specifically permitted by the Articles of Association, a Director cannot cast a vote on any contract, transaction, arrangement or any other kind of proposal in which he has an interest and which he knows is material. For this purpose, interests of a person who is connected with a Director (including any of his associates) are treated as the interests of the Director himself. Interests purely as a result of an interest in the Company's shares, debentures or other securities are disregarded. A Director may not be included in the quorum for such part of a meeting that relates to a resolution he is not allowed to vote on but he shall be included in the quorum for all other parts of that Meeting. This reduces potential conflicts which might otherwise arise between the Company's business and an individual Director's other interests or appointments.

Matters to be decided at Board Meetings are decided by a majority of votes from Directors allowed to vote although the usual practice is that decisions reflect the consensus of the Board.

Board Meetings

The Board held seven regular Meetings and one ad hoc Meeting in 2010. In this regard, the Company again *well exceeds* the requirement of the Code which requires every listed issuer to hold Board Meetings at least four times a year.

During 2010 and in addition to the regular reports on the business and financial performance, examples of other key matters discussed at the Board Meetings included Hong Kong's train service (including operations of the Fare Adjustment Mechanism) and railway projects (such as West Island Line and Hong Kong Section of the Guangzhou-Shenzhen-Hong Kong Express Rail Link), Mainland of China's railway projects (for example, Shenzhen Metro Line 4 and the Daxing Line) and Beijing Metro Line 4's operations, overseas train operations (London Overground, Stockholm's Metro and Melbourne's Metropolitan train system), property development, shareholders' analysis and investors' feedback, corporate governance, enterprise risk management, corporate sustainability, pay review, and staff relations. A special Board Meeting was held in July on Octopus Holdings Limited's management of personal data.

Private/Other Board Meetings

In addition to the above regular Board Meetings, the Chairman held three private/other Board Meetings during the year.

The first Meeting was held on 30 April 2010 with all non-executive Directors and the Chief Executive Officer without the presence of other Members of Executive Directorate to discuss executive development and succession.

A Meeting on 9 July 2010 was with a majority of other non-executive Directors without the presence of the Chief Executive Officer and other Members of Executive Directorate, to discuss Executive Directorate performance and succession plan.

Another Meeting was held on 7 December 2010 with all non-executive Directors without the presence of the Chief Executive Officer and other Members of Executive Directorate. The Chief Executive Officer's succession planning, commencement of an international search for suitable candidates in 2011 to fill the Chief Executive Officer position, shareholder relations and key executive's pay matters were discussed.

The attendance record of each Member of the Board (and relevant Members of Executive Directorate who are Members of Corporate Responsibility Committee) is set out below:

Meetings Held in 2010

Directors	Board	Private/ Other Board	Audit Committee	Remuneration Committee	Nominations Committee	Corporate Responsibility Committee	Annual General Meeting
Number of Meetings	8	3	4	4	1	2	1
Non-executive Directors							
Dr. Raymond Ch'ien Kuo-fung *(Chairman)*	7/8	3/3			1/1	2/2	1/1
Commissioner for Transport (Joseph Lai Yee-tak)	8/8 (Note 2)	3/3	4/4				0/1
Secretary for Transport and Housing (Eva Cheng)	8/8 (Note 3)	2/3 (Note 3)			1/1	2/2 (Note 3)	0/1
Professor Chan Ka-keung, Ceajer	8/8 (Note 4)	3/3 (Note 4)		4/4 (Note 4)	1/1		1/1 (Note 4)
Independent Non-executive Directors							
Vincent Cheng Hoi-chuen	6/8 (Note 5)	2/3		3/4 (Note 5)		1/2	1/1
Christine Fang Meng-sang	8/8	3/3			1/1	2/2	1/1
Edward Ho Sing-tin	8/8	3/3		4/4	1/1		1/1
T. Brian Stevenson	8/8	3/3	4/4	4/4			1/1
Ng Leung-sing	6/8	3/3	4/4		1/1		1/1
Abraham Shek Lai-him	7/8	2/3	2/2		1/1	1/2	1/1
Alasdair George Morrison (Note 1)	5/5	2/2	1/2	1/2			
Executive Directors							
Chow Chung-kong *(Chief Executive Officer)*	8/8	1/1					1/1
Leonard Bryan Turk *(Legal Director & Secretary)*						2/2	
Thomas Ho Hang-kwong *(Property Director)*						2/2	

Notes

1 Mr. Alasdair George Morrison was appointed as an independent non-executive Director, as well as a member of the Audit Committee and the Remuneration Committee respectively, on 9 July 2010. 2 Board Meetings attended by Mr. Alasdair George Morrison were by teleconference.

2 2 Board Meetings were attended by the alternate director of Mr. Joseph Lai Yee-tak.

3 2 Board Meetings, 1 Private/Other Board Meeting and 1 Corporate Responsibility Committee Meeting were attended by an alternate director of Ms. Eva Cheng.

4 4 Board Meetings, 2 Private/Other Board Meetings, 2 Remuneration Committee Meetings and the Annual General Meeting were attended by an alternate director of Professor Chan Ka-keung, Ceajer.

5 2 Board Meetings and 1 Remuneration Committee Meeting attended by Mr. Vincent Cheng Hoi-chuen were by teleconference.

The minutes of Board Meetings are prepared by Legal Manager – Company Secretarial, the Secretary of the Meetings with details of the matters considered by the Board and decisions reached, including any concerns raised by the Members of the Board or dissenting views expressed. The draft minutes are circulated to all Members of the Board for their comment within a reasonable time after the Meeting. The approved procedure is that the Board formally adopts the draft minutes at the subsequent Meeting. If Members of the Board have any comment on the draft minutes, they will discuss it at that Meeting, followed by a report on what has been agreed in the minutes of that Meeting. Minutes of Board Meetings are kept by the Legal Director & Secretary and open for inspection by all Members of the Board at the Company's registered office.

Material Interests and Voting

All Directors are required to comply with their common law duty to act in the best interests of the Company and have particular regard to the interest of the shareholders as a whole.

Amongst others, all Directors are required to declare their interests, if any, in any transaction, arrangement or other proposal to be considered by the Board at Board Meetings and to abstain from voting on any related resolutions.

Government's Representatives on the Board

The Government is a substantial shareholder of the Company and the Chief Executive of the HKSAR may, pursuant to Section 8 of the MTR Ordinance, appoint up to three persons as "additional directors". Out of a total of 12 Board Members, three are Government-nominated representatives (being the office of the S for T&H, the office of the C for T (both pursuant to Section 8 of the MTR Ordinance) and Professor Chan Ka-keung, Ceajer) and seven of them (being the *majority*) are independent non-executive Directors.

Each Director appointed by the Chief Executive of the HKSAR pursuant to Section 8 of the MTR Ordinance or by the Government through its shareholding must, like any other Director, act in the best interests of the Company.

On appointment to the Board and same as any other Director, each Government-nominated Director is given a comprehensive, formal and tailored induction programme highlighting, among other things, his/her duties under general law, statutes and the Listing Rules (including the fiduciary duty to act in good faith in the best interests of the Company as a whole, considering the interests of all its shareholders, majority or minority, present and future).

If a conflict arises between the interests of the Company and those of the Government, a Director appointed by the Chief Executive of the HKSAR pursuant to Section 8 of the MTR Ordinance or by the Government through its shareholding, would not be included in the quorum of part of a Meeting that relates to the transaction, arrangement or other proposal being considered by the Board and would not be allowed to vote on the related resolution.

Please refer to pages 87 and 88 regarding the Board proceedings in 2010.

There are a number of contractual arrangements that have been entered into between the Company and the Government (and its related entities), some of which are continuing in nature. As the Government is a substantial shareholder of the Company, such contractual arrangements are connected transactions (and in some cases continuing connected transactions) for the purposes of the Listing Rules. The section headed "Connected Transactions" on pages 122 to 136 explains how, in accordance with the Listing Rules, these transactions are treated.

Appointment, Re-election and Removal of Members of the Board

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 by the Nominations Committee of the Company. Directors who are appointed by the Board must retire at the first annual general meeting after their appointment. A Director who retires in this way is eligible for election at that annual general meeting, but is not taken into account when deciding which and how many Directors should retire by rotation. 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, if the number of Directors is not divisible by three, such number as is nearest to and less than one third) must retire as Directors 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". Directors appointed in this way may not be removed from office except by the Chief Executive of the HKSAR. These Directors are not subject to any requirement to retire by rotation nor will they be counted in the calculation of the number of Directors who must retire by rotation. In all other respects, the "additional directors" are treated for all purposes in the same way as other Directors and are, therefore, subject to the normal common law duties of directors, including to act in the best interests of the Company. The Chief Executive of the HKSAR has appointed the office of the S for T&H and the office of the C for T as "additional directors".

The Company has a service contract with each of the non-executive Directors (including Dr. Raymond Ch'ien Kuo-fung (non-executive Chairman) and Professor Chan Ka-keung, Ceajer (Secretary for Financial Services and the Treasury of the Government)) (save for the "additional directors") specifying the terms of his/her continuous appointment as a non-executive Director and a Member of the relevant Board Committees, for a period not exceeding three years.

At the 2011 Annual General Meeting and in accordance with Articles 87 and 88 of the Articles of Association, Messrs. Edward Ho Sing-tin, Ng Leung-sing and Abraham Shek Lai-him will retire by rotation and will offer themselves for re-election.

Mr. Edward Ho Sing-tin, an independent non-executive Director and the chairman of both the Nominations Committee and the Remuneration Committee of the Board, joined the Board of the Mass Transit Railway Corporation in 1991. As an architect and the Group Chairman of Wong Tung Group of companies, as well as the only current independent non-executive Director on the Board since the Company's listing in 2000 (hence, has served the Board for more than nine years as contemplated in the Recommended Best Practices of the Code), Mr. Ho brings his valuable business and professional experience to the Board for promoting the best interests of the Company and its shareholders. Under his leadership as the chairman of the Independent Board Committee (which was established in connection with the Rail Merger between the Company and the Kowloon-Canton Railway Corporation), the Rail Merger was successfully implemented in 2007. At the 2008 Annual General Meeting, over 99.9% of the votes were in favour of the re-election of Mr. Ho as a Member of the Board.

The Company entered into a service contract with Mr. Ho for three years with effect from 2008, and has continued to receive written confirmation from him annually on his independence in accordance with the Listing Rules.

Accordingly, the Board has resolved that Mr. Ho continues to be independent and should be re-elected as a Director at the 2011 Annual General Meeting.

The re-appointment of Mr. Ho will be in accordance with the Recommended Best Practices of the Code.

At the 2011 Annual General Meeting and in relation to the retirement by rotation of directors, the Company will continue to comply with its Articles of Association which require one third of the current Directors who are subject to Articles 87 and 88 must retire as directors (i.e. three out of the nine Directors (excluding two Directors appointed pursuant to Section 8 of the MTR Ordinance)). The re-organisation in the Government of the HKSAR and the Rail Merger of the Company with Kowloon-Canton Railway Corporation have brought an increase in the number of Directors last elected/re-elected in the 2008 Annual General Meeting three years ago. For this reason, the Company will, for the first time, not also meet Code provision A.4.2 (which requires every director to be subject to retirement by rotation at least once every three years) in 2011. For Directors retiring and standing for election/re-election at the 2011 Annual General Meeting, please refer to page 112.

Mr. Alasdair George Morrison, who was appointed by the Board after the 2010 Annual General Meeting, will retire under Article 85 of the Articles of Association and will offer himself for election at the 2011 Annual General Meeting.

On appointment to the Board, each of the Directors (including alternate directors) is given a comprehensive, formal and tailored induction programme on key areas of business operations and practices of the Company, as well as the general and specific duties of the directors under general law (common law and legislation) and the Listing Rules. All Directors (including alternate directors) are also given a Directors' Manual on their appointment which sets out, amongst other things, the Directors' duties and the Terms of Reference of the Board Committees. The Directors' Manual is updated from time to time to reflect developments in those areas, following a report on the same at relevant Board Meeting(s).

To assist Directors' continuing professional development, the Legal Director & Secretary recommends Directors to attend relevant seminars and courses. The costs of such training are borne by the Company. In addition, the Company is in the course of exploring an annual development programme for Directors. During 2010 and in preparing for succeeding Mr. Andrew McCusker as the Operations Director with effect from 1 January 2011, a one to one training programme covering the roles of a director from the strategic, planning and management perspective, as well as the legal and practical aspects of corporate governance and the trends, had been arranged for Dr. Jacob Kam Chak-pui.

Accountability

The Members of the Board are responsible for preparing the accounts of the Company and of the Group. The accounts are prepared on a going concern basis and give a true and fair view of the state of affairs of the Company and of the Group as at 31 December 2010, and of the Group's profit and cash flow for the year then ended. In preparing the accounts for the year ended 31 December 2010, the Members of the Board have selected appropriate accounting policies and, apart from those new and amended accounting policies as disclosed in the notes to the accounts for the year ended 31 December 2010, have applied them consistently with previous financial periods. Judgments and estimates have been made that are prudent and reasonable. The reporting responsibilities of the External Auditor are set out on page 138.

In support of the above, the accounts presented to the Board have been reviewed by the Members of the Executive Directorate. For both the annual and interim reports and accounts, the Finance Division is responsible for clearing them with the External Auditor and then the Audit Committee. In addition, all new and amended accounting standards and requirements, as well as changes in accounting policies adopted by the Company have been discussed and approved at the Audit Committee before adoption by the Company.

Board Committees

As an integral part of good corporate governance, the Board has established a total of *four* Board Committees to oversee particular aspects of the Company's affairs. Each of these Committees is governed by its respective Terms of Reference which are available on the Company's website: www.mtr.com.hk.

The Audit Committee, Remuneration Committee and Nominations Committee comprise *only* non-executive Directors (with the *majority* being independent non-executive Directors). The Corporate Responsibility Committee has seven Members with the *majority* being non-executive Directors. There are two Members of the Executive Directorate on that Board Committee to facilitate discussion and implementation of policies.

All Committees are provided with sufficient resources to discharge their duties.

Audit Committee

The Audit Committee consists of four non-executive Directors, three of whom are independent non-executive Directors. The Members of the Committee are Mr. T. Brian Stevenson (chairman), Mr. Ng Leung-sing, the C for T (Mr. Joseph Lai Yee-tak), and Mr. Alasdair George Morrison (effective from 9 July 2010). Mr. Abraham Shek Lai-him served the Committee during the period from 1 February to 9 July 2010. Mr. Stevenson, Mr. Ng, Mr. Morrison and Mr. Shek are also independent non-executive Directors. None of the Committee Members is a partner or former partner of KPMG, the Company's External Auditor. The Finance & Business Development Director, the Head of Internal Audit and representatives of the External Auditor 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 meets regularly, and the External Auditor or the Finance & Business Development Director may request a Meeting if they consider it necessary.

Duties of Audit Committee

Under its Terms of Reference, the duties of the Audit Committee include financial and efficiency aspects as described below. Amongst other things, the Committee is required to oversee the relationship with the Company's External Auditor, to review the financial information of the Company, and to oversee the Company's financial reporting system and internal control procedures. The Committee discusses with the External Auditor the nature and scope of audit and reporting obligations before the audit commences. Apart from giving pre-approval of all audit services, the Committee also pre-approves any non-audit services for complying with relevant legal requirements. The Committee is primarily responsible for making recommendations to the Board on the appointment and removal of the External Auditor, and approving the remuneration and terms of such engagement.

With respect to financial information of the Company, the Committee monitors the integrity of financial statements, annual and interim reports and accounts, together with the preliminary announcement of results and other announcements regarding the Company's financial information to be made public. In dealing with the financial information, the Committee liaises with the Board and the Executive Directorate (including the Finance & Business Development Director), and the chairman of the Committee further meets on an ad hoc basis with the Head of Internal Audit, representatives of the External Auditor, and Management. Apart from considering issues arising from the audit, the Committee discusses any matters that auditor(s) may wish to raise either privately or together with executive Director(s) and any other person.

The Committee is required to review, at least annually, the effectiveness of the Company's financial controls, internal control and risk management systems and to report to the Board that such a review has been carried out. These controls and systems allow the Board to monitor the Company's overall financial position and to protect its assets. The Committee's review for 2010 also covered its role in overseeing the Management's review of the adequacy of resources, qualifications and experience of staff of the Company's accounting and financial reporting function, and their training programmes and budget. (Please refer to the section headed "Internal Controls" below.) The Committee reviews and approves the annual Internal Audit Plan which includes audits on the efficiency of chosen activities or operations of the Company. In addition, the Committee reviews periodic reports from the Head of Internal Audit and the follow-up of major action plans recommended, and puts forward recommendations to the Board where appropriate.

The chairman of the Committee summarises activities of the Committee and highlights issues arising therefrom by a report to the Board after each Audit Committee Meeting.

The minutes of the Audit Committee Meetings are prepared by the secretary of the meeting with details of the matters considered by the Committee Members and decisions reached, including any concerns raised by the Committee Members and dissenting views expressed. The draft minutes are circulated to the Committee Members for comments and the final version of the minutes is sent to the Committee Members for their records within a reasonable time after the Meeting and the minutes are open for inspection by the Committee Members at the Company's registered office. With reference to the Agenda Framework, the chairman of the Committee makes final determination on the agenda for the regular Committee Meetings.

Work Performed by Audit Committee

In 2010, the Audit Committee held four Meetings and, based on the Agenda Framework pre-agreed with the chairman of the Committee, a total of four Meetings had been scheduled for 2011. Among the four Meetings held in 2010, the Audit Committee had two separate Meetings for reviewing the annual results for the year ended 31 December 2009. The first Meeting concentrated on the operational, compliance and risk management related items while the second Meeting focused on the accounting and financial reporting matters.

The attendance record of each Audit Committee Member is set out on page 89 under the section "Board Proceedings". The major work performed by the Committee in 2010 included:

- Review of and recommendation for the Board's approval the draft 2009 Annual Report and Accounts and 2010 Interim Report and Accounts;
- Approval of the 2011 Internal Audit Plan;
- Pre-approval of the audit and non-audit services provided by KPMG, the External Auditor, for 2010;
- Approval of the remuneration and terms of engagement of KPMG for the 2010 audit;
- Review of KPMG's ethical and independence policies and procedures;
- Preview of 2010 annual accounting and financial reporting issues;
- Review of the effectiveness of the Company's internal control systems;
- Review of the effectiveness of the Internal Audit Department for 2009;
- Review of a report on staff complaints for 2009;
- Review of enterprise risk management for 2009;
- Review of the outstanding litigation and compliance with statutes and regulations relevant to the business of the Company; and
- Confirmation of the financial figures for the 2009 payout under '2008 Variable Incentive Scheme'.

Representatives of the External Auditor, the Finance & Business Development Director and the Head of Internal Audit attended all those Meetings for reporting and answering questions about their work. Further to that and by invitation, the Operations Director, the Property Director and the Legal Director & Secretary (or their representatives) had respectively provided an overview of the Company's railway operations, property business as well as outstanding litigation, compliance and enterprise risk management matters to the Members at the Meetings. The Finance & Business Development Director also provided an overview of the business development and expansion outside of Hong Kong.

Remuneration Committee

The Remuneration Committee consists of five non-executive Directors, four of whom are independent non-executive Directors. The Members of the Remuneration Committee are Mr. Edward Ho Sing-tin (chairman), Mr. T. Brian Stevenson, Mr. Vincent Cheng Hoi-chuen, Professor Chan Ka-keung, Ceajer and Mr. Alasdair George Morrison (effective from 9 July 2010). Mr. Ho, Mr. Stevenson, Mr. Cheng and Mr. Morrison are independent non-executive Directors.

Duties of Remuneration Committee

The principal responsibilities of the Remuneration Committee include formulating a remuneration policy and practices that facilitate the employment of top quality personnel, recommending to the Board the remuneration of the Members of the Board who are non-executive Directors, determining the remuneration packages of the Members of the Board who are executive Directors and other Members of the Executive Directorate, and reviewing and approving performance-based remuneration by reference to the Company's goals and objectives.

Work Performed by Remuneration Committee

In 2010, the Remuneration Committee held four Meetings. The attendance record of each Committee Member is set out on page 89 under the section "Board Proceedings". In accordance with its Terms of Reference, the Committee performed the following work during the year:

- Approved the 2009 Remuneration Report as incorporated in the 2009 Annual Report;

- Reviewed and approved payouts under the Company's performance-based variable incentive scheme for the 2009 performance period;
- Conducted an annual review of the remuneration packages for Members of the Executive Directorate, which took effect in July 2010;
- Reviewed and approved share options awards for Members of the Executive Directorate and other eligible employees; and
- Reviewed and approved the remuneration package for Dr. Jacob Kam Chak-pui, the new Operations Director whose appointment took effect from 1 January 2011.

The Remuneration Committee also met on 25 February 2011 to approve the 2010 Remuneration Report, which is set out on pages 100 to 103 and includes a description of the remuneration policy of the Company.

Nominations Committee

The Nominations Committee consists of seven non-executive Directors, four of whom are independent non-executive Directors. Members of the Nominations Committee are Mr. Edward Ho Sing-tin (chairman), Dr. Raymond Ch'ien Kuo-fung, Ms. Christine Fang Meng-sang, Mr. Abraham Shek Lai-him, Mr. Ng Leung-sing, Professor Chan Ka-keung, Ceajer and the S for T&H (Ms. Eva Cheng). Mr. Ho, Ms. Fang, Mr. Shek and Mr. Ng are also independent non-executive Directors.

Duties of Nominations Committee

The Nominations Committee nominates and recommends to the Board candidates for filling vacancies on the Board, and the positions of Chief Executive Officer ("CEO"), Finance Director ("FD") and Chief Operating Officer ("COO") (provided that the COO position exists). For the positions of FD and COO, the Committee may consider candidates recommended by the CEO, or any other candidates (provided that the CEO shall have the right to first agree to such other candidates).

Work Performed by Nominations Committee

In 2010, the Nominations Committee held one Meeting. Attended by all Members of the Committee at the Meeting on 9 July 2010 and after discussion, the Committee agreed to recommend to the Board the appointment of Mr. Alasdair George Morrison, a businessman with international exposure through his holding of a number of senior executive positions in leading multinational enterprises particularly in Asia (Mr. Morrison's biography is set out on page 106), as a Member of the Board, and as a Member of the Audit Committee and the Remuneration Committee respectively, all to take effect from 9 July 2010. Mr. Morrison was invited by chairman of the Committee to meet a majority of the Members on 10 May 2010. The appointment was approved by the Board on 9 July 2010.

Attendance record of each Committee Member is shown on page 89 under the section "Board Proceedings".

Corporate Responsibility Committee

The Corporate Responsibility Committee consists of five non-executive Directors (three of whom are independent non-executive Directors) and two Members of the Executive Directorate. The Chairman of the Company is the chairman of the Committee. Current Members of the Committee are Dr. Raymond Ch'ien Kuo-fung (Chairman), S for T&H (Ms. Eva Cheng), Ms. Christine Fang Meng-sang, Mr. Abraham Shek Lai-him, Mr. Vincent Cheng Hoi-chuen, Mr. Leonard Bryan Turk (Legal Director & Secretary) and Mr. Thomas Ho Hang-kwong (Property Director). Ms. Fang, Mr. Shek and Mr. Cheng are independent non-executive Directors.

Duties of Corporate Responsibility Committee

The duties of the Committee are to recommend a corporate responsibility policy to the Board for approval, monitor and oversee the implementation of the Company's corporate responsibility policy and initiatives, identify emerging corporate responsibility issues arising from external trends, review annual Sustainability Report and recommend endorsement by the Board, and provide updates to the Board as required. Please also refer to the "Corporate Responsibility" section on pages 83 to 84 of this Annual Report.

Work Performed by Corporate Responsibility Committee

In 2010, the Corporate Responsibility Committee held two Meetings. The attendance record of each Committee Member is set out on page 89 under the section "Board Proceedings". The major work performed by the Committee in 2010 included:

- Review of the implementation of the Company's community and staff engagement and communication programmes;
- Review of the sustainability development and environmental management of the Company;
- Review of corporate responsibility development of the Company; and
- Review of and recommendation for the Board's approval the draft 2009 Sustainability Report.

Internal Controls

The Board is responsible for the system of internal controls of the Company and its subsidiaries, setting appropriate policies and reviewing the effectiveness of such controls. Internal control is defined as a process effected by the Board, Management and other personnel, designed to manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable, and not absolute assurance of the following:

- effectiveness and efficiency of operations
- reliability of financial reporting
- compliance with applicable laws and regulations
- effectiveness of risk management functions

Pursuant to the Protocol adopted by the Board, the Board has delegated the day-to-day management of the Company's business to the Executive Committee, and focuses its attention on matters affecting the Company's overall strategic policies, finances and shareholders.

Supported by the Members of the Executive Committee, the Chief Executive Officer who chairs the Executive Committee is responsible to the Board for the conduct of the business of the Company.

A number of committees have been established to assist the Executive Committee in the day-to-day management and control of the various core businesses and functions of the Company and its subsidiaries. Key committees include:

- Operations Executive Management Committee
- Operations Business Meeting
- Property Executive Management Committee
- Project Control Group
- Railway Development Steering Group
- Consultancy Services Management Committee
- European Business Executive Committee
- China Business Executive Committee
- Information Technology Executive Management Committee
- Financial Planning Committee
- Investment Committee
- Corporate Safety Management Committee
- Enterprise Risk Committee
- Code of Conduct Steering Committee
- Tender Board
- Executive Tender Panel
- Corporate Responsibility Steering Committee

The Executive Committee is responsible for implementing the Board's policies on risk and control. In fulfilling its responsibilities, the Executive Committee identifies and evaluates the risks faced by the Company for consideration by the Board, and designs, operates and monitors a suitable system of internal controls which implements the policies adopted by the Board. The Executive Committee is accountable to the Board for monitoring the system of internal controls and providing assurance to the Board that it has done so. Additionally, all employees have responsibility for internal controls within their areas of accountability.

Various risk management strategies have been established by the Board as advised by the Executive Committee to identify, assess and reduce risks, including construction, business operations, finance, treasury, safety and enterprise risks as well as to ensure appropriate insurance coverage.

Risk Assessment and Management

The Company's Enterprise Risk Management framework is an essential and integral part of corporate governance to help in sustaining business success and creating value for stakeholders. It is a corporate-wide systematic risk management process which aims to assist the Executive Committee and individual business areas to manage the key risks and support the Board in discharging its corporate governance responsibilities.

More details of the framework and process are given in the section headed Risk Management on page 85.

Control Activities and Processes

To ensure the efficient and effective operation of business units and functions, and safety of operating railway and construction works in railway projects, Corporate General Instructions ("CGIs"), divisional/departmental procedures and manuals, committees, working groups and quality assurance units are established to achieve, monitor and enforce internal controls and evaluate their effectiveness.

CGIs and various departmental procedures and manuals are established for preventing or detecting unauthorised expenditures/payments, safeguarding the Company's assets, ensuring the accuracy and completeness of accounting records and timely preparation of reliable financial information.

All Department Heads, including Business and Project Managers for overseas projects, are responsible for ensuring the compliance with statutes and regulations applicable to their own functional units. They are required to identify any new or updated statutes, to assess their impact on the Company's operations, and to review at least once a year that relevant statutes/regulations are complied with. Potential and actual non-compliances are also reported and followed up by Department Heads and significant cases are reported to the respective Divisional Directors and the Executive Committee. Issues relating to compliance with statutes and regulations including potential and actual non-compliances, if any, and the status of rectification and actions taken to prevent recurrence are reported annually to the Executive Committee and Audit Committee.

The Internal Audit Department plays a major role, independent of the Company's management, in assessing and monitoring the internal controls of the Company. The Head of Internal Audit reports to the Chief Executive Officer and has direct access to the Audit Committee. The Department has unrestricted access to information that allows it to review all aspects of the Company's risk management, control and governance processes. On a regular basis, it conducts audits on financial, operational and compliance controls, and effectiveness of risk management functions of all business and functional units as well as subsidiaries. Management is responsible for ensuring that control deficiencies highlighted in internal audits are rectified within a reasonable period. The Department produces an annual internal audit plan derived from risk assessment for the Audit Committee's approval. On a half-yearly basis, the Head of Internal Audit reports the audit findings and opinion on the system of internal controls to the Audit Committee.

On behalf of the Board, the Audit Committee evaluates the effectiveness of the Company's system of internal controls, including the reliability of financial reporting, effectiveness and efficiency of operations, compliance with applicable laws and regulations and effectiveness of risk management functions. This is achieved primarily through approving the annual internal audit plan and reviewing the findings of internal audit work, in addition to reviewing the annual and interim financial statements, and the nature, scope of work, and report of the external auditors, and consideration of the following:

- the changes in the nature and extent of significant risks since the previous review and the Company's ability to respond to changes in its business and external environment;
- the scope and quality of management's ongoing monitoring of risks and the system of internal controls, the work of the Internal Audit Department, and the assurance provided by the Executive Committee;
- the extent and frequency with which the results of monitoring are communicated, enabling the Audit Committee to build up a cumulative assessment of the state of control in the Company and the effectiveness with which risk is being managed;
- the incidence of any significant control failings or weaknesses that have been identified at any time during the period and the extent to which they have resulted in unforeseen outcomes or contingencies that have had, could have had, or may in the future have, a material impact on the Company's financial performance or condition; and
- the effectiveness of the Company's processes in relation to financial reporting and statutory and regulatory compliance.

The processes for assessing internal controls by the Audit Committee have included: regular interviews with Members of the Executive Committee in relation to key business operations, internal control and compliance issues, both financial and non-financial; review of significant issues arising from internal audit reports and external audit report, private sessions with internal and external auditors, and review of annual assessment and certification of internal controls from Members of the Executive Committee and department heads within their areas of responsibility. The Audit Committee has also reviewed the papers prepared by the Executive Committee and Internal Audit Department covering: 2009 Annual Report and Accounts, Preview of 2010 Annual Accounting issues, 2010 Interim Accounts, 2011 Internal Audit Plan, Internal Audit Department's Half-yearly Reports, Annual Report on Staff Complaints, Report on the Company's Internal Control System, Reporting of Outstanding Litigation and Compliance Issues, Enterprise Risk Management Report 2009 and Evaluation of Effectiveness of Internal Audit Department. The chairman of the Committee meets on an ad hoc basis with the Head of Internal Audit, representatives of the External Auditor and Management of the Company as appropriate. He summarizes activities of the Committee and highlights issues arising therefrom by a report to the Board after each Audit Committee Meeting.

The Company is committed to recruit, train and develop a team of qualified and competent accountants in order to oversee its financial reporting and other accounting-related issues. A process to capture and update relevant laws, rules and regulations applicable to the reporting and accounting function is in place. Designated officers will ensure relevant standards and ordinances including Hong Kong Financial Reporting Standards, the Listing Rules and the Companies Ordinance under their responsibility are complied with. Resources and provisions required to deliver accounting and financial reporting function are critically reviewed during the annual budgeting exercise. Company-wide recruitment process and staff development programmes are in place to address the competency, qualifications and experience required. Adherence to the process is confirmed on an annual basis by the designated officers to the Finance & Business Development Director who will conduct a formalized annual review and report to the Audit Committee for the review results. Confirmation of the process is also monitored by the Internal Audit Department. Based on the above, the Audit Committee considered the resources, qualifications and experience of staff of the Company's accounting and financial reporting function, and their training programmes and budget were adequate.

The Board has, through the Audit Committee, conducted the review of the effectiveness of the Company's system of internal controls for the year ended 31 December 2010, covering all material financial, operational and compliance controls, and risk management function, and concluded that adequate and effective internal controls are maintained to safeguard the shareholders' investment and the Company's assets. There were no significant control failings, weaknesses or significant areas of concern identified during the year which might affect shareholders.

Crisis Management Committee

To uphold the reputation of being one of the best companies in Hong Kong and in order to help ensure that the Company will respond to and recover from crises in an organised and effective manner, including timely communications with principal stakeholders such as shareholders, the Company established a Crisis Management Committee in 1995. The Committee comprises relevant Members of the Executive Directorate and Executive Managers, and its operation is governed by a Crisis Management Manual which, among other things, sets out the duties of respective members. The Manual is kept up-to-date through regular reviews. The Crisis Management Committee conducts regular exercises to validate the crisis management organisation and arrangements and to provide practices for members. The latest exercise was conducted in December 2010.

Continuous Disclosure Obligations regarding Price Sensitive Information

The Company has developed a system with established policies, processes and procedures across all relevant Division(s) and Department(s) for complying with the disclosure obligations regarding price sensitive information. Further, a task force comprising all relevant heads of department reviewed the system in detail and thoroughly went through the checklist sent by the Stock Exchange to all issuers in late 2008. The recommendation that the Company has an effective system in dealing with the disclosure obligations was reported to the Executive Committee, and then to the Board of Directors in December 2008. The system continues to be effective throughout 2010. Efforts to further enhance the system in the light of the business operation and development of the Company will continue.

Governance of Subsidiaries and Affiliate Companies

The Company has a number of subsidiaries and affiliate companies which operate independent businesses in Hong Kong, the Mainland of China and overseas. Notwithstanding these subsidiaries and affiliate companies are separate legal entities, the Company has implemented a new management governance structure ('Governance Structure') to ensure that it exercises an appropriate level of control and oversight as a shareholder of these subsidiaries and affiliate companies.

Pursuant to the Governance Structure, the Company exercises its control and oversight in a number of forms: imposition of internal controls, requirements for consent or consultation, reporting requirements and assurance. The management of each subsidiary or affiliate company is responsible for the adoption of management practices and policies that are appropriate to the business nature and local situation, taking into account the management governance requirements of the Company, and developing a corporate governance manual for the entity which reflects both such management practices and policies as well as management governance requirements for approval by the relevant board of directors. Ongoing compliance with the manual is reported on a regular basis.

The Executive Committee will review the Governance Structure and compliance by the subsidiaries and affiliate companies with it on an annual basis.

Model Code for Securities Transactions by Directors of Listed Issuers

The Company has adopted the Model Code set out in Appendix 10 of the Listing Rules ('Model Code'). After having made specific enquiry, the Company confirms that Members of the Board and the Executive Directorate complied throughout the year with the Model Code. Senior managers, other nominated managers and staff 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. In addition, every employee is bound by the Code of Conduct issued by the Company, amongst other things, to keep unpublished price sensitive information in strict confidence.

Business Ethics

The Company is committed to upholding a high standard of integrity and business ethics. The Company's Code of Conduct, Corporate Guidebook for All Staff and Corporate Guidebook for Managers ("Guidebooks") are important tools to help employees understand and follow requirements on ethical practices. The Code of Conduct and the Guidebooks are reviewed and updated every two years to ensure they are appropriate and in compliance with legislation. The Company also requires all employees to acknowledge their understanding of and agreement to comply with the Code of Conduct and the Guidebooks every two years. All employees are encouraged to report existing or potential violations and malpractices. Staff who have genuine suspicions about wrongdoings are also provided with proper procedures and a safe environment to speak up pursuant to the Speaking Up policy in place. New recruits are briefed on the Code of Conduct and the Guidebooks, and such briefings form an integral part of the staff induction and orientation programmes. The Code of Conduct is available on the Company's website: www.mtr.com.hk.

A similar biennial certification programme is enforced in the Company's subsidiaries in the Mainland of China and overseas with a view to upholding the ethical culture in these subsidiaries. For other joint venture companies, guidelines on business ethics have been published for staff's observation and compliance.

External Auditor

The Company engages KPMG as its External Auditor. In order to maintain KPMG's independence and objectivity and the effectiveness of the audit process in accordance with applicable standards, the Audit Committee, under its Terms of Reference, pre-approves all audit services to be provided by KPMG and discusses with KPMG the nature and scope of their audit and reporting obligations before the audit commences.

The Audit Committee also reviews and pre-approves the engagement of KPMG to provide any non-audit services for complying with relevant legal requirements and seeks to balance the maintenance of objectivity with value for money.

The nature of audit and non-audit services provided by KPMG and fees paid to KPMG (including any entity that is under common control, ownership or management with the audit firm or any entity that a reasonable and informed third party having knowledge of all relevant information would reasonably conclude as part of the audit firm nationally or internationally) are set out in note 8D to the accounts on page 160.

On the part of KPMG, for maintaining integrity and objectivity, KPMG implements policies and procedures to comply with professional ethics and independence policies and requirements applicable to the work KPMG performs. In addition, KPMG requires its audit partner serving the Group to rotate off the audit engagement with the Company at least once every seven years.

Communication with Shareholders

Annual General Meeting ("AGM")

The Company's AGM is one of the principal channels of communication with its shareholders. It provides an opportunity for shareholders to communicate face to face with the Directors about the Company's performance and operations. The Chairman of the Company, the chairmen of the Board Committees, all Members of the Executive Committee and the Auditors of the Company were present at the 2010 AGM to answer shareholders' questions. The AGM for 2010 was held on 27 May at Rotunda 3 (6/F), Hongkong International Trade & Exhibition Centre (renamed as Kowloonbay International Trade & Exhibition Centre), Kowloon Bay, Hong Kong. The 2011 AGM has been scheduled for 6 May, approximately three weeks earlier than 2010. This is the second consecutive year of bringing forward the date of AGM in order to facilitate a direct dialogue between shareholders and Directors/ Management on annual results and other performance of the Company of the preceding year.

Chairman's Statement

The Chairman started the formal business of the AGM by reporting an overall good year for MTR, despite the challenging economic conditions and the threat posed by human swine influenza in 2009.

The Chairman then gave an overview of the Company's business performance including the ridership, train service performance, station commercial and rail related businesses, property development, property rental and management, Ngong Ping Cable Car and associated theme village and Octopus Cards. Early months of operations of rail franchises in Stockholm and Melbourne as well as Beijing Metro Line 4 were reported.

On business development, the Chairman reported the good progress of the five new railway projects in Hong Kong including the construction of the West Island Line (since 2009) and Hong Kong Section of the Guangzhou-Shenzhen-Hong Kong Express Rail Link (from 2010), and the status of detailed design for the South Island Line (East), the Kwun Tong Line Extension and Shatin to Central Link respectively.

The Chairman then gave a brief account of the growth strategy in the Mainland of China and overseas which was gaining momentum step by step. In addition to the rail franchises in Stockholm, Melbourne, London Overground and Beijing Metro Line 4, he covered the signing of a Concession Agreement for the operation and maintenance of the Daxing Line as an extension of Beijing Metro Line 4, the expected take over of the operation of the Shenzhen Metro Line 4 Phase 1 in 2010 and full operations (i.e. with Phase 2 together) sometime in 2011, and the signing of a Concession Agreement for Hangzhou Metro Line 1.

The important roles of corporate governance, sustainability, corporate responsibility and community involvement, in the continued success of the Company, were recognised by the Chairman.

Looking ahead, the Chairman said it was expected that patronage in Hong Kong would be benefited from improvements in the economy and the full year impact of the Kowloon Southern Link and the LOHAS Park Station. Apart from being the first full year for operating the Stockholm and Melbourne railway franchises, he said 2010 was also the first time in 13 years that MTR fares would be adjusted according to the Fare Adjustment Mechanism. Regarding other recurrent businesses, advertising, station retail and property rental businesses were market driven. For property development, the Chairman expected to make profit booking of Le Prestige and the small retail shopping mall in Area 56 of Tseung Kwan O, in 2010. As announced, he said Austin Sites C and D were awarded to a consortium about two months before the AGM.

Before closing, the Chairman thanked Mr. Russell Black who retired in January 2010 as the Projects Director. He also welcomed Mr. Vincent Cheng joining the Board as an independent non-executive director (since July 2009) and Mr. T C Chew who succeeded Mr. Black as the Projects Director with effect from January 2010.

Resolutions passed at the 2010 AGM

After the Chairman's Statement, separate resolutions were proposed for each substantially separate issue at that AGM. Before the resolutions were considered, the Chairman exercised his right as the Chairman of the Meeting under Article 67 of the Articles of Association to call a poll on all resolutions. Being the first listed company in Hong Kong to conduct electronic poll voting since 2007, the Company conducted electronic poll voting at the AGM.

A total of nine resolutions were passed at the 2010 AGM (with resolution no. 3 comprising three separate resolutions), each by over 97% of the votes cast at the Meeting. The full text of the resolutions is set out in the AGM Circular (which comprised Notice of the AGM) to shareholders dated 24 April 2010. For the benefit of those shareholders who did not attend the 2010 AGM, below is a succinct summary of the resolutions passed:

(1) Adoption of the audited Statement of Accounts and the Reports of the Directors and the Auditors of the Company for the year ended 31 December 2009;

(2) Declaration of a final dividend of HK$0.38 per share for the year ended 31 December 2009;

(3) (a) Election of Mr. Vincent Cheng Hoi-chuen as a Member of the Board of Directors of the Company;

(b) Re-election of Mr. Chow Chung-kong as a Member of the Board of Directors of the Company; and

(c) Re-election of Ms. Christine Fang Meng-sang as a Member of the Board of Directors of the Company.

(4) Re-appointment of KPMG as Auditors of the Company and authorisation of the Board of Directors to determine their remuneration;

(5) Grant of a general mandate to the Board of Directors to allot, issue, grant, distribute and otherwise deal with additional shares in the Company, not exceeding ten per cent. of the Company's issued share capital as at the date of this resolution*;

(6) Grant of a general mandate to the Board of Directors to purchase shares in the Company, not exceeding ten per cent. of the Company's issued share capital as at the date of this resolution*; and

(7) Conditional on the passing of resolutions 5 and 6, authorisation of the Board of Directors to exercise powers to allot, issue, grant, distribute and otherwise deal with additional shares in the Company under resolution 5 in respect of the aggregate nominal amount of share capital in the Company purchased by the Company*.

* (The full text of the resolution is set out in the Notice of the AGM.)

The poll results were posted on the websites of both the Company and the Stock Exchange on the same day after the AGM. The webcast of the AGM was also posted on the Company's website in the same evening after the AGM.

Extraordinary General Meeting ("EGM")

The Company may also communicate with its shareholders through EGMs if and when appropriate.

If shareholders want to convene an EGM of the Company, those shareholders may requisition the Directors of the Company to do so, provided that at the date of requisition they hold, in aggregate, not less than one-twentieth of the paid-up capital of the Company. The shareholders' requisition must state the objects of the meeting requested and must be deposited at the registered office of the Company. The requisition may consist of several documents in like form, each signed by one or more of the shareholders concerned.

If, within 21 days from the date of the deposit of the requisition, the Directors of the Company do not proceed duly to convene an EGM for a day not more than 28 days after the date on which the notice convening the EGM is given, the relevant shareholders, or any of them representing more than one-half of the total voting rights of all of them, may themselves convene an EGM, provided that any EGM so convened is held within three months from the date of the original requisition.

Procedures for Shareholders Putting Forward Proposals

Shareholders may put forward proposals for consideration at a general meeting according to the Companies Ordinance and the Company's Articles of Association.

Enquiries from Shareholders

Details of other means of communication with shareholders are set out in the section of Investor Relations on pages 80 and 81.

Remuneration Report

Introduction

The Remuneration Committee has been delegated the authority to consider and recommend to the Board the Company's remuneration policy and the remuneration packages of the non-executive Directors, as well as to review and determine the remuneration packages for the Chief Executive Officer and other Members of the Executive Directorate.

Throughout the year, the Committee meets regularly to discuss and approve remuneration issues pertaining to the Company's variable incentive scheme, share option scheme, and also the remuneration packages of the non-executive Directors, Chief Executive Officer and other Members of the Executive Directorate in the light of the Company's remuneration policy. In determining the remuneration of the Chief Executive Officer, the Committee consults with the Chairman and in the case of other Members of the Executive Directorate, the Committee consults with both the Chairman and the Chief Executive Officer in respect of their recommendations.

Currently, the Committee has five non-executive Directors, four of whom are independent non-executive Directors. As necessary and with the agreement of the Chairman, the Remuneration Committee is authorised to obtain outside independent professional advice to support the Committee on relevant issues. No individual Director or any of his associates is involved in deciding his own remuneration.

A summary of the work performed by the Remuneration Committee during 2010 is set out in the "Corporate Governance Report" on pages 93 and 94.

This Remuneration Report has been reviewed and authorised by the Remuneration Committee of the Company.

Remuneration policy

It is the Company's policy to ensure that remuneration is appropriate and aligns with the Company's goals, objectives and performance. To achieve this, the Company has taken into consideration a number of relevant factors such as salaries paid by comparable companies, job responsibilities, duties and scope, employment conditions elsewhere in the Company and its subsidiaries, market practices, financial and non-financial performance, and desirability of performance-based remuneration.

The Company is committed to effective corporate governance and employing and motivating top quality personnel. The Company also recognises the importance of a formal and transparent remuneration policy covering its Board and Executive Directorate.

Remuneration for Non-Executive Directors

The Remuneration Committee makes recommendations to the Board from time to time on the remuneration of the Members of the Board who are non-executive Directors. The remuneration of non-executive Directors is in the form of annual director's fees.

To ensure that non-executive Directors are appropriately remunerated for their time and responsibilities devoted to the Company, the Committee undertakes periodic reviews and considers the following factors as they put forward recommendations to the Board:

- Fees paid by comparable companies;
- Time commitment;
- Responsibilities of the non-executive Directors; and
- Employment conditions elsewhere in the Company.

Details of remuneration for non-executive Directors are set out in note 9 to the accounts.

Remuneration for Employees

The Company's remuneration structure for its employees, including the Chief Executive Officer and other Members of the Executive Directorate, comprises

- Fixed compensation – base salary, allowances and benefits-in-kind (e.g. medical);
- Variable incentives – discretionary award; performance-based payment and other business-specific cash incentive plans;
- Long-term incentives – e.g. share options;
- Retirement schemes.

The specifics of these components are described below.

Fixed Compensation

Base salary and allowances are set and reviewed annually. The annual review process takes into consideration the Company's remuneration policy, competitive market positioning, market practice, as well as the Company's and individuals' performance. Benefits-in-kind are reviewed regularly taking into consideration market practices.

Variable Incentives

The Chief Executive Officer, other Members of the Executive Directorate and selected management of the Company are eligible to receive an annual cash incentive under the Company's Variable Incentive Scheme, the rules of which are regularly reviewed by the Remuneration Committee.

Under the current scheme rules, the payouts are based on the performance of the Company and individual performance. The Company's performance is measured by both financial and non-financial factors including:

- Return on fixed assets;
- Rolling three-year operating profit;
- Fulfillment of the Customer Service Pledges; and
- Fulfillment of Performance Requirements in relation to "Train Service Delivery", "Passenger Journeys on Time" and "Train Punctuality" as defined in Schedule 2, Part 1 of the Operating Agreement.

If the Company does not achieve one or more of the Performance Requirements or the Customer Service Pledges, the payouts under the scheme are automatically reduced.

Following the end of each year, the Company engages an independent expert to conduct review and audit of its performance versus the Performance Requirements and Customer Services Pledges. The results of this audit are shared with the Remuneration Committee to determine if adjustments to the payouts under the scheme are appropriate.

Individual performance ratings are part of the thorough annual performance assessment process that is applied throughout the Company. The performance ratings and assessments reflect the full range of factors over which the individual has accountability, including operational, other non-financial and financial factors. Individual performance ratings for the Members of the Executive Directorate are determined by the Chief Executive Officer, and the performance for the Chief Executive Officer is assessed by the Chairman.

A portion of the target incentive levels under the scheme was originally funded by participants by foregoing their 13th month pay and portions of their fixed allowances. If performance exceeds pre-defined threshold standards, then payouts under the scheme are made annually. Target incentive levels for the Chief Executive Officer and other Members of the Executive Directorate represent approximately 15-30% of total remuneration.

In addition, the Company operates other business-related incentive schemes to motivate the staff concerned to reach specific business targets of the Company.

Discretionary Awards

In 2010, special discretionary awards were provided to staff with competent or above performance as a recognition of their contribution to the Company's good performance and achievements in the past year and to motivate staff to strive for continuous business growth.

Long-Term Incentives

During 2010, the Company maintained three share option schemes, namely the Pre-Global Offering Share Option Scheme (the "Pre-IPO Scheme"), the New Joiners Share Option Scheme (the "New Option Scheme") and the 2007 Share Option Scheme (the "2007 Scheme").

No further options are outstanding and exercisable under the Pre-IPO Scheme following its expiration on 11 September 2010. While options remain outstanding under the New Option Scheme, no new grants were made under this Scheme since the adoption of the 2007 Scheme.

The 2007 Scheme was approved and adopted by shareholders at the Company's Annual General Meeting on 7 June 2007. The 2007 Scheme is intended to provide employees of the Company and its subsidiaries the opportunity to participate in the growth and success of the Company. Awards under this Scheme were granted to the Chief Executive Officer, other Members of the Executive Directorate and selected employees of the Company in 2010. The Scheme continues to include a provision which specifies that options cannot be exercised under the Scheme unless the Company has satisfied each of the three Key Performance Requirements included in the Operating Agreement in order for any options to be exercised.

Options exercised and outstanding in respect of each Member of the Executive Directorate as at 31 December 2010 under the three Schemes are set out under the paragraph "Board Members' and Executive Directorate's Interests in Shares" of the Report of the Members of the Board.

Details of the three Schemes and options granted to Members of the Executive Directorate and selected employees of the Company under the Schemes are set out in notes 9 and 52 to the accounts.

Remuneration Report

The Chief Executive Officer does not participate in the Pre-IPO and New Option Schemes. He is entitled to receive an equivalent value in cash of 222,161 Shares on completion of his current contract on 31 December 2011.

Retirement Schemes

In Hong Kong, the Company operates five retirement schemes, the MTR Corporation Limited Retirement Scheme (the "MTR Retirement Scheme"), the MTR Corporation Limited Retention Bonus Scheme (the "MTR RBS"), the MTR Corporation Limited Provident Fund Scheme (the "MTR Provident Fund Scheme") and two Mandatory Provident Fund Schemes (the "MTR MPF Scheme" and the "KCRC MPF Scheme") with details as follows:

(a) MTR Retirement Scheme

The MTR Retirement Scheme is a registered scheme under the Occupational Retirement Schemes Ordinance (Cap. 426) and has been granted an MPF Exemption by the Mandatory Provident Fund Schemes Authority so that it can be offered to employees as an alternative to the MTR MPF Scheme.

The MTR Retirement Scheme originally contained both a hybrid benefit section and a defined contribution section. The hybrid benefit section of the MTR Retirement Scheme has been closed to new employees since 31 March 1999. All employees who joined the Company between 1 April 1999 and 29 February 2008 and who would have been eligible to join the MTR Retirement Scheme could choose to join either the defined contribution section or, from 1 December 2000, the MTR MPF Scheme.

Following the Rail Merger with Kowloon-Canton Railway Corporation ("KCRC") and with the approval of the scheme's trustees, the defined contribution section of the MTR Retirement Scheme was transferred to the MTR Provident Fund Scheme effective from 1 March 2008. After the transfer, the MTR Retirement Scheme only contains the hybrid benefit section which provides benefits based on the greater of a multiple of final salary times service or the accumulated contributions with investment returns. Members' contributions to the MTR Retirement Scheme are based on fixed percentages of base salary. The Company's contributions are determined by reference to an annual actuarial valuation carried out by an independent actuarial consulting firm.

(b) MTR RBS

The MTR RBS is a registered scheme under the Occupational Retirement Schemes Ordinance. It is a top-up scheme to supplement the MTR Retirement Scheme for employees who are classified by the Company as staff working on designated projects and who are not on gratuity terms. It provides benefits only in the event of redundancy for service accrued up to 31 December 2002, offset by any benefits payable from the MTR Retirement Scheme (including any benefits transferred to the MTR Provident Fund Scheme from the defined contribution section of the MTR Retirement Scheme). Members are not required to contribute while the Company's contributions are determined by reference to an annual actuarial valuation carried out by an independent actuarial consulting firm.

(c) MTR Provident Fund Scheme

The MTR Provident Fund Scheme, in order to reflect its integrated nature, was renamed from the KCRC Retirement Benefit Scheme following its incorporation of the defined contribution section of the MTR Retirement Scheme on 1 March 2008. It contains three sections, all of which are defined contribution schemes. One section consists of the members of the KCRC Retirement Benefit Scheme prior to 1 March 2008, the second section consists of the members transferred from the defined contribution section of the MTR Retirement Scheme prior to 1 March 2008, and the final section consists of those appointees eligible to join the MTR Provident Fund Scheme on or after 1 March 2008.

The MTR Provident Fund Scheme is a registered scheme under the Occupational Retirement Schemes Ordinance and has been granted an MPF Exemption by the Mandatory Provident Fund Schemes Authority so that it can be offered to employees as an alternative to the MPF Scheme. On or after 1 March 2008, employees who are eligible to join the MTR Provident Fund Scheme can choose between the MTR Provident Fund Scheme and the MTR MPF Scheme, except where they were previously members of the KCRC MPF Scheme, whereupon they can choose between the MTR Provident Fund Scheme and the KCRC MPF Scheme. All benefits payable under the MTR Provident Fund Scheme are calculated by reference to the Company's contributions and members' own contributions, together with investment returns on these contributions. Both members' and the Company's contributions are based on fixed percentages of members' base salary.

(d) MTR MPF Scheme

The MTR MPF Scheme, which has been registered with the Mandatory Provident Fund Schemes Authority, covers those employees who did not opt for or who are not eligible to join the MTR Retirement Scheme or the MTR Provident Fund Scheme. Both members and the Company each contribute to the MTR MPF Scheme at the mandatory levels as required by the Mandatory Provident Fund Schemes Ordinance ("the MPF Ordinance"). The Company makes additional contributions above the mandatory level for eligible members who joined the MTR MPF Scheme before 1 April 2008, subject to individual terms of employment.

(e) KCRC MPF Scheme

The KCRC MPF Scheme, which has been registered with the Mandatory Provident Fund Schemes Authority, covers those former KCRC employees who did not opt for or who were not eligible to join the former KCRC Retirement Benefit Scheme, now known as MTR Provident Fund Scheme, and those employees who, on or after 1 March 2008, were previously members of the KCRC MPF scheme and are eligible to join the MTR Provident Fund Scheme but opt to re-join the KCRC MPF Scheme. Both members and the Company each contribute to the KCRC MPF Scheme at the mandatory levels as required by the MPF Ordinance.

The executive Directors who were hired by the Company before 1 April 1999 are eligible to join the hybrid benefit section of the MTR Retirement Scheme.

Other executive Directors are eligible to join either the MTR Provident Fund Scheme or the MTR MPF Scheme.

The Chief Executive Officer participates in the MTR MPF Scheme. Both the Company and the Chief Executive Officer each contribute to the MTR MPF Scheme at the mandatory levels as required by the MPF Ordinance.

For subsidiary companies in Hong Kong, Mainland of China, United Kingdom, Sweden and Australia, the Group operates retirement schemes established in accordance with, in the case of subsidiaries in Hong Kong, the MPF Ordinance and, in the case of subsidiaries in Mainland of China and overseas, their respective local regulations.

Remuneration of Non-Executive and Executive Directors

(i) The total remuneration of the Members of the Board and the Executive Directorate (excluding share-based payments) is shown below and the remuneration details are set out in note 9 to the accounts.

in HK$ million	2010	2009
Fees	**4.2**	4.0
Base salaries, allowances and other benefits-in-kind	**34.6**	33.4
Variable remuneration related to performance	**18.3**	18.8
Retirement scheme contributions	**1.6**	5.4
	58.7	61.6

(ii) The gross remuneration of non-executive and executive Directors (excluding share-based payments) were within the following bands:

Remuneration	2010 Number	2009 Number
HK$0 – HK$500,000	**10**	11
HK$500,001 – HK$1,000,000	**1**	–
HK$1,000,001 – HK$1,500,000	**1**	1
HK$5,000,001 – HK$5,500,000	**1**	–
HK$6,000,001 – HK$6,500,000	**1**	–
HK$6,500,001 – HK$7,000,000	**3**	–
HK$7,000,001 – HK$7,500,000	**–**	6
HK$7,500,001 – HK$8,000,000	**1**	–
HK$13,500,001 – HK$14,000,000	**1**	1
	19	19

The information shown in the above table includes the five highest paid employees. The independent non-executive Directors' emoluments are included in the first remuneration band except the non-executive Chairman, whose emolument is included in the third remuneration band.

Edward Ho Sing-tin, *Chairman, Remuneration Committee*
MTR Corporation Limited
Hong Kong, 25 Feb 2011

Board and Executive Directorate

From Left to Right (1st row):
Dr. Raymond Ch'ien Kuo-fung *(Chairman)*, CK Chow *(Chief Executive Officer)*, Joseph Lai Yee-tak *(Commissioner for Transport)*, Christine Fang Meng-sang, Edward Ho Sing-tin, Vincent Cheng Hoi-chuen

From Left to Right (2nd row):
Ng Leung-sing, Abraham Shek Lai-him, Alasdair George Morrison, T. Brian Stevenson, Eva Cheng *(Secretary for Transport and Housing)*, Professor Chan Ka-keung, Ceajer *(Secretary for Financial Services and the Treasury)*

Members of the Board

Dr. Raymond Ch'ien Kuo-fung 59, was appointed Non-Executive Chairman in July 2003. He has been a member of the Board since 1998. Dr. Ch'ien is chairman of CDC Corporation, as well as chairman and a director respectively of its subsidiaries, China.com Inc. and CDC Software Corporation. He is also chairman and an independent non-executive director of Hang Seng Bank Limited. Dr. Ch'ien is an independent non-executive director of each of Convenience Retail Asia Limited, The Wharf (Holdings) Limited, Swiss Reinsurance Company Limited, and China Resources Power Holdings Company Limited (from 22 April 2010). He also serves on the boards of The Hongkong and Shanghai Banking Corporation Limited and Hong Kong Mercantile Exchange Limited. Dr. Ch'ien is chairman of the Hong Kong/European Union Business Cooperation Committee and a member of the Standing Committee of the Tianjin Municipal Committee of the Chinese People's Political Consultative Conference. In addition, Dr. Ch'ien is the honorary president and past chairman of the Federation of Hong Kong Industries. He was a member of the Executive Council of Hong Kong, then under British Administration, from 1992 to 1997, and a member of the Executive Council of the Hong Kong SAR from 1 July 1997 to June 2002. Dr. Ch'ien was appointed a Justice of the Peace in 1993. He was made a Commander in the Most Excellent Order of the British Empire in 1994 and awarded the Gold Bauhinia Star medal in 1999. In 2008, he was conferred the honour of Chevalier de l'Ordre du Merite Agricole of France. Dr. Ch'ien received a doctoral degree in economics from the University of Pennsylvania in 1978 and became a Trustee of the University in 2006. He was non-executive chairman of HSBC Private Equity (Asia) Limited (until 29 November 2010), a non-executive director of Inchcape plc., a Hong Kong member of APEC Business Advisory Council and chairman of the Advisory Committee on Corruption of the Independent Commission Against Corruption.

Chow Chung-kong 60, was appointed Chief Executive Officer on 1 December 2003. He was formerly chief executive officer of Brambles Industries Ltd, a global support services company. From 1997 to 2001, Mr. Chow was chief executive of GKN PLC, a leading engineering company based in the United Kingdom. Mr. Chow is a chartered engineer. He holds Bachelor of Science and Master of Science degrees in Chemical Engineering from The University of Wisconsin and The University of California respectively. He also holds a Master of Business Administration degree from The Chinese University of Hong Kong and attended the Advanced Management Program of Harvard Business School. He was awarded an Honorary Doctor of Engineering degree by The University of Bath. In 2000, Mr. Chow was knighted in the United Kingdom for his contribution to industry. Mr. Chow is an independent non-executive director of Anglo American plc, and AIA Group Limited (from 28 September 2010). He was the non-

executive chairman of Standard Chartered Bank (Hong Kong) Limited until 31 December 2010. In public service, Mr. Chow is a member of the Commission on Strategic Development, the Standing Committee on Directorate Salaries and Conditions of Service, the Standing Committee on Judicial Salaries and Conditions of Service (from 1 January 2010), as well as the Independent Commission on Remuneration for Members of the Executive Council and the Legislature, and Officials under the Political Appointment System of the HKSAR Government. Mr. Chow is a member of the Council of The Chinese University of Hong Kong and the Deputy Chairman of The Hong Kong General Chamber of Commerce (from 31 May 2010). He is also a board member of The Community Chest of Hong Kong and a member of the Standing Committee of the Shenzhen Municipal Committee of the Chinese People's Political Consultative Conference.

Vincent Cheng Hoi-chuen 62, joined the Board as an independent non-executive Director on 10 July 2009. Mr. Cheng is chairman of HSBC Bank (China) Company Limited, and HSBC Bank (Taiwan) Limited (from 21 January 2010). He is also an executive director of HSBC Holdings plc. Mr. Cheng was chairman of The Hongkong and Shanghai Banking Corporation Limited and a non-executive director of HSBC Bank (Vietnam) Limited. He is also an independent non-executive director of Great Eagle Holdings Limited, and a non-executive director of Swire Properties Limited (from 14 April 2010). In public service, Mr. Cheng is vice chairman of the China Banking Association and chairman of the Independent Commission on Remuneration for Members of the Executive Council and the Legislature, and Officials under the Political Appointment System of the HKSAR Government. He was a member of the Exchange Fund Advisory Committee of the Hong Kong Monetary Authority (until 31 January 2010). In 2008, Mr. Cheng was appointed a member of the National Committee of the 11th Chinese People's Political Consultative Conference (the 'CPPCC') and a senior adviser to the 11th Beijing Municipal Committee of the CPPCC. He was also a member of the Executive Council from 1995 to 1997, Hong Kong Affairs Adviser to the People's Republic of China from 1994 to 1997 as well as a member of the Legislative Council from 1991 to 1995. In 2005, Mr. Cheng was conferred the degree of Doctor of Social Science, *honoris causa*, by The Chinese University of Hong Kong and the degree of Doctor of Business Administration, *honoris causa*, by The Open University. He was also awarded the Gold Bauhinia Star medal in 2005. Mr. Cheng holds a Bachelor of Social Science degree in Economics from The Chinese University of Hong Kong and a Master of Philosophy degree in Economics from The University of Auckland.

Board and Executive Directorate

Christine Fang Meng-sang 52, is an independent non-executive Director and has been a member of the Board since 2004. Ms. Fang has been the chief executive of the Hong Kong Council of Social Service since 2001. Prior to joining the Hong Kong Council of Social Service, she worked for the Hong Kong Red Cross from 1989 to 2001 and held the position of Secretary General from 1993 to 2001. By training, Ms. Fang is a social worker and has a strong background in community service. She sits on various government advisory committees, including the Sustainable Development Council, the Digital 21 Strategy Advisory Committee, the Charities Sub-committee of The Law Reform Commission of Hong Kong, the Independent Police Complaints Council, and the Steering Committee on the Community Care Fund (from 11 November 2010). She is also a member of the Commission on Strategic Development.

Edward Ho Sing-tin 72, is an independent non-executive Director and has been a member of the Board since 1991. He is an architect and the Group Chairman of Wong Tung Group of companies. Mr. Ho was an elected member of the Legislative Council of Hong Kong from 1991 to 2000, representing the architectural, surveying and planning functional constituency. He was president of the Hong Kong Institute of Architects in 1983 and 1984 and was chairman of the Hong Kong Industrial Estates Corporation from 1992 to 2001. He was also a member of the Hong Kong Housing Authority, chairman of the Antiquities Advisory Board, chairman of the Hong Kong Philharmonic Society, and a member of the Town Planning Board and the Hospital Authority respectively.

Allister George Morrison (also known as Alasdair George Morrison) 62, joined the Board as an independent non-executive Director on 9 July 2010. Mr. Morrison is currently Senior Advisor of Citigroup Asia Pacific, and an independent non-executive director of Pacific Basin Shipping Limited and Hong Kong Mercantile Exchange Limited. He is also a member of the Board of Grosvenor Group Limited in the United Kingdom, a member of the Hong Kong/European Union Business Cooperation Committee, a member of the Operations Review Committee of the Independent Commission Against Corruption and a Director of the Hong Kong Forum. He was non-executive chairman of North Asia Investment Corporation (until 15 August 2010), vice chairman of Harvard Business School Association of Hong Kong (until 26 August 2010) and a member of the Bloomberg Asia Pacific Advisory Board (until 26 October 2010). From 1971 to 2000, Mr. Morrison worked for the Jardine Matheson Group, where he was Group Managing Director from 1994 to 2000. Subsequently, and until April 2007, Mr. Morrison was a Managing Director of Morgan Stanley Dean Witter Asia Limited and then also a member of Morgan Stanley's Management Committee. From 2000 to 2007, he was Chairman of Morgan Stanley Asia, based in Hong Kong. From 2002 to February 2006, he was concurrently Chairman and Chief Executive Officer of Morgan Stanley Asia. Mr. Morrison is a graduate of Eton College and obtained a Bachelor of Arts (subsequently Master of Arts) from Cambridge University in 1971. He also attended the Program for Management Development at Harvard Business School in 1983.

Ng Leung-sing 61, joined the Board as an independent non-executive Director on 18 December 2007. Mr. Ng is vice chairman of Chiyu Banking Corporation, chairman of Bank of China (Hong Kong) Trustees Limited and an independent non-executive director of SmarTone Telecommunications Holdings Limited. He is a director of the BOCHK Charitable Foundation and a member of the Court of Lingnan University. He was general manager, Bank-wide Operation Department of Bank of China (Hong Kong) Limited. Mr. Ng is also a Hong Kong Deputy to the 10th and 11th National People's Congress, People's Republic of China. Mr. Ng is a graduate of University of East Asia, Graduate College, Macau and holds a diploma in Chinese Law.

Abraham Shek Lai-him 65, joined the Board as an independent non-executive Director on 18 December 2007. Mr. Shek is an independent non-executive director and an audit committee member of each of Midas International Holdings Limited, Paliburg Holdings Limited, Lifestyle International Holdings Limited, Chuang's Consortium International Limited, NWS Holdings Limited, Regal Portfolio Management Limited, Titan Petrochemicals Group Limited, Eagle Asset Management (CP) Limited, ITC Corporation Limited, Country Garden Holdings Company Limited, SJM Holdings Limited, Kosmopolito Hotels International Limited (from 10 September 2010) and China Resources Cement Holdings Limited (from 1 January 2011). He is also an independent non-executive director of Hsin Chong Construction Group Ltd. and Hop Hing Group Holdings Limited. Mr. Shek is chairman an independent non-executive director of Chuang's China Investments Limited. He is also vice chairman, an independent non-executive director and a member of the audit committee of ITC Properties Group Limited (from 30 September 2010). Mr. Shek was appointed as Justice of the Peace in 1995 and was awarded the Silver Bauhinia Star in 2007. He is vice chairman of the Independent Police Complaints Council. Mr. Shek is a graduate of the University of Sydney and holds a Bachelor of Arts degree and a Diploma in Education.

T. Brian Stevenson 66, is an independent non-executive Director and has been a member of the Board since October 2002. He is a non-executive director of The Hongkong and Shanghai Banking Corporation Limited, an Advisor to BT Asia Pacific and Chairman of the Hong Kong Jockey Club (from 31 August 2010). He was a member of the Public Service Commission (up to 31 January 2010). Mr. Stevenson was previously the Senior Partner of Ernst & Young, Hong Kong from 1981 to 1999. He served on the Council of the Hong Kong Society of Accountants from 1991 to 1997 and was president of the Society in 1996. Mr. Stevenson is a chartered accountant and holds law degrees from Glasgow and Hong Kong Universities. He was awarded the Silver Bauhinia Star medal in 1998. He is also a Justice of the Peace.

Commissioner for Transport (Joseph Lai Yee-tak 50, joined the Board as a non-executive Director appointed as an "additional director" under section 8 of the MTR Ordinance by virtue of his appointment to the post of the Commissioner for Transport of the Government of the Hong Kong SAR on 17 August 2009. Since 1983, Mr. Lai has served in various bureaux and departments of the

Government of the Hong Kong SAR. Before joining the Transport Department, he was Director-General of Trade and Industry. As Commissioner for Transport, Mr. Lai is also a director of several transport-related companies including The Kowloon Motor Bus Company (1933) Limited, Long Win Bus Company Limited, New World First Bus Services Limited, New Lantao Bus Company (1973) Limited, Citybus Limited, The Star Ferry Company Limited, The New Hong Kong Tunnel Company Limited, Western Harbour Tunnel Company Limited, Tate's Cairn Tunnel Company Limited and Route 3 (CPS) Company Limited. He is a graduate of the University of Hong Kong and holds a Bachelor's Degree in Social Sciences.)

Secretary for Transport and Housing (Eva Cheng 50, joined the Board as a non-executive Director appointed as an "additional director" under section 8 of the MTR Ordinance on 1 July 2007 upon her appointment as the Secretary for Transport and Housing of the Government of the Hong Kong SAR. Ms. Cheng has served in various bureaux and departments of the Government of the HKSAR since 1983. Before joining the Transport and Housing Bureau, Ms. Cheng was the Permanent Secretary for Economic Development. She is a graduate of the University of Hong Kong and holds a Bachelor of Social Sciences degree.)

Professor Chan Ka-keung, Ceajer 54, joined the Board as a non-executive Director on 10 July 2007 after his appointment as the Secretary for Financial Services and the Treasury of the Government of the Hong Kong SAR with effect from 1 July 2007. He received his Bachelor's degree in economics from Wesleyan University in the US and both his M.B.A. and Ph.D. in finance from the University of Chicago. Professor Chan sits on the boards of several public bodies including the Mandatory Provident Fund Schemes Authority and The Hong Kong Mortgage Corporation Limited and is the Chairman of the Kowloon-Canton Railway Corporation in his official capacity. Before joining the Government, Professor Chan was Dean of Business and Management of the Hong Kong University of Science and Technology from 1 July 2002. He was an independent non-executive Director of Shui On Construction and Materials Limited.

Members of the Executive Directorate

Chow Chung-kong Biographical details are set out on page 104.

William Chan Fu-keung 62, has been the Human Resources Director since August 1998. He joined the Company as Human Resources Manager in 1989. He oversees human resource management, people development, organisation development, operations and management training, administration and security management. Prior to joining the Company, Mr. Chan held senior management positions in both the commercial and utility sectors in Hong Kong, including the Government, the Hong Kong Productivity Council, Hutchison Whampoa Limited and Hong Kong Telecommunications Limited. He is a fellow member of the Hong Kong Institute of Human Resource Management since 1985 and is also a council member of the Institute. He is a council member of Employers' Federation of Hong Kong, a member of the Standing Committee on Disciplined Services Salaries and Conditions of Service, the Pensions Appeal Panel and the School of Business Advisory Committee of Hong Kong Baptist University. Mr. Chan received a Bachelor of Social Science degree from The University of Hong Kong in 1971, majoring in economics.

Chew Tai Chong 59, has been the Projects Director of the Company since 1 February 2010. He joined the Company in May 2009 as Deputy Projects Director – New Projects. Mr. Chew has worked in the rail transit industry, in the United Kingdom, Singapore and overseas, for over 30 years. Between 2003 and 2008, he was the President of Bombardier London Underground Projects Division. Up to 2003, he held the position of Senior Director, Projects and Engineering, for Land Transit Authority of Singapore. Mr. Chew is a member of the Hong Kong Construction Industry Council. He holds a Bachelor of Science degree and a Master of Science degree in Electrical Engineering from University of Manchester. Mr. Chew is a chartered engineer and a fellow of a number of professional institutions in the United Kingdom and Hong Kong Institution of Engineers as well as Hong Kong Academy of Engineering Sciences. Mr. Chew is also a director in some of the members of the Company's group.

Thomas Ho Hang-kwong 59, has served as the Property Director since joining the Company in 1991. Mr. Ho is responsible for the development and management of all properties above and adjacent to MTR stations and depots. He leads a multi-disciplinary team of managers involved in the planning, design, construction and management of large-scale property developments. Between 1971 and 1990, Mr. Ho worked for the Hong Kong Government specialising in land administration and latterly held a directorate post in the Lands Department, responsible for formulating policies and procedures to make land available for the airport and the Airport Railway project. Mr. Ho qualified in 1974 as a chartered surveyor in Hong Kong. He is serving The Community Chest of Hong Kong as a Campaign Committee Member and Corporate and Employee Contribution Programme Organising Committee Co-chairman. Mr. Ho is Honorary Professor of the Department of Real Estate and Construction of The University of Hong Kong. In November 2010, he was awarded the first "Outstanding BRE Alumni Award" by The Hong Kong Polytechnic University. Mr. Ho is also a director in some of the members of the Company's group.

Andrew McCusker 65, was the Operations Director of the Company from 2005 to December 2010. He retired from the Company on 1 January 2011 after cumulatively 22 years of service.

Dr. Jacob Kam Chak-pui 49, has been the Operations Director and a Member of the Executive Directorate since 1 January 2011. He was appointed as Deputy Operations Director on 1 July 2010. Dr. Kam joined the Company in 1995. During his 15 years of service, he gained both technical and business experience through taking up different managerial positions in Operations, Projects and China & International Business Divisions. Dr. Kam holds a Bachelor of Science degree in Civil Engineering from the University of Southampton, and a doctoral degree in Mechanical Engineering from the University of London (University College London), both in United Kingdom. He also attended the Wharton Advanced Management Programme at

Board and Executive Directorate

the University of Pennsylvania, U.S.A. in 2005. Dr. Kam qualified as a chartered engineer in the United Kingdom in 1989. He is a member of both the Institution of Mechanical Engineers, United Kingdom, and The Hong Kong Institution of Engineers. He is also a chartered fellow of the Institution of Occupational Safety and Health, United Kingdom. Dr. Kam is also a director in some of the members of the Company's group.

Lincoln Leong Kwok-kuen 50, has served as the Finance & Business Development Director since May 2008. Mr. Leong joined the Company in February 2002 as the Finance Director and is responsible for the financial management of all of the Company's affairs, including financial planning and control, budgeting, accounting and reporting and the treasury function. In addition, he has responsibility for the Company's information technology function and serves as chairman of the board of trustees of the Company's retirement schemes. On 1 May 2008, he was re-titled the Finance & Business Development Director to reflect his additional role in overseeing growth business in the Mainland of China and overseas. Mr. Leong graduated from Cambridge University in 1982 and later qualified as a chartered accountant in England in 1985 and Canada in 1986. Prior to joining the Company as Finance Director, he worked in both the accountancy and investment banking industries. Mr. Leong had worked as an accountant in London and Vancouver, Canada and for a number of years as an investment banker in Hong Kong. Mr. Leong is a non-official member of the Family Council and a member of the executive committee of the Hong Kong Housing Society. He also serves on the Board of Governor of the Chinese International School. Mr. Leong is a non-executive director of both Hong Kong Aircraft Engineering Company Limited and Tai Ping Carpets International Limited. He was non-executive chairman of Octopus Holdings Limited (until 31 December 2010). Mr. Leong is also a director in some of the members of the Company's group.

Leonard Bryan Turk 61, is a solicitor admitted to practise both in England and Wales and in Hong Kong. He joined the Company in 1981 and has been the Legal Director & Secretary to the Board since 1988. Mr. Turk is responsible for legal advice including agreements for new rail Projects, overseas and Mainland of China rail concessions, property development joint ventures, finance and related instruments as well as any contentious or non-contentious legal work, corporate secretarial services, insurance, procurement and contracts for the operational railway and property portfolio, as well as related to the new rail Projects, enterprise risk management

From Left to Right (back):
Andrew McCusker, William Chan Fu-keung, Lincoln Leong Kwok-kuen, Thomas Ho Hang-kwong, Leonard Bryan Turk

From Left to Right (front): Jeny Yeung Mei-chun, CK Chow, Chew Tai Chong, Miranda Leung Chan Che-ming

and corporate responsibility functions within the Company. His other responsibilities include all matters of corporate governance as well as tender and award of construction contracts, contract administration and dispute resolution. Before joining the Company, Mr. Turk worked in local government in England, concentrating particularly on commercial property development and the financing of large projects. Mr. Turk is also a director in some of the members of the Company's group.

Members of the Executive Committee

The Executive Committee comprises all Members of the Executive Directorate (whose biographies are on pages 107 to 109), General Manager – Corporate Relations, and General Manager – Marketing & Station Commercial.

Miranda Leung Chan Che-ming 58, has served the Company since 1976 and was appointed Head of the Corporate Relations Department in 1994. As General Manager – Corporate Relations, she is responsible for formulating and directing the implementation of corporate relations strategy and policies to project, maintain and enhance the public image of the Company. Her responsibilities include corporate communications, community and customer engagement, stakeholder management and political lobbying. In 1985, Mrs. Leung qualified as a chartered member of The Chartered Institute of Transport (renamed as The Chartered Institute of Logistics and Transport) in UK. She is a member of UK's Chartered Institute of Public Relations and a chartered fellow of The Chartered Institute of Logistics & Transport in Hong Kong. Mrs. Leung is a member of the Council for Sustainable Development.

Jeny Yeung Mei-chun 46, joined the Company in November 1999 as the Marketing Manager. Being the General Manager – Marketing & Station Commercial, Ms. Yeung is responsible for the marketing of the Company's railway services including fare management and promoting their usage as well as managing and enhancing the MTR Brand. She is also responsible for the management of the various non fare businesses including advertising and shop rental within the stations. Ms. Yeung graduated from the University of Hong Kong and holds a Bachelor degree in Social Sciences majoring in Management Studies. She is a fellow of the Chartered Institute of Marketing. Before joining the Company, she held various marketing and business development positions in Standard Chartered Bank (Hong Kong) Limited and Citibank in Hong Kong. Ms. Yeung is also a director in some of the members of the Company's group.

Key Corporate Management

Chow Chung-kong
Chief Executive Officer

Operations

Andrew McCusker
Operations Director (up to 31 December 2010)

Jacob Kam Chak-pui
Operations Director (w.e.f. 1 January 2011)

Morris Cheung Siu-wa
Chief of Operations Engineering (w.e.f. 1 January 2011)

Choi Tak-tsan
Head of Operating – Control & East Region

Ivan Lai Ching-kai
Head of Operating – Support & West Region

William Leung Hon-wai
Head of Operations Strategic Business Management

David Leung Chuen-choi
General Manager – Technical & Engineering Services

Ronald Cheng Kin-wai
Deputy General Manager – Asset Engineering

Richard Keefe
General Manager – Infrastructure

Tony Lee Kar-yun
Rolling Stock Fleet Manager

Chan Chi-kit
Rolling Stock Workshop Manager

George Lee Kai-wing
General Manager – Safety & Quality

Ho Chun-wing
Planning & Development Manager

Francis Li Shing-kee
Head of Operations Interface (w.e.f. 1 January 2011)

Carmen Li Wai-ching
General Manager – Intercity

China & International Business

Lincoln Leong Kwok-kuen
Finance and Business Development Director

Wilfred Lau Cheuk-man
Head of Operations – China & International Business

Richard Wong Shiu-ki
General Manager – Beijing & Tianjin

Adi Lau Tin-shing
General Manager – Shenzhen

Antonio Choi Fung-chung
Chief Project Manager – Shenzhen Line 4

Leung Kwok-yiu
General Manager – Special Projects
(China & International Business)(w.e.f. 1 January 2011)

Jeremy Long
Chief Executive Officer – European Business

Projects

Chew Tai Chong
Projects Director

Paul Lo Po-hing
General Manager – XRL

David Sorton
General Manager – XRL Civil Construction

Alvin Luk Wing-kwok
Project Manager – XRL E&M

Alan Morris
Project Manager – XRL Tunnels

Calum Smith
Project Manager – XRL Terminus

Roderic Hockin
General Manager – WIL/SIL

Barry Hill
Project Manager – WIL/SIL E&M

Julian Saunders
Project Manager – WIL Civil

Mark Cuzner
Project Manager – SIL Civil

Henry Lam Hing-cheung
General Manager – SCL/KTE

James Chow So-hung
Project Manager – SCL/KTE Civil

Lee Tze-man
Project Manager – SCL/KTE E&M

Dono Tong Kwok-wai
Project Manager – Operations Projects

Mike Yeoman
Project Manager – Rolling Stock

Karl Dodsworth
Project Manager – Signalling

Malcolm Gibson
Head of Project Engineering (up to 31 March 2011)

Wilfred Yeung Sze-wai
Chief Architect

Alan Myers
Chief Civil Construction Engineer

Stephen Chik Wai-keung
Chief Civil & Planning Engineer

Leung Chi-lap
Chief E&M Engineer

Property

Thomas Ho Hang-kwong
Property Director

Roger Poon Fat-chi
Head of Property Investment & Management

James Hor Wai-hong
Head of Property Development (w.e.f. 1 January 2011)

David Tang Chi-fai
Head of Property Project

Steve Yiu Chin
Head of Town Planning

Mingo Kwan Sze-ming
General Manager – Property Management

Betty Leong Sin-ling
General Manager – Investment Property

Victor Chan Hin-fu
General Manager – Guangdong & Shenzhen Property
(w.e.f. 1 January 2011)

Finance

Lincoln Leong Kwok-kuen
Finance and Business Development Director

Ricky Tsang Tin-for
General Manager – Financial Control

Herbert Hui Leung-wah
General Manager – Corporate Finance

Jeff Kwan Wai-hung
Treasurer

Daniel Lai Sik-cheung
Head of Information Technology

Candy Ng Chui-lok
Head of Investor Relations and Retirement Benefits

Legal & Procurement

Leonard Turk
Legal Director & Secretary

David Fleming
Deputy Legal Director (up to 31 December 2010)

Gillian Meller
Deputy Legal Director (w.e.f. 1 December 2010)

Martin Dunn
General Manager – Procurement & Contracts

Teresa Tang Sui-ching
Procurement & Contracts Manager – Operations

Stephen Griffin
Procurement & Contracts Manager – HK Projects (E&M)

Scott Mackenzie
Procurement & Contracts Manager – HK Projects (Civil)

Lila Fong Man-lee
Legal Manager – Company Secretarial

Linda Li Sau-lin
Legal Manager – Property

Human Resources & Administration

William Chan Fu-keung
Human Resources Director

Vincent Luk Kin-ping
General Manager – Human Resources

Daniel Shim Ming-yi
General Manager – Human Resources Development

Marketing

Jeny Yeung Mei-chun
General Manager – Marketing & Station Commercial

Corporate Relations

Miranda Leung Chan Che-ming
General Manager – Corporate Relations

May Wong May-kay
Deputy General Manager – Corporate Relations

Internal Audit

Denise Ng Kee Wing-man
Head of Internal Audit

Report of the Members of the Board

The Members of the Board have pleasure in submitting their Report and the audited statement of Accounts for the financial year ended 31 December 2010.

Principal Activities of the Group

The principal activities of the Company and its subsidiaries are:

A the operation of a modern railway system with lines from Central to Tsuen Wan (Tsuen Wan Line), from Yau Ma Tei to Tiu Keng Leng (Kwun Tong Line), from Po Lam and LOHAS Park to North Point (Tseung Kwan O Line), from Chai Wan to Sheung Wan (Island Line), from Hong Kong to Tung Chung (Tung Chung Line), from Hong Kong to the Hong Kong International Airport and then AsiaWorld-Expo both at Chek Lap Kok (Airport Express), from Sunny Bay to Disneyland Resort (Disneyland Resort Line), from Hung Hom to the boundary at Lo Wu and Lok Ma Chau (East Rail Line), from Tai Wai to Wu Kai Sha (Ma On Shan Line), from Hung Hom to Tuen Mun (West Rail Line), the North-west Railway (commonly known as Light Rail) in the North-West New Territories of Tuen Mun, Tin Shui Wai and Yuen Long, an intercity railway system between Hong Kong and some major cities in the Mainland of China, and feeder bus services in support of West Rail Line, East Rail Line and Light Rail;

B property development, either as owner or as an agent for KCRC, at locations along the related railway lines including the Tseung Kwan O Line, the Ma On Shan Line, the East Rail Line, the Light Rail and the West Rail Line;

C related commercial activities, including the letting of advertising and retail space, enabling telecommunication services on the railway system, property management and leasing management of investment properties (including shopping malls, offices and residential units);

D the investment in a 50% equity share in the operation of the 7-year UK's London Overground Concession, consisting of 5 London railway lines (including the East London Line from Dalston Junction to West Croydon and Crystal Palace which was refurbished and extended, and commenced operation in May 2010), increasing the total route length to 110 kilometres;

E the investment in the operation (including rolling stock maintenance which is undertaken by a 50:50 joint venture) of the 8-year Sweden's Stockholm Metro Concession, consisting of three lines measuring a total of 108 kilometres, linking the Swedish capital's central areas with surrounding suburbs;

F the investment in a 60% equity share in the operation and maintenance of Australia's Melbourne train system, consisting of 15 lines measuring a total of 372 kilometres, linking Melbourne's central business district with surrounding suburbs, under a franchise agreement with an initial period of 8 years;

G the design and construction of the West Island Line as an extension of the Island Line;

H the design, construction, procurement of services and equipment, and all other matters associated with bringing the Hong Kong section of the Guangzhou-Shenzhen-Hong Kong Express Rail Link into service;

I the design of the Kwun Tong Line Extension and the South Island Line (East) as the railway system extensions for which scheme authorisation has been granted;

J the planning and design of the Shatin to Central Link as a major project for which the Government has confirmed policy support;

K the operation of the Tung Chung to Ngong Ping Cable Car System and the Theme Village in Ngong Ping, Lantau Island, Hong Kong;

L worldwide consultancy services covering all areas of expertise required in the project management, planning, construction, operation, maintenance and up-grading of railways plus fare collection, property integration/development advice including other property related services and advice on generation of non-fare revenues;

M investment in Octopus Holdings Limited, a subsidiary of the Company, which has business activities both in Hong Kong and overseas including the operation of a smart card system by its subsidiary Octopus Cards Limited for the collection of payments for both transport and non-transport applications in Hong Kong;

N equity investments and long term operations and maintenance contracts outside of Hong Kong;

O property management, shopping mall investment and railway related property development business in the Mainland of China;

P the investment in a 49% equity interest in a joint venture for the investment, construction and operations of Beijing Metro Line 4, consisting of 28 kilometres with 24 stations forming the main north-south traffic artery for Beijing, Mainland of China under a 30-year concession agreement with the Beijing Municipal Government, and operations and maintenance of Beijing Metro Daxing Line, an extension to the Beijing Metro Line 4, consisting of 22 kilometres with 11 stations, under a 10-year operations and maintenance concession agreement with Beijing Metro Daxing Line Investment Company Limited, a wholly owned subsidiary of Beijing Municipal Government; and

Q the investment in the design, construction and future operations of Phase 2, together with operations of Phase 1 (which started in July 2010) of Shenzhen Metro Line 4, a 20.5 kilometres double-track urban railway running from Futian Checkpoint at the boundary between Hong Kong and Shenzhen, Mainland of China, to Longhua New Town in Shenzhen with a total of 15 stations, under a 30-year Build-Operate-Transfer concession agreement with the Shenzhen Municipal Government.

Report of the Members of the Board

A Concession Agreement for a Public-Private Partnership project for the investment, construction and operations of Hangzhou Metro Line 1 for a term of 25 years was entered into by MTR Hangzhou Line 1 Investment Company Limited (a wholly-owned subsidiary of the Company) and a subsidiary of Hangzhou Metro Group Company Limited together with Hangzhou Municipal Government. The Concession Agreement is pending for the regulatory Central Government approval.

The Company had wound down its freight business in June 2010 to better utilize train paths thus providing greater flexibility for passenger train services.

Dividend

The Directors have recommended a final dividend of HK$0.45 per Ordinary Share to be payable to shareholders whose names appear on the Register of Members of the Company on 24 March 2011. Subject to the passing of the necessary resolutions at the forthcoming Annual General Meeting, such dividend will be payable on or about 18 May 2011, in cash in Hong Kong dollars, with a scrip dividend alternative.

Members of the Board

Members of the Board who served during the year were Raymond Ch'ien Kuo-fung (non-executive Chairman), Chow Chung-kong (Chief Executive Officer), Vincent Cheng Hoi-chuen, Christine Fang Meng-sang, Edward Ho Sing-tin, Allister George Morrison (also known as Alasdair George Morrison) [appointed on 9 July 2010], Ng Leung-sing, Abraham Shek Lai-him, T. Brian Stevenson, Chan Ka-keung, Ceajer, the Secretary for Transport and Housing (Eva Cheng) and the Commissioner for Transport (Joseph Lai Yee-tak).

In December 2010, Chow Chung-kong informed the Board that he would retire from the position of Chief Executive Officer and cease to be a Member of the Board when his current contract as the Chief Executive Officer expires on 31 December 2011.

At the Annual General Meeting on 27 May 2010 and pursuant to the Articles of Association, Chow Chung-kong, Christine Fang Meng-sang and Vincent Cheng Hoi-chuen retired under the Articles of Association and were re-elected/elected as Members of the Board.

At the 2011 Annual General Meeting and in accordance with the Articles of Association, Edward Ho Sing-tin, Ng Leung-sing and Abraham Shek Lai-him will retire by rotation and will offer themselves for re-election. Alasdair George Morrison, who was appointed by the Board after the 2010 Annual General Meeting, will retire under Article 85 of the Articles of Association and will offer himself for election at the 2011 Annual General Meeting. Please also refer to pages 90 to 91 of the Corporate Governance Report.

Biographical details for Board Members are set out on pages 104 to 107.

Alternate Directors

The Alternate Directors in office during the year were:

- for Chan Ka-keung, Ceajer: Ying Yiu-hong, Leung Cheuk-man [ceased on 25 October 2010] and Chu Man-ling [with effect from 25 October 2010];
- for the office of the Secretary for Transport and Housing: (i) the Under Secretary for Transport and Housing (Yau Shing-mu); (ii) the Permanent Secretary for Transport and Housing (Transport) (Ho Suen-wai); and (iii) the Deputy Secretary for Transport and Housing (Transport) (Yung Wai-hung and Shirley Yuen [who ceased to be Deputy Secretaries for Transport and Housing (Transport) and accordingly ceased to be alternate directors to the office of the Secretary for Transport and Housing, with effect from 1 February 2010 and 1 October 2010 respectively], Maisie Cheng Mei-sze [with effect from 1 February 2010] and Rebecca Pun Ting-ting [with effect from 1 October 2010]); and
- for the Commissioner for Transport: the Deputy Commissioner for Transport/Transport Services and Management (Carolina Yip Lai-ching).

Executive Directorate

The Members of the Executive Directorate who served during the year were Chow Chung-kong (Chief Executive Officer and a Member of the Board), Russell John Black [retired on 1 February 2010], William Chan Fu-keung, Chew Tai Chong [appointed on 1 February 2010], Thomas Ho Hang-kwong, Lincoln Leong Kwok-kuen, Andrew McCusker [retired with effect from 1 January 2011] and Leonard Bryan Turk.

Russell John Black retired as Projects Director and a Member of the Executive Directorate, and Chew Tai Chong was appointed as Projects Director and a Member of the Executive Directorate, both with effect from 1 February 2010. Mr. Chew joined the Company as Deputy Projects Director – New Projects in May 2009.

As announced on 21 June 2010, Andrew McCusker retired as Operations Director and a Member of the Executive Directorate, and Jacob Kam Chak-pui was appointed as Operations Director and a Member of the Executive Directorate, both with effect from 1 January 2011. Dr. Kam joined the Company in 1995, and was appointed as Deputy Operations Director in July 2010.

Biographical details for Members of the Executive Directorate during the year are set out on pages 107 to 109.

Internal Audit

The Company's Internal Audit Department provides independent, objective assurance and consulting services designed to add value and improve the Company's operations. Key responsibilities of the Department include:

- Assessment of the adequacy and effectiveness of the Company's system of internal controls over its activities and risk management.
- Identification of opportunities for improving management control, resources utilisation and profitability.
- Special reviews and/or investigations as commissioned by Company management or the Audit Committee.

The Head of Internal Audit reports directly to the Chief Executive Officer and has direct access to the Audit Committee.

Business Ethics

Please refer to pages 97 to 98.

Policies

The Board has adopted the following risk management strategies and policies:

A Construction and Insurance Risk Management Strategy;

B Finance Risk Management Strategy;

C Treasury Risk Management Strategy;

D Safety Risk Management Strategy;

E Enterprise Risk Management Strategy;

F Security Risk Management Policy; and

G Environmental Risk Management Policy.

Public Float

The Stock Exchange granted to the Company, at the time of its listing on the Main Board of the Stock Exchange in 2000, a waiver from strict compliance with Rule 8.08(1) of the Listing Rules ("Public Float Waiver"). Pursuant to the Public Float Waiver, the Company's prescribed minimum percentage of shares which must be in the hands of the public must not be less than 10% of the total issued share capital of the Company. Based on the information that is publicly available to the Company and within the knowledge of the Directors, the Company has maintained the prescribed amount of public float during the year and up to the date of this report as required by the Public Float Waiver.

Bank Overdrafts, Bank Loans and Other Borrowings

The total borrowings of the Group as at 31 December 2010 amounted to HK$21,057 million (2009: HK$23,868 million). Particulars of borrowings including bank overdrafts and bank loans are set out in note 42 to the accounts.

Accounts

The state of affairs of the Company and the Group as at 31 December 2010 and of the Group's results, changes in equity and cash flows for the year are set out in the accounts on pages 139 to 234.

Ten-Year Statistics

A summary of the results and of the assets and liabilities of the Group together with some major operational statistics for the last ten years are set out on pages 78 to 79.

Fixed Assets and Railway Construction in Progress

Movements in fixed assets and railway construction in progress during the year are set out in notes 22 to 24 and 26 to the accounts respectively.

Movements in Reserves

Movements in reserves during the year are set out in the Consolidated Statement of Changes in Equity and notes 50 and 51 to the accounts.

Share Capital

As at 31 December 2009, the authorised share capital of the Company was HK$6.5 billion, divided into 6.5 billion Ordinary Shares, 5,727,833,692 of which were issued and credited as fully paid.

During the year, the Company issued a total of 44,729,339 Ordinary Shares. Of this number:

A 2,922,500 Ordinary Shares were issued by the Company pursuant to the exercise of share options which had been granted under the Company's Pre-Global Offering Share Option Scheme (as referred in note 50A to the accounts). In respect of each Ordinary Share issued, the relevant exercise price per share of options is HK$8.44 to the Company;

B 195,000 Ordinary Shares were issued by the Company pursuant to the exercise of share options which had been granted under the Company's New Joiners Share Option Scheme (as referred in note 50A to the accounts). In respect of each Ordinary Share issued, the relevant exercise price per share of options are HK$9.75, HK$18.05 and HK$20.66 to the Company;

C 1,573,500 Ordinary Shares were issued by the Company pursuant to the exercise of share options which had been granted under the Company's 2007 Share Option Scheme (as referred in note 50A to the accounts). In respect of each Ordinary Share issued, the relevant exercise price per share of options are HK$18.30, HK$24.50, HK$26.52, HK$26.85, and HK$27.60 to the Company;

D 37,130,522 Ordinary Shares were issued by the Company in order to satisfy shareholders' scrip dividend elections in respect of the final dividend of the Company for the year ended 31 December 2009 (for which the cash dividend was HK$0.38 per Ordinary Share); and

E 2,907,817 Ordinary Shares were issued by the Company in order to satisfy shareholders' scrip dividend elections in respect of the interim dividend of the Company for the six months ended 30 June 2010 (for which the cash dividend was HK$0.14 per Ordinary Share).

As at 31 December 2010, the authorised share capital of the Company was HK$6.5 billion, divided into 6.5 billion Ordinary Shares, 5,772,563,031 of which were issued and credited as fully paid.

Redemption of Listed Securities

The Company redeemed its US$600 million global notes on 8 November 2010. The notes were listed on the Luxembourg Stock Exchange prior to the redemption.

Saved as disclosed above, neither the Company nor any of its subsidiaries has purchased, sold or redeemed any of its listed securities during the financial year 2010.

Properties

Particulars of the principal investment properties and properties held for sale of the Company are shown on pages 52 to 53.

Donations

During the year, the Company donated a total of HK$2,401,000 to charitable and other organisations, including donations of HK$1 million and HK$500,000 to the victims of the Qinghai and Haiti earthquake respectively to help provide clothing, medical supplies and other emergency materials.

In addition, the MTR HONG KONG Race Walking 2010 raised over HK$1.13 million (including over HK$64,000 from MTR staff) for the Hospital Authority Health InfoWorld to promote good health.

The Company helped raise funds for the Community Chest and the Hong Kong Cancer Fund with a total cash donation of over HK$310,000 through different activities such as CARE Scheme, Green Day, Love Teeth Day and Dress Special Day for the former organisation and Dress Pink Day for the latter.

Reporting and Monitoring

There is a comprehensive budgeting system for all operational and business activities, with an annual budget approved by the Board. Monthly results of the Company's operations, businesses and projects are reported against the budget to the Board and updated forecasts for the year are prepared regularly.

Treasury Management

The Company's Treasury Department operates within approved guidelines from the Board. It manages the Company's debt profile with reference to the Preferred Financing Model which defines the preferred mix of financing instruments, fixed and floating rate debts, maturities, interest rate risks, currency exposure and financing horizon. The model is reviewed and refined periodically to reflect changes in the Company's financing requirements and market environment. Derivative financial instruments such as interest rate swaps and cross currency swaps are used only as hedging tools to manage the Group's exposure to interest rate and currency risks. Prudent guidelines and procedures are in place to control the Company's derivatives activities, including a comprehensive credit risk management system for monitoring counterparty credit exposure using the Value-at-Risk approach. There is also appropriate segregation of duties within the Company's Treasury Department.

Major financing transactions and guidelines for derivatives transactions including credit risk management framework are approved at the Board level.

Capital and Revenue Expenditure

There are defined procedures for the appraisal, review and approval of major capital and revenue expenditures. All project expenditure over 0.2% of the net assets of the Company and the employment of consultancy services over 0.1% of the net assets of the Company require the approval of the Board.

Bonds and Notes Issued

The Group has not issued any bonds or notes during the financial year 2010.

Computer Processing

There are defined procedures, controls and regular quality reviews on the operation of computer systems to ensure the accuracy and completeness of financial records and efficiency of data processing. The Company's computer centre operation and support, help desk operation and support services, and also software development and maintenance, have been certified under ISO 9001:2008. Disaster recovery rehearsal on critical applications is conducted annually.

Interests in Contracts of Members of the Board and the Executive Directorate

There was no contract of significance, to which the Company or any of its subsidiaries was a party and in which a Member of the Board or a Member of the Executive Directorate had a material interest (whether direct or indirect), which subsisted at the end of the year or at any time during the year.

Board Members' and Executive Directorate's Interests in Shares

As at 31 December 2010, the interests or short positions of the Members of the Board and the Executive Directorate in the shares, underlying shares and debentures of the Company (within the meaning of Part XV of the Securities and Futures Ordinance (Cap. 571 of the Laws of Hong Kong) ("SFO")) as recorded in the register required to be kept under section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code were as follows:

Long Positions in Shares and Underlying Shares of the Company

	Number of Ordinary Shares held			Derivatives: Share Options	Derivatives: Other		
Member of the Board or the Executive Directorate	Personal* interests	Family† interests	Corporate interests	Personal* interests	Personal* interests	Total interests	Percentage of aggregate interests to total issued share capital
Raymond Ch'ien Kuo-fung	51,499	–	–	–	–	51,499	0.00089
Chow Chung-kong	–	–	–	2,130,000 (Note 1)	222,161 (Note 2)	2,352,161	0.04075
Vincent Cheng Hoi-chuen	1,675	1,675	–	–	–	3,350	0.00006
Christine Fang Meng-sang	1,712	–	–	–	–	1,712	0.00003
T. Brian Stevenson	5,072	–	–	–	–	5,072	0.00009
William Chan Fu-keung	124,849	–	–	680,000 (Note 1)	–	804,849	0.01394
Chew Tai Chong	–	–	–	425,000 (Note 1)	–	425,000	0.00736
Thomas Ho Hang-kwong	148,850	2,541	–	637,500 (Note 1)	–	788,891	0.01367
Lincoln Leong Kwok-kuen	23,000	–	23,000 (Note 3)	(i) 417,500 (Note 4) (ii) 680,000 (Note 1)	–	1,143,500	0.01981
Andrew McCusker	–	–	–	453,000 (Note 1)	–	453,000	0.00785
Leonard Bryan Turk	–	–	–	637,500 (Note 1)	–	637,500	0.01104

Long Positions in Shares and Underlying Shares of the Company *(continued)*

Member of the Executive Directorate	Number of Ordinary Shares held: Personal* interests	Family† interests	Corporate interests	Derivatives – Share Options: Personal* interests	Derivatives – Other: Personal* interests	Total interests	Percentage of aggregate interests to total issued share capital
Jacob Kam Chak-pui (Note 5)	2,283	–	–	425,000 (Note 1)	–	427,283	0.00740

Notes

1 Further details of the above share options are set out in the table below showing details of the options to subscribe for ordinary shares granted under the 2007 Share Option Scheme.

2 Chow Chung-kong has a derivative interest in respect of 222,161 shares in the Company within the meaning of Part XV of the SFO. That derivative interest represents Mr. Chow's entitlement to receive an equivalent value in cash of 222,161 shares in the Company on completion of his existing contract (on 31 December 2011).

3 The 23,000 shares are held by Linsan Investment Ltd., a private limited company beneficially wholly owned by Lincoln Leong Kwok-kuen.

4 Further details of the above share options are set out in the table below showing details of the options to subscribe for ordinary shares granted under the New Joiners Share Option Scheme.

5 Jacob Kam Chak-pui became the Operations Director and a Member of the Executive Directorate on 1 January 2011.

* Interests as beneficial owner

† Interests of spouse or child under 18 as beneficial owner

Options to subscribe for Ordinary Shares granted under the Pre-Global Offering Share Option Scheme, as referred to in Notes 9B(i) and 52A(i) to the Accounts

Executive Directorate and eligible employees	Date granted	No. of options granted	Period during which rights exercisable (day/month/year)	Options outstanding as at 1 January 2010	Options vested during the year	Options lapsed during the year	Options exercised during the year	Exercise price per share of options (HK$)	Options outstanding as at 31 December 2010	Weighted average closing price of shares immediately before the date(s) on which options were exercised (HK$)
William Chan Fu-keung	20/9/2000	1,066,000	5/4/2001 – 11/9/2010	117,500	–	–	117,500	8.44	–	28.65
Other eligible employees	20/9/2000	41,409,000	5/4/2001 – 11/9/2010	2,830,500	–	25,500	2,805,000	8.44	–	27.86

Notes

1 The Pre-Global Offering Share Option Scheme ("Pre-IPO Option Scheme") was valid and effective for a period of ten years after 12 September 2000. No option might be offered to be granted under the Pre-IPO Option Scheme on or after the commencement of dealings in shares of the Company on Stock Exchange on 5 October 2000 ("Listing Date").

2 The number of shares to which the option granted to each participant under the Pre-IPO Option Scheme did not exceed 25% of the number of the shares issued and issuable under the Pre-IPO Option Scheme.

3 The above share options fully vested on 5 October 2003. The proportion of underlying shares in respect of which the share options had vested was as follows:

Date	Proportion of underlying shares in respect of which an option is vested
Before 5 October 2001	none
5 October 2001 to 4 October 2002	one-third
5 October 2002 to 4 October 2003	two-thirds
After 4 October 2003	all

Vesting of the share options might be accelerated to an earlier date in some circumstances. However, no such option should vest and become exercisable before 5 April 2001, i.e. the date falling six months after the Listing Date.

4 The Pre-IPO Option Scheme expired on 11 September 2010.

Options to subscribe for Ordinary Shares granted under the New Joiners Share Option Scheme, as referred to in Notes 9B(ii) and 52A(ii) to the Accounts

Executive Directorate and eligible employees	Date granted	No. of options granted	Period during which rights exercisable (day/month/year)	Options outstanding as at 1 January 2010	Options granted during the year	Options vested during the year	Options lapsed during the year	Options exercised during the year	Exercise price per share of options (HK$)	Options outstanding as at 31 December 2010	Weighted average closing price of shares immediately before the date(s) on which options were exercised (HK$)
Lincoln Leong Kwok-kuen	1/8/2003	1,066,000	14/7/2004 – 14/7/2013	417,500	–	–	–	–	9.75	417,500	–
Other eligible employees	1/8/2003	495,200	14/7/2004 – 14/7/2013	139,200	–	–	–	31,000	9.75	108,200	28.51
	23/9/2005	213,000	9/9/2006 – 9/9/2015	213,000	–	–	–	–	15.97	213,000	–
	31/3/2006	94,000	20/3/2007 – 20/3/2016	94,000	–	–	–	94,000	18.05	–	29.20
	5/10/2006	94,000	29/9/2007 – 29/9/2016	94,000	–	–	–	–	19.732	94,000	–
	12/5/2006	266,500	25/4/2007 – 25/4/2016	266,500	–	–	–	–	20.66	266,500	–
	15/5/2006	213,000	25/4/2007 – 25/4/2016	92,000	–	–	–	70,000	20.66	22,000	28.64

Notes

1 No option may be exercised later than ten years after its date of offer and no option may be offered to be granted more than five years after the adoption of the New Joiners Share Option Scheme ("New Option Scheme") on 16 May 2002.

2 Unless approved by shareholders in the manner as required by the Listing Rules, the total number of shares issued and issuable upon exercise of the options granted to any eligible employee under the New Option Scheme together with the total number of shares issued and issuable upon the exercise of any option granted to such eligible employee under any other share option scheme of the Company (including, in each case, both exercised and outstanding options) in any 12-month period must not exceed 1% of the shares of the Company in issue at the date of offer in respect of such option under the New Option Scheme.

3 The proportion of underlying shares in respect of which the above share options will vest is as follows:

Date	Proportion of underlying shares in respect of which an option is vested
Before the first anniversary of the date of offer of the option (the "Offer Anniversary")	none
From the first Offer Anniversary to the date immediately before the second Offer Anniversary	one-third
From the second Offer Anniversary to the date immediately before the third Offer Anniversary	two-thirds
From the third Offer Anniversary and thereafter	all

Options to subscribe for Ordinary Shares granted under the 2007 Share Option Scheme, as referred to in Notes 9B(iii) and 52A(iii) to the Accounts

Executive Directorate and eligible employees	Date granted	No. of options granted	Period during which rights exercisable (day/month/year)	Options outstanding as at 1 January 2010	Options granted during the year	Options vested during the year	Options lapsed during the year	Options exercised during the year	Exercise price per share of options (HK$)	Options outstanding as at 31 December 2010	Weighted average closing price of shares immediately before the date(s) on which options were exercised (HK$)
Chow Chung-kong	13/12/2007	720,000	10/12/2008 – 10/12/2014	720,000	–	240,000	–	–	27.60	720,000	–
	9/12/2008	470,000	8/12/2009 – 8/12/2015	470,000	–	157,000	–	–	18.30	470,000	–
	9/12/2009	470,000	8/12/2010 – 8/12/2016	470,000	–	157,000	–	–	26.85	470,000	–
	17/12/2010	470,000	16/12/2011 – 16/12/2017	–	470,000	–	–	–	28.84	470,000	–
William Chan Fu-keung	13/12/2007	170,000	10/12/2008 – 10/12/2014	170,000	–	56,000	–	–	27.60	170,000	–
	9/12/2008	170,000	8/12/2009 – 8/12/2015	170,000	–	57,000	–	–	18.30	170,000	–
	10/12/2009	170,000	8/12/2010 – 8/12/2016	170,000	–	57,000	–	–	26.85	170,000	–
	17/12/2010	170,000	16/12/2011 – 16/12/2017	–	170,000	–	–	–	28.84	170,000	–
Chew Tai Chong	18/6/2009	85,000	12/6/2010 – 12/6/2016	85,000	–	28,500	–	–	24.50	85,000	–
	10/12/2009	170,000	8/12/2010 – 8/12/2016	170,000	–	57,000	–	–	26.85	170,000	–
	17/12/2010	170,000	16/12/2011 – 16/12/2017	–	170,000	–	–	–	28.84	170,000	–
Thomas Ho Hang-kwong	12/12/2007	170,000	10/12/2008 – 10/12/2014	170,000	–	56,000	–	–	27.60	170,000	–
	11/12/2008	170,000	8/12/2009 – 8/12/2015	170,000	–	57,000	–	–	18.30	170,000	–
	14/12/2009	170,000	8/12/2010 – 8/12/2016	170,000	–	57,000	–	–	26.85	170,000	–
	17/12/2010	127,500	16/12/2011 – 16/12/2017	–	127,500	–	–	–	28.84	127,500	–
Lincoln Leong Kwok-kuen	12/12/2007	170,000	10/12/2008 – 10/12/2014	170,000	–	56,000	–	–	27.60	170,000	–
	9/12/2008	170,000	8/12/2009 – 8/12/2015	170,000	–	57,000	–	–	18.30	170,000	–
	10/12/2009	170,000	8/12/2010 – 8/12/2016	170,000	–	57,000	–	–	26.85	170,000	–
	17/12/2010	170,000	16/12/2011 – 16/12/2017	–	170,000	–	–	–	28.84	170,000	–
Andrew McCusker	12/12/2007	170,000	10/12/2008 – 10/12/2014	170,000	–	56,000	–	–	27.60	170,000	–
	12/12/2008	170,000	8/12/2009 – 8/12/2015	170,000	–	57,000	–	57,000	18.30	113,000	26.80
	10/12/2009	170,000	8/12/2010 – 8/12/2016	170,000	–	57,000	–	–	26.85	170,000	–
Leonard Bryan Turk	12/12/2007	170,000	10/12/2008 – 10/12/2014	170,000	–	56,000	–	–	27.60	170,000	–
	9/12/2008	170,000	8/12/2009 – 8/12/2015	170,000	–	57,000	–	–	18.30	170,000	–
	10/12/2009	170,000	8/12/2010 – 8/12/2016	170,000	–	57,000	–	–	26.85	170,000	–
	17/12/2010	127,500	16/12/2011 – 16/12/2017	–	127,500	–	–	–	28.84	127,500	–
Jacob Kam Chak-pui (Note 4)	13/12/2007	75,000	10/12/2008 – 10/12/2014	75,000	–	25,000	–	–	27.60	75,000	–
	8/12/2008	65,000	8/12/2009 – 8/12/2015	65,000	–	22,000	–	–	18.30	65,000	–
	14/12/2009	65,000	8/12/2010 – 8/12/2016	65,000	–	22,000	–	–	26.85	65,000	–
	21/7/2010	50,000	28/6/2011 – 28/6/2017	–	50,000	–	–	–	27.73	50,000	–
	17/12/2010	170,000	16/12/2011 – 16/12/2017	–	170,000	–	–	–	28.84	170,000	–
Other eligible employees	11/12/2007	45,000	10/12/2008 – 10/12/2014	45,000	–	15,000	–	–	27.60	45,000	–
	12/12/2007	2,050,000	10/12/2008 – 10/12/2014	1,736,000	–	577,000	12,000	116,000	27.60	1,608,000	29.61
	13/12/2007	840,000	10/12/2008 – 10/12/2014	840,000	–	272,000	–	–	27.60	840,000	–
	14/12/2007	1,005,000	10/12/2008 – 10/12/2014	973,000	–	319,000	35,500	65,500	27.60	872,000	29.89
	15/12/2007	435,000	10/12/2008 – 10/12/2014	370,000	–	121,000	–	27,000	27.60	343,000	29.20
	17/12/2007	835,000	10/12/2008 – 10/12/2014	773,000	–	256,000	–	22,000	27.60	751,000	30.35
	18/12/2007	445,000	10/12/2008 – 10/12/2014	380,000	–	124,000	–	92,000	27.60	288,000	29.27
	19/12/2007	115,000	10/12/2008 – 10/12/2014	115,000	–	26,000	35,000	–	27.60	80,000	–
	20/12/2007	190,000	10/12/2008 – 10/12/2014	190,000	–	63,000	–	–	27.60	190,000	–
	21/12/2007	45,000	10/12/2008 – 10/12/2014	45,000	–	15,000	–	30,000	27.60	15,000	28.55
	22/12/2007	35,000	10/12/2008 – 10/12/2014	35,000	–	11,000	–	–	27.60	35,000	–
	24/12/2007	118,000	10/12/2008 – 10/12/2014	118,000	–	39,000	–	–	27.60	118,000	–

Options to subscribe for Ordinary Shares granted under the 2007 Share Option Scheme, as referred to in Notes 9B(iii) and 52A(iii) to the Accounts *(continued)*

Executive Directorate and eligible employees	Date granted	No. of options granted	Period during which rights exercisable (day/month/year)	Options outstanding as at 1 January 2010	Options granted during the year	Options vested during the year	Options lapsed during the year	Options exercised during the year	Exercise price per share of options (HK$)	Options outstanding as at 31 December 2010	Weighted average closing price of shares immediately before the date(s) on which options were exercised (HK$)
Other eligible employees	28/12/2007	35,000	10/12/2008 – 10/12/2014	35,000	–	11,000	–	–	27.60	35,000	–
	31/12/2007	130,000	10/12/2008 – 10/12/2014	130,000	–	43,000	–	–	27.60	130,000	–
	2/1/2008	75,000	10/12/2008 – 10/12/2014	75,000	–	24,000	27,000	–	27.60	48,000	–
	3/1/2008	40,000	10/12/2008 – 10/12/2014	40,000	–	13,000	–	–	27.60	40,000	–
	7/1/2008	125,000	10/12/2008 – 10/12/2014	125,000	–	41,000	–	–	27.60	125,000	–
	28/3/2008	255,000	26/3/2009 – 26/3/2015	255,000	–	87,500	–	51,000	26.52	204,000	29.25
	31/3/2008	379,000	26/3/2009 – 26/3/2015	379,000	–	131,000	–	30,000	26.52	349,000	29.32
	1/4/2008	261,000	26/3/2009 – 26/3/2015	261,000	–	91,000	–	12,000	26.52	249,000	30.55
	2/4/2008	296,000	26/3/2009 – 26/3/2015	296,000	–	103,000	6,000	14,000	26.52	276,000	28.40
	3/4/2008	171,000	26/3/2009 – 26/3/2015	171,000	–	59,500	–	12,000	26.52	159,000	29.15
	4/4/2008	23,000	26/3/2009 – 26/3/2015	23,000	–	8,000	–	–	26.52	23,000	–
	5/4/2008	17,000	26/3/2009 – 26/3/2015	17,000	–	6,000	–	–	26.52	17,000	–
	7/4/2008	390,000	26/3/2009 – 26/3/2015	358,000	–	124,000	–	16,000	26.52	342,000	30.55
	8/4/2008	174,000	26/3/2009 – 26/3/2015	155,000	–	54,000	23,000	16,000	26.52	116,000	30.70
	9/4/2008	85,000	26/3/2009 – 26/3/2015	85,000	–	29,500	–	–	26.52	85,000	–
	10/4/2008	58,000	26/3/2009 – 26/3/2015	58,000	–	20,000	–	–	26.52	58,000	–
	11/4/2008	134,000	26/3/2009 – 26/3/2015	117,000	–	40,500	–	–	26.52	117,000	–
	12/4/2008	48,000	26/3/2009 – 26/3/2015	48,000	–	16,500	–	–	26.52	48,000	–
	14/4/2008	40,000	26/3/2009 – 26/3/2015	40,000	–	14,000	–	–	26.52	40,000	–
	15/4/2008	34,000	26/3/2009 – 26/3/2015	34,000	–	12,000	–	–	26.52	34,000	–
	16/4/2008	57,000	26/3/2009 – 26/3/2015	40,000	–	14,000	–	–	26.52	40,000	–
	17/4/2008	147,000	26/3/2009 – 26/3/2015	124,000	–	43,000	–	–	26.52	124,000	–
	18/4/2008	32,000	26/3/2009 – 26/3/2015	15,000	–	5,000	–	–	26.52	15,000	–
	19/4/2008	25,000	26/3/2009 – 26/3/2015	25,000	–	8,500	–	–	26.52	25,000	–
	21/4/2008	66,000	26/3/2009 – 26/3/2015	66,000	–	23,000	–	–	26.52	66,000	–
	23/4/2008	34,000	26/3/2009 – 26/3/2015	19,000	–	6,500	–	–	26.52	19,000	–
	8/12/2008	90,000	8/12/2009 – 8/12/2015	45,000	–	15,500	–	–	18.30	45,000	–
	9/12/2008	483,000	8/12/2009 – 8/12/2015	483,000	–	154,500	16,500	13,500	18.30	453,000	27.46
	10/12/2008	2,176,400	8/12/2009 – 8/12/2015	2,161,400	–	734,000	–	120,500	18.30	2,040,900	28.92
	11/12/2008	2,294,200	8/12/2009 – 8/12/2015	2,294,200	–	772,500	–	173,000	18.30	2,121,200	29.28
	12/12/2008	1,311,500	8/12/2009 – 8/12/2015	1,305,000	–	442,000	–	126,000	18.30	1,179,000	28.35
	13/12/2008	84,500	8/12/2009 – 8/12/2015	84,500	–	28,500	–	–	18.30	84,500	–
	14/12/2008	88,200	8/12/2009 – 8/12/2015	79,700	–	30,000	–	–	18.30	79,700	–
	15/12/2008	1,084,700	8/12/2009 – 8/12/2015	1,084,700	–	351,500	44,000	110,500	18.30	930,200	27.92
	16/12/2008	581,500	8/12/2009 – 8/12/2015	581,500	–	180,000	41,500	52,500	18.30	487,500	28.84
	17/12/2008	513,500	8/12/2009 – 8/12/2015	513,500	–	173,000	–	28,000	18.30	485,500	27.86
	18/12/2008	611,500	8/12/2009 – 8/12/2015	611,500	–	206,500	21,000	107,500	18.30	483,000	28.97
	19/12/2008	198,000	8/12/2009 – 8/12/2015	198,000	–	67,000	–	–	18.30	198,000	–
	20/12/2008	19,000	8/12/2009 – 8/12/2015	19,000	–	6,500	–	–	18.30	19,000	–
	22/12/2008	772,500	8/12/2009 – 8/12/2015	767,500	–	259,500	–	78,000	18.30	689,500	29.85
	23/12/2008	306,000	8/12/2009 – 8/12/2015	299,500	–	97,000	14,000	39,000	18.30	246,500	29.02
	24/12/2008	500,500	8/12/2009 – 8/12/2015	485,500	–	168,500	–	30,000	18.30	455,500	29.59
	25/12/2008	45,000	8/12/2009 – 8/12/2015	45,000	–	15,000	–	–	18.30	45,000	–
	29/12/2008	148,000	8/12/2009 – 8/12/2015	148,000	–	50,000	15,000	–	18.30	133,000	–
	30/12/2008	19,000	8/12/2009 – 8/12/2015	19,000	–	6,500	–	–	18.30	19,000	–
	18/6/2009	170,000	12/6/2010 – 12/6/2016	170,000	–	57,000	53,000	27,000	24.50	90,000	30.45

Options to subscribe for Ordinary Shares granted under the 2007 Share Option Scheme, as referred to in Notes 9B(iii) and 52A(iii) to the Accounts *(continued)*

Executive Directorate and eligible employees	Date granted	No. of options granted	Period during which rights exercisable (day/month/year)	Options outstanding as at 1 January 2010	Options granted during the year	Options vested during the year	Options lapsed during the year	Options exercised during the year	Exercise price per share of options (HK$)	Options outstanding as at 31 December 2010	Weighted average closing price of shares immediately before the date(s) on which options were exercised (HK$)
Other eligible employees	6/7/2009	45,000	12/6/2010 – 12/6/2016	45,000	–	15,000	–	–	24.50	45,000	–
	9/7/2009	45,000	12/6/2010 – 12/6/2016	45,000	–	15,000	–	15,000	24.50	30,000	31.20
	9/12/2009	200,000	8/12/2010 – 8/12/2016	200,000	–	39,000	85,000	–	26.85	115,000	–
	10/12/2009	2,001,000	8/12/2010 – 8/12/2016	2,001,000	–	661,000	73,000	24,000	26.85	1,904,000	29.76
	11/12/2009	2,362,000	8/12/2010 – 8/12/2016	2,362,000	–	788,000	25,000	15,000	26.85	2,322,000	28.55
	12/12/2009	610,000	8/12/2010 – 8/12/2016	610,000	–	205,500	–	–	26.85	610,000	–
	13/12/2009	19,000	8/12/2010 – 8/12/2016	19,000	–	6,500	–	6,500	26.85	12,500	28.50
	14/12/2009	2,273,000	8/12/2010 – 8/12/2016	2,273,000	–	745,500	64,000	–	26.85	2,209,000	–
	15/12/2009	2,838,000	8/12/2010 – 8/12/2016	2,838,000	–	953,500	19,000	15,000	26.85	2,804,000	28.58
	16/12/2009	1,550,000	8/12/2010 – 8/12/2016	1,550,000	–	518,000	35,500	23,500	26.85	1,491,000	28.74
	17/12/2009	1,000,000	8/12/2010 – 8/12/2016	1,000,000	–	329,500	25,000	–	26.85	975,000	–
	18/12/2009	389,000	8/12/2010 – 8/12/2016	389,000	–	131,500	–	8,500	26.85	380,500	28.10
	19/12/2009	70,000	8/12/2010 – 8/12/2016	70,000	–	23,500	–	–	26.85	70,000	–
	20/12/2009	75,000	8/12/2010 – 8/12/2016	75,000	–	25,500	–	–	26.85	75,000	–
	21/12/2009	520,000	8/12/2010 – 8/12/2016	520,000	–	176,000	–	–	26.85	520,000	–
	22/12/2009	256,000	8/12/2010 – 8/12/2016	256,000	–	80,500	19,000	–	26.85	237,000	–
	21/7/2010	305,000	28/6/2011 – 28/6/2017	–	305,000	–	–	–	27.73	305,000	–
	16/12/2010	194,000	16/12/2011 – 16/12/2017	–	194,000	–	–	–	28.84	194,000	–
	17/12/2010	4,062,000	16/12/2011 – 16/12/2017	–	4,062,000	–	–	–	28.84	4,062,000	–
	18/12/2010	673,000	16/12/2011 – 16/12/2017	–	673,000	–	–	–	28.84	673,000	–
	19/12/2010	174,000	16/12/2011 – 16/12/2017	–	174,000	–	–	–	28.84	174,000	–
	20/12/2010	4,854,500	16/12/2011 – 16/12/2017	–	4,854,500	–	–	–	28.84	4,854,500	–
	21/12/2010	3,020,000	16/12/2011 – 16/12/2017	–	3,020,000	–	–	–	28.84	3,020,000	–
	22/12/2010	975,000	16/12/2011 – 16/12/2017	–	975,000	–	–	–	28.84	975,000	–
	23/12/2010	189,000	16/12/2011 – 16/12/2017	–	189,000	–	–	–	28.84	189,000	–

Notes

1 No option may be exercised later than seven years after its date of offer and no option may be offered to be granted more than seven years after the adoption of the 2007 Share Option Scheme ("2007 Option Scheme") on 7 June 2007.

2 Unless approved by shareholders in the manner as required by the Listing Rules, the total number of shares issued and issuable upon exercise of the options granted to any eligible employee under the 2007 Option Scheme together with the total number of shares issued and issuable upon the exercise of any option granted to such eligible employee under any other share option scheme of the Company (including, in each case, both exercised and outstanding options) in any 12-month period must not exceed 0.2% of the shares of the Company in issue at the date of offer in respect of such option under the 2007 Option Scheme.

3 The proportion of underlying shares in respect of which the above share options will vest is as follows:

Date	Proportion of underlying shares in respect of which an option is vested
Before the first anniversary of the date of offer of the option (the "Offer Anniversary")	none
From the first Offer Anniversary to the date immediately before the second Offer Anniversary	one-third
From the second Offer Anniversary to the date immediately before the third Offer Anniversary	two-thirds
From the third Offer Anniversary and thereafter	all

4 Jacob Kam Chak-pui became the Operations Director and a Member of the Executive Directorate on 1 January 2011.

During the year ended 31 December 2010, 1,235,000 and 14,666,500 options to subscribe for shares of the Company were granted to 6 Members of the Executive Directorate and 411 employees respectively under the 2007 Share Option Scheme. Details of the grant are set out in the tables above. The respective closing price per share immediately before the respective date of grant of the options is set out below. Pursuant to the terms of the Scheme, each grantee undertakes to pay HK$1.00, on demand, to the Company, in consideration for the grant of the options. The share options granted are recognised on an accrued vesting basis in the accounts. The weighted average value per option granted, estimated at the respective date of grant using the Black-Scholes pricing model is as follows:

Date granted	Closing price per share immediately before the date of grant (HK$)	Estimated risk-free interest rate (%)	Expected life (Years)	Estimated Volatility	Expected dividend per share (HK$)	Weighted average value per option granted (HK$)
21/7/2010	27.35	0.89	3.5	0.32	0.52	5.53
16/12/2010	28.55	1.21	3.5	0.32	0.52	5.86
17/12/2010	28.35	1.28	3.5	0.32	0.52	5.77
18/12/2010	28.45	1.28	3.5	0.32	0.52	5.83
19/12/2010	28.45	1.28	3.5	0.32	0.52	5.83
20/12/2010	28.45	1.20	3.5	0.32	0.52	5.79
21/12/2010	28.05	1.21	3.5	0.32	0.52	5.56
22/12/2010	28.40	1.20	3.5	0.32	0.52	5.76
23/12/2010	28.50	1.20	3.5	0.32	0.52	5.81

The Black-Scholes option pricing model was developed for use in estimating the fair value of traded options and requires input of highly subjective assumptions, including the expected life and stock price volatility. Since the Company's share options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimates, the Black-Scholes option pricing model does not necessarily provide a reliable measure of the fair value of the share options.

Save as disclosed above:

A none of the Members of the Board or the Executive Directorate of the Company had any interest or short position in the shares, underlying shares or debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO); and

B during the year ended 31 December 2010, no Member of the Board or the Executive Directorate nor any of their spouses or children under 18 years of age held any rights to subscribe for equity or debt securities of the Company nor had there been any exercises of any such rights by any of them,

as recorded in the register kept by the Company under section 352 of the SFO or otherwise notified to the Company and the HKSE pursuant to the Model Code.

Directors' Service Contracts

No director proposed for election or re-election at the forthcoming Annual General Meeting has a service contract which is not determinable by the Company or any of its subsidiaries within one year without payment of compensation, other than statutory compensation.

No Director has a service contract with the Company or any of its subsidiaries which is for a duration which may exceed three years or which requires the Company to, in order to terminate such contract, give a notice period in excess of one year or pay or make other payments equivalent to more than one year's emoluments.

Substantial Shareholders' Interests

Set out below is the name of the party which was interested in 5% or more of the nominal value of the share capital of the Company and the number of shares in which it was interested as at 31 December 2010 as recorded in the register kept by the Company under section 336 of the SFO:

Name	No. of Ordinary Shares	Percentage of Ordinary Shares to total issued share capital
The Financial Secretary Incorporated (in trust on behalf of the Government)	4,434,552,207	76.82

The Company has been informed by the Government that, as at 31 December 2010, approximately 0.56% of the shares of the Company were held for the account of the Exchange Fund. The Exchange Fund is a fund established under the Exchange Fund Ordinance (Cap. 66 of the Laws of Hong Kong) under the control of the Financial Secretary.

Loan Agreements with Covenant Relating to Specific Performance of the Controlling Shareholder

As at 31 December 2010, the Group had borrowings of HK$18,026 million with maturities ranging 2011 to 2020 and available uncommitted banking and other facilities of HK$12,212 million, which were subject to the condition that the Government, being the Company's controlling shareholder, owns more than half in nominal value of the voting share capital of the Company during the lives of the borrowings and the undrawn facilities. Otherwise, immediate repayment of borrowings may be demanded and cancellation of the undrawn facilities may result.

Major Suppliers and Customers

Less than 30% in value of supplies (which were not of a capital nature) purchased during the year ended 31 December 2010 was attributable to the Company's five largest suppliers. Less than 30% in value of the Company's turnover during the year ended 31 December 2010 was attributable to the Company's five largest customers combined by value.

Going Concern

The accounts on pages 139 to 234 have been prepared on a going concern basis. The Board has reviewed the Company's budget for 2011, together with the longer-term forecast for the following five years and is satisfied that the Company has sufficient resources to continue as a going concern for the foreseeable future.

Connected Transactions

During the year under review, the following transactions and arrangements described below were entered into with the Government which is a substantial shareholder of the Company as defined in the Listing Rules. The Government is therefore a "connected person" of the Company for the purposes of the Listing Rules, and the transactions described below are connected transactions for the Company under the Listing Rules.

As disclosed in the announcement of the Company dated 13 January 2005, the Stock Exchange has granted a waiver to the Company from strict compliance with the requirements under Chapter 14A of the Listing Rules which would otherwise apply to connected transactions and continuing connected transactions between the Company and Government, subject to certain conditions (the "Waiver").

Consequently, the Company makes the disclosures below in accordance with Rule 14A.45 of the Listing Rules and in accordance with paragraph (B)(I)(i) of the Waiver.

Land Agreements

A Conditions of Grant No. 20102 dated 11 June 2010 and Conditions of Grant No. 20103 dated 11 June 2010 for the development at Kowloon Inland Lot No. 11126 (Site C, Canton Road, Kowloon) (building covenant expiry date 30 June 2016) and Kowloon Inland Lot No. 11129 (Site D, Canton Road, Kowloon) (building covenant expiry date 30 June 2017) respectively with a total consideration or value of HK$4,958,821,000 and HK$6,748,821,000 respectively.

B In respect of the Remaining Portion of Mass Transit Railway Lot No. 1:

A Supplemental Lease was signed on 11 February 2002 between the Government and the Company in which the Government leased to the Company land occupied by the

Quarry Bay Congestion Relief Works or the Quarry Bay Relief Works connecting Quarry Bay Station to North Point Station at an annual rent of 3% of the rateable value of the leased area for a term commencing 1 October 2001 to 29 June 2050 on terms and conditions substantially similar to the lease for the Mass Transit Railway Lot No. 1. By a Modification Letter dated 13 May 2002 entered into between the Government and the Company, the lease for the Remaining Portion of Mass Transit Railway Lot No. 1 was modified in areas indicated in the lease plans attached to the Modification Letter for an administration fee of HK$16,200. By a Modification Letter dated 20 December 2003 entered into between the Government and the Company, the lease for the Remaining Portion of Mass Transit Railway Lot No. 1 was modified in areas indicated in the lease plans attached to the Modification Letter in consideration of a premium of HK$1,000 and an administration fee of HK$16,200. By a Modification Letter executed by the Government and the Company dated 31 May 2004, the lease for the Remaining Portion of Mass Transit Railway Lot No. 1 was modified in areas indicated in the lease plans attached to the Modification Letter in consideration of a premium of HK$1,000 and an administrative fee of HK$16,200. By a Modification Letter dated 1 March 2005 entered into between the Government and the Company, the lease for the Remaining Portion of Mass Transit Railway Lot No.1 was modified in areas indicated in the lease plans attached to the Modification Letter in consideration of a premium of HK$1,000 and an administrative fee of HK$16,200. By a Modification Letter dated 9 March 2007 entered into between the Government and the Company, the lease for the Remaining Portion of Mass Transit Railway Lot No.1 was modified in areas indicated in the lease plans attached to the Modification Letter in consideration of a premium of HK$1,000 and an administrative fee of HK$18,650. By a Modification Letter which was effective from 1 January 2009 entered into between the Government and the Company, the lease for the Remaining Portion of Mass Transit Railway Lot No.1 was modified in areas indicated in the lease plans attached to the Modification Letter in consideration of a premium of HK$1,000 and an administrative fee of HK$21,450. By a Modification Letter dated 30 October 2009 entered into between the Government and the Company, the lease for the Remaining Portion of Mass Transit Railway Lot No.1 was modified in areas indicated in the lease plans attached to the Modification Letter in consideration of a premium of HK$1,000 and an administrative fee of HK$21,450. By a Modification Letter dated 27 September 2010 entered into between the Government and the Company, the lease for the Remaining Portion of Mass Transit Railway Lot No.1 was modified in areas indicated in the lease plans attached to the Modification Letter in consideration of a premium of HK$1,000 and an administrative fee of HK$21,450.

Continuing Connected Transactions

During the year under review, the following transactions and arrangements described below involved the provision of goods or services on an ongoing basis with the Government and/or KCRC, the Airport Authority (the "AA"), and United Group Rail Services Limited ("UGL"). As noted above under the section headed "Connected Transactions", the Government is a substantial shareholder of the Company. KCRC and the AA are both associates of the Company as defined in the Listing Rules. As explained under Section III below, UGL is a substantial shareholder of a subsidiary of the Company. The Government, KCRC, the AA and UGL are therefore each "connected persons" for the purposes of the Listing Rules and each transaction set out at paragraphs I, II and III below constitutes a continuing connected transaction for the Company under the Listing Rules.

I Merger-related Continuing Connected Transactions

Each of the transactions listed in paragraphs A to F below and which formed part of the Rail Merger, was approved by the independent shareholders of the Company at an Extraordinary General Meeting held on 9 October 2007. These paragraphs should be read in conjunction with the paragraphs contained in the section below headed "Additional Information in respect of the Rail Merger".

As disclosed in the circular issued by the Company on 3 September 2007 in connection with the Rail Merger, the Stock Exchange granted a waiver to the Company from strict compliance with the requirements under Chapter 14A of the Listing Rules which would otherwise apply to continuing connected transactions between the Company, the Government and/or KCRC arising as a result of the Rail Merger, subject to certain conditions (the "Merger-related Waiver").

A Merger Framework Agreement

The Merger Framework Agreement was entered into on 9 August 2007 between the Company, KCRC and the Secretary for Transport and Housing and the Secretary for Financial Services and the Treasury for and on behalf of the Government.

The Merger Framework Agreement contains provisions for the overall structure and certain specific aspects of the Rail Merger, including in relation to:

- a seamless interchange programme;
- corporate governance of the Company Post-Rail Merger;
- payments relating to property enabling works;
- arrangements relating to the establishment of a rolling programme on the level of flat production arising from tenders for railway property development;

- arrangements in relation to the assessment of land premium amounts;
- arrangements in relation to the employees of the Company and KCRC, including provisions preventing the Company from terminating the employment of relevant frontline staff for any reason that relates to the process of integrating the operations of the Company and KCRC;
- the implementation of certain fare reductions;
- arrangements in relation to the proposed Shatin to Central Link;
- KCRC's continuing responsibility for its existing financial arrangements;
- treatment of KCRC's cross border leases;
- the payment of HK$7.79 billion in respect of the Property Package (as described on pages 125 to 127 and in paragraph F below);
- the allocation of liability for any Pre-Rail Merger and Post-Rail Merger claims by third parties; and
- the Company's retention of its English name and (pursuant to the MTR Ordinance) the change of its Chinese name to "香港鐵路有限公司".

B KSL Project Management Agreement

The KSL Project Management Agreement was entered into between the Company and KCRC on 9 August 2007.

Pursuant to the terms of the KSL Project Management Agreement (as amended), the Company is appointed:

- to manage the performance of KCRC's principal obligations to the Government in relation to the design and construction of the Kowloon Southern Link ("KSL") (other than obligations relating to payment);
- to act as the engineer under the various KSL construction contracts;
- to act as KCRC's representative under the various KSL consultancy agreements; and
- to act as KCRC's agent in connection with the KSL under certain circumstances.

The Company itself will not construct, nor be responsible for the costs of, the KSL works.

In return for the performance of these services, the Company has received a project management fee of approximately HK$710.8 million. In addition, in the event that the final outturn cost of the KSL is under budget, the Company will receive an incentive payment (calculated with reference to the amount by which the final outturn cost of the project is under budget) of up to HK$110 million.

C West Rail Agency Agreement

The West Rail Agency Agreement and related agreements were entered into on 9 August 2007 between the Company, KCRC and certain KCRC subsidiary companies ("West Rail Subsidiaries"). Pursuant to the terms of the West Rail Agency Agreement, the Company was appointed:

- to act as KCRC's agent, and donee under powers of attorney, to exercise certain rights and perform certain obligations relating to specified development sites along West Rail; and
- to act as agent for, and donee under powers of attorney from, each of the West Rail Subsidiaries to exercise certain rights and perform certain obligations relating to specified development sites along West Rail.

The Company will receive an agency fee of 0.75% of the gross sale proceeds in respect of the unawarded West Rail development sites and 10% of the net profits accrued to the West Rail Subsidiaries under the development agreements in respect of the awarded West Rail development sites. The Company will also recover from the West Rail Subsidiaries its costs (including internal costs) incurred in respect of the West Rail development sites plus 16.5% on-cost, together with interest accrued thereon.

D Outsourcing Agreement

An Outsourcing Agreement was entered into on 9 August 2007 between the Company and KCRC. For the period from 2 December 2007 to 2 December 2009 (subsequently extended to 31 December 2009), KCRC, pursuant to the terms of the Outsourcing Agreement, outsourced certain financial and administrative functions to the Company. On 6 November 2009, a new Outsourcing Agreement was entered into for the period from 1 January 2010 to 31 December 2011, under which the Company would continue to:

- provide a number of financial and administrative services to KCRC;
- provide certain staff to enable KCRC to operate after the Rail Merger; and

- receive an annual fee of not more than HK$20 million from KCRC.

The scope of the services to be provided by the Company includes services relating to treasury, financial control, information technology, company secretarial, legal and other corporate functions, human resources, office administration and management of claims.

E KCRC Cross Border Lease Agreements

US CBL Assumption Agreements

Separate US CBL Assumption Agreements were entered into on 30 November 2007 between the Company, KCRC and, variously, Wilmington Trust Company, Buoyant Asset Limited, BA Leasing & Capital Corporation, Utrecht-America Finance Co., Cooperatieve Cenrale Raiffeisen-Boerenleenbank B.A., Advanced Asset Limited, Washoe Asset Management Company, Quality Asset Limited, Kasey Asset Limited, Key Equipment Finance Inc., Mercantile Leasing Company (No. 132) Limited, Landesbank Sachsen Aktiengesellschaft, Barclays Bank PLC, Bayerische Landesbank Girozentrale, U.S. Bank National Association, Circuit Asset Limited, Citicorp USA Inc., Shining Asset Limited, Banc of America FSC Holdings Inc., Fluent Asset Limited, Anzef Limited, Societe Generale, Australia and New Zealand Banking Group Limited, Statesman Asset Limited, State Street Bank and Trust Company and Bowman Asset Limited and became effective on 3 December 2007, with respect to each of the US cross border leases originally entered into between KCRC and certain counterparties (each, a "CBL"). Pursuant to each US CBL Assumption Agreement, the Company undertakes to perform, on a joint and several basis with KCRC, the obligations of KCRC under the respective CBLs. As a result thereof, the Company is generally liable to the CBL counterparties in respect of KCRC's obligations under the CBLs and has the right to exercise certain of KCRC's rights under the CBLs.

US CBL Allocation Agreement

The US CBL Allocation Agreement was entered into between the Company, KCRC and the subsidiaries of KCRC (the "KCRC Subsidiaries") on 2 December 2007. Pursuant to the US CBL Allocation Agreement, rights, obligations and responsibility for risks relating to the CBLs are delineated and allocated between KCRC and the Company (each of which is jointly and severally liable to specified CBL counterparties, as referred to in the paragraph above headed "US CBL Assumption Agreements"). Under the terms of the US CBL Allocation Agreement, as between the Company and KCRC, the Company is responsible for specified obligations. The Company and KCRC each made representations under the US CBL Allocation Agreement, which include, in the case of those made by KCRC, representations with respect to the status of the CBLs. The Company and KCRC agreed to indemnify each other for certain losses in relation to the CBLs.

F Property Package Agreements

Category 2A Properties

On 9 August 2007, the Government entered into an undertaking that it would, within twelve months of the Merger Date or such further period of time as the Government and the Company may agree, issue to KCRC an offer for the grant at nil premium of Government leases in respect of the land upon which certain properties (the "Category 2A Properties") are situate (the "said Government Leases"). The Category 2A Properties were held by KCRC as vested land under the Kowloon-Canton Railway Corporation Ordinance (Cap. 372 of the Laws of Hong Kong) ("KCRC Ordinance"). On 9 August 2007, KCRC entered into an undertaking that it would, immediately after the grant of the said Government Leases referred to in the preceding sentence, enter into agreements for sale and purchase to sell the Category 2A Properties to the Company (the "said Agreements for Sale and Purchase"). Assignments of the Category 2A Properties to the Company shall then take place pursuant to the said Agreements for Sale and Purchase (the said "Assignments"). Pursuant to the KCRC undertaking and as interim arrangements until the grant of the Government leases, on 9 August 2007 the following agreements were entered into between KCRC and the Company:

- an agreement that KCRC (as lessor) shall enter into tenancy agreements with the Company (as lessee) at market rent in respect of the Category 2A Properties' vacant units (with the intention that the Company will then sub-let the vacant units to sub-tenants);
- two licence agreements in respect of the common areas within the Category 2A Properties, pursuant to which KCRC granted the Company the right to use certain common areas until the execution of the Category 2A Properties assignment referred to above;
- a lease enforcement agency agreement appointing the Company as its enforcement agent to enforce KCRC's current Category 2A Properties tenancy agreements against tenants; and
- an assignment of rental proceeds whereby the proceeds received under KCRC's current Category 2A Properties tenancy agreements with tenants are assigned to the Company.

The said Government Leases were issued to KCRC respectively on 27 March 2009 and 31 March 2009. The said Agreements for Sale and Purchase were entered into between KCRC and the Company on 27 March 2009 and 31 March 2009 respectively and the said Assignments to the Company were executed on 27 March 2009 and 31 March 2009 respectively. Deeds of Mutual Grant were also entered into between the Company and KCRC on 27 March 2009 and 31 March 2009 respectively setting out the easements, rights, entitlements, privileges and liberties of the Company and KCRC in the land on which the Category 2A Properties are situated.

Category 2B Property

On 9 August 2007, the Government entered into an undertaking that it would, within twenty four months of the Merger Date or such further period of time as the Government and the Company may agree, issue to the Company an offer for the grant of a Government Lease of a certain property (the "Category 2B Property") on terms to be agreed. The Category 2B Property is currently held by KCRC as vested land under the KCRC Ordinance for use as staff quarters and a recreational club.

On 9 August 2007, KCRC entered into an undertaking relating to interim arrangements to ensure that, as from the Merger Date, the Company shall be responsible for KCRC's obligations under licence agreements relating to the Category 2B Property, and for enforcing such agreements. The Company is entitled to proceeds received by KCRC in respect of those licence agreements. The interim arrangements include, inter alia, as from the Merger Date:

- an agreement that KCRC (as licensor) shall grant to the Company (as licensee) possession of the Category 2B Property (without payment of any licence fee or premium), subject to existing licences and the Second Schedule of the KCRC Ordinance, with the right of the Company to sub-license all or any part of the Category 2B Property (subject to it being used as staff quarters and a recreation club);
- until the grant of the Government lease of the Category 2B Property, KCRC has appointed the Company as its enforcement agent to enforce KCRC's current Category 2B Property licence agreements against licensees; and
- KCRC has assigned to the Company the proceeds received under KCRC's current Category 2B Property licence agreements with licensees.

The basic terms offer for the Category 2B Property (i.e. Trackside Villas) was issued and accepted by the Company on 31 December 2009 and the Government Lease in respect of Tai Po Town Lot No. 199 dated 29 March 2010 was issued for a term of 50 years from 2 December 2007.

Category 3 Properties

On 9 August 2007, the Company entered into three agreements (the "Category 3 Agreements") and related powers of attorney with KCRC. Each Category 3 Agreement relates to a certain property (each a "Category 3 Property"). KCRC has previously entered into a development agreement in respect of each Category 3 Property. None of the rights and obligations granted to or undertaken by the Company under the Category 3 Agreements may be exercised or performed by the Company if they relate exclusively to concession property situate on any Category 3 Property. Matters affecting the concession property situate on any Category 3 Property are dealt with under the terms of the Service Concession Agreement (as defined and summarised on pages 134 to 135).

Pursuant to the terms of each Category 3 Agreement, the Company has been appointed to act as KCRC's agent, and donee under powers of attorney, to exercise rights and to perform obligations of KCRC which relate to the Category 3 Property (but excluding the right or obligation to dispose of the relevant Category 3 Property).

The Company is required at all times to comply with statutory restrictions and obligations binding on KCRC which relate to the Category 3 Property, and shall pay all amounts due and payable from KCRC which have been incurred by KCRC as a result of the Company's actions.

In acting as KCRC's agent, the Company is required to act according to prudent commercial principles, and aim to maximise gross profits under the Category 3 Property and to run a safe and efficient railway. In order to assist the Company in performing its agency functions, KCRC has granted powers of attorney to the Company. The Company may only use the powers of attorney to exercise rights and perform obligations conferred or undertaken by it under the relevant Category 3 Agreement. As well as acting as KCRC's agent, the Company has the right to give KCRC instructions in respect of any action or matter relating to each Category 3 Property (including its related development agreement) which the Company is unable to take by reason of the limitation of the scope of its agency powers. KCRC is required to comply promptly with those instructions provided that it is permitted under law, and under the relevant Government grant, to carry out those instructions.

KCRC is required to account for revenue received in respect of a Category 3 Property by way of balance sheet movement (rather under its profit and loss account), provided that such treatment is permitted under law and accounting principles and practices.

KCRC shall not take any action in respect of a Category 3 Property which is not carried out by the Company (acting as KCRC's agent), or according to the Company's instructions, or otherwise in accordance with the terms of the Category 3 Agreement.

As consideration for acting as KCRC's agent, the Company shall be paid a fee which is expected to be similar in quantum to the profits made by KCRC in respect of the relevant Category 3 Property (after deducting certain initial and upfront payments and consultant contribution costs, in each case paid or to be paid by the relevant developer to KCRC). Generally, the Company's fee shall be payable in instalments promptly following receipt of relevant funds by KCRC (but subject to specified deductions of amounts due from KCRC to the relevant Category 3 Property developer).

The Company has agreed to give certain indemnities to KCRC in respect of each Category 3 Property.

The Company shall be the first manager, or shall ensure that a manager is appointed in respect of, each Category 3 Property (once developed).

The Company's appointment as agent shall terminate when KCRC ceases to have any undivided share in the relevant Category 3 Property, other than concession property, and neither KCRC nor the developer nor the guarantors have any further rights to exercise, or obligations to perform, under the development agreement relating to the relevant Category 3 Property.

In relation to the Merger Framework Agreement, the KSL Project Management Agreement, the West Rail Agency Agreement (and related powers of attorney), the US CBL Assumption Agreements, the US CBL Allocation Agreement, the Outsourcing Agreement and the agreements in relation to Category 2A, Category 2B and Category 3 Properties (together the "Merger-related Continuing Connected Transactions") and in accordance with paragraph B(I)(i) of the Merger-related Waiver, the Company confirms that the Independent Non-executive Directors of the Company have reviewed each of the Merger-related Continuing Connected Transactions and confirmed that the Merger-related Continuing Connected Transactions were entered into:

(1) in the ordinary and usual course of business of the Company;

(2) on normal commercial terms or on terms which are no less favourable to the Company than terms available to or from independent third parties; and

(3) in accordance with the relevant agreement governing them on terms that are fair and reasonable and in the interests of the shareholders of the Company as a whole.

The Company has engaged the auditors of the Company to carry out a review of each of the Merger-related Continuing Connected Transactions in accordance with Hong Kong Standard on Assurance Engagements 3000 "Assurance Engagements Other Than Audits or Reviews of Historical Financial Information" and with reference to Practice Note 740 "Auditor's Letter on Continuing Connected Transactions under the Hong Kong Listing Rules" issued by the Hong Kong Institute of Certified Public Accountants. In accordance with paragraph B(I)(ii) of the Merger-related Waiver, the auditors have provided a letter to the Board confirming that:

(a) nothing has come to their attention that causes them to believe that the Merger-related Continuing Connected Transactions have not been approved by the Board; and

(b) nothing has come to their attention that causes them to believe that the Merger-related Continuing Connected Transactions were not entered into, in all material respects, in accordance with the relevant agreements governing such transactions.

II Non Merger-related Continuing Connected Transactions with Government and/or its Associates

The following disclosures are made in accordance with paragraph (B)(I)(i) of the Waiver and Rule 14A.46 of the Listing Rules.

A Entrustment Agreement for Design and Site Investigation in Relation to the Shatin to Central Link

The Entrustment Agreement for Design and Site Investigation in Relation to the Shatin to Central Link (the "SCL Agreement") was entered into on 24 November 2008 between the Company and the Secretary for Transport and Housing for and on behalf of the Government.

The SCL Agreement contains provisions for the design of and site investigation and procurement activities in relation to the proposed Shatin to Central Link, including in relation to:

- the Government's obligation to pay the Company up to a maximum aggregate amount of HK$1,500,000,000 in respect of certain costs incurred by the Company pursuant to the SCL Agreement, including the Company's in-house design costs and certain on-costs and preliminary costs;
- the Government's obligation to bear and finance the total cost of the design and site investigation activities under the SCL Agreement (subject to the limit noted above in respect of payments to the Company) and arrangements for the payment of these costs directly by the Government;
- the Company's obligation to carry out or procure the carrying out of the design and site investigation activities in relation to the proposed Shatin to Central Link;
- the limitation of the Company's liability to the Government under the SCL Agreement, except in respect of death or personal injury caused by the negligence of the Company, to HK$600,000,000; and
- should the railway scheme for the Shatin to Central Link be authorised under the Railways Ordinance (Cap. 519 of the Laws of Hong Kong), the execution of a further agreement by the Government and the Company setting out each of their rights, obligations, duties and powers with respect to the financing, construction, completion, testing, commissioning and putting into service the works necessary for the construction and operation of the Shatin to Central Link.

B1 Entrustment Agreement for Design and Site Investigation in Relation to the Express Rail Link (Hong Kong Section of the Guangzhou-Shenzhen-Hong Kong Express Rail Link)

The Entrustment Agreement for Design and Site Investigation in Relation to the Express Rail Link (the "First XRL Agreement") was entered into on 24 November 2008 between the Company and the Secretary for Transport and Housing for and on behalf of the Government.

The First XRL Agreement contains provisions for the design of and site investigation and procurement activities in relation to the proposed Express Rail Link, including in relation to:

- the Government's obligation to pay the Company, up to a maximum aggregate amount of HK$1,500,000,000, in respect of certain costs incurred by the Company pursuant to the First XRL Agreement, including the Company's in-house design costs and certain on-costs, preliminary costs and recruited staff costs;
- the Government's obligation to bear and finance the total cost of the design and site investigation activities under the First XRL Agreement (subject to the limit noted above in respect of payments to the Company) and arrangements for the payment of these costs directly by the Government;
- the Company's obligation to carry out or procure the carrying out of the design and site investigation activities in relation to the proposed Express Rail Link;
- the limitation of the Company's liability to the Government under the First XRL Agreement, except in respect of death or personal injury caused by the negligence of the Company, to HK$700,000,000; and
- should the railway scheme for the Express Rail Link be authorised under the Railways Ordinance (Cap. 519 of the Laws of Hong Kong), the execution of a further agreement by the Government and the Company setting out each of their rights, obligations, duties and powers with respect to the financing, construction, completion, testing, commissioning and putting into service the works necessary for the construction and operation of the Express Rail Link.

B2 Entrustment Agreement for Construction, Testing and Commissioning of the Express Rail Link

The Entrustment Agreement for the construction and commissioning of the Express Rail Link was entered into on 26 January 2010 between the Company and the Secretary for Transport and Housing for and on behalf of the Government (the "Second XRL Agreement").

The scheme in respect of the Express Rail Link was first gazetted under the Railways Ordinance (Cap. 519 of the Laws of Hong Kong) on 28 November 2008, with amendments and corrections gazetted on 30 April 2009. The scheme, as amended with such minor modifications as deemed necessary, was authorised by the Chief Executive in Council on 20 October 2009 and funding support approved by the Finance Committee on 16 January 2010.

The Second XRL Agreement contains the following provisions:

- in consideration of the Company executing or procuring the execution of certain entrustment activities as set out in the Second XRL Agreement and carrying out its other obligations under the Second XRL Agreement and the First XRL Agreement, Government shall pay to the Company HK$4,590 million, to be paid in cash quarterly in advance on a scheduled basis as such sum may be varied in accordance with the Second XRL Agreement, subject to the maximum payment limits stated in the Second XRL Agreement (being HK$2,000 million annually and HK$10,000 million in total) (the "Maximum Payment Limits");
- the Company and Government may agree that the Company will carry out (or procure the carrying out of) certain additional works for Government (such agreed additional works being "Miscellaneous Works"). Miscellaneous Works (if any) are to be carried out by the Company in the same manner as if they had formed part of the activities specified to be carried out under the Second XRL Agreement and in consideration of the Company executing or procuring the execution of the Miscellaneous Works (if any) and carrying out its other obligations under the Second XRL Agreement in relation to the Miscellaneous Works (if any), Government shall pay to the Company an amount equal to an agreed fixed percentage of third party costs attributable to the Miscellaneous Works from time to time subject to the Maximum Payment Limits;
- the Company will provide to Government by the end of each calendar month, a progress report on the activities under the Second XRL Agreement that were carried out in the immediately preceding calendar month and, within three months following the earlier of handover of the Express Rail Link project to the Government or termination of the Second XRL Agreement, a final report on the activities required to be carried out under the Second XRL Agreement;
- the Company shall be responsible for the care of all works constructed under the Express Rail Link project from the commencement of construction until the date of handover of those works to the Government (or to a third party directed by the Government) and for completing or procuring the completion of any outstanding works and/or defective works identified prior to the handover of the works;
- during the period of twelve years following the issue of a certificate of completion by the Company in respect of work carried out under any contract with any third party, the Company shall be responsible for the repair of any defects in such work that are identified following the expiry of any defects liability period under the relevant contract;
- the Company warrants that:

  – in the case of those activities under the Second XRL Agreement that relate to the provision of project management services, such activities shall be carried out with the skill and care reasonably to be expected of a professional and competent project manager;

  – in the case of those activities under the Second XRL Agreement that relate to the provision of design services, such activities shall be carried out with the skill and care reasonably to be expected of a professional and competent design engineer; and

  – in the case of those activities under the Second XRL Agreement that relate to the carrying out of construction activities, such activities shall be carried out with the skill and care reasonably to be expected of, and by utilising such plant, goods and materials reasonably to be expected from, a competent and workmanlike construction contractor.
- the Government is required to bear (i) any costs payable to third parties, (ii) any charges, costs or amounts payable to any Government department, bureau, agency or body in relation to the activities to be carried out under the Second XRL Agreement, (iii) any and all amounts payable to the Kowloon-Canton Railway Corporation as compensation for damage arising as a result of the Company and/or a third party contractor carrying out activities under the Second XRL Agreement; and (iv) all land acquisition, clearance and related costs (including all amounts arising as a result of any claim for compensation by any third party) and those costs which are incurred by the Lands Department in connection with the Express Rail Link project; and
- the Government further undertakes to use reasonable endeavours to provide the Company with assistance of a non-financial nature, including taking all reasonable steps to procure that all necessary licences and consents, required in connection with the design, construction and operation of the Express Rail Link are given or granted.

The Government has agreed that the Company has been asked to proceed with the construction, testing and commissioning of the Express Rail Link (pursuant to and on the terms of the Second XRL Agreement) on the understanding that the Company will be invited to undertake the operation of the Express Rail Link under the concession approach.

The Second XRL Agreement remains in full force and effect until the completion of the activities set out in the Second XRL Agreement or until terminated earlier in accordance with the terms of the Second XRL Agreement. The Company expects that the substantial majority of the activities to be carried out under the Second XRL Agreement will be complete by the time of the projected handover of the completed Express Rail Link in mid-2015. However certain activities involve the provision of specified administrative services to the Government, the Company expects to provide these services for a number of years following the completion of the Express Rail Link project. Notwithstanding this, certain provisions will remain in force following completion of the activities set out in the Second XRL Agreement, for example, provisions regarding confidentiality and dispute resolution.

C Renewal of the existing Maintenance Agreement for the Automated People Mover System at the Hong Kong International Airport

The Company has had entered into a Maintenance Agreement with the AA for the maintenance of the Automated People Mover system at the Hong Kong International Airport since 2002. It was signed on 18 March 2002 for a period of three years, which expired on 6 July 2005. A Supplemental Agreement was agreed with the AA, and approved by the Board in June 2005, to extend the Maintenance Agreement for another three years until 6 July 2008, which also included options for the Automated People Mover serving the Sky Plaza and Sky Pier terminal buildings.

On 21 August 2008, the Company entered into a new Maintenance Agreement with the AA, for the renewal of the then expired Maintenance Agreement for the Automated People Mover system for a five year period (the "New Maintenance Agreement"), effective from 6 July 2008. It is expected that the highest amount per year receivable from the AA under the New Maintenance Agreement will be HK$37 million.

The New Maintenance Agreement contains provisions relating to the operation and maintenance by the Company of the automated people mover system installed at Hong Kong International Airport (the "System") and the carrying out by the Company of certain specified services in respect of the System, they including the following:

- provisions stating that the duration of the New Maintenance Agreement shall be five years from 6 July 2008 up to and including 5 July 2013;
- provisions relating to the performance of scheduled maintenance works and overhaul of the System by the Company;
- provisions relating to monitoring the System for any breakdown and the Company providing repair services where necessary;
- provisions relating to the standards to which the Company must operate the System; and
- provisions relating to the carrying out by the Company (as additional services), in certain circumstances, of upgrade work on the System.

D Project Agreement for the Financing, Design, Construction and Operation of the West Island Line

The Project Agreement for the Financing, Design, Construction and Operation of the West Island Line (the "WIL Project Agreement") was entered into on 13 July 2009 between the Company and the Secretary for Transport and Housing for and on behalf of the Government.

The WIL Project Agreement contains provisions for the financing of and the carrying out, or procuring the carrying out, of the design, construction, completion, testing and commissioning by the Company of the railway works required in order to bring the West Island Line into operation in accordance with the MTR Ordinance, the Operating Agreement between the Company and the Secretary for Transport and Housing for and on behalf of the Government dated 9 August 2007 and the WIL Project Agreement. The West Island Line will be owned, operated and maintained by the Company for its own account for the period of the Company's railway franchise. The WIL Project Agreement includes provisions in relation to:

- payment by the Government of HK$12,252 million to the Company in consideration of the Company's obligations under the WIL Project Agreement, such sum constituting funding support from the Government for the Company to implement the West Island Line project;
- within 24 months of commercial operations commencing on the West Island Line on a revenue earning basis and providing scheduled transport for the public, payment by the Company to the Government of any "Repayment Amounts" for any over-estimation of certain capital expenditure, price escalation costs, land costs and the amount of contingency in relation to the railway works and reprovisioning, remedial and improvement works (together with interest);

- the design, construction and completion of the associated reprovisioning, remedial and improvement works (the cost of which shall be the responsibility of the Company) and the associated essential public infrastructure works (the cost of which shall be the responsibility of the Government);
- the Company's responsibility for costs relating to land acquisition, clearance and related costs arising from the implementation of the West Island Line project (save for costs arising from certain claims for compensation by third parties) and all costs, expenses and other amounts incurred or paid by the Lands Department pursuant to the involvement of the Lands Department in connection with the implementation of the West Island Line project; and
- the Company carrying out measures specified in the environmental impact assessment and the environmental permit issued by the Government to the Company in relation to the West Island Line on 12 January 2009.

The construction of the West Island Line is scheduled to take place between the date of the WIL Project Agreement and 2014.

In relation to the SCL Agreement, the First XRL Agreement, the Second XRL Agreement, the New Maintenance Agreement and the WIL Project Agreement (together the "Non Merger-related Continuing Connected Transactions") and in accordance with paragraph B(I)(iii)(a) of the Waiver, the Company confirms that the Independent Non-executive Directors of the Company have reviewed each of the Non Merger-related Continuing Connected Transactions and confirmed that the Non Merger-related Continuing Connected Transactions were entered into:

(1) in the ordinary and usual course of business of the Company;

(2) on normal commercial terms or on terms which are no less favourable to the Company than terms available to or from independent third parties; and

(3) in accordance with the relevant agreement governing them on terms that are fair and reasonable and in the interests of the shareholders of the Company as a whole.

The Company has engaged the auditors of the Company to carry out a review of each of the Non Merger-related Continuing Connected Transactions in accordance with Hong Kong Standard on Assurance Engagements 3000 "Assurance Engagements Other Than Audits or Reviews of Historical Financial Information" and with reference to Practice Note 740 "Auditor's Letter on Continuing Connected Transactions under the Hong Kong Listing Rules" issued by the Hong Kong Institute of Certified Public Accountants. In accordance with paragraph B(I)(iii)(b) of the Waiver, the auditors have provided a letter to the Board confirming that:

(a) nothing has come to their attention that causes them to believe that the Non Merger-related Continuing Connected Transactions have not been approved by the Board; and

(b) nothing has come to their attention that causes them to believe that the Non Merger-related Continuing Connected Transactions were not entered into, in all material respects, in accordance with the relevant agreements governing such transactions.

III Non Merger-related Continuing Connected Transactions with parties other than Government and/or its Associates

A Pre-Existing UGL Contract and Pre-Existing Supplemental UGL Contract for the provision of maintenance and other services for certain trains

The following disclosures are made in accordance with Rule 14A.46 of the Listing Rules.

On 31 August 2009, the Company, UGL and John Holland Pty Limited ("JHL") each agreed to subscribe for shares in Metro Trains Melbourne Pty Ltd ("MTM"), a joint venture company incorporated in Australia. As a result, the Company controls 60% of the voting power at any general meeting of MTM and each of UGL and JHL controls 20% of the voting power at any general meeting of MTM. Accordingly, subsequent to the Company entering into the Pre-Existing UGL Contract as amended by the Pre-Existing Supplemental UGL Contract (each, as defined below), UGL is treated as a substantial shareholder of MTM (a subsidiary of the Company) and therefore a "connected person" of the Company within the meaning of Chapter 14A of the Listing Rules. The Pre-Existing UGL Contract (as amended by the Pre-Existing Supplemental UGL Contract) is therefore a "continuing connected transaction" within the meaning of Rule 14A.14 of the Listing Rules.

On 11 January 2002, the Company entered into a contract with UGL for the provision of maintenance and other services in respect of trains at certain depots for a period of seven years commencing on or around 1 October 2002 to 30 September 2009 (the "Pre-Existing UGL Contract"). The commencement date was subsequently advanced by three months. On 14 April 2009, the Company entered into a supplemental agreement with UGL for the extension of the Pre-Existing UGL Contract for a further period of seven years from 1 August 2009 and for the transfer of the provision of certain services to the Kowloon depot (the "Pre-Existing Supplemental UGL Contract").

The Pre-Existing UGL Contract (as amended by the Pre-Existing Supplemental UGL Contract) provides for the provision of maintenance and other services by UGL in respect of 15 G/H stock trains used by the Company on the Kwun Tong Line, the Island Line, the Tsuen Wan Line and the Tseung Kwan O Line, in each case at the Tseung Kwan O depot and the Kowloon depot, including provisions in relation to:

- payment by the Company of a total sum of approximately HK$171,966,450 to UGL (including for variations and additional works) in consideration of UGL providing certain services between 1 August 2002 and 31 July 2009 and payment by the Company of HK$152,940,000 to UGL for the extended term of seven years pursuant to the Pre-Existing Supplemental UGL Contract (which amount is to be paid on a scheduled basis), subject to certain adjustments, including for the level of performance by the relevant trains;
- indemnification by UGL of the Company against certain losses and expenses sustained by the Company arising out of or in connection with UGL carrying out its obligations under the Pre-Existing UGL Contract (as amended by the Pre-Existing Supplemental UGL Contract);
- maintenance by UGL of insurance in relation to certain liabilities to the Company;
- the Company effecting and maintaining third party insurance covering the legal liability of both UGL and the Company for accidental death or injury to persons or accidental loss of or damage to property, in each case, arising out of the UGL's obligations under the Pre-Existing UGL Contract (as amended by the Pre-Existing Supplemental UGL Contract); and
- the Company maintaining "Contractors All Risks" insurance covering loss or damage to certain goods, equipment and temporary buildings at the Tseung Kwan O depot and the Kowloon depot.

The terms of the Pre-existing UGL Contract were agreed upon subsequent to a tender process that invited submissions from a number of contractors, including UGL. UGL was selected by the Company in accordance with the Company's established procedures for the assessment of tenders.

The Company regularly outsources certain services to third parties that specialise in the type of work outsourced, thereby improving the efficiency of the Company's operations and allowing the Company to concentrate its resources on its core business areas. UGL is a specialist in the provision of construction, refurbishment and maintenance services to the railway industry.

B Supplemental Agreement for the extension of the Original Contract for the Mid-Life Refurbishment of Phase 1 Light Rail Vehicles

The Supplemental Agreement for the extension of the Original Contract (defined below) for the Mid-Life Refurbishment of Phase 1 Light Rail Vehicles ("Phase 1 LRVs"), was entered into on 26 February 2010 between the Company and UGL (the "Supplemental Agreement").

On 30 November 2007, KCRC entered into the Original Contract with UGL (the "Original Contract"), for the refurbishment of the Phase 1 LRVs for a period of 45 months from 30 November 2007 to 31 August 2011. On 2 December 2007, the rights and obligations of KCRC under the Original Contract were vested in the Company pursuant to section 52(B) of the MTR Ordinance. The Supplemental Agreement extends the Original Contract for a further period of 16 months from 31 August 2011 until 31 December 2012. The Original Contract (as amended and supplemented by the Supplemental Agreement) is in substantially the same form as KCRC's standard conditions of contract for engineering works and contains the following provisions:

- in consideration of UGL providing the Refurbishment Works (defined below) under the Original Contract, the Company is obliged to pay UGL a total sum of approximately HK$48,260,000 (excluding amounts for variations and additional works). The Supplemental Agreement, inter alia, extended the scope of the Refurbishment Works of the Original Contract and the consideration payable by the Company to UGL for such extension is HK$83,736,143, as adjusted by an additional HK$14,435,327 (the "Contract Sum"). The total sum under the Original Contract plus the Contract Sum is to be paid progressively based on materials delivered and on works completed as set out in the Supplemental Agreement, subject to adjustments to take account of variations made by the Company's Chief Electrical and Mechanical Engineer (the "Engineer") to the scope of the Refurbishment Works. The maximum aggregate amount payable annually by the Company under the Original Contract plus the Contract Sum is approximately HK$78,632,000;

- the Company is obliged to effect "Contractor's All Risks" and "Third Party Liability" insurance with a third party liability limit of not less than HK$30,000,000;
- UGL shall carry out a carbody structure review to assess the mechanical condition of the Phase 1 LRVs; refurbish the drivers' consoles, the operators' seats and the passenger saloons of the Phase 1 LRVs; conduct a brake software upgrade of the Phase 1 LRVs; and carry out further miscellaneous repairs to the Phase 1 LRVs (together the "Refurbishment Works");
- UGL shall indemnify the Company against any certain losses or expenses which may arise out of or in connection with the Refurbishment Works, subject to any proportionate reduction in liability on account of any related negligence by the Company, its employees or agents, the Engineer or those appointed by the Engineer;
- UGL shall indemnify the Company against certain damages, compensation, costs and expenses in respect of any damages or compensation payable at law in respect of or in consequence of any accident, injury or illness to any person in the employment of UGL arising out of and in the course of such employment;
- UGL shall effect and maintain insurance with a limit of not less than HK$100,000,000 in relation to certain of its liabilities for the period commencing on 30 November 2007 until the date of the completion of the Refurbishment Works;
- UGL's liability to indemnify the Company is reduced proportionally to the extent that any act or omission of the Company, its employees or agents, the Engineer or those appointed by the Engineer, caused or contributed to the relevant death, illness, injury, loss or damage and the total liability of UGL shall not exceed 100% of the total sum payable under the Original Contract, save and except for UGL's liability for death, personal injury, wilful misconduct, fraud and infringement of third party intellectual property rights; and
- the total liability of UGL to the Company for liquidated damages arising as a result of delay is limited to 10% of the total sum payable under the Original Contract and, subject to the provisions regarding liquidated damages, UGL is not liable for any kind of economic, financial, indirect or consequential loss or damage, including but not limited to loss of profit, loss of use, loss of production, loss of any contract and the like, suffered by the Company.

Pursuant to the Original Contract, a bank guarantee issued by HSBC Bank Australia Limited has been provided to the Company in respect of the obligations of UGL under the Original Contract.

If UGL fails to complete the Refurbishment Works within the contract period, the Engineer may terminate the contract by notice in writing to UGL.

In relation to the Pre-Existing UGL Contract as amended by the Pre-Existing Supplemental UGL Contract and the Original Contract (as amended) (the "Continuing Connected Transactions with UGL") and in accordance with Rule 14A.37 of the Listing Rules, the Company confirms that the Independent Non-executive Directors of the Company have reviewed the Continuing Connected Transactions with UGL and confirmed that each of the Continuing Connected Transactions with UGL was entered into:

(1) in the ordinary and usual course of business of the Company;

(2) on normal commercial terms or on terms which are no less favourable to the Company than terms available to or from independent third parties; and

(3) in accordance with the relevant agreement governing them on terms that are fair and reasonable and in the interests of the shareholders of the Company as a whole.

The Company has engaged the auditors of the Company to carry out a review of the Continuing Connected Transactions with UGL in accordance with Hong Kong Standard on Assurance Engagements 3000 "Assurance Engagements Other Than Audits or Reviews of Historical Financial Information" and with reference to Practice Note 740 "Auditor's Letter on Continuing Connected Transactions under the Hong Kong Listing Rules" issued by the Hong Kong Institute of Certified Public Accountants. In accordance with Rule 14A.38 of the Listing Rules, the auditors have provided a letter to the Board confirming that:

(a) nothing has come to their attention that causes them to believe that the Continuing Connected Transactions with UGL have not been approved by the Board;

(b) for transactions involving the provision of goods or services by the Group, nothing has come to their attention that causes them to believe that the Continuing Connected Transactions with UGL were not, in all material respects, in accordance with the pricing policies of the Group;

(c) nothing has come to their attention that causes them to believe that the Continuing Connected Transactions with UGL were not entered into, in all material respects, in accordance with the relevant agreements governing such transactions; and

(d) with respect to the aggregate amount of each of the Continuing Connected Transactions with UGL, nothing has come to their attention that causes them to believe that the Continuing Connected Transactions with UGL have exceeded the maximum aggregate annual value disclosed in the previous announcements dated 1 September 2009 and 26 February 2010 made by the Company in respect of each of the Continuing Connected Transactions with UGL.

Additional Information in respect of the Rail Merger

The Rail Merger consisted of a number of separate agreements, each of which was detailed in the circular issued by the Company on 3 September 2007 in connection with the Rail Merger, and which together formed a complete package deal which was approved by the independent shareholders of the Company at an Extraordinary General Meeting held on 9 October 2007. The information set out at paragraph A below describes the payment framework adopted in respect of the Rail Merger and paragraphs B to F below set out, summaries of the various agreements entered into by the Company in respect of the Rail Merger in addition to those agreements disclosed above under the heading "Merger-related Continuing Connected Transactions".

A Payments in connection with Merger-related Agreements

In connection with the Rail Merger, the following initial payments were made by the Company to KCRC on 2 December 2007 (being the Merger Date):

- an upfront payment of HK$4.25 billion, payable under the Service Concession Agreement (as described in paragraph B below), being the upfront fee for the right to operate the Service Concession (as defined in paragraph B below) and the consideration for the purchased rail assets; and
- an upfront payment of HK$7.79 billion payable under the Merger Framework Agreement (as described on pages 123 to 124) in consideration for the execution of the Property Package Agreements (as described on pages 135 to 136 and in paragraph E below) and the sale of the shares in the KCRC Subsidiaries (as defined on page 125) that were transferred to the Company under the Sale and Purchase Agreement which was entered into on 9 August 2007 between the Company and KCRC.

In addition to the initial payments above, the Company is also required to make the following payments to KCRC going forward:

- fixed annual payments of HK$750 million payable under the Service Concession Agreement, for the right to use and operate the concession property for the operation of the service concession, in arrears on the day immediately preceding each anniversary of the Merger Date which falls during the concession period in respect of the 12 month period up to and including the date on which such payment falls due; and
- variable annual payments payable under the Service Concession Agreement, for the right to use and operate the concession property for the operation of the service concession, in each case, calculated on a tiered basis by reference to the amount of revenue from the KCRC system (as determined in accordance with the Service Concession Agreement) for each financial year of the Company. No variable annual payment is payable in respect of the first 36 months following the Merger Date.

As a complete package deal, other than the payment elements described above and unless stated otherwise in the relevant paragraph below, no specific allocation was made between the various elements of the Rail Merger.

B Service Concession Agreement

The Service Concession Agreement was entered into on 9 August 2007 between the Company and KCRC.

The Service Concession Agreement contains provisions in relation to the grant and operation of a service concession and licence granted by KCRC to the Company ("Service Concession"), including in relation to:

- the grant of the Service Concession to the Company to access, use and operate the concession property (other than KCRC railway land referred to immediately below) to certain specified standards;
- the grant of a licence to access and use certain KCRC railway land;
- the term (being an initial period of 50 years from the Merger Date) of the Service Concession and redelivery of the KCRC system upon expiry or termination of the concession period. The Service Concession will end if the Company's franchise relating to the KCRC railway is revoked;

- the payments of an upfront payment of HK$4.25 billion and fixed annual payments and variable annual payments (as described in paragraph A above);
- KCRC remaining the legal and beneficial owner of the concession property as at the Merger Date and the Company being the legal and beneficial owner of certain future concession property ("Additional Concession Property");
- the regime for compensation payable by KCRC to the Company if Additional Concession Property is returned to KCRC at the end of the concession period;
- the rights and restrictions of the Company and KCRC in relation to the concession property; and
- subject to certain conditions, the Company bearing all risks, liabilities and/or costs whatsoever associated with or arising from the concession property and the land on which any of the concession property is located during the concession period.

C Sale and Purchase Agreement

The Sale and Purchase Agreement was entered into on 9 August 2007 between the Company and KCRC.

The Sale and Purchase Agreement provides the terms pursuant to which the Company acquired certain assets and contracts (the "Purchased Rail Assets") from KCRC.

The consideration for the sale of the Purchased Rail Assets (excluding the shares in the KCRC Subsidiaries) formed part of the upfront payment of HK$4.25 billion. The consideration for the sale of the shares in the KCRC Subsidiaries (which own the Category 1A Properties referred to at paragraph E below and act as property managers) formed part of the payment of HK$7.79 billion for the property package (as described in paragraph A above and in paragraph E below).

D Operating Agreement

The Operating Agreement was entered into on 9 August 2007 between the Company and the Secretary for Transport and Housing for and on behalf of the Government as contemplated in the MTR Ordinance.

The Operating Agreement is based on the previous Operating Agreement which was signed on 30 June 2000. The Operating Agreement differs from the previous Operating Agreement to provide for, amongst other things, the nature of the combined MTRC railway and KCRC railway. The Operating Agreement includes terms relating to:

- the extension of the Company's franchise under the MTR Ordinance;
- the design, construction and maintenance of the railway;
- passenger services;
- a framework for the award of new projects and the operation and ownership structure of new railways;
- the adjustment mechanism to be applied to certain of the Company's fares; and
- compensation which may be payable under the MTR Ordinance to the Company in relation to a suspension, expiry or termination of the franchise.

E Additional Property Package Agreements

Category 1A Properties

The Category 1A Properties are held by the KCRC Subsidiaries. Under the terms of the Sale and Purchase Agreement, the Company acquired from KCRC the shares in the KCRC Subsidiaries (and thereby indirectly acquired the "Category 1A Properties").

Category 1B Properties

On 9 August 2007, KCRC and the Company entered into an agreement for sale of purchase under which KCRC agreed to assign certain properties (the "Category 1B Properties") to the Company on the Merger Date. The relevant assignment was executed between KCRC and the Company on 2 December 2007.

Category 4 Properties

On 9 August 2007, the Government entered into an undertaking that it would, within periods to be agreed between the Company and the Government, offer to the Company a private treaty grant in respect of certain development sites ("Category 4 Properties"). The terms of each private treaty grant shall generally be determined by the Government, and the premium for each private treaty grant shall be assessed on a full market value basis ignoring the presence of the railway other than the Tin Shui Wai Terminus, Light Rail, Yuen Long, New Territories.

On 9 August 2007, the Company issued a letter to KCRC confirming that, if there should be any railway premises on the Category 4 Properties, the Company would assign the railway premises to KCRC.

Metropolis Equity Sub-participation Agreement

The Metropolis Equity Sub-participation Agreement was entered into on 9 August 2007 between KCRC and the Company. KCRC is obliged to act on the Company's instructions, and pay to the Company any distributions, or proceeds of sale, relating to its shareholding in the property management company The Metropolis Management Company Limited ("Metropolis"). The issued share capital of Metropolis is 25,500 A shares (which are held by KCRC) and 24,500 B shares (which are held by Cheung Kong Property Management Limited). Metropolis' business is property management.

F Liaison Committee Letter

The Liaison Committee Letter was issued on 9 August 2007 by KCRC, the terms of which were acknowledged and agreed to by the Company and the Government.

The letter sets out the agreement between the parties regarding a "Liaison Committee" established for the purposes of governing certain matters of KCRC between 9 August 2007 and the Merger Date. Upon the completion of the Rail Merger the Liaison Committee was dissolved.

G Application of Merger-related Waiver

In relation to the Operating Agreement and the Service Concession Agreement, pursuant to paragraph A of the Merger-related Waiver, the Stock Exchange granted a waiver to the Company from strict compliance with all the continuing connected transaction requirements of Chapter 14A of the Listing Rules.

Auditors

The retiring auditors, KPMG, have signified their willingness to continue in office. A resolution will be proposed at the Annual General Meeting to reappoint them and to authorise the Directors to fix their remuneration.

By order of the Board

Leonard Bryan Turk
Secretary to the Board
Hong Kong, 3 March 2011

Contents of Accounts and Notes

Independent Auditor's Report

Independent Auditor's Report to the Shareholders of MTR Corporation Limited

(Incorporated in Hong Kong with limited liability)

We have audited the consolidated accounts of MTR Corporation Limited (the "Company") and its subsidiaries (together "the Group") set out on pages 139 to 234, which comprise the consolidated and company balance sheets as at 31 December 2010, and the consolidated profit and loss account, the consolidated statement of comprehensive income, the consolidated statement of changes in equity and the consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory information.

Directors' Responsibility for the Consolidated Accounts

The directors of the company are responsible for the preparation of consolidated accounts that give a true and fair view in accordance with Hong Kong Financial Reporting Standards issued by the Hong Kong Institute of Certified Public Accountants and the Hong Kong Companies Ordinance, and for such internal control as the directors determine is necessary to enable the preparation of consolidated accounts that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated accounts based on our audit. This report is made solely to you, as a body, in accordance with section 141 of the Hong Kong Companies Ordinance, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

We conducted our audit in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated accounts are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated accounts. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the consolidated accounts, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation of consolidated accounts that give a true and fair view in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the consolidated accounts.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated accounts give a true and fair view of the state of affairs of the Company and of the Group as at 31 December 2010, and of the Group's profit and cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards and have been properly prepared in accordance with the Hong Kong Companies Ordinance.

KPMG

Certified Public Accountants

8th Floor, Prince's Building
10 Chater Road
Central, Hong Kong
3 March 2011

Consolidated Profit and Loss Account

for the year ended 31 December in HK$ million	Note	2010	2009
Hong Kong fare revenue	4	**12,459**	11,498
Station commercial and rail related revenue	5A	**3,715**	3,328
Rental, management and other revenue	5B	**3,200**	2,928
Revenue from railway subsidiaries outside of Hong Kong	6	**10,144**	1,043
Other net income	7	**–**	–
		29,518	18,797
Expenses relating to Hong Kong fare revenue			
– Staff costs and related expenses	8A	**(3,398)**	(3,387)
– Energy and utilities		**(1,067)**	(1,020)
– Operational rent and rates		**(184)**	(183)
– Stores and spares consumed		**(421)**	(403)
– Maintenance and related works	8B	**(912)**	(915)
– Railway support services		**(139)**	(127)
– General and administration expenses		**(379)**	(329)
– Other expenses		**(228)**	(179)
		(6,728)	(6,543)
Expenses relating to station commercial and rail related businesses		**(975)**	(632)
Expenses relating to property ownership, management and other businesses		**(817)**	(866)
Expenses relating to railway subsidiaries outside of Hong Kong	6	**(9,865)**	(1,035)
Project study and business development expenses	8C	**(216)**	(206)
Operating expenses before depreciation, amortisation and variable annual payment arising from the Rail Merger	8D,E&F	**(18,601)**	(9,282)
Operating profit from railway and related businesses before depreciation, amortisation and variable annual payment arising from the Rail Merger		**10,917**	9,515
Profit on property developments	10	**4,034**	3,554
Operating profit before depreciation, amortisation and variable annual payment arising from the Rail Merger		**14,951**	13,069
Depreciation and amortisation	11	**(3,120)**	(2,992)
Variable annual payment arising from the Rail Merger	12	**(45)**	–
Merger related expenses	13	**–**	(12)
Operating profit before interest and finance charges		**11,786**	10,065
Interest and finance charges	14	**(1,237)**	(1,504)
Change in fair value of investment properties	22	**4,074**	2,798
Share of profits of non-controlled subsidiaries and associates	15	**139**	160
Profit before taxation		**14,762**	11,519
Income tax	16A	**(2,590)**	(1,880)
Profit for the year		**12,172**	9,639
Attributable to:			
– Equity shareholders of the Company	17	**12,059**	9,639
– Non-controlling interests		**113**	–
Profit for the year		**12,172**	9,639
Earnings per share:	19		
– Basic		**HK$2.10**	HK$1.69
– Diluted		**HK$2.10**	HK$1.69

The notes on pages 145 to 234 form part of the accounts.

Consolidated Statement of Comprehensive Income

for the year ended 31 December in HK$ million	Note	2010	2009
Profit for the year		**12,172**	9,639
Other comprehensive income for the year (after taxation and reclassification adjustments):			
Exchange differences on translation of:			
– financial statements of overseas subsidiaries		**141**	(10)
– non-controlling interests		**16**	–
	21A	**157**	(10)
Cash flow hedges: net movement in hedging reserve	21A&B	**(26)**	102
Self-occupied land and buildings: net movement in fixed assets revaluation reserve	21A&B	**285**	172
		416	264
Total comprehensive income for the year		**12,588**	9,903
Attributable to:			
– Equity shareholders of the Company		**12,459**	9,903
– Non-controlling interests		**129**	–
Total comprehensive income for the year		**12,588**	9,903

The notes on pages 145 to 234 form part of the accounts.

Consolidated Balance Sheet

at 31 December in HK$ million	Note	2010	2009
Assets			
Fixed assets			
– Investment properties	22	**45,314**	40,993
– Other property, plant and equipment	23	**77,276**	77,844
– Service concession assets	24	**21,467**	19,351
		144,057	138,188
Property management rights	25	**31**	31
Railway construction in progress	26	**–**	–
Property development in progress	28A	**9,128**	6,718
Deferred expenditure	29	**1,079**	558
Interests in non-controlled subsidiaries	30	**541**	490
Interests in associates	32	**836**	823
Deferred tax assets	49B	**9**	12
Investments in securities	33	**3,912**	227
Staff housing loans	34	**4**	7
Properties held for sale	35	**1,936**	3,783
Derivative financial assets	36	**375**	370
Stores and spares	37	**1,061**	1,040
Debtors, deposits and payments in advance	38	**3,057**	2,428
Loan to a property developer	39	**1,975**	1,916
Amounts due from the Government and other related parties	40	**330**	12,788
Cash, bank balances and deposits	41	**13,334**	7,115
		181,665	176,494
Liabilities			
Bank overdrafts	42A	**16**	21
Short-term loans	42A	**300**	25
Creditors and accrued charges	43	**15,491**	20,497
Current taxation	49A	**1,018**	430
Contract retentions	44	**404**	354
Amounts due to the Government and other related parties	45	**892**	923
Loans and other obligations	42A	**20,741**	23,822
Obligations under service concession	46	**10,749**	10,625
Derivative financial liabilities	36	**148**	237
Loan from holders of non-controlling interests	47	**154**	136
Deferred income	48	**605**	167
Deferred tax liabilities	49B	**13,854**	12,804
		64,372	70,041
Net assets		**117,293**	106,453
Capital and reserves			
Share capital, share premium and capital reserve	50A	**43,734**	42,497
Other reserves	51	**73,416**	63,890
Total equity attributable to equity shareholders of the Company		**117,150**	106,387
Non-controlling interests		**143**	66
Total equity		**117,293**	106,453

Approved and authorised for issue by the Members of the Board on 3 March 2011

Raymond K F Ch'ien
C K Chow
Lincoln K K Leong

The notes on pages 145 to 234 form part of the accounts.

Balance Sheet

at 31 December in HK$ million	Note	2010	2009
Assets			
Fixed assets			
– Investment properties	22	**44,166**	39,879
– Other property, plant and equipment	23	**76,845**	77,533
– Service concession assets	24	**15,963**	15,725
		136,974	133,137
Property management rights	25	**31**	31
Railway construction in progress	26	**–**	–
Property development in progress	28A	**9,128**	6,718
Deferred expenditure	29	**1,079**	558
Investments in subsidiaries	31	**1,256**	1,219
Investments in securities	33	**3,627**	–
Staff housing loans	34	**4**	7
Properties held for sale	35	**1,936**	3,783
Derivative financial assets	36	**375**	370
Stores and spares	37	**874**	874
Debtors, deposits and payments in advance	38	**1,775**	1,939
Loan to a property developer	39	**1,975**	1,916
Amounts due from the Government and other related parties	40	**4,365**	15,955
Cash, bank balances and deposits	41	**12,273**	5,622
		175,672	172,129
Liabilities			
Bank overdrafts	42A	**16**	21
Short-term loans	42A	**300**	25
Creditors and accrued charges	43	**13,308**	18,581
Current taxation	49A	**910**	425
Contract retentions	44	**221**	204
Amounts due to the Government and other related parties	45	**12,079**	13,159
Loans and other obligations	42A	**7,700**	10,381
Obligations under service concession	46	**10,592**	10,625
Derivative financial liabilities	36	**148**	237
Deferred income	48	**568**	124
Deferred tax liabilities	49B	**13,840**	12,798
		59,682	66,580
Net assets		**115,990**	105,549
Capital and reserves			
Share capital, share premium and capital reserve	50A	**43,734**	42,497
Other reserves	51	**72,256**	63,052
Total equity		**115,990**	105,549

Approved and authorised for issue by the Members of the Board on 3 March 2011

Raymond K F Ch'ien
C K Chow
Lincoln K K Leong

The notes on pages 145 to 234 form part of the accounts.

Consolidated Statement of Changes in Equity

for the year ended 31 December in HK$ million	Note	Share capital, share premium and capital reserve	Other reserves: Fixed assets revaluation reserve	Other reserves: Hedging reserve	Other reserves: Employee share-based capital reserve	Other reserves: Exchange reserve	Retained profits	Total equity attributable to equity shareholders of the Company	Non-controlling interests	Total equity
2010										
Balance as at 1 January 2010		**42,497**	**1,132**	**(52)**	**52**	**53**	**62,705**	**106,387**	**66**	**106,453**
Changes in equity for the year ended 31 December 2010:										
– Profit for the year		**–**	**–**	**–**	**–**	**–**	**12,059**	**12,059**	**113**	**12,172**
– Other comprehensive income	21	**–**	**285**	**(26)**	**–**	**141**	**–**	**400**	**16**	**416**
– Total comprehensive income		**–**	**285**	**(26)**	**–**	**141**	**12,059**	**12,459**	**129**	**12,588**
– 2009 final dividend	51	**1,087**	**–**	**–**	**–**	**–**	**(2,177)**	**(1,090)**	**–**	**(1,090)**
– 2010 interim dividend	51	**81**	**–**	**–**	**–**	**–**	**(807)**	**(726)**	**–**	**(726)**
– Dividend paid to holders of non-controlling interests		**–**	**–**	**–**	**–**	**–**	**–**	**–**	**(52)**	**(52)**
– Employee share-based payments		**–**	**–**	**–**	**57**	**–**	**–**	**57**	**–**	**57**
– Employee share options exercised	50A, 51	**69**	**–**	**–**	**(6)**	**–**	**–**	**63**	**–**	**63**
– Employee share options lapsed		**–**	**–**	**–**	**(1)**	**–**	**1**	**–**	**–**	**–**
Balance as at 31 December 2010		**43,734**	**1,417**	**(78)**	**102**	**194**	**71,781**	**117,150**	**143**	**117,293**
2009										
Balance as at 1 January 2009		41,119	960	(154)	25	63	55,788	97,801	21	97,822
Changes in equity for the year ended 31 December 2009:										
– Profit for the year		–	–	–	–	–	9,639	9,639	–	9,639
– Other comprehensive income	21	–	172	102	–	(10)	–	264	–	264
– Total comprehensive income		–	172	102	–	(10)	9,639	9,903	–	9,903
– 2008 final dividend	51	962	–	–	–	–	(1,925)	(963)	–	(963)
– 2009 interim dividend	51	399	–	–	–	–	(800)	(401)	–	(401)
– Employee share-based payments		–	–	–	32	–	–	32	–	32
– Employee share options exercised	51	17	–	–	(2)	–	–	15	–	15
– Employee share options lapsed		–	–	–	(3)	–	3	–	–	–
– Increase in non-controlling interests arising from shares issued by a subsidiary		–	–	–	–	–	–	–	45	45
Balance as at 31 December 2009		42,497	1,132	(52)	52	53	62,705	106,387	66	106,453

The notes on pages 145 to 234 form part of the accounts.

Consolidated Cash Flow Statement

for the year ended 31 December in HK$ million	Note	2010		2009	
Cash flows from operating activities					
Operating profit from railway and related businesses before depreciation, amortisation and variable annual payment arising from the Rail Merger		**10,917**		9,515	
Adjustments for:					
Increase in provision for obsolete stock		**2**		–	
Loss on disposal of fixed assets		**50**		6	
Amortisation of deferred income from transfers of assets from customers		**(6)**		(2)	
Increase in fair value of derivative instruments		**(1)**		(3)	
Unrealised loss on revaluation of investment in securities		**2**		1	
Employee share-based payment expenses		**61**		40	
Exchange loss		**14**		4	
Operating profit from railway and related businesses before working capital changes		**11,039**		9,561	
Increase in debtors, deposits and payments in advance		**(246)**		(490)	
Increase in stores and spares		**(5)**		(350)	
Increase in creditors and accrued charges		**1,130**		758	
Cash generated from operations		**11,918**		9,479	
Current tax paid					
Hong Kong Profits Tax paid		**(1,007)**		(1,369)	
Overseas tax paid		**(4)**		(3)	
Net cash generated from operating activities			**10,907**		8,107
Cash flows from investing activities					
Capital expenditure					
– Purchase of Hong Kong operational railway assets		**(1,953)**		(2,250)	
– West Island Line Project		**(3,218)**		(851)	
– South Island Line Project		**(347)**		(214)	
– Kwun Tong Line Extension Project		**(190)**		(78)	
– Shenzhen Metro Line 4 Project		**(1,846)**		(1,203)	
– Property development projects		**(4,279)**		(231)	
– Property renovation, fitting out works and other development projects		**(338)**		(300)	
– Other capital projects		**(165)**		(214)	
Net receipts/(payments) in respect of entrustment works of Shatin to Central Link and Express Rail Link		**84**		(50)	
Fixed annual payment arising from the Rail Merger		**(750)**		(750)	
Receipts in respect of property development		**5,249**		11,784	
Loan repayment from a property developer		**–**		2,000	
Receipt of Government funding support for West Island Line Project		**12,252**		–	
Increase in bank deposits with more than three months to maturity when placed		**(9,610)**		–	
Purchase of investments in securities		**(3,844)**		(47)	
Proceeds from sale of investments in securities		**159**		283	
Proceeds from disposal of fixed assets		**7**		43	
Investment in and loan to associates		**–**		(123)	
Dividend received from non-controlled subsidiaries		**75**		40	
Receipts from holders of non-controlling interests for investment in a subsidiary		**–**		185	
Principal repayments under Staff Housing Loan Scheme		**2**		3	
Net cash (used in) / generated from investing activities			**(8,712)**		8,027
Cash flows from financing activities					
Proceeds from shares issued under share option schemes		**63**		16	
Drawdown of loans		**8,153**		7,954	
Proceeds from issuance of capital market instruments		**–**		500	
Repayment of loans		**(5,390)**		(8,637)	
Repayment of capital market instruments		**(5,778)**		(7,111)	
Interest paid		**(861)**		(1,127)	
Interest received		**123**		14	
Finance charges paid		**(19)**		(21)	
Dividends paid to equity shareholders of the Company		**(1,814)**		(1,362)	
Dividends paid to holders of non-controlling interests		**(58)**		–	
Net cash used in financing activities			**(5,581)**		(9,774)
Net (decrease)/increase in cash and cash equivalents			**(3,386)**		6,360
Cash and cash equivalents at 1 January			**7,094**		734
Cash and cash equivalents at 31 December	41		**3,708**		7,094

The notes on pages 145 to 234 form part of the accounts.

Notes to the Accounts

1 Statement of Compliance

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

The HKICPA has issued certain new and revised HKFRSs that are effective for accounting periods beginning on or after 1 January 2010. Changes in accounting policies resulting from the initial application of these developments to the extent that they are relevant to the Group for the current and prior accounting periods reflected in these accounts are disclosed in note 2A(iii).

2 Principal Accounting Policies

A Basis of Preparation of the Accounts

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

- investment properties (see note 2F(i));
- other leasehold land and buildings, where the leasehold land is classified as being held under a finance lease (see note 2F(ii));
- financial instruments classified as investments in securities other than those intended to be held to maturity (see note 2M); and
- derivative financial instruments (see note 2T).

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

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

Judgements made by management in the application of HKFRSs that have significant effect on the accounts and estimates are discussed in note 58.

(iii) The HKICPA has issued the following new HKFRS, amendments to HKFRSs or new Interpretations that are first effective for the current accounting period of the Group and relevant to the Group's accounts:

- Revised HKFRS 1, *First-time adoption of Hong Kong Financial Reporting Standards*
- HKFRS 3 (revised 2008), *Business combinations*
- Amendments to HKAS 27, *Consolidated and separate financial statements*
- Amendments to HKAS 39, *Financial instruments: Recognition and measurement – Eligible hedged items*
- HK(IFRIC) 17, *Distribution of non-cash assets to owners*
- HK(Int) 5, *Presentation of Financial Statements – Classification by the borrower of a term loan that contains a repayment on demand clause*
- Improvements to HKFRSs (2009)
- Amendments to HKFRS 1, *First-time adoption of Hong Kong Financial Reporting Standards – Additional exemptions for first-time adopters*
- Amendments to HKFRS 2, *Share-based payment – Group cash-settled share-based payment transactions*

The "Improvements to HKFRSs (2009)" comprises a number of minor and non-urgent amendments to a range of HKFRSs which the HKICPA has issued as an omnibus batch of amendments. Of these, only the amendment relating to HKAS 17, *Leases*, has impact on the Group's accounts. As a result of the amendment to HKAS 17, the Group has re-evaluated the classification of its interests in leasehold land as to whether, in the Group's judgement, the lease transfers significantly all the risks and rewards of ownership of the land such that the Group is in a position economically similar to that of a purchaser. The Group has concluded that its interests in leasehold land, which are registered and located in the Hong Kong Special Administrative Region ("HKSAR") and subject to the HKSAR Government's land policy of renewal without payment of additional land premium, are no longer classified as operating leases. The Group's position in respect of its interests in leasehold land is economically similar to that of a purchaser and therefore such interests of leasehold land should be re-classified as finance leases. In accordance with the amendment to HKAS 17, this change in accounting policy has been applied retrospectively. Corresponding amounts of previous periods have been re-classified with the balance of prepaid land lease payments as at 31 December 2009 of HK$554 million (1 January 2009: HK$567 million) re-classified as other property, plant and equipment on the consolidated and the Company's balance sheets and the related amortisation for the year ended 31 December 2009 of HK$13 million re-classified from other expenses to depreciation and amortisation in the consolidated profit and loss account.

Other HKFRS developments have no material impact on the Group's accounts as the amendments and interpretations are consistent with policies already adopted by the Group.

The Group has not applied any new standard or interpretation that is not yet effective for the current accounting period (see note 59).

2 Principal Accounting Policies *(continued)*

B Basis of Consolidation

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

C Subsidiaries and Non-controlling Interests

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

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

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

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

D Non-controlled Subsidiaries

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

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

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

E Associates and Jointly Controlled Entities

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

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

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

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

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

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

2 Principal Accounting Policies *(continued)*

F Fixed Assets

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

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

(ii) Leasehold land registered and located in the HKSAR is accounted for as being held under a finance lease and is stated at cost less accumulated depreciation and impairment losses (see note 2H(ii)). Land held for own use under operating leases and buildings thereon, where the fair value of the leasehold interest in the land and buildings cannot be measured separately at inception of the lease are accounted for as being held under a finance lease, unless the buildings are also clearly held under an operating lease. The self-occupied land and buildings are stated on the balance sheet at their fair value on the basis of their existing use at the date of revaluation less any subsequent accumulated depreciation. Revaluations are performed by independent qualified valuers semi-annually, with changes in the value arising on revaluations treated as movements in the fixed assets revaluation reserve, except:

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

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

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

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

(v) Leased Assets

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

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

(c) Land held for own use under an operating lease, where its fair value cannot be measured separately from the fair value of a building situated thereon at inception of the lease, is accounted for as being held under a finance lease, unless the building is also clearly held under an operating lease (see note 2F(ii)). For these purposes, inception of the lease is the time that the lease was first entered into by the Group, or taken over from the previous lessee, or at the date of construction of those buildings, if later.

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

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

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

2 Principal Accounting Policies *(continued)*

F Fixed Assets *(continued)*

(vii) Service Concession Assets

Where the Group enters into service concession arrangements under which the Group acquires the right to access, use and operate certain assets for the provision of public services ("concession infrastructure"):

- Upfront payments at inception of the service concession are capitalised and amortised on a straight-line basis over the period of the service concession;
- Annual payments over the period of the service concession with the amounts fixed at inception are capitalised at the present value of the total fixed annual payments discounted at the incremental long-term borrowing rate determined at inception, and amortised on a straight-line basis over the period of the service concession with a corresponding liability recognised as obligations under service concession when the Group has a right to charge for usage of the concession infrastructure;
- Annual payments for the service concession which are not fixed or determinable at inception and which are contingent on future revenues generated from the service concession over certain thresholds are charged to the profit and loss account in the period when incurred;
- Expenditure directly attributable to the acquisition of the service concession up to inception, including the assumption of certain obligations of the grantor of the service concession, are capitalised and amortised on a straight-line basis over the period of the service concession; and
- Payments for the replacement and/or upgrade of assets subject to the service concession arrangement are capitalised and amortised on a straight-line basis over the shorter of the assets' useful lives and the remaining period of the service concession.

Where the Group enters into service concession arrangements under which the Group constructs, uses and operates certain assets for the provision of public services, construction revenues and costs are recognised in the profit and loss account by reference to the stage of completion at the balance sheet date while service concession assets are recognised in the balance sheet at fair value upon initial recognition and amortised on a straight-line basis over the period of the service concession. Expenditures for the replacement and/or upgrade of the assets subject to service concession are capitalised and amortised on a straight-line basis over the shorter of the assets' useful lives and the remaining period of the service concession.

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

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

G Property Management Rights

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

H Impairment of Assets

(i) Impairment of Debtors and Other Receivables

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

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

(ii) Impairment of Other Assets

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

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

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

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

2 Principal Accounting Policies *(continued)*

H Impairment of Assets *(continued)*

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

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

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

I Depreciation

(i) Investment properties are not depreciated.

(ii) Fixed assets other than investment properties and assets under construction are depreciated on a straight-line basis at rates sufficient to write off their cost or valuation, less their estimated residual value, if any, over their estimated useful lives as follows:

Land and Buildings

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

Civil Works

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

Plant and Equipment

Rolling stock and components	4 – 50 years
Platform screen doors	35 years
Rail track	7 – 30 years
Environmental control systems, lifts and escalators, fire protection and drainage system	7 – 30 years
Power supply systems	7 – 40 years
Aerial ropeway and cabin	5 – 27 years
Automatic fare collection systems, metal station kiosks, and other mechanical equipment	20 years
Train control and signalling equipment, station announcement systems, telecommunication systems and advertising panels	5 – 20 years
Station architectural finishes	20 – 30 years
Fixtures and fittings	10 – 15 years
Maintenance equipment	4 – 15 years
Office furniture and equipment	2 – 15 years
Computer software licences and applications	2.5 – 7 years
Computer equipment	3 – 5 years
Cleaning equipment and tools	5 years
Motor vehicles	5 years

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

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

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

2 Principal Accounting Policies *(continued)*

J Construction Costs

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

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

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

K Property Development

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

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

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

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

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

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

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

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

L Jointly Controlled Operations

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

2 Principal Accounting Policies *(continued)*

M Investments in Securities

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

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

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

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

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

N Stores and Spares

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

O Long-term Contracts

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

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

P Cash and Cash Equivalents

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

Q Debtors, Deposits and Payments in Advance

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

R Interest-bearing Borrowings

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

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

S Creditors and Accrued Charges

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

2 Principal Accounting Policies *(continued)*

T Derivative Financial Instruments and Hedging Activities

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

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

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

(i) Fair Value Hedge

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

(ii) Cash Flow Hedge

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

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

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

(iii) Derivatives That Do Not Qualify for Hedge Accounting

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

U Employee Benefits

(i) Salaries, annual leave, leave passage allowance and other costs of non-monetary benefits are accrued and recognised as an expense in the year in which the associated services are rendered by employees of the Group, except those benefits incurred for staff in respect of construction projects, capital works and property developments, which are capitalised as part of the cost of the qualifying assets.

(ii) Contributions to defined contribution retirement plans, including contributions to Mandatory Provident Funds ("MPF") as required under the Hong Kong Mandatory Provident Fund Schemes Ordinance, are recognised as an expense in the profit and loss account as incurred, except those contributions incurred for staff in respect of construction projects, capital works and property developments, which are capitalised as part of the cost of the qualifying assets.

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

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

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

2 Principal Accounting Policies *(continued)*

U Employee Benefits *(continued)*

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

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

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

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

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

V Retirement Schemes

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

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

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

W Income Tax

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

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

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

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

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

2 Principal Accounting Policies *(continued)*

W Income Tax *(continued)*

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

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

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

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

X Financial Guarantee Contracts

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

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

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

Y Provisions and Contingent Liabilities

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

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

Z Revenue Recognition

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

(i) Hong Kong fare revenue is recognised when the journey is provided.

(ii) Advertising income and service fees from telecommunication services provided within the railway are recognised when the services are provided.

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

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

(v) Franchise revenue from railway subsidiaries outside of Hong Kong is recognised when the services are provided.

2 Principal Accounting Policies *(continued)*

AA Operating Lease Charges

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

BB Interest and Finance Charges

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

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

CC Foreign Currency Translation

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

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

DD Segment Reporting

Operating segments are identified from the financial information provided regularly to the Group's most senior executive management for the purposes of allocated resources to, and assessing the performance of, the Group's various lines of business and geographical locations.

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

EE Related Parties

For the purposes of these accounts, parties are considered to be related to the Group if the Group has the ability, directly or indirectly, to control the party or exercise significant influence over the party in making financial and operating decisions, or vice versa, or where the Group and the party are subject to common control or common significant influence. Related parties may be individuals (being members of key management personnel, significant shareholders and/or their close family members) or other entities including entities which are under the significant influence of related parties of the Group where those parties are individuals, and post-employment benefit plans which are for the benefit of employees of the Group or of any entity that is a related party of the Group.

FF Government Grants

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

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

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

- The expansion of the Company's existing franchise under the Mass Transit Railway Ordinance ("MTR Ordinance") to cover the construction, operation and regulation of railways in addition to the MTRC railway for an initial period of 50 years from the Appointed Day ("Franchise Period"), which may be extended pursuant to the provisions of the MTR Ordinance (note 56I);

- 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;

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

- Under the SCA, the Company is responsible for the expenditure incurred in relation to the maintenance, repair, replacement and upgrade of the KCRC system (with any new assets acquired being classified as "additional concession property"). To the extent that such expenditure exceeds an agreed threshold ("Capex Threshold"), the Company will be reimbursed for any above threshold expenditure at the end of the Concession Period with such reimbursement to be on the basis of depreciated book value;
- In the event that the Concession Period is extended, the fixed annual payment and the variable annual payment will continue to be payable by the Company. On such extension, the Capex Threshold may also be adjusted; and
- Property Package Agreements and Merger Framework agreement setting out the acquisition of certain properties, property management rights and property development rights by the Company as well as the framework for the Rail Merger including the implementation of the Fare Adjustment Mechanism.

4 Hong Kong Fare Revenue

Hong Kong fare revenue comprises:

in HK$ million	**2010**	2009
Domestic Service	**8,668**	7,986
Cross-boundary Service	**2,487**	2,327
Airport Express	**694**	617
Light Rail, Bus and Intercity	**610**	568
	12,459	11,498

The Domestic Service comprises the Kwun Tong, Tsuen Wan, Island, Tung Chung, Tseung Kwan O, Disneyland Resort, East Rail (excluding Cross-boundary Service), West Rail and Ma On Shan lines. In 2009, the Tseung Kwan O Line was extended when the LOHAS Park Station opened on 26 July 2009 and the West Rail Line was extended with the commencement of passenger operation of the Kowloon Southern Link on 16 August 2009.

5 Non-fare Revenue

A Station Commercial and Rail Related Revenue

Station commercial and rail related revenue comprises:

in HK$ million	**2010**	2009
Duty free shops and kiosk rental	**1,716**	1,605
Advertising	**734**	597
Telecommunication income	**290**	273
Consultancy income	**113**	159
Project management income from KCRC and the Government	**557**	396
Miscellaneous business revenue	**305**	298
	3,715	3,328

5 Non-fare Revenue *(continued)*

B Rental, Management and Other Revenue

in HK$ million	2010	2009
Property rental income:		
– Telford Plaza	**614**	585
– Elements	**509**	442
– Maritime Square	**377**	355
– Luk Yeung Galleria	**153**	147
– Paradise Mall	**118**	115
– Citylink Plaza	**112**	118
– International Finance Centre	**390**	322
– Ginza Mall – Beijing	**105**	108
– Other properties	**380**	356
	2,758	2,548
Property management income	**203**	207
	2,961	2,755
Ngong Ping 360 business revenue	**239**	173
	3,200	2,928

Included in property rental income is HK$116 million (2009: HK$111 million) in respect of the provision of air conditioning services.

Ngong Ping 360 business revenue comprises revenue generated from the cable car operations in Tung Chung and related businesses at the Ngong Ping Theme Village.

6 Revenue and Expenses from Railway Subsidiaries outside of Hong Kong

The operations and maintenance of the Stockholm Metro, Melbourne metropolitan train network ("Melbourne Train") and Phase 1 of Line 4 of Shenzhen Metro System ("Shenzhen Line 4") were taken over by the Group on 2 November 2009, 30 November 2009 and 1 July 2010 respectively. Details of the respective concession arrangements are set out in notes 57H(ii), 57H(iii) and 57G(i). Revenue and expenses relating to railway subsidiaries outside of Hong Kong comprise:

in HK$ million	Stockholm Metro	Melbourne Train	Shenzhen Line 4	Total
2010				
Revenue				
– Franchise income	**2,858**	**5,226**	**20**	**8,104**
– Project income	**–**	**2,013**	**27**	**2,040**
	2,858	**7,239**	**47**	**10,144**
Expenses				
– Staff salary and related expenses	**1,026**	**2,626**	**14**	**3,666**
– Operating lease expenses	**882**	**33**	**20**	**935**
– Maintenance and related works	**552**	**1,623**	**5**	**2,180**
– Expenses relating to project income	**–**	**1,870**	**26**	**1,896**
– Other expenses	**404**	**761**	**23**	**1,188**
	2,864	**6,913**	**88**	**9,865**
2009				
Revenue				
– Franchise income	494	464	–	958
– Project income	–	85	–	85
	494	549	–	1,043
Expenses				
– Staff salary and related expenses	178	219	–	397
– Operating lease expenses	150	33	–	183
– Maintenance and related works	89	73	–	162
– Expenses relating to project income	–	80	–	80
– Other expenses	77	136	–	213
	494	541	–	1,035

Included in expenses relating to project income are staff costs and related expenses amounting to HK$182 million for the year ended 31 December 2010 (2009: nil).

7 Other Net Income

Other net income relates to the construction of Shenzhen Line 4 Phase 2 and comprises:

in HK$ million	**2010**	2009
Construction revenue	**1,719**	1,889
Construction cost	**(1,719)**	(1,889)
	–	–

Construction revenue is recognised by reference to the construction costs incurred since signing of the Project Concession Agreement on 18 March 2009 (note 57G(i)). As of 31 December 2010, total construction cost incurred for Shenzhen Line 4 Phase 2 since the signing of concession agreement on 18 March 2009 was HK$3,608 million (31 December 2009: HK$1,889 million). There was no cumulative net profit or loss recognised in respect of the construction as at 31 December 2010 and 2009.

8 Operating Expenses

A Staff costs and related expenses comprise:

in HK$ million	2010	2009
Amount charged to profit and loss account under:		
– staff costs and related expenses	**3,398**	3,387
– maintenance and related works	**78**	73
– expenses relating to station commercial and rail related businesses	**574**	324
– expenses relating to property ownership, management and other businesses	**144**	155
– expenses relating to railway subsidiaries outside of Hong Kong	**3,848**	397
– project study and business development expenses	**142**	110
– other line items	**22**	23
Amount capitalised in:		
– railway construction in progress before offset by government funding support	**183**	124
– property development in progress	**90**	85
– assets under construction and other projects	**399**	329
– service concession assets	**251**	172
Amount recoverable	**542**	633
Total staff costs	**9,671**	5,812

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

The following expenditure is included in staff costs and related expenses:

in HK$ million	2010	2009
Share-based payments	**61**	40
Contributions to defined contribution retirement plans and Mandatory Provident Fund	**362**	191
Expenses recognised in respect of defined benefit retirement plans	**173**	214
	596	445

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

C Project study and business development expenses comprise:

in HK$ million	2010	2009
Business development expenses	**192**	189
Miscellaneous project study expenses and project cost written off	**24**	17
	216	206

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

8 Operating Expenses *(continued)*

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

in HK$ million	2010	2009
Audit services	**10**	8
Tax services	**1**	1
Other audit related services	**3**	2
	14	11

E Operating expenses include the following charges/(credits):

in HK$ million	2010	2009
Loss on disposal of fixed assets	**50**	6
Derivative financial instruments:		
– foreign exchange contracts – ineffective portion of cash flow hedges	**(1)**	(4)
– transfer from hedging reserve (note 21B)	**(1)**	1
Unrealised loss on revaluation of investments in securities	**2**	1

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

in HK$ million	2010	2009
Shopping centre, office building, staff quarters and bus depot	**84**	83
Rolling stock, stations, office buildings, depots, depot equipment and other minor assets for railway subsidiaries	**935**	183
Amount capitalised	**(20)**	(18)
	999	248

9 Remuneration of Members of the Board and the Executive Directorate

A Remuneration of Members of the Board and the Executive Directorate

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

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

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

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

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

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

in HK$ million	Fees	Base pay, allowances and benefits in kind	Retirement scheme contribution	Variable remuneration related to performance	Total
2009					
Members of the Board					
– Raymond Ch'ien Kuo-fung	1.2	–	–	–	1.2
– Cheung Yau-kai (retired on 4 June 2009)	0.1	–	–	–	0.1
– Vincent Cheng Hoi-chuen (appointed on 10 July 2009)	0.1	–	–	–	0.1
– Christine Fang Meng-sang	0.3	–	–	–	0.3
– Edward Ho Sing-tin	0.4	–	–	–	0.4
– Ng Leung-sing	0.3	–	–	–	0.3
– Abraham Shek Lai-him	0.3	–	–	–	0.3
– T. Brian Stevenson	0.4	–	–	–	0.4
– Ceajer Chan Ka-keung	0.3	–	–	–	0.3
– Eva Cheng	0.3	–	–	–	0.3
– Alan Wong Chi-kong (up to 16 August 2009)	0.2	–	–	–	0.2
– Joseph Lai Yee-tak (since 17 August 2009)	0.1	–	–	–	0.1
Members of the Executive Directorate					
– Chow Chung-kong	–	6.5	–*	7.3	13.8
– Russell John Black	–	4.5	1.0	1.9	7.4
– William Chan Fu-keung	–	4.3	0.9	1.9	7.1
– Thomas Ho Hang-kwong	–	4.6	0.9	1.9	7.4
– Lincoln Leong Kwok-kuen	–	4.7	0.8	2.0	7.5
– Andrew McCusker	–	4.5	0.9	1.9	7.3
– Leonard Bryan Turk	–	4.3	0.9	1.9	7.1
	4.0	33.4	5.4	18.8	61.6

* During the year ended 31 December 2009, the total contributions paid by the Company for C K Chow, who participated in the MTR MPF Scheme, were HK$12,000.

Russell J Black and Andrew McCusker received a lump sum benefit payment of HK$20.8 million and HK$20.7 million respectively from the MTR Retirement Scheme upon their retirements in January 2010 and December 2010 respectively.

In addition, on 1 December 2009, C K Chow was paid HK$11.3 million, representing his entitlement to receive an equivalent value in cash of 418,017 shares on completion of his three-year contract ended on 30 November 2009 (note 52B(i)). On 12 April 2010, Lincoln K K Leong was paid HK$4.6 million, representing the derivative interest granted to him on 12 April 2007 to receive an equivalent value in cash of 160,000 shares (note 52B(ii)).

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

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

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

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

- C K Chow was granted options in respect of 720,000 shares on 13 December 2007 and 470,000 shares each on 9 December 2008, 9 December 2009 and 17 December 2010, of which 554,000 options were vested in 2010 (2009: 397,000), and the respective fair value of the share-based payments recognised for the year ended 31 December 2010 was HK$2.5 million (2009: HK$1.7 million);
- Lincoln K K Leong was granted options in respect of 170,000 shares each on 12 December 2007, 9 December 2008, 10 December 2009 and 17 December 2010, of which 170,000 options were vested in 2010 (2009: 114,000), and the respective fair value of the share-based payments recognised for the year ended 31 December 2010 was HK$0.7 million (2009: HK$0.5 million);
- Leonard B Turk was granted options in respect of 170,000 shares each on 12 December 2007, 9 December 2008 and 10 December 2009 and 127,500 shares on 17 December 2010, of which 170,000 options were vested in 2010 (2009: 114,000), and the respective fair value of the share-based payments recognised for the year ended 31 December 2010 was HK$0.7 million (2009: HK$0.5 million);
- Russell J Black was granted options in respect of 170,000 shares each on 12 December 2007 and 9 December 2008 and 42,500 shares on 10 December 2009, of which 127,500 options were vested in 2010 (2009: 114,000), and the respective fair value of the share-based payments recognised for the year ended 31 December 2010 was HK$0.5 million (2009: HK$0.4 million);
- Thomas H K Ho was granted options in respect of 170,000 shares each on 12 December 2007, 11 December 2008 and 14 December 2009 and 127,500 shares on 17 December 2010, of which 170,000 options were vested in 2010 (2009: 114,000), and the respective fair value of the share-based payments recognised for the year ended 31 December 2010 was HK$0.8 million (2009: HK$0.5 million);
- Andrew McCusker was granted options in respect of 170,000 shares each on 12 December 2007, 12 December 2008 and 10 December 2009, of which 170,000 options were vested in 2010 (2009: 114,000), and the respective fair value of the share-based payments recognised for the year ended 31 December 2010 was HK$0.7 million (2009: HK$0.5 million);
- William F K Chan was granted options in respect of 170,000 shares each on 13 December 2007, 9 December 2008, 10 December 2009 and 17 December 2010, of which 170,000 options were vested in 2010 (2009: 114,000), and the respective fair value of the share-based payments recognised for the year ended 31 December 2010 was HK$0.8 million (2009: HK$0.5 million);
- Chew Tai-chong was granted options in respect of 85,000 shares on 18 June 2009 and 170,000 shares each on 10 December 2009 and 17 December 2010, of which 85,500 options were vested in 2010 (2009: nil), and the respective fair value of the share-based payments recognised for the year ended 31 December 2010 was HK$0.5 million (2009: HK$0.1 million); and
- Jacob Kam Chak-pui replaced Andrew McCusker, who retired from the Company on 31 December 2010, as a Member of the Executive Directorate with effect from 1 January 2011. Under the 2007 Option Scheme, Jacob C P Kam was granted options in respect of 75,000 shares on 13 December 2007, 65,000 shares each on 8 December 2008 and 14 December 2009, 50,000 shares on 21 July 2010 and 170,000 shares on 17 December 2010, of which 69,000 options were vested in 2010 (2009: 47,000), and the respective fair value of the share-based payments recognised for the year ended 31 December 2010 was HK$0.3 million (2009: HK$0.2 million).

The details of directors' interest in the Company's shares are disclosed under the paragraph "Board Members' and Executive Directorate's Interests in Shares" of the Report of the Members of the Board and note 52.

(ii) On 1 December 2009, C K Chow was granted a derivative interest in respect of 222,161 shares in the Company within the meaning of Part XV of the Securities and Futures Ordinance ("SFO"). The derivative interest represents C K Chow's entitlement to receive an equivalent value in cash of 222,161 shares upon completion of his existing contract on 31 December 2011.

The arrangement was offered to C K Chow in order to provide a competitive level of compensation which is also closely tied to the performance of the Company.

(iii) The aggregate emoluments of Members of the Board and the Executive Directorate for the year pursuant to section 161 of the Hong Kong Companies Ordinance was HK$70.5 million (2009: HK$77.5 million).

(iv) Non-executive directors of the Company are not appointed for a specific term but are subject (save for those appointed pursuant to Section 8 of the Mass Transit Railway Ordinance (Chapter 556 of the Laws of Hong Kong)) to retirement by rotation and re-election at the Company's annual general meetings in accordance with Articles 87 and 88 of the Company's Articles of Association. Dr. Raymond Ch'ien Kuo-fung, a Member of the Board, was appointed as the non-executive Chairman of the Company with effect from 21 July 2003 for a term of three years. In July 2006, he was re-appointed as the non-executive Chairman of the Company until 31 July 2007. In July 2007, Dr. Ch'ien was re-appointed as the non-executive Chairman of the Company with effect from 1 August 2007 for a term up to 31 December 2007 or the day to be appointed by the Secretary for Transport and Housing by notice published in the Gazette under the Rail Merger Ordinance, whichever was the earlier. On 8 August 2007, he was appointed as the non-executive Chairman of the Company after the Rail Merger for a term of two years commencing from 2 December 2007. On 11 November 2009, he was re-appointed as the non-executive Chairman of the Company with effect from 2 December 2009 to 31 December 2012.

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

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

B Share Options

Options exercised and outstanding in respect of each Member of the Executive Directorate as at 31 December 2010 are set out under the paragraph "Board Members' and Executive Directorate's Interests in Shares" of the Report of the Members of the Board. Details of the options granted to Members of the Executive Directorate are as follows:

(i) Pre-Global Offering Share Option Scheme

Under the Company's Pre-Global Offering Share Option Scheme (the "Pre-IPO Option Scheme") described in note 52A(i), each Member of the Executive Directorate, except C K Chow, Lincoln K K Leong, Andrew McCusker and T C Chew, was granted options on 20 September 2000 to acquire 1,066,000 shares. C K Chow, Lincoln K K Leong and T C Chew joined the Company on 1 December 2003, 1 February 2002 and 11 May 2009 respectively, and are not beneficiaries of the Pre-IPO Option Scheme. Andrew McCusker and Jacob C P Kam were granted options of 266,500 and 117,500 shares respectively on 20 September 2000 under the Pre-IPO Option Scheme and no additional share options were granted upon their appointments as Members of the Executive Directorate on 1 October 2005 and 1 January 2011 respectively.

Under the vesting terms of the Pre-IPO Option Scheme, each eligible Member of the Executive Directorate must continue to beneficially own (i) at all times after 26 October 2001, at least 23,000 shares; and (ii) at all times after 26 October 2002, at least 46,000 shares, in each case, up to and including the date on which he has exercised his option in full or the date on which his option lapses (whichever is earlier). The Pre-IPO Option Scheme expired on 11 September 2010.

(ii) New Joiners Share Option Scheme

Under the New Joiners Share Option Scheme (the "New Option Scheme") as described in note 52A(ii), Lincoln K K Leong, a Member of the Executive Directorate, was granted options to acquire 1,066,000 shares on 1 August 2003.

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

(iii) 2007 Share Option Scheme

Under the 2007 Share Option Scheme (the "2007 Option Scheme") as described in note 52A(iii), all Members of the Executive Directorate were granted options to acquire shares in 2007, 2008, 2009 and 2010. C K Chow was granted options to acquire 720,000 shares in 2007 and 470,000 shares each in 2008, 2009 and 2010. William F K Chan and Lincoln K K Leong were each granted options to acquire 170,000 shares in each of 2007, 2008, 2009 and 2010. Thomas H K Ho and Leonard B Turk were each granted options to acquire 170,000 shares in each of 2007, 2008 and 2009 and 127,500 shares in 2010. Andrew McCusker was granted options to acquire 170,000 shares in each of 2007, 2008 and 2009. Russell J Black was granted options to acquire 170,000 shares in both 2007 and 2008 and 42,500 shares in 2009. T C Chew was granted options to acquire 85,000 shares in June 2009 and 170,000 shares each in December 2009 and 2010. Jacob C P Kam was granted options to acquire 75,000 shares in December 2007, 65,000 shares each in December 2008 and 2009, 50,000 shares in July 2010 and 170,000 shares in December 2010.

Under the vesting terms of the options granted in 2007, 2008, 2009 and 2010, options granted will be evenly vested in respect of their underlying shares over a period of three years from the date of offer to grant such options (note 9A(i)).

10 Profit on Property Developments

Profit on property developments comprises:

in HK$ million	**2010**	2009
Transfer from deferred income on		
– payments received from developers (note 28B(i))	**–**	16
– sharing in kind (note 28B(ii))	**17**	1
Share of surplus from development	**990**	3,497
Income recognised from sharing in kind	**3,026**	72
Miscellaneous income net of other overhead costs	**1**	(32)
	4,034	3,554

11 Depreciation and Amortisation

Depreciation and amortisation comprise:

in HK$ million	2010	2009
Depreciation charge on:		
Hong Kong railway operations	**2,517**	2,476
Assets relating to station commercial and rail related businesses	**93**	91
Assets relating to property ownership, management and other businesses	**72**	71
Railway subsidiaries outside of Hong Kong	**24**	2
	2,706	2,640
Amortisation charge on:		
Service concession assets		
– KCRC Rail Merger	**400**	347
– Railway subsidiaries outside of Hong Kong	**14**	1
Property management rights	**–**	4
	414	352
	3,120	2,992

12 Variable Annual Payment Arising from the Rail Merger

Commencing after the third year from the Appointed Day of the Rail Merger, i.e. 2 December 2010, the Company is obliged to pay variable annual payments to KCRC, calculated on a tiered basis by reference to the revenue generated from the operation of the KCRC service concession over certain thresholds. For the year ended 31 December 2010, the variable annual payment amounted to HK$45 million (2009: nil).

13 Merger Related Expenses

Merger related expenses incurred after the Rail Merger and not eligible for capitalisation were charged to the profit and loss account.

14 Interest and Finance Charges

in HK$ million	2010	2010	2009	2009
Interest expenses in respect of:				
Bank loans, overdrafts and capital market instruments wholly repayable within 5 years	**560**		719	
Bank loans and capital market instruments not wholly repayable within 5 years	**206**		172	
Obligations under service concession	**721**		719	
Other obligations (note 23E)	**15**		15	
Finance charges	**27**		47	
Exchange (gain)/loss	**(37)**		27	
		1,492		1,699
Derivative financial instruments:				
Fair value hedges	**–**		68	
Cash flow hedges:				
– transfer from hedging reserve	**86**		84	
– ineffective portion	**(1)**		–	
Derivatives not qualified for hedge accounting	**–**		3	
		85		155
Interest expenses capitalised		**(178)**		(139)
		1,399		1,715
Interest income in respect of:				
Deposits with banks and other financial institutions	**(114)**		(11)	
Investment in bank medium term notes	**(34)**		–	
Investment in debt securities	**–**		(3)	
Loan to non-controlled subsidiary and associate	**–**		(1)	
		(148)		(15)
Interest income capitalised		**78**		–
		1,329		1,700
Accreted interest on loan to a property developer		**(92)**		(196)
		1,237		1,504

Interest expenses capitalised were calculated at the average cost of borrowings while the interest income capitalised was calculated at the average return from deposits and investments in bank medium term notes to the Group on a monthly basis. During the year ended 31 December 2010, the average cost of borrowings for each month varied from 3.0% to 5.0% per annum (2009: 3.4% to 4.0% per annum) while the average return from deposits and investments in bank medium term notes for each month varied from 0.8% to 1.2% per annum.

During the year, the gain resulting from fair value changes of hedging instruments comprising interest rate and cross currency swaps was HK$119 million (loss in 2009: HK$208 million) and the loss resulting from fair value changes of the underlying financial assets and liabilities being hedged was also HK$119 million (gain in 2009: HK$140 million), with no net gain or loss (2009: net loss of HK$68 million).

15 Share of Profits of Non-controlled Subsidiaries and Associates

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

in HK$ million	2010	2009
Share of profit before taxation of non-controlled subsidiaries (note 30)	**148**	165
Share of profit before taxation of associates (note 32)	**22**	19
	170	184
Share of income tax of non-controlled subsidiaries (note 30)	**(22)**	(16)
Share of income tax of associates (note 32)	**(9)**	(8)
	139	160

16 Income Tax

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

in HK$ million	2010	2009
Current tax		
– Provision for Hong Kong Profits Tax at 16.5% (2009: 16.5%) for the year	**1,495**	1,347
– Overseas tax for the year	**93**	4
	1,588	1,351
Deferred tax		
– Origination and reversal of temporary differences on:		
– change in fair value of investment properties	**672**	462
– disposal of investment properties	**–**	(2)
– utilisation/(provision) of tax losses	**10**	(6)
– depreciation allowances in excess of related depreciation	**287**	59
– provision and others	**33**	16
	1,002	529
	2,590	1,880

The provision for Hong Kong Profits Tax for 2010 is calculated at 16.5% (2009: 16.5%) of the estimated assessable profits for the year after deducting accumulated tax losses brought forward, if any.

Current tax for overseas subsidiaries is charged at the appropriate current rates of taxation ruling in the relevant countries.

Provision for deferred tax on temporary differences arising in Hong Kong is calculated at the Hong Kong Profits Tax rate of 16.5% (2009: 16.5%).

16 Income Tax *(continued)*

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

	2010		2009	
	HK$ million	%	HK$ million	%
Profit before taxation	**14,762**		11,519	
Notional tax on profit before taxation, calculated at the rates applicable to profits in the tax jurisdictions concerned	**2,451**	**16.6**	1,866	16.2
Tax effect of non-deductible expenses	**200**	**1.4**	122	1.1
Tax effect of non-taxable revenue	**(90)**	**(0.6)**	(114)	(1.0)
Tax effect of unused tax losses not recognised	**29**	**0.2**	6	0.1
Actual tax expenses	**2,590**	**17.6**	1,880	16.4

17 Profit Attributable to Equity Shareholders

The consolidated profit attributable to equity shareholders includes a profit of HK$11,878 million (2009: HK$9,663 million) which has been dealt with in the accounts of the Company. Details of dividend paid and payable to equity shareholders of the Company are set out in note 18.

18 Dividends

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

in HK$ million	2010	2009
Dividends paid/payable attributable to the year		
– Interim dividend of 14 cents (2009: 14 cents) per share approved and paid during the year	**807**	800
– Final dividend proposed after the balance sheet date of 45 cents (2009: 38 cents) per share	**2,598**	2,177
	3,405	2,977
Dividends paid attributable to the previous year		
– Final dividend of 38 cents (2008: 34 cents) per share approved and paid during the year	**2,177**	1,925

The final dividend proposed after the balance sheet date has not been recognised as a liability at the balance sheet date.

During the year, scrip dividend elections were offered to all shareholders except shareholders with registered addresses in the United States of America or any of its territories or possessions. The financial year ended 31 December 2009 was the last year in which the Company's majority shareholder, The Financial Secretary Incorporated ("FSI"), had elected to receive part of its entitlement to dividends in the form of scrip to the extent necessary to ensure that the amount payable in cash would not exceed 50% of the total dividend payable. Details of dividends paid to the FSI are disclosed in note 56X.

19 Earnings Per Share

A Basic Earnings Per Share

The calculation of basic earnings per share is based on the profit for the year attributable to equity shareholders of HK$12,059 million (2009: HK$9,639 million) and the weighted average number of ordinary shares of 5,751,035,100 in issue during the year (2009: 5,691,839,821), calculated as follows:

	2010	2009
Issued ordinary shares at 1 January	**5,727,833,692**	5,661,143,113
Effect of scrip dividends issued	**20,911,122**	30,084,773
Effect of share options exercised	**2,290,286**	611,935
Weighted average number of ordinary shares at 31 December	**5,751,035,100**	5,691,839,821

19 Earnings Per Share *(continued)*

B Diluted Earnings Per Share

The calculation of diluted earnings per share is based on the profit for the year attributable to equity shareholders of HK$12,059 million (2009: HK$9,639 million) and the weighted average number of ordinary shares of 5,756,548,816 in issue during the year (2009: 5,697,441,733) after adjusting for the number of dilutive potential ordinary shares under the employee share option schemes, calculated as follows:

	2010	2009
Weighted average number of ordinary shares at 31 December	**5,751,035,100**	5,691,839,821
Effect of dilutive potential shares under the Company's share option schemes	**5,513,716**	5,601,912
Weighted average number of ordinary shares (diluted) at 31 December	**5,756,548,816**	5,697,441,733

C Both basic and diluted earnings per share would have been HK$1.51 (2009: HK$1.28) if the calculation is based on profit from underlying businesses attributable to equity shareholders, i.e. excluding change in fair value of investment properties net of related deferred tax, adjusted as follows:

in HK$ million	**2010**	2009
Profit attributable to equity shareholders	**12,059**	9,639
Change in fair value of investment properties	**(4,074)**	(2,798)
Deferred tax on change in fair value of investment properties		
– Effect of the change during the year (note 16A)	**672**	462
Profit from underlying businesses attributable to equity shareholders	**8,657**	7,303

20 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 railway operations: The operation of an urban mass transit railway system within Hong Kong, an Airport Express serving both the Hong Kong International Airport and the AsiaWorld-Expo at Chek Lap Kok, cross-boundary railway service, light rail and bus services in the north-west New Territories, intercity passenger services and freight business.

(ii) Hong Kong station commercial activities: Commercial activities including letting of advertising, retail and car parking space at railway stations, bandwidth services on the railway telecommunication system and rail related subsidiaries' businesses in Hong Kong.

(iii) Hong Kong property rental and management: The letting of office, retail and car parking space in investment properties and the provision of estate management services in Hong Kong.

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

(v) Property developments: Property development at locations relating to the railway system in Hong Kong.

(vi) All others: Including operations relating to the Ngong Ping 360, railway consultancy services, rental and estate management services in the Mainland of China and share of profits of non-controlled subsidiaries and associates.

20 Segmental Information *(continued)*

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

in HK$ million	Hong Kong railway operations	Hong Kong station commercial activities	Hong Kong property rental and manage-ment	Railway subsidiaries outside of Hong Kong	All others	Property develop-ments	Total
2010							
Revenue	**12,486**	**3,018**	**2,845**	**10,144**	**1,025**	**–**	**29,518**
Operating expenses before depreciation, amortisation and variable annual payment arising from the Rail Merger	**(6,755)**	**(374)**	**(556)**	**(9,865)**	**(835)**	**–**	**(18,385)**
	5,731	**2,644**	**2,289**	**279**	**190**	**–**	**11,133**
Profit on property developments	**–**	**–**	**–**	**–**	**–**	**4,034**	**4,034**
Operating profit before depreciation, amortisation and variable annual payment arising from the Rail Merger	**5,731**	**2,644**	**2,289**	**279**	**190**	**4,034**	**15,167**
Depreciation and amortisation	**(2,901)**	**(109)**	**(4)**	**(38)**	**(68)**	**–**	**(3,120)**
Variable annual payment arising from the Rail Merger	**(35)**	**(10)**	**–**	**–**	**–**	**–**	**(45)**
	2,795	**2,525**	**2,285**	**241**	**122**	**4,034**	**12,002**
Project studies and business development expenses							**(216)**
Operating profit before interest and finance charges							**11,786**
Interest and finance charges							**(1,237)**
Change in fair value of investment properties			**4,074**				**4,074**
Share of profits of non-controlled subsidiaries and associates				**13**	**126**		**139**
Income tax							**(2,590)**
Profit for the year ended 31 December 2010							**12,172**
Assets							
Operational assets *	**73,924**	**1,674**	**45,837**	**2,410**	**1,399**	**652**	**125,896**
Assets under construction	**2,161**	**10**	**–**	**26**	**–**	**–**	**2,197**
Service concession assets	**15,963**	**–**	**–**	**5,504**	**–**	**–**	**21,467**
Property management rights	**–**	**–**	**31**	**–**	**–**	**–**	**31**
Property development in progress	**–**	**–**	**–**	**–**	**–**	**9,128**	**9,128**
Deferred expenditure	**1,021**	**–**	**21**	**–**	**–**	**37**	**1,079**
Deferred tax assets	**–**	**1**	**5**	**3**	**–**	**–**	**9**
Investments in securities	**–**	**–**	**–**	**–**	**285**	**–**	**285**
Properties held for sale	**–**	**–**	**–**	**–**	**–**	**1,936**	**1,936**
Loan to a property developer	**–**	**–**	**–**	**–**	**–**	**1,975**	**1,975**
Interests in non-controlled subsidiaries	**–**	**–**	**–**	**–**	**541**	**–**	**541**
Interests in associates	**–**	**–**	**–**	**836**	**–**	**–**	**836**
	93,069	**1,685**	**45,894**	**8,779**	**2,225**	**13,728**	**165,380**
Unallocated assets							**16,285**
Total assets							**181,665**

20 Segmental Information *(continued)*

in HK$ million	Hong Kong railway operations	Hong Kong station commercial activities	Hong Kong property rental and manage-ment	Railway subsidiaries outside of Hong Kong	All others	Property develop-ments	Total
2010							
Liabilities							
Segment liabilities	**11,064**	**1,061**	**1,195**	**2,193**	**171**	**1,357**	**17,041**
Obligations under service concession	**10,592**	**–**	**–**	**157**	**–**	**–**	**10,749**
Deferred income	**–**	**37**	**–**	**–**	**–**	**568**	**605**
	21,656	**1,098**	**1,195**	**2,350**	**171**	**1,925**	**28,395**
Unallocated liabilities							**35,977**
Total liabilities							**64,372**
Other Information							
Capital expenditure on:							
Operational assets	**65**	**3**	**13**	**95**	**10**	**1**	**187**
Assets under construction	**1,561**	**142**	**–**	**24**	**2**	**–**	**1,729**
Investment properties	**–**	**–**	**247**	**–**	**–**	**–**	**247**
Service concession assets	**566**	**–**	**–**	**1,757**	**–**	**–**	**2,323**
Railway construction in progress	**3,462**	**–**	**–**	**–**	**–**	**–**	**3,462**
Property development in progress	**–**	**–**	**–**	**–**	**–**	**4,372**	**4,372**
Non-cash expenses other than depreciation and amortisation	**44**	**2**	**–**	**4**	**–**	**–**	**50**

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

20 Segmental Information *(continued)*

in HK$ million	Hong Kong railway operations	Hong Kong station commercial activities	Hong Kong property rental and manage-ment	Railway subsidiaries outside of Hong Kong	All others	Property develop-ments	Total
2009							
Revenue	11,530	2,741	2,633	1,043	850	–	18,797
Operating expenses before depreciation and amortisation	(6,591)	(315)	(616)	(1,035)	(519)	–	(9,076)
	4,939	2,426	2,017	8	331	–	9,721
Profit on property developments	–	–	–	–	–	3,554	3,554
Operating profit before depreciation and amortisation	4,939	2,426	2,017	8	331	3,554	13,275
Depreciation and amortisation	(2,816)	(97)	(7)	(3)	(69)	–	(2,992)
	2,123	2,329	2,010	5	262	3,554	10,283
Project studies and business development expenses							(206)
Merger related expenses							(12)
Operating profit before interest and finance charges							10,065
Interest and finance charges							(1,504)
Change in fair value of investment properties			2,798				2,798
Share of profits of non-controlled subsidiaries and associates				11	149		160
Income tax							(1,880)
Profit for the year ended 31 December 2009							9,639
Assets							
Operational assets *	87,342	2,069	41,453	2,029	1,482	808	135,183
Assets under construction	1,350	16	–	–	–	–	1,366
Service concession assets	15,725	–	–	3,626	–	–	19,351
Property management rights	–	–	31	–	–	–	31
Property development in progress	–	–	–	–	–	6,718	6,718
Deferred expenditure	529	–	8	–	–	21	558
Deferred tax assets	–	2	6	–	4	–	12
Investments in securities	–	–	–	–	227	–	227
Properties held for sale	–	–	–	–	–	3,783	3,783
Loan to a property developer	–	–	–	–	–	1,916	1,916
Interests in non-controlled subsidiaries	–	–	–	–	490	–	490
Interests in associates	–	–	–	823	–	–	823
	104,946	2,087	41,498	6,478	2,203	13,246	170,458
Unallocated assets							6,036
Total assets							176,494

20 Segmental Information *(continued)*

in HK$ million	Hong Kong railway operations	Hong Kong station commercial activities	Hong Kong property rental and manage-ment	Railway subsidiaries outside of Hong Kong	All others	Property develop-ments	Total
2009							
Liabilities							
Segment liabilities	13,446	939	1,048	1,764	118	4,597	21,912
Obligations under service concession	10,625	–	–	–	–	–	10,625
Deferred income	–	43	–	–	–	124	167
	24,071	982	1,048	1,764	118	4,721	32,704
Unallocated liabilities							37,337
Total liabilities							70,041
Other Information							
Capital expenditure on:							
Operational assets	56	51	6	67	15	–	195
Assets under construction	1,297	201	–	–	–	–	1,498
Investment properties	–	–	123	–	–	–	123
Service concession assets	486	–	–	1,977	–	–	2,463
Railway construction in progress	1,086	–	–	–	–	–	1,086
Property development in progress	–	–	–	–	–	303	303
Non-cash expenses other than depreciation and amortisation	18	10	(20)	–	–	–	8

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

Unallocated assets and liabilities mainly comprise cash, bank balances and deposits, derivative financial assets and liabilities, interest-bearing loans and borrowings.

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

	Revenue from external customers		Specified non-current assets	
in HK$ million	**2010**	2009	**2010**	2009
Hong Kong (place of domicile)	**19,177**	17,525	**149,073**	142,211
Australia	**7,239**	549	**123**	43
Mainland of China	**175**	148	**6,268**	4,390
Sweden	**2,858**	494	**151**	124
Other countries	**69**	81	**57**	40
	10,341	1,272	**6,599**	4,597
	29,518	18,797	**155,672**	146,808

21 Other Comprehensive Income

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

in HK$ million	2010 Before-tax amount	2010 Tax benefit/ (expense)	2010 Net-of-tax amount	2009 Before-tax amount	2009 Tax expense	2009 Net-of-tax amount
Exchange differences on translation of:						
– Financial statements of overseas subsidiaries	**141**	**–**	**141**	(10)	–	(10)
– Non-controlling interests	**16**	**–**	**16**	–	–	–
	157	**–**	**157**	(10)	–	(10)
Cash flow hedges: net movement in hedging reserve	**(31)**	**5**	**(26)**	122	(20)	102
Self-occupied land and building: net movement in fixed assets revaluation reserve	**341**	**(56)**	**285**	206	(34)	172
Other comprehensive income	**467**	**(51)**	**416**	318	(54)	264

B Reclassification adjustments relating to components of other comprehensive income of the Group are as follows:

in HK$ million	2010	2009
Cash flow hedges:		
Effective portion of changes in fair value of hedging instruments recognised during the year	**(104)**	41
Amounts transferred to initial carrying amount of hedged items	**(12)**	(4)
Transferred to profit or loss:		
– Interest and finance charges (note 14)	**86**	84
– Other expenses (note 8E)	**(1)**	1
Net deferred tax credited/(debited) to other comprehensive income resulting from:		
– Changes in fair value of hedging instruments recognised during the year	**17**	(7)
– Amounts transferred to initial carrying amount of hedged items	**2**	1
– Transferred to profit or loss	**(14)**	(14)
Net movement in the hedging reserve during the year recognised in other comprehensive income	**(26)**	102
Self-occupied land and buildings:		
Changes in fair value recognised during the year	**341**	206
Net deferred tax debited to other comprehensive income resulting from changes in fair value recognised during the year	**(56)**	(34)
Net movement in fixed assets revaluation reserve during the year recognised in other comprehensive income	**285**	172

22 Investment Properties

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

	The Group		The Company	
in HK$ million	**2010**	2009	**2010**	2009
Cost or Valuation				
At 1 January	**40,993**	37,737	**39,879**	36,618
Additions	**247**	123	**229**	117
Disposal	**–**	(17)	**–**	(17)
Change in fair value	**4,074**	2,798	**4,058**	2,809
Reclassification from assets under construction (note 23)	**–**	352	**–**	352
At 31 December	**45,314**	40,993	**44,166**	39,879
Long leases	**1,589**	1,591	**1,589**	1,591
Medium-term leases	**43,725**	39,402	**42,577**	38,288
	45,314	40,993	**44,166**	39,879

All investment properties of the Group were revalued at open market value at 31 December 2010 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$4,074 million (2009: HK$2,798 million) arising from the revaluation has been credited to the consolidated profit and loss account.

The Group's future minimum lease receipts in respect of investment properties under non-cancellable operating leases are disclosed together with those in respect of other properties under note 23D.

23 Other Property, Plant and Equipment

The Group

in HK$ million	Leasehold land	Self-occupied land and buildings	Civil works	Plant and equipment	Assets under construction	Total
2010						
Cost or Valuation						
At 1 January 2010	732	2,120	46,507	61,026	1,366	111,751
Additions	–	–	–	187	1,729	1,916
Capitalisation adjustments *	–	–	(9)	(2)	–	(11)
Disposals/write-offs	–	–	(1)	(360)	(19)	(380)
Surplus on revaluation (note 21B)	–	283	–	–	–	283
Reclassification within other property, plant and equipment	–	–	12	(31)	19	–
Transfer to additional concession property (note 24)	–	–	–	(6)	(68)	(74)
Other assets commissioned	–	–	133	699	(832)	–
Exchange differences	–	–	–	21	2	23
At 31 December 2010	732	2,403	46,642	61,534	2,197	113,508
At Cost	732	–	46,642	61,534	2,197	111,105
At 31 December 2010 Valuation	–	2,403	–	–	–	2,403
Aggregate depreciation						
At 1 January 2010	178	–	5,008	28,721	–	33,907
Charge for the year	13	58	403	2,232	–	2,706
Written back on disposal	–	–	(1)	(324)	–	(325)
Written back on revaluation (note 21B)	–	(58)	–	–	–	(58)
Exchange differences	–	–	–	2	–	2
At 31 December 2010	191	–	5,410	30,631	–	36,232
Net book value at 31 December 2010	541	2,403	41,232	30,903	2,197	77,276

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

The Group

in HK$ million	Leasehold land	Self-occupied land and buildings	Civil works	Plant and equipment	Assets under construction	Total
2009						
Cost or Valuation						
At 1 January 2009, as previously reported	–	1,965	46,359	59,473	1,400	109,197
Reclassification on adoption of the amendment to HKAS 17 (note 2A(iii))	732	–	–	–	–	732
At 1 January 2009, as reclassified	732	1,965	46,359	59,473	1,400	109,929
Additions	–	–	–	195	1,498	1,693
Capitalisation adjustments *	–	–	–	(6)	–	(6)
Disposals/write-offs	–	–	(4)	(270)	(2)	(276)
Surplus on revaluation (note 21B)	–	155	–	–	–	155
Reclassification within other property, plant and equipment	–	–	4	(15)	11	–
Reclassification to investment properties (note 22)	–	–	–	–	(352)	(352)
Transfer to additional concession property (note 24)	–	–	–	(79)	(46)	(125)
Transfer from railway construction in progress (note 26)	–	–	134	599	–	733
Other assets commissioned	–	–	14	1,129	(1,143)	–
At 31 December 2009	732	2,120	46,507	61,026	1,366	111,751
At Cost	732	–	46,507	61,026	1,366	109,631
At 31 December 2009 Valuation	–	2,120	–	–	–	2,120
Aggregate depreciation						
At 1 January 2009, as previously reported	–	–	4,612	26,781	–	31,393
Reclassification on adoption of the amendment to HKAS 17 (note 2A(iii))	165	–	–	–	–	165
At 1 January 2009, as reclassified	165	–	4,612	26,781	–	31,558
Charge for the year	13	51	399	2,177	–	2,640
Written back on disposal	–	–	(3)	(235)	–	(238)
Transfer to additional concession property (note 24)	–	–	–	(2)	–	(2)
Written back on revaluation (note 21B)	–	(51)	–	–	–	(51)
At 31 December 2009	178	–	5,008	28,721	–	33,907
Net book value at 31 December 2009	554	2,120	41,499	32,305	1,366	77,844

* Capitalisation adjustments relate to certain railway assets capitalised at the time of commissioning based on contractors' claimed values. Such assets' final values have been adjusted following finalisation of contract claims with contractors at final contract values during the year.

Depreciation charge for the year was HK$2,706 million (2009: HK$2,640 million), comprising depreciation for the year of HK$2,707 million (2009: HK$2,640 million) less HK$1 million (2009: nil) capitalisation adjustment.

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

The Company

in HK$ million	Leasehold land	Self-occupied land and buildings	Civil works	Plant and equipment	Assets under construction	Total
2010						
Cost or Valuation						
At 1 January 2010	732	2,120	46,507	60,177	1,350	110,886
Additions	–	–	–	89	1,678	1,767
Capitalisation adjustments *	–	–	(9)	(2)	–	(11)
Disposals/write-offs	–	–	(1)	(364)	(19)	(384)
Surplus on revaluation (note 21B)	–	283	–	–	–	283
Reclassification within other property, plant and equipment	–	–	12	(31)	19	–
Transfer to additional concession property (note 24)	–	–	–	(6)	(68)	(74)
Other assets commissioned	–	–	133	666	(799)	–
At 31 December 2010	732	2,403	46,642	60,529	2,161	112,467
At Cost	732	–	46,642	60,529	2,161	110,064
At 31 December 2010 Valuation	–	2,403	–	–	–	2,403
Aggregate depreciation						
At 1 January 2010	178	–	5,008	28,167	–	33,353
Charge for the year	13	58	403	2,177	–	2,651
Written back on disposal	–	–	(1)	(323)	–	(324)
Written back on revaluation (note 21B)	–	(58)	–	–	–	(58)
At 31 December 2010	191	–	5,410	30,021	–	35,622
Net book value at 31 December 2010	541	2,403	41,232	30,508	2,161	76,845

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

The Company

in HK$ million	Leasehold land	Self-occupied land and buildings	Civil works	Plant and equipment	Assets under construction	Total
2009						
Cost or Valuation						
At 1 January 2009, as previously reported	–	1,965	46,359	58,763	1,390	108,477
Reclassification on adoption of the amendment to HKAS 17 (note 2A(iii))	732	–	–	–	–	732
At 1 January 2009, as reclassified	732	1,965	46,359	58,763	1,390	109,209
Additions	–	–	–	78	1,470	1,548
Capitalisation adjustments *	–	–	–	(6)	–	(6)
Disposals/write-offs	–	–	(4)	(270)	(2)	(276)
Surplus on revaluation (note 21B)	–	155	–	–	–	155
Reclassification within other property, plant and equipment	–	–	4	(15)	11	–
Reclassification to investment properties (note 22)	–	–	–	–	(352)	(352)
Transfer to additional concession property (note 24)	–	–	–	(79)	(46)	(125)
Transfer from railway construction in progress (note 26)	–	–	134	599	–	733
Other assets commissioned	–	–	14	1,107	(1,121)	–
At 31 December 2009	732	2,120	46,507	60,177	1,350	110,886
At Cost	732	–	46,507	60,177	1,350	108,766
At 31 December 2009 Valuation	–	2,120	–	–	–	2,120
Aggregate depreciation						
At 1 January 2009, as previously reported	–	–	4,612	26,252	–	30,864
Reclassification on adoption of the amendment to HKAS 17 (note 2A(iii))	165	–	–	–	–	165
At 1 January 2009, as reclassified	165	–	4,612	26,252	–	31,029
Charge for the year	13	51	399	2,152	–	2,615
Written back on disposal	–	–	(3)	(235)	–	(238)
Transfer to additional concession property (note 24)	–	–	–	(2)	–	(2)
Written back on revaluation (note 21B)	–	(51)	–	–	–	(51)
At 31 December 2009	178	–	5,008	28,167	–	33,353
Net book value at 31 December 2009	554	2,120	41,499	32,010	1,350	77,533

* Capitalisation adjustments relate to certain railway assets capitalised at the time of commissioning based on contractors' claimed values. Such assets' final values have been adjusted following finalisation of contract claims with contractors at final contract values during the year.

Depreciation charge for the year was HK$2,651 million (2009: HK$2,615 million), comprising depreciation for the year of HK$2,652 million (2009: HK$2,615 million) less HK$1 million (2009: nil) capitalisation adjustment.

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

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

The Group and the Company

in HK$ million	2010	2009
At net book value		
– long leases	**146**	148
– medium-term leases	**395**	406
	541	554

The lease of the land on which civil works as well as plant and equipment are situated for Hong Kong railway operation was granted to the Company under a running line lease which is coterminous with the Company's franchise to operate the mass transit railway under the Operating Agreement (notes 56C, 56D and 56I).

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

B All of the Group's self-occupied land and buildings are held in Hong Kong under medium-term leases and carried at fair value. All self-occupied land and buildings were revalued at open market value on an existing use basis at 31 December 2010 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$341 million (2009: HK$206 million), which net of deferred tax provision of HK$56 million (2009: HK$34 million) (note 21B), has been recognised in other comprehensive income and accumulated in fixed assets revaluation reserve account (note 51).

The carrying amount of the self-occupied land and buildings at 31 December 2010 would have been HK$899 million (2009: HK$924 million) had the land and buildings been stated at cost less accumulated depreciation.

C Assets under construction include capital works on operating railway.

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

The gross carrying amounts of investment properties of the Group and the Company held for use in operating leases were HK$45,314 million (2009: HK$40,993 million) and HK$44,166 million (2009: HK$39,879 million) respectively. The gross carrying amounts of station kiosks of the Group and the Company held for use in operating leases were HK$551 million (2009: HK$499 million) and the related accumulated depreciation charges were HK$190 million (2009: HK$162 million).

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

	The Group		The Company	
in HK$ million	2010	2009	2010	2009
Within 1 year	**3,846**	3,265	**3,592**	3,208
After 1 year but within 5 years	**5,486**	3,651	**4,664**	3,610
Later than 5 years	**391**	54	**74**	54
	9,723	6,970	**8,330**	6,872

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

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

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

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

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

24 Service Concession Assets

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

The Group

	KCRC Rail Merger				
in HK$ million	Initial concession property	Additional concession property	Shenzhen Line 4	Stockholm Metro	Total
2010					
Cost					
At 1 January 2010	**15,226**	**1,183**	**3,539**	**88**	**20,036**
Net additions during the year	**–**	**566**	**1,757**	**–**	**2,323**
Disposal	**–**	**(5)**	**–**	**–**	**(5)**
Transfer from other property, plant and equipment (note 23)	**–**	**74**	**–**	**–**	**74**
Exchange differences	**–**	**–**	**133**	**3**	**136**
At 31 December 2010	**15,226**	**1,818**	**5,429**	**91**	**22,564**
Accumulated amortisation					
At 1 January 2010	**634**	**50**	**–**	**1**	**685**
Charge for the year	**305**	**95**	**2**	**12**	**414**
Written-off on disposal	**–**	**(3)**	**–**	**–**	**(3)**
Exchange differences	**–**	**–**	**–**	**1**	**1**
At 31 December 2010	**939**	**142**	**2**	**14**	**1,097**
Net book value at 31 December 2010	**14,287**	**1,676**	**5,427**	**77**	**21,467**

24 Service Concession Assets *(continued)*

The Group

in HK$ million	KCRC Rail Merger Initial concession property	KCRC Rail Merger Additional concession property	Shenzhen Line 4	Stockholm Metro	Total
2009					
Cost					
At 1 January 2009	15,226	572	–	–	15,798
Net additions during the year	–	486	1,889	88	2,463
Transfer from other property, plant and equipment (note 23)	–	125	–	–	125
Transfer from deferred expenditure (note 29)	–	–	1,650	–	1,650
At 31 December 2009	15,226	1,183	3,539	88	20,036
Accumulated amortisation					
At 1 January 2009	329	6	–	–	335
Charge for the year	305	42	–	1	348
Transfer from other property, plant and equipment (note 23)	–	2	–	–	2
At 31 December 2009	634	50	–	1	685
Net book value at 31 December 2009	14,592	1,133	3,539	87	19,351

The Company

in HK$ million	Initial concession property	Additional concession property	Total
2010			
Cost			
At 1 January 2010	**15,226**	**1,183**	**16,409**
Net additions during the year	**–**	**566**	**566**
Disposal	**–**	**(5)**	**(5)**
Transfer from other property, plant and equipment (note 23)	**–**	**74**	**74**
At 31 December 2010	**15,226**	**1,818**	**17,044**
Accumulated amortisation			
At 1 January 2010	**634**	**50**	**684**
Charge for the year	**305**	**95**	**400**
Written-off on disposal	**–**	**(3)**	**(3)**
At 31 December 2010	**939**	**142**	**1,081**
Net book value at 31 December 2010	**14,287**	**1,676**	**15,963**

24 Service Concession Assets *(continued)*

The Company

in HK$ million	Initial concession property	Additional concession property	Total
2009			
Cost			
At 1 January 2009	15,226	572	15,798
Net additions during the year	–	486	486
Transfer from other property, plant and equipment (note 23)	–	125	125
At 31 December 2009	15,226	1,183	16,409
Accumulated amortisation			
At 1 January 2009	329	6	335
Charge for the year	305	42	347
Transfer from other property, plant and equipment (note 23)	–	2	2
At 31 December 2009	634	50	684
Net book value at 31 December 2009	14,592	1,133	15,725

Initial concession property and additional concession property are in respect of the Group's right to access, use and operate the KCRC system pursuant to the Rail Merger (note 3). The cost of initial concession property comprises the balance of upfront payment of HK$4,250 million net of HK$326 million in respect of stores and spares acquired, the present value of the total fixed annual payments of HK$750 million per annum discounted at the Company's estimated long-term incremental borrowing rate at inception of 6.75%, the non-recoverable amount of net liabilities assumed from KCRC of HK$226 million and merger-related expenses eligible for capitalisation of HK$389 million. Additional concession property represents expenditures incurred in relation to the replacement and upgrade of the KCRC system.

Service concession assets in respect of Shenzhen Line 4 relate to the Build-Operate-Transfer project of Shenzhen Metro System Line 4 ("Shenzhen Line 4") (note 57G(i)). The cost of the service concession assets comprises the value of construction services provided in respect of the construction of Shenzhen Line 4 Phase 2 and the capitalised present value of the total annual lease payments for the operation of Shenzhen Line 4 Phase 1 of RMB132 million (HK$151 million), calculated as the total annual lease payments of RMB319 million over the concession period discounted at the estimated long-term incremental borrowing rate at inception of 5.35%. The concession property is amortised and charged to the consolidated profit and loss account over the concession period starting from operation commencement.

Service concession assets in respect of Stockholm Metro relate to the costs incurred between the announcement of the Group's winning of the tender on 20 January 2009 and the commencement of the franchise on 2 November 2009 for preparing the Group to operate Stockholm Metro. The concession property is amortised and charged to the consolidated profit and loss account over the term of the franchise.

25 Property Management Rights

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

The Group and The Company

in HK$ million	2010	2009
Cost		
At 1 January	**40**	40
Additions during the year	**–**	–
At 31 December	**40**	40
Accumulated amortisation		
At 1 January	**9**	5
Charge for the year	**–**	4
At 31 December	**9**	9
Net book value at 31 December	**31**	31

26 Railway Construction in Progress

The Group and The Company

in HK$ million	Balance at 1 January	Transferred from deferred expenditure (note 29)	Expenditure	Capitalised on commissioning (note 23)	Balance at 31 December
2010					
West Island Line Project					
Construction costs	**891**	**–**	**3,064**	**–**	**3,955**
Consultancy fees	**364**	**–**	**66**	**–**	**430**
Staff costs and other expenses	**418**	**–**	**332**	**–**	**750**
Finance costs/(interest income)	**12**	**–**	**(70)**	**–**	**(58)**
Utilisation of government funding support	**(1,685)**	**–**	**(3,392)**	**–**	**(5,077)**
Total	**–**	**–**	**–**	**–**	**–**
2009					
LOHAS Park Station Project					
Construction costs	490	–	50	(540)	–
Consultancy fees	13	–	–	(13)	–
Staff costs and other expenses	114	–	11	(125)	–
Finance costs	41	–	14	(55)	–
	658	–	75	(733)	–
West Island Line Project					
Construction costs	–	38	853	–	891
Consultancy fees	–	316	48	–	364
Staff costs and other expenses	–	318	100	–	418
Finance costs	–	2	10	–	12
Utilisation of government funding support	–	(400)	(1,285)	–	(1,685)
	–	274	(274)	–	–
Total	658	274	(199)	(733)	–

A LOHAS Park Station Project

The construction of the LOHAS Park Station is covered by the TKE Project Agreement with the Government signed on 4 November 1998. The project was completed and LOHAS Park Station was opened on 26 July 2009. Negotiation on the final accounts with various contractors is in progress.

B West Island Line ("WIL") Project

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

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

The project's target completion date is in 2014. The capital cost for the project based on the defined scope of works and this programme is estimated at HK$17,344 million. As at 31 December 2010, the Company has incurred cumulative expenditure of HK$5,077 million (2009: HK$1,685 million), which was wholly offset by the Government funding support, and has authorised outstanding commitments on contracts totalling HK$7,042 million (2009: HK$3,340 million) and estimated future project costs of HK$5,225 million in relation to the project.

27 Other Railway Construction in Progress under Entrustment by Kowloon-Canton Railway Corporation or the Government

A Kowloon Southern Link ("KSL") Project

Subsequent to the Rail Merger, the construction of the KSL remains a responsibility of KCRC who continues to fund the related construction costs. Pursuant to the KSL Project Management Agreement, the Company acts as a project management agent to KCRC in connection with the KSL under certain circumstances in return for a project management fee plus incentive payment if the construction of KSL is completed ahead of time and under budget. Expenditure incurred by the Company for the project management is charged to the consolidated profit and loss account while the project management fee is recognised as revenue in accordance with the Group's accounting policy on revenue recognition of contracts.

KSL was completed and forms an integral part of the service concession arrangement with KCRC upon service commencement on 16 August 2009. During the year ended 31 December 2010, project management fee of HK$52 million (2009: HK$317 million) and incentive payment of HK$55 million (2009: HK$55 million) were recognised as income in the consolidated profit and loss account.

B Shatin to Central Link ("SCL") Project

On 11 March 2008, the Executive Council approved further planning and design of the SCL. On 24 November 2008, the Government and the Company entered into an Entrustment Agreement for the design of and site investigation and procurement activities in relation to the SCL.

Pursuant to the Entrustment Agreement, the Company shall carry out or procure the carrying out of the design, site investigation and procurement activities and the Government shall fund directly the total cost of such activities and pay to the Company a maximum amount of HK$1.5 billion in respect of certain costs incurred by the Company, including the Company's in-house design costs and certain on-costs and preliminary costs.

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

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

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

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

28 Property Development in Progress

The Airport Railway Agreement entered into in 1995 between the Company and the Government for the construction of the Airport Railway included provisions for the granting to the Company development rights on the land over the five station sites along the Tung Chung and Airport Express Lines ("Airport Railway Property Projects").

The Tseung Kwan O Extension ("TKE") Project Agreement entered into in 1998 between the Company and the Government in respect of the construction of the Tseung Kwan O Extension provides the Company with the right to undertake property developments at four station and depot sites along the Tseung Kwan O Line ("Tseung Kwan O Extension Property Projects") under separate land grant agreements.

Pursuant to the Property Package Agreements in respect of the Rail Merger, the Company acquired property development rights on eight development sites, comprising three awarded and five not yet awarded sites along the East Rail Line, Kowloon Southern Link and Light Rail ("ERL/KSL/LR Property Projects") on the Appointed Day from KCRC (note 3).

Costs incurred by the Company for the acquisition of property development rights and preparation of the sites for development including land premium are capitalised as property development in progress and offset by payments received from developers in respect of the same development. In cases where payments received from developers exceed the related expenditure incurred by the Company, such excess is recorded as deferred income (note 28B(i)). In these cases, any subsequent expenditure incurred by the Company in respect of that development will be charged against deferred income. The remaining deferred income is to be recognised as profits of the Company at the appropriate time after taking into account the outstanding risks and obligations retained by the Company relating to each development. Until such time as deferred income is recognised as profit, it is recorded as a liability of the Company in recognition of the Company's obligations under the grant of the development rights.

A Property Development in Progress

The Group and The Company

in HK$ million	Balance at 1 January	Expenditure	Offset against payments received from developers (note 28B(i))	Transfer out on project completion	Balance at 31 December
2010					
Airport Railway Property Projects	**–**	**14**	**(14)**	**–**	**–**
Tseung Kwan O Extension Property Projects	**2,245**	**331**	**(12)**	**(1,413)**	**1,151**
ERL/KSL/LR Property Projects	**4,473**	**4,027**	**(523)**	**–**	**7,977**
	6,718	**4,372**	**(549)**	**(1,413)**	**9,128**
2009					
Airport Railway Property Projects	–	7	(2)	(5)	–
Tseung Kwan O Extension Property Projects	2,081	177	(13)	–	2,245
ERL/KSL/LR Property Projects	5,814	119	–	(1,460)	4,473
	7,895	303	(15)	(1,465)	6,718

As at 31 December 2009, Tseung Kwan O Extension Property Projects include capitalised interest of HK$769 million in connection with the Company's interest-free loan of HK$4,000 million extended to the developer of Package 2, Tseung Kwan O Area 86 property development project in 2006 (note 39). The amount was transferred out on project completion during 2010.

ERL/KSL/LR Property Projects include the acquisition cost for the property development rights on the development sites from KCRC and mandatory payments in respect of enabling works carried out by KCRC for such sites. As at 31 December 2010, outstanding mandatory payments including interest accrued amounted to HK$699 million (2009: HK$840 million). Expenditure during the year ended 31 December 2010 included HK$3,900 million of land premium in respect of the property development of Austin Station Sites C and D.

28 Property Development in Progress *(continued)*

B Deferred Income on Property Development

The Group and The Company

in HK$ million	2010	2009
Deferred income on property development comprises:		
– Payments received from developers (note 28B(i))	**568**	107
– Sharing in kind (note 28B(ii))	**–**	17
	568	124

(i) Deferred Income on Payments Received from Developers

The Group and The Company

in HK$ million	Balance at 1 January	Payments received from developers	Offset against development in progress (note 28A)	Amount recognised as profit (note 10)	Balance at 31 December
2010					
Airport Railway Property Projects	**52**	**–**	**(14)**	**–**	**38**
Tseung Kwan O Extension Property Projects	**55**	**–**	**(12)**	**–**	**43**
ERL/KSL/LR Property Projects	**–**	**1,010**	**(523)**	**–**	**487**
	107	**1,010**	**(549)**	**–**	**568**
2009					
Airport Railway Property Projects	70	–	(2)	(16)	52
Tseung Kwan O Extension Property Projects	68	–	(13)	–	55
	138	–	(15)	(16)	107

(ii) Deferred Income on Sharing in Kind

Under the development agreement of the Airport Railway Property Projects, the Company received during 2004 certain portions of the shell of a retail centre at Kowloon Station ("Elements") and its car parking spaces. Part of the property development profit is deferred as the Company has an obligation under the development agreement to complete the fitting-out works. On this basis, movements of the deferred income on this sharing in kind during the year are set out below:

The Group and The Company

in HK$ million	2010	2009
Balance as at 1 January	**17**	18
Less: Amount recognised as profit (note 10)	**(17)**	(1)
Balance as at 31 December	**–**	17

28 Property Development in Progress *(continued)*

C Stakeholding Funds

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

The Group and The Company

in HK$ million	2010	2009
Balance as at 1 January	**6,455**	4,575
Stakeholding funds received	**43,110**	39,540
Add: Interest earned thereon	**18**	17
	49,583	44,132
Disbursements during the year	**(45,875)**	(37,677)
Balance as at 31 December	**3,708**	6,455
Represented by :		
Balances in designated bank accounts as at 31 December	**3,706**	6,453
Retention receivable	**2**	2
	3,708	6,455

In addition to the above, there are certain deposit monies and sales proceeds in respect of an East Rail Line property development site, amounting to HK$1,225 million at 31 December 2010 (2009: HK$124 million) that are under the custody of the solicitors and managed by the Company on behalf of KCRC as KCRC's agent.

D West Rail Property Developments

As part of the Rail Merger, the Company was appointed to act as the agent of KCRC and certain KCRC subsidiary companies ("West Rail Subsidiaries") in the development of specified development sites along the West Rail. The Company will receive an agency fee of 0.75% of the gross sale proceeds in respect of the developments except for the Tuen Mun development on which the Company will receive 10% of the net profits accrued under the development agreement. The Company will also recover from the West Rail Subsidiaries all the costs incurred in respect of the West Rail development sites plus 16.5% on-cost, together with interest accrued thereon. During 2010, the reimbursable costs incurred by the Company including on-cost and interest accrued were HK$60 million (2009: HK$72 million).

29 Deferred Expenditure

	The Group		The Company	
in HK$ million	2010	2009	2010	2009
Balance at 1 January	**558**	1,988	**558**	338
Expenditure during the year	**521**	494	**521**	494
Transfer to service concession assets (note 24)	**–**	(1,650)	**–**	–
Transfer to railway construction in progress (note 26)	**–**	(274)	**–**	(274)
Balance at 31 December	**1,079**	558	**1,079**	558

During the year ended 31 December 2009, with the concession agreement in respect of Shenzhen Metro Line 4 signed on 18 March 2009, expenditure on Shenzhen Metro Line 4, amounting to HK$1,650 million as at 31 December 2008, was transferred to service concession assets upon signing of the concession agreement. During the same year, expenditure on the West Island Line Project, amounting to HK$274 million after netting off Government funding support of HK$400 million received prior to that date, was transferred to railway construction in progress upon signing of the project agreement. Deferred expenditure as at 31 December 2010 mainly related to design works for the proposed capital projects of the Kwun Tong Line Extension and South Island Line (East) Projects in Hong Kong.

30 Interests in Non-controlled Subsidiaries

	The Group		The Company	
in HK$ million	**2010**	2009	**2010**	2009
Unlisted shares, at cost	**–**	–	**24**	24
Share of net assets	**541**	490	**–**	–
	541	490	**24**	24

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

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

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

During the year ended 31 December 2010, the Company incurred HK$109 million (2009: HK$100 million) of expenses for the central clearing services provided by OCL. OCL incurred HK$48 million (2009: HK$24 million) of expenses for the load agent and Octopus card issuance and refund services, computer equipment and relating services, staff secondment, project administration services as well as warehouse storage space provided by the Company. During the year, OHL distributed dividends of HK$75 million (2009: HK$40 million) to the Company.

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

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

Consolidated Profit and Loss Account

Year ended 31 December in HK$ million	2010 (Audited)	2009 (Audited)
Turnover	**662**	629
Other operating income	**6**	5
	668	634
Staff costs	**(119)**	(120)
Load agent fees and bank charges for add value services	**(80)**	(72)
Other expenses	**(222)**	(159)
Operating profit before depreciation	**247**	283
Depreciation	**(43)**	(62)
Operating profit before interest and finance charges	**204**	221
Net interest income	**56**	66
Share of loss from a jointly controlled entity	**(2)**	–
Profit before taxation	**258**	287
Income tax	**(39)**	(28)
Profit for the year	**219**	259
Group's share of profit before taxation (note 15)	**148**	165
Group's share of income tax (note 15)	**(22)**	(16)

Consolidated Balance Sheet

at 31 December in HK$ million	2010 (Audited)	2009 (Audited)
Assets		
Fixed assets	**189**	159
Investments	**2,195**	2,427
Other assets	**277**	209
Cash at banks and on hand	**671**	245
	3,332	3,040
Liabilities		
Card floats and card deposits due to cardholders	**(2,004)**	(1,834)
Amounts due to related parties	**(24)**	(24)
Other liabilities	**(362)**	(329)
	(2,390)	(2,187)
Net assets	**942**	853
Equity		
Share capital	**42**	42
Retained profits	**900**	811
	942	853
Group's share of net assets	**541**	490

31 Investments in Subsidiaries

The Company

in HK$ million	2010	2009
Unlisted shares, at cost	**1,256**	1,222
Less: Impairment losses	**–**	(3)
	1,256	1,219

Investments in subsidiaries include HK$24 million (2009: HK$24 million) in respect of investments in non-controlled subsidiaries, the relevant details of which are disclosed in note 30. The following list contains details of controlled subsidiaries as defined under note 2C as at 31 December 2010, which have been consolidated into the Group's accounts.

		Proportion of ownership interest				
Name of company	Issued and paid up ordinary/ registered share capital	Group's effective interest	Held by the Company	Held by subsidiary	Place of incorporation and operation	Principal activities
Subsidiaries held throughout 2010						
Glory Goal Limited	HK$10,000	100%	100%	–	Hong Kong	Investment holding
Hanford Garden Property Management Company Limited	HK$10,000	100%	100%	–	Hong Kong	Property management
MTR (Estates Management) Limited	HK$1,000	100%	100%	–	Hong Kong	Investment holding and property management
MTR (Shanghai Project Management) Limited	HK$1,000	100%	100%	–	Hong Kong	Railway consultancy services, property investment and development
MTR Beijing Line 4 Investment Company Limited	HK$1	100%	100%	–	Hong Kong	Investment holding
MTR China Commercial Management No. 1 Holdings Limited	HK$1,000	100%	100%	–	Hong Kong	Investment holding
MTR China Consultancy Company Limited	HK$1,000	100%	100%	–	Hong Kong	Railway consultancy services
MTR China Property Limited	HK$1,000	100%	100%	–	Hong Kong	Property management
MTR Engineering Services Limited	HK$1,000	100%	100%	–	Hong Kong	Engineering services
MTR Hangzhou Line 1 Investment Company Limited	HK$1,000	100%	100%	–	Hong Kong	Investment holding
MTR Information Solutions Company Limited	HK$1,000	100%	100%	–	Hong Kong	License MTR software to MTR's subsidiaries and associates
MTR Property Agency Co. Limited	HK$2	100%	100%	–	Hong Kong	Property agency
MTR Rail Transport Training (International) Company Limited	HK$2,800,000	100%	100%	–	Hong Kong	Provide rail transport training in Mainland China
MTR Shenyang Holdings Limited	HK$1,000	100%	100%	–	Hong Kong	Investment holding
MTR Shenyang Investment Holdings Limited	HK$1	100%	100%	–	Hong Kong	Investment holding
MTR Shenyang Property No. 1 Limited	HK$1	100%	–	100%	Hong Kong	Property development, investment, management and other property related businesses

31 Investments in Subsidiaries *(continued)*

Name of company	Issued and paid up ordinary/ registered share capital	Proportion of ownership interest: Group's effective interest	Held by the Company	Held by subsidiary	Place of incorporation and operation	Principal activities
MTR Shenzhen Investment Holding Limited	HK$400,000	100%	100%	–	Hong Kong	Investment holding
MTR Telecommunication Company Limited	HK$100,000,000	100%	100%	–	Hong Kong	Mobile telecommunication network services
MTR Travel Limited	HK$2,500,000	100%	100%	–	Hong Kong	Travel services
Ngong Ping 360 Limited	HK$2	100%	100%	–	Hong Kong	Operate the Tung Chung to Ngong Ping cable car system and Theme Village in Ngong Ping
Pierhead Garden Management Company Limited	HK$50,000	100%	100%	–	Hong Kong	Property management
Rail Sourcing Solutions (International) Limited	HK$2	100%	100%	–	Hong Kong	Global railway supply and sourcing services
Royal Ascot Management Company Limited	HK$50,000	100%	100%	–	Hong Kong	Property management
Sun Tuen Mun Centre Management Company Limited	HK$50,000	100%	100%	–	Hong Kong	Property management
TraxComm Limited	HK$15,000,000	100%	100%	–	Hong Kong	Fixed telecommunication network services
V-Connect Limited	HK$1,000	100%	100%	–	Hong Kong	Mobile telecommunication network services
360 Holidays Limited	HK$500,000	100%	–	100%	Hong Kong	Guided tour services
Metro Trains Melbourne Pty. Ltd. *	AUD16,250,000	60% on ordinary shares; 30% on Class A shares	60% on ordinary shares; 30% on Class A shares	–	Australia	Railway operations and maintenance
Fasttrack Insurance Ltd.	HK$77,500,000	100%	100%	–	Bermuda	Insurance underwriting
Candiman Limited *	US$1	100%	100%	–	British Virgin Islands	Investment holding
MTR Corporation (C.I.) Limited	US$1,000	100%	100%	–	Cayman Islands/ Hong Kong	Finance
MTR Finance Lease (001) Limited	US$1	100%	100%	–	Cayman Islands/ Hong Kong	Finance
MTR (Macau) Property Management Company Limited	MOP25,000	100%	–	100%	Macau	Property management, consultancy and other property management related businesses
MTR Stockholm AB	SEK40,000,000	100%	–	100%	Sweden	Railway operations and maintenance
Chongqing Premier Property Management Company Limited *	US$150,000	70%	–	70%	The People's Republic of China	Property management

31 Investments in Subsidiaries *(continued)*

Name of company	Issued and paid up ordinary/ registered share capital	Proportion of ownership interest: Group's effective interest	Held by the Company	Held by subsidiary	Place of incorporation and operation	Principal activities
MTR (Beijing) Commercial Facilities Management Company Limited	HK$93,000,000	100%	–	100%	The People's Republic of China	Property leasing and management
MTR (Beijing) Property Services Company Limited *	RMB3,000,000	100%	100%	–	The People's Republic of China	Property management
MTR Consultancy (Beijing) Co. Ltd. (Incorporated)	HK$1,000,000	100%	100%	–	The People's Republic of China	Railway consultancy services, marketing and promotion
MTR Consulting (Shenzhen) Co. Ltd. (Incorporated)	HK$1,000,000	100%	100%	–	The People's Republic of China	Railway consultancy services
MTR Corporation (Shenzhen) Limited (Incorporated)	HK$2,636,000,000	100%	–	100%	The People's Republic of China	Railway construction, operation and management
MTR Corporation (Shenzhen) Training Centre * (Incorporated)	RMB2,000,000	100%	–	100%	The People's Republic of China	Provide rail transport training
Shanghai Hong Kong Metro Construction Management Co. Ltd. (Incorporated)	HK$15,000,000	60%	–	60%	The People's Republic of China	Railway construction management and development
MTR Corporation (Silverlink) Limited	GBP1	100%	–	100%	United Kingdom	Investment holding
MTR Corporation (UK) Limited	GBP29	100%	100%	–	United Kingdom	Investment holding
Rail Sourcing Solutions (UK) Limited *	GBP1	100%	–	100%	United Kingdom	Railway supply and sourcing services
<u>Subsidiaries established during 2010</u>						
Extensive Growth Limited	HK$1	100%	100%	–	Hong Kong	Investment holding
MTR Property (Beijing) No.1 Company Limited	HK$1	100%	–	100%	Hong Kong	Property development, investment, management and other property related businesses
MTR Property (Shenzhen) Company Limited	HK$1	100%	100%	–	Hong Kong	Property development, investment and management
MTR Commercial Management (Beijing) Company Limited *	HK$120,000	100%	–	100%	The People's Republic of China	Business management, business consultancy, commercial facilities strategy and consultancy services

* Subsidiaries not audited by KPMG

During the year ended 31 December 2010, Rail Sourcing Solutions (UK) Limited was wound up.

32 Interests in Associates

The Group

in HK$ million	**2010**	2009
Share of net assets	**836**	823

The Group and the Company had interests in the following associates as at 31 December 2010:

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

* Companies not audited by KPMG

During the year ended 31 December 2010, Tunnelbanan Teknik Stockholm AB provided rolling stock maintenance and other supporting services to MTR Stockholm AB at an amount of SEK511 million (HK$550 million) (2009: SEK104 million or HK$113 million). MTR Stockholm AB leased depots, depot equipment and provided other supporting services to Tunnelbanan Teknik Stockholm AB at a total amount of SEK114 million (HK$122 million) (2009: SEK23 million or HK$24 million).

During the year, the Company provided staff secondment, information technology and other support services to Beijing MTR Corporation Limited at a total amount of HK$32 million (2009: HK$48 million) and staff secondment and consultancy service to LOROL at an amount of HK$1 million (2009: HK$1 million). During the year ended 31 December 2009, the Company also provided staff secondment to Shenyang MTR Corporation Limited at an amount of HK$14 million.

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

in HK$ million	**2010**	2009
Non-current assets	**2,435**	2,771
Current assets	**747**	434
Non-current liabilities	**(972)**	(83)
Current liabilities	**(1,374)**	(2,299)
Net assets	**836**	823
Income	**1,612**	2,115
Expenses	**(1,590)**	(2,096)
Profit before taxation	**22**	19
Income tax	**(9)**	(8)
Net profit for the year	**13**	11

33 Investments in Securities

Investments in securities represent debt securities held by the overseas insurance underwriting subsidiary and bank medium term notes held by the Company comprising:

The Group

in HK$ million	**2010**	2009
Held-to-maturity securities, at amortised cost		
– maturing within 1 year	**1,000**	–
– maturing after 1 year	**2,627**	–
	3,627	–
Trading securities listed overseas, at fair value (Level 1, see note 36 for definition)		
– maturing within 1 year	**67**	107
– maturing after 1 year	**218**	120
	285	227
	3,912	227

The Company

in HK$ million	**2010**	2009
Held-to-maturity securities, at amortised cost		
– maturing within 1 year	**1,000**	–
– maturing after 1 year	**2,627**	–
	3,627	–

34 Staff Housing Loans

The Group and The Company

in HK$ million	2010	2009
Balance at 1 January	**7**	10
Redemption	**(1)**	(1)
Repayment	**(2)**	(2)
Balance at 31 December	**4**	7

The Group and The Company

in HK$ million	2010	2009
Amounts receivable:		
– within 1 year	**1**	2
– after 1 year	**3**	5
	4	7

The MTR Staff Housing Loan Scheme, a Company financed scheme, was introduced in 1997 to replace, on a phased basis, the previous arrangements whereby interest subsidies were paid by the Company to eligible employees. All housing loans granted to employees carry interest either at the prevailing Best Lending Rate less 1.75% per annum or at the Company's Average Cost of Borrowings plus 0.75% per annum, and are secured by mortgages over the relevant properties. Since December 2001, the scheme has been closed for application and eligible employees have been provided with an option to switch the property mortgage to a specified commercial bank based on agreed terms.

The Company considers that the nominal value of housing loans is not significantly different from their fair values.

35 Properties Held for Sale

The Group and The Company

in HK$ million	2010	2009
Properties held for sale		
– at cost	**1,829**	3,676
– at net realisable value	**107**	107
	1,936	3,783

Properties held for sale at 31 December 2010 comprised mainly residential units and car parking spaces at The Palazzo at Fo Tan Station along the East Rail Line and Lake Silver at Wu Kai Sha Station along the Ma On Shan Line. They represent either properties received by the Company as sharing in kind or as part of the profit distribution upon completion of the development. The properties are stated on the balance sheet at the lower of cost, which is deemed to be their fair value upon initial recognition as determined by reference to an independent open market valuation at the date of receipt (notes 2K(iv) and (v)), and their net realisable value at the balance sheet date. Net realisable value represents the estimated selling price less costs to be incurred in selling the properties. The net realisable values as at 31 December 2010 and 2009 were determined by reference to an open market valuation of the properties as at those dates, undertaken by an independent firm of surveyors, Jones Lang LaSalle Limited, who have among their staff, Members of the Hong Kong Institute of Surveyors.

Properties held for sale at net realisable value are stated net of provision of HK$12 million (2009: HK$12 million), made in order to state these properties at the lower of their cost and estimated net realisable value.

36 Derivative Financial Assets and Liabilities

A Fair Value

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

The Group and The Company

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

36 Derivative Financial Assets and Liabilities *(continued)*

A Fair Value *(continued)*

The Group and The Company

in HK$ million	Notional amount	Fair value	Level*	Contractual undiscounted cash flow maturing in Less than 1 year	1-2 years	2-5 years	Over 5 years	Total
2009								
Derivative Financial Assets								
Gross settled:								
Foreign exchange forwards								
– cash flow hedges :	756	32	2					
– inflow				639	92	58	–	789
– outflow				(617)	(85)	(54)	–	(756)
– not qualified for hedge accounting :	5	–	2					
– inflow				4	1	–	–	5
– outflow				(4)	(1)	–	–	(5)
Cross currency swaps								
– fair value hedges :	1,275	59	2					
– inflow				64	50	841	450	1,405
– outflow				(30)	(25)	(828)	(465)	(1,348)
Net settled:								
Interest rate swaps								
– fair value hedges	3,780	256	2	128	68	103	2	301
– cash flow hedges	350	23	2	(7)	(3)	13	29	32
	6,166	370		177	97	133	16	423
Derivative Financial Liabilities								
Gross settled:								
Foreign exchange forwards								
– cash flow hedges :	67	1	2					
– inflow				51	11	4	–	66
– outflow				(52)	(11)	(4)	–	(67)
– not qualified for hedge accounting :	76	2	2					
– inflow				65	9	–	–	74
– outflow				(67)	(9)	–	–	(76)
Cross currency swaps								
– fair value hedges :	9,342	97	2					
– inflow				4,664	29	4,728	–	9,421
– outflow				(4,700)	(39)	(4,812)	–	(9,551)
Net settled:								
Interest rate swaps								
– fair value hedges	500	15	2	5	(1)	(18)	–	(14)
– cash flow hedges	2,242	122	2	(81)	(30)	(36)	–	(147)
	12,227	237		(115)	(41)	(138)	–	(294)
Total	18,393							

* The levels are defined in HKFRS 7 as follows:

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

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

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

36 Derivative Financial Assets and Liabilities *(continued)*

A Fair Value *(continued)*

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

The Group's derivative financial instruments consist predominantly of interest rate and cross currency swaps, and the relevant interest rate swap curves as of 31 December 2010 and 2009 were used to discount the cash flows of financial instruments. For Hong Kong dollars, interest rates used ranged from 0.045% to 3.407% (2009: 0.080% to 3.713%), U.S dollars from 0.392% to 3.509% (2009: 0.193% to 4.703%) and Euro from 0.379% to 3.393% (2009: 0.236% to 4.247%).

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

B Financial Risks

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

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

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

(i) Liquidity Risk

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

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

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

The Group

	2010				2009			
in HK$ million	Capital market instruments	Bank loans and overdrafts	Others	Total	Capital market instruments	Bank loans and overdrafts	Others	Total
Loans and other obligations								
Amounts repayable beyond 5 years	**3,218**	**2,315**	**598**	**6,131**	3,851	2,006	557	6,414
Amounts repayable within a period of between 2 and 5 years	**8,717**	**1,318**	**1**	**10,036**	8,573	2,532	–	11,105
Amounts repayable within a period of between 1 and 2 years	**603**	**6,569**	**1**	**7,173**	1,012	140	–	1,152
Amounts repayable within 1 year	**1,013**	**480**	**1**	**1,494**	6,622	3,195	–	9,817
	13,551	**10,682**	**601**	**24,834**	20,058	7,873	557	28,488

36 Derivative Financial Assets and Liabilities *(continued)*

B Financial Risks *(continued)*

The Company

	2010				2009			
in HK$ million	Capital market instruments	Bank loans and overdrafts	Others	Total	Capital market instruments	Bank loans and overdrafts	Others	Total
Loans and other obligations								
Amounts repayable beyond 5 years	**577**	**–**	**598**	**1,175**	593	134	557	1,284
Amounts repayable within a period of between 2 and 5 years	**117**	**531**	**–**	**648**	115	1,835	–	1,950
Amounts repayable within a period of between 1 and 2 years	**39**	**6,457**	**–**	**6,496**	39	60	–	99
Amounts repayable within 1 year	**39**	**376**	**–**	**415**	5,031	3,118	–	8,149
	772	**7,364**	**598**	**8,734**	5,778	5,147	557	11,482

Others represent obligations under lease out/lease back transaction (note 23E).

(ii) Interest Rate Risk

The Group's interest rate risk arises principally from its borrowing activities. Borrowings based on fixed and floating rates expose the Group to fair value and cash flow interest rate risk respectively due to fluctuations in market interest rates. The Group manages and controls its interest rate risk exposure by maintaining a level of fixed rate debt between 40% and 70% of total debt outstanding as specified by the Model. Should the actual fixed rate debt level deviate substantially from the Model, derivative financial instruments such as interest rate swaps would be procured to align the fixed and floating mix with the Model. As at 31 December 2010, 45% of the Group's total debt outstanding was denominated either in or converted to fixed interest rate after taking into account outstanding cross currency and interest rate swaps.

The Group's exposure due to its floating rate borrowings is offset by the floating rate interest income it earns from its cash balances, bank deposits and other investment instruments. As at 31 December 2010, the Group had total cash balances and bank deposits of HK$11,948 million from which it derived floating rate interest income, compared with total floating rate borrowings of HK$11,237 million.

As at 31 December 2010, it is estimated that a 100 basis points increase/50 basis points decrease in interest rates, with all other variables held constant, would increase/decrease the Group's profit after tax and retained profits by approximately HK$85/HK$24 million. Other components of consolidated equity would increase/decrease by approximately HK$49/HK$26 million.

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

In 2009, a similar analysis was performed based on the assumption of a general increase/decrease of 100/50 basis points in interest rates, which would decrease/decrease the Group's profit after tax and retained profits by approximately HK$4/HK$5 million. Other components of consolidated equity would increase/decrease by approximately HK$67/HK$35 million.

(iii) Foreign Exchange Risk

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

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

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

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

36 Derivative Financial Assets and Liabilities *(continued)*

B Financial Risks *(continued)*

(iv) Credit Risk

Credit risk refers to the risk that a counterparty will be unable to pay amounts in full when due. For the Group, this arises mainly from the deposits it maintains and the derivative financial instruments that it has entered into with various banks and counterparties as well as from the Defeasance Securities it procured under the lease out/lease back transaction (note 23E). The Group limits its exposure to credit risk by placing deposits and transacting derivative financial instruments only with financial institutions with acceptable investment grade credit ratings or guarantee, and diversifying its exposure to various counterparties.

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

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

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

In addition, the Company also manages and controls its exposure to credit risks in respect of receivables and loan to a property developer as stated in notes 38 and 39 respectively.

37 Stores and Spares

	The Group		The Company	
in HK$ million	**2010**	2009	**2010**	2009
Stores and spares expected to be consumed:				
– within 1 year	**643**	629	**519**	547
– after 1 year	**426**	417	**363**	333
	1,069	1,046	**882**	880
Less: Provision for obsolete stock	**(8)**	(6)	**(8)**	(6)
	1,061	1,040	**874**	874

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

38 Debtors, Deposits and Payments in Advance

	The Group		The Company	
in HK$ million	**2010**	2009	**2010**	2009
Debtors, deposits and payments in advance relate to:				
– Property development projects	**636**	805	**636**	805
– Railway operations and others	**2,421**	1,623	**1,139**	1,134
	3,057	2,428	**1,775**	1,939

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

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

(i) The majority of Hong Kong fare revenue 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 Hong Kong fare revenue collected through pre-sale agents is due within 21 days.

(ii) Franchise revenue in Shenzhen is collected either through Shenzhen Tong Cards with daily settlement on the next working day or in cash for other ticket types. Franchise revenue in Melbourne is collected either weekly or monthly depending on its nature. The majority of the franchise revenue in Stockholm is collected in the transaction month with the remainder being collected in the following month.

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

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

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

(vi) 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.

The ageing of debtors included above is analysed as follows:

	The Group		The Company	
in HK$ million	**2010**	2009	**2010**	2009
Amounts not yet due	**1,900**	1,414	**1,088**	1,117
Overdue by 30 days	**157**	209	**61**	200
Overdue by 60 days	**27**	11	**21**	9
Overdue by 90 days	**8**	3	**3**	1
Overdue by more than 90 days	**11**	13	**6**	7
Total debtors	**2,103**	1,650	**1,179**	1,334
Deposits and payments in advance	**785**	600	**427**	427
Prepaid pension costs	**169**	178	**169**	178
	3,057	2,428	**1,775**	1,939

Amounts not yet due includes HK$634 million (2009: HK$805 million) in respect of property development which are due according to the terms of the relevant development agreements or sale and purchase agreements, receivable from certain stakeholding funds (note 28C) awaiting finalisation of the respective development accounts as well as other receivables on miscellaneous recoverable expenses.

As at 31 December 2010, all debtors, deposits and payments in advance were expected to be recovered within one year except for HK$153 million (2009: HK$198 million) included in the amounts relating to deposits and receivables in respect of railway operations and others, which were expected to be recovered between one to three years. The nominal values less impairment losses for bad and doubtful debts are not discounted as it is considered that the effect of discounting would not be significant.

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

	The Group		The Company	
	2010	2009	**2010**	2009
Dirhams (in million)	**–**	6	**–**	6
New Taiwan dollars (in million)	**2**	3	**2**	3
Pound sterling (in million)	**–**	1	**–**	1
United States dollars (in million)	**9**	11	**8**	10

39 Loan to a Property Developer

The Group and The Company

in HK$ million	**2010** Nominal amount	**2010** Carrying amount	2009 Nominal amount	2009 Carrying amount
Interest-free loan to a property developer	**2,000**	**1,975**	2,000	1,916

The loan was provided to the developer of Package 2, Tseung Kwan O Area 86 (LOHAS Park) property development project under the terms of the development agreement. The loan is interest-free and guaranteed by the developer's ultimate holding company (the "Guarantor") and is repayable on completion of the respective phases of the project. The Company monitors the exposure to credit risk in respect of the loan by regularly assessing the credit quality of the Guarantor, taking into account the Guarantor's current financial position, the Company's past experience on transactions with the Guarantor and other relevant factors.

40 Amounts Due from the Government and Other Related Parties

	The Group		**The Company**	
in HK$ million	**2010**	2009	**2010**	2009
Amounts due from:				
– the Government	**156**	12,432	**156**	12,432
– KCRC	**25**	165	**25**	165
– non-controlled subsidiaries	**17**	15	**17**	15
– associates	**132**	176	**71**	94
– other subsidiaries of the Company (net of impairment losses)	**–**	–	**4,096**	3,249
	330	12,788	**4,365**	15,955

As at 31 December 2010, the amount due from the Government relates to outstanding receivables and retention as well as provision for contract claims recoverable from the Government in connection with infrastructure works entrusted to the Company, reimbursable costs incurred by the Company for the West Rail property developments (note 28D) and outstanding receivables in respect of the costs recoverable from the Government for the Shatin to Central Link and Express Rail Link Projects (notes 27B and 27C). Other than these items, the amount due from the Government as at 31 December 2009 also included Government funding support receivable for the construction of the WIL Project of HK$12,252 million, which was received in March 2010 (note 26B).

The amount due from KCRC relates to payments to the Company in respect of the Outsourcing Agreement and KSL Project Management Agreement, costs on certain capital works recoverable from KCRC in accordance with the Merger Framework Agreement, as well as certain reimbursable expenditures of KCRC settled by the Company on KCRC's behalf.

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

The amounts due from associates of the Group as at 31 December 2010 include the outstanding balances of loans to London Overground Rail Operations Ltd, amounting to HK$12 million (GBP1 million) (2009: HK$13 million or GBP 1 million) (note 57H(i)) and to Tunnelbanan Teknik Stockholm AB, amounting to HK$75 million (SEK65 million) (2009: HK$71 million or SEK65 million) (note 57H(ii)).

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

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

41 Cash, Bank Balances and Deposits

	The Group		The Company	
in HK$ million	**2010**	2009	**2010**	2009
Deposits with banks and other financial institutions	**12,337**	5,493	**12,065**	5,455
Cash at banks and on hand	**997**	1,622	**208**	167
Cash, bank balances and deposits	**13,334**	7,115	**12,273**	5,622
Less: Bank deposits with more than three months to maturity when placed	**(9,610)**	–	**(9,355)**	–
Less: Bank overdrafts (note 42A)	**(16)**	(21)	**(16)**	(21)
Cash and cash equivalents in the cash flow statement	**3,708**	7,094	**2,902**	5,601

During the year, the Group recognised deferred income and received properties in kind for long term investment purpose in respect of property development of HK$59 million (2009: HK$89 million), which did not involve movements of cash or cash equivalents.

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

	The Group		The Company	
	2010	2009	**2010**	2009
Australian dollars (in million)	**11**	–	**11**	–
Euros (in million)	**5**	4	**5**	4
Japanese Yen (in million)	**100**	369	**100**	369
New Taiwan dollars (in million)	**10**	12	**10**	12
Pound sterling (in million)	**–**	3	**–**	3
Swedish krona (in million)	**2**	–	**2**	–
United States dollars (in million)	**679**	270	**676**	265

42 Loans and Other Obligations

A By Type

The Group

	2010			2009		
in HK$ million	Carrying amount	Fair value	Repayable amount	Carrying amount	Fair value	Repayable amount
Capital market instruments						
Listed or publicly traded:						
US dollar Global notes due 2010	**–**	**–**	**–**	4,656	4,927	4,679
Debt issuance programme (Eurobond due 2014)	**4,759**	**5,144**	**4,663**	4,692	5,045	4,663
	4,759	**5,144**	**4,663**	9,348	9,972	9,342
Unlisted:						
Debt issuance programme notes due 2010 to 2020	**6,679**	**7,202**	**6,447**	7,719	8,178	7,547
	6,679	**7,202**	**6,447**	7,719	8,178	7,547
Total capital market instruments	**11,438**	**12,346**	**11,110**	17,067	18,150	16,889
Bank loans	**8,971**	**8,973**	**8,972**	6,443	6,438	6,428
Others	**332**	**370**	**332**	312	321	312
Loans and others	**20,741**	**21,689**	**20,414**	23,822	24,909	23,629
Bank overdrafts	**16**	**16**	**16**	21	21	21
Short-term loans	**300**	**300**	**300**	25	25	25
Total	**21,057**	**22,005**	**20,730**	23,868	24,955	23,675

42 Loans and Other Obligations *(continued)*

A By Type *(continued)*

The Company

in HK$ million	2010 Carrying amount	2010 Fair value	2010 Repayable amount	2009 Carrying amount	2009 Fair value	2009 Repayable amount
Capital market instruments						
Listed or publicly traded:						
US dollar Global notes due 2010	–	–	–	4,656	4,927	4,679
	–	–	–	4,656	4,927	4,679
Unlisted:						
Debt issuance programme notes due 2018	**457**	**646**	**466**	447	628	479
	457	**646**	**466**	447	628	479
Total capital market instruments	**457**	**646**	**466**	5,103	5,555	5,158
Bank loans	**6,915**	**6,918**	**6,916**	4,966	4,961	4,951
Others	**328**	**366**	**328**	312	321	312
Loans and others	**7,700**	**7,930**	**7,710**	10,381	10,837	10,421
Bank overdrafts	**16**	**16**	**16**	21	21	21
Short-term loans	**300**	**300**	**300**	25	25	25
Total	**8,016**	**8,246**	**8,026**	10,427	10,883	10,467

Others include non-defeased obligations under lease out/lease back transaction (note 23E).

As at 31 December 2010, the Group had available undrawn committed bank loan facilities amounting to HK$2,294 million (2009: HK$10,513 million). In addition, the Group had a number of uncommitted facilities with undrawn amounts totalling HK$15,028 million (2009: HK$14,155 million), comprising a debt issuance programme and short-term bank loan facilities.

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

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

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

The Group

	Before hedging activities 2010	Before hedging activities 2009	After hedging activities 2010	After hedging activities 2009
Euros (in million)	**1**	3	**–**	–
Pound sterling (in million)	**–**	2	**–**	2
United States dollars (in million)	**761**	1,363	**1**	3

The Company

	Before hedging activities 2010	Before hedging activities 2009	After hedging activities 2010	After hedging activities 2009
Euros (in million)	**1**	3	**–**	–
Pound sterling (in million)	**–**	2	**–**	2
United States dollars (in million)	**61**	663	**1**	3

42 Loans and Other Obligations *(continued)*

B By Repayment Terms

The Group

in HK$ million	2010 Capital market instruments	2010 Bank loans and overdrafts	2010 Others	2010 Total	2009 Capital market instruments	2009 Bank loans and overdrafts	2009 Others	2009 Total
Long-term loans and others								
Amounts repayable beyond 5 years	**2,715**	**1,471**	**328**	**4,514**	3,215	1,155	312	4,682
Amounts repayable within a period of between 2 and 5 years	**7,793**	**1,084**	**2**	**8,879**	7,395	2,222	–	9,617
Amounts repayable within a period of between 1 and 2 years	**102**	**6,400**	**1**	**6,503**	500	16	–	516
Amounts repayable within 1 year	**500**	**17**	**1**	**518**	5,779	3,035	–	8,814
	11,110	**8,972**	**332**	**20,414**	16,889	6,428	312	23,629
Bank overdrafts	**–**	**16**	**–**	**16**	–	21	–	21
Short-term loans	**–**	**300**	**–**	**300**	–	25	–	25
	11,110	**9,288**	**332**	**20,730**	16,889	6,474	312	23,675
Less: Unamortised discount/premium/ finance charges outstanding	**(38)**	**(5)**	**–**	**(43)**	(57)	(1)	–	(58)
Adjustment due to fair value change of financial instruments	**366**	**4**	**–**	**370**	235	16	–	251
Total carrying amount of debt	**11,438**	**9,287**	**332**	**21,057**	17,067	6,489	312	23,868

The Company

in HK$ million	2010 Capital market instruments	2010 Bank loans and overdrafts	2010 Others	2010 Total	2009 Capital market instruments	2009 Bank loans and overdrafts	2009 Others	2009 Total
Long-term loans and others								
Amounts repayable beyond 5 years	**465**	**–**	**328**	**793**	465	132	312	909
Amounts repayable within a period of between 2 and 5 years	**1**	**511**	**–**	**512**	14	1,768	–	1,782
Amounts repayable within a period of between 1 and 2 years	**–**	**6,389**	**–**	**6,389**	–	16	–	16
Amounts repayable within 1 year	**–**	**16**	**–**	**16**	4,679	3,035	–	7,714
	466	**6,916**	**328**	**7,710**	5,158	4,951	312	10,421
Bank overdrafts	**–**	**16**	**–**	**16**	–	21	–	21
Short-term loans	**–**	**300**	**–**	**300**	–	25	–	25
	466	**7,232**	**328**	**8,026**	5,158	4,997	312	10,467
Less: Unamortised discount/premium/ finance charges outstanding	**(5)**	**(5)**	**–**	**(10)**	(13)	(1)	–	(14)
Adjustment due to fair value change of financial instruments	**(4)**	**4**	**–**	**–**	(42)	16	–	(26)
Total carrying amount of debt	**457**	**7,231**	**328**	**8,016**	5,103	5,012	312	10,427

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

42 Loans and Other Obligations *(continued)*

C Bonds and Notes Issued and Redeemed

Bonds and notes issued during the year ended 31 December 2010 and 2009 comprise:

The Group

in HK$ million	2010		2009	
	Principal amount	Net consideration received	Principal amount	Net consideration received
Debt issuance programme notes	–	–	500	500

The above 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. The net proceeds received from the issues were on lent to the Company for general working capital, refinancing or other corporate purposes.

During the year ended 31 December 2010, the Group redeemed HK$1,100 million (2009: HK$1,300 million) of its unlisted debt securities and US$600 million (2009: US$750 million) of its listed debt securities.

D Guarantees and Pledges

(i) There were no guarantees given by the Government in respect of the loan facilities of the Group as at 31 December 2010 and 2009.

(ii) As at 31 December 2010, certain assets held by MTR Corporation (Shenzhen) Limited, an indirect wholly owned subsidiary of the Company in the Mainland of China, were pledged as security for a RMB4,000 million (2009: RMB4,000 million) bank loan facility granted to it.

(iii) As at 31 December 2010, certain assets held by Metro Trains Melbourne Pty. Ltd., a 60% owned subsidiary of the Company in Australia, were pledged as security for an AUD13 million (2009: nil) bank loan facility granted to it.

Apart from the above, none of the other assets of the Group was charged or subject to any encumbrance as at 31 December 2010.

43 Creditors and Accrued Charges

	The Group		The Company	
in HK$ million	**2010**	2009	**2010**	2009
Creditors and accrued charges				
– Airport Railway Project	**57**	63	**57**	63
– Tseung Kwan O Extension Project	**4**	10	**4**	10
– LOHAS Park Station Project	**5**	19	**5**	19
– WIL Project	**512**	303	**512**	303
– Property projects and management	**1,887**	4,849	**1,798**	4,760
– Hong Kong railway operations and others	**3,738**	2,797	**3,342**	2,444
– Shenzhen Metro Line 4 Project	**535**	715	**–**	–
– Railway subsidiaries outside of Hong Kong	**1,163**	759	**–**	–
Gross amount due to customers for contract work	**15**	15	**15**	15
Government funding support on WIL Project un-utilised	**7,575**	10,967	**7,575**	10,967
	15,491	20,497	**13,308**	18,581

As at 31 December 2010, creditors and accrued charges mainly related to capital projects to be settled upon certification of work in progress and swap interest payable. The Group has no significant balances of trade creditors resulting from its provision of transportation services.

As at 31 December 2010, the aggregate amount of contract costs incurred plus recognised profits less recognised losses included in the gross amount due to customers for contract works was HK$294 million (2009: HK$290 million).

The gross amount due to customers for contract work that is expected to be settled after more than one year as at 31 December 2010 was nil (2009: HK$15 million).

43 Creditors and Accrued Charges *(continued)*

The analysis of creditors included above by due dates is as follows:

	The Group		The Company	
in HK$ million	**2010**	2009	**2010**	2009
Due within 30 days or on demand	**2,331**	5,005	**1,025**	3,692
Due after 30 days but within 60 days	**1,603**	1,082	**1,077**	771
Due after 60 days but within 90 days	**341**	280	**331**	268
Due after 90 days	**1,725**	1,439	**1,530**	1,302
	6,000	7,806	**3,963**	6,033
Rental and other refundable deposits	**1,517**	1,437	**1,472**	1,323
Accrued employee benefits	**399**	287	**298**	258
Government funding support	**7,575**	10,967	**7,575**	10,967
Total	**15,491**	20,497	**13,308**	18,581

Creditors and accrued charges in respect of the capital projects and other construction works include provisions for claims on completed contracts, which were capitalised as part of the related assets. Most of these claims have been resolved and it is anticipated that, subject to unforeseen circumstances, the remaining amount required to be paid will be sufficiently covered by the above mentioned provisions of the respective projects. The carrying amounts of such claim provisions and their movements are not separately disclosed in view of their commercial sensitivity.

Creditors and accrued charges were expected to be settled within one year except for HK$963 million (2009: HK$828 million) included in amounts relating to railway operations and others, which were expected to be settled after one year. The amounts due after one year are mainly rental deposits received from shop and station kiosk tenants and advance income received from telecommunication services operators, majority of which are due to be repaid within three years. The Group considers the effect of discounting these deposits would be immaterial.

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

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

	The Group		The Company	
	2010	2009	**2010**	2009
Australian dollars (in million)	**1**	1	**1**	1
Euros (in million)	**6**	4	**6**	4
Japanese Yen (in million)	**31**	80	**31**	80
Pound sterling (in million)	**1**	1	**1**	1
Swiss franc (in thousand)	**–**	470	**–**	470
United States dollars (in million)	**17**	23	**2**	8

44 Contract Retentions

The Group

in HK$ million	Due for release within 12 months	Due for release after 12 months	Total
2010			
Railway extension projects	**3**	**123**	**126**
Railway operations	**105**	**173**	**278**
	108	**296**	**404**
2009			
Railway extension projects	18	216	234
Railway operations	69	51	120
	87	267	354

44 Contract Retentions *(continued)*

The Company

in HK$ million	Due for release within 12 months	Due for release after 12 months	Total
2010			
Railway extension projects	**3**	**123**	**126**
Railway operations	**46**	**49**	**95**
	49	**172**	**221**
2009			
Railway extension projects	18	66	84
Railway operations	69	51	120
	87	117	204

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

Included in contract retentions are the following amounts denominated in a currency other than the functional currency of the entity to which they relate:

	The Group		The Company	
	2010	2009	**2010**	2009
Australian dollars (in thousand)	**522**	522	**522**	522
Euros (in thousand)	**144**	460	**144**	460
Japanese Yen (in million)	**4**	4	**4**	4

45 Amounts Due to the Government and Other Related Parties

	The Group		The Company	
in HK$ million	**2010**	2009	**2010**	2009
Amounts due to:				
– the Government	**27**	19	**27**	19
– KCRC	**809**	904	**809**	904
– an associate	**56**	–	**–**	–
– subsidiaries	**–**	–	**11,243**	12,236
	892	923	**12,079**	13,159

The amount due to KCRC relates to mandatory payments and interest payable to KCRC in respect of the property development sites along the East Rail Line, Kowloon Southern Link and Light Rail as well as the accrued portion of the fixed annual payment and variable annual payment for the service concession.

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

The amount due to the Company's subsidiaries includes HK$11,162 million (2009: HK$12,156 million) due to MTR Corporation (C.I.) Limited in respect of proceeds from bonds and notes issued by the subsidiary, which were on-lent to the Company for its general corporate purposes with specified repayment dates and interest rates (note 42C), and accrued interest. These amounts are stated at their fair values. The remaining balances due to subsidiaries are non-interest bearing and have not been discounted as they do not have any fixed repayment terms and the amount is not material. Out of the total amount due to subsidiaries as at 31 December 2010, HK$10,481 million (2009: HK$10,851 million) is expected to be settled after one year.

46 Obligations under Service Concession

Obligations under service concession are the corresponding liabilities recognised in relation to the total fixed annual payments capitalised as service concession assets in respect of the Rail Merger and the total annual lease payments capitalised as service concession assets in respect of the operation of Shenzhen Line 4 Phase 1 (notes 3 and 24). During the year ended 31 December 2010, the Group recognised HK$151 million (2009: nil) of the obligation under service concession in respect of Shenzhen Line 4 Phase 1.

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

	The Group		The Company	
in HK$ million	**2010**	2009	**2010**	2009
Balance as at 1 January	**10,625**	10,656	**10,625**	10,656
Add: Total annual lease payments capitalised at inception	**151**	–	**–**	–
Add: Increase in interest payable	**4**	–	**–**	–
Less: Amount repaid/payable during the year	**(36)**	(31)	**(33)**	(31)
Exchange difference	**5**	–	**–**	–
Balance as at 31 December	**10,749**	10,625	**10,592**	10,625

The outstanding balances as at 31 December 2010 and 2009 are repayable as follows:

The Group

	2010			2009		
in HK$ million	Present value of fixed annual payments	Interest expense relating to future periods	Total fixed annual payments	Present value of fixed annual payments	Interest expense relating to future periods	Total fixed annual payments
Amounts repayable beyond 5 years	**10,549**	**21,232**	**31,781**	10,437	21,750	32,187
Amounts repayable within a period of between 2 and 5 years	**128**	**2,140**	**2,268**	120	2,130	2,250
Amounts repayable within a period of between 1 and 2 years	**37**	**719**	**756**	35	715	750
Amounts repayable within 1 year	**35**	**721**	**756**	33	717	750
	10,749	**24,812**	**35,561**	10,625	25,312	35,937

The Company

	2010			2009		
in HK$ million	Present value of fixed annual payments	Interest expense relating to future periods	Total fixed annual payments	Present value of fixed annual payments	Interest expense relating to future periods	Total fixed annual payments
Amounts repayable beyond 5 years	**10,392**	**21,045**	**31,437**	10,437	21,750	32,187
Amounts repayable within a period of between 2 and 5 years	**128**	**2,122**	**2,250**	120	2,130	2,250
Amounts repayable within a period of between 1 and 2 years	**37**	**713**	**750**	35	715	750
Amounts repayable within 1 year	**35**	**715**	**750**	33	717	750
	10,592	**24,595**	**35,187**	10,625	25,312	35,937

47 Loan from Holders of Non-controlling Interests

Loan from holders of non-controlling interests represents that portion of total shareholder loan of AUD48.75 million (HK$386 million) granted to Metro Trains Melbourne Pty. Ltd. ("MTM") by the holders of its non-controlling interests. The loan carries an interest rate of 7.5% per annum and is repayable at the discretion of MTM or on the expiry of the operation and maintenance franchise on 29 November 2017, whichever is earlier.

48 Deferred Income

in HK$ million	The Group 2010	The Group 2009	The Company 2010	The Company 2009
Deferred income on property development (note 28B)	**568**	124	**568**	124
Deferred income on transfer of assets from customers	**45**	45	**–**	–
Less : Amount recognised as income	**(8)**	(2)	**–**	–
	37	43	**–**	–
	605	167	**568**	124

49 Income Tax in the Balance Sheet

A Current taxation in the consolidated balance sheet comprised provision for Hong Kong Profits Tax for the Company and certain subsidiaries for the year ended 31 December 2010, chargeable at Hong Kong Profits Tax Rate at 16.5% (2009: 16.5%) and after netting off provisional tax paid, and overseas tax chargeable at the appropriate current tax rates of taxation ruling in the relevant countries.

in HK$ million	The Group 2010	The Group 2009	The Company 2010	The Company 2009
Provision for Hong Kong Profits Tax for the year (note 16)	**1,495**	1,347	**1,484**	1,340
Hong Kong Provisional Profits Tax paid	**(581)**	(921)	**(574)**	(915)
	914	426	**910**	425
Balance relating to overseas tax	**104**	4	**–**	–
	1,018	430	**910**	425

B Deferred Tax Assets and Liabilities Recognised

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

The Group

	Deferred tax arising from					
in HK$ million	Depreciation allowances in excess of related depreciation	Revaluation of properties	Provision and other temporary differences	Cash flow hedges	Tax losses	Total
2010						
At 1 January 2010	**8,382**	**4,316**	**121**	**(10)**	**(17)**	**12,792**
Charged to consolidated profit and loss account	**287**	**672**	**33**	**–**	**10**	**1,002**
Charged/(credited) to reserves	**–**	**56**	**–**	**(5)**	**–**	**51**
At 31 December 2010	**8,669**	**5,044**	**154**	**(15)**	**(7)**	**13,845**
2009						
At 1 January 2009	8,323	3,822	105	(30)	(11)	12,209
Charged/(credited) to consolidated profit and loss account	59	460	16	–	(6)	529
Charged to reserves	–	34	–	20	–	54
At 31 December 2009	8,382	4,316	121	(10)	(17)	12,792

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

B Deferred Tax Assets and Liabilities Recognised *(continued)*

The Company

in HK$ million	Deferred tax arising from: Depreciation allowances in excess of related depreciation	Revaluation of properties	Provision and other temporary differences	Cash flow hedges	Tax losses	Total
2010						
At 1 January 2010	**8,362**	**4,325**	**121**	**(10)**	**–**	**12,798**
Charged to profit and loss account	**289**	**670**	**32**	**–**	**–**	**991**
Charged/(credited) to reserves	**–**	**56**	**–**	**(5)**	**–**	**51**
At 31 December 2010	**8,651**	**5,051**	**153**	**(15)**	**–**	**13,840**
2009						
At 1 January 2009	8,315	3,829	105	(30)	–	12,219
Charged to profit and loss account	47	462	16	–	–	525
Charged to reserves	–	34	–	20	–	54
At 31 December 2009	8,362	4,325	121	(10)	–	12,798

in HK$ million	The Group 2010	The Group 2009	The Company 2010	The Company 2009
Net deferred tax assets recognised on the balance sheet	**(9)**	(12)	**–**	–
Net deferred tax liabilities recognised on the balance sheet	**13,854**	12,804	**13,840**	12,798
	13,845	12,792	**13,840**	12,798

C The Group has not recognised deferred tax assets in respect of some of its subsidiaries' cumulative tax losses of HK$395 million (2009: HK$283 million) as it is not probable that future taxable profits against which the losses can be utilised will be available in the relevant tax jurisdictions and entities.

50 Share Capital and Capital Management

A Share Capital, Share Premium and Capital Reserve

in HK$ million	2010	2009
Authorised:		
6,500,000,000 shares of HK$1.00 each	**6,500**	6,500
Issued and fully paid:		
5,772,563,031 shares (2009: 5,727,833,692 shares) of HK$1.00 each	**5,773**	5,728
Share premium	**10,773**	9,581
Capital reserve	**27,188**	27,188
	43,734	42,497

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.

50 Share Capital and Capital Management *(continued)*

A Share Capital, Share Premium and Capital Reserve *(continued)*

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

	Number of shares	Option/ scrip price	Proceeds received/Transfer from employee share-based capital reserve: Share capital account	Share premium account	Total
		HK$	HK$ million	HK$ million	HK$ million
Employee share options exercised					
– Pre-Global Offering Share Option Scheme	**2,922,500**	**8.44**	**3**	**22**	**25**
– New Joiners Share Option Scheme	**31,000**	**9.75**	**–**	**–**	**–**
	94,000	**18.05**	**–**	**2**	**2**
	70,000	**20.66**	**–**	**2**	**2**
– 2007 Share Option Scheme	**935,500**	**18.30**	**1**	**19**	**20**
	42,000	**24.50**	**–**	**1**	**1**
	151,000	**26.52**	**–**	**4**	**4**
	92,500	**26.85**	**–**	**3**	**3**
	352,500	**27.60**	**1**	**11**	**12**
Issued as 2009 final scrip dividends	**37,130,522**	**29.28**	**37**	**1,050**	**1,087**
Issued as 2010 interim scrip dividends	**2,907,817**	**27.84**	**3**	**78**	**81**
	44,729,339		**45**	**1,192**	**1,237**

An analysis of the Company's outstanding share options as at 31 December 2010 are disclosed in note 52.

B Capital Management

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

The Group manages the amount of capital in proportion to risk, and makes adjustments to its capital structure through the amount of dividend payment to shareholders, issuance of scrip and new shares, and managing its debt portfolio in conjunction with projected financing requirement. The Financial Secretary Incorporated of the Government of the Hong Kong SAR is the majority shareholder of the Company holding 4,434,552,207 shares as at 31 December 2010, representing 76.8% of total equity interest in the Company.

The Group monitors capital on the basis of the net debt-to-equity ratio, which is calculated on net borrowings as a percentage of the total equity attributable to shareholders of the Company where net borrowings are represented by the aggregate of loans and other obligations, bank overdrafts, obligations under service concession and loan from holders of non-controlling interests net of cash and cash equivalents and bank medium term notes. The Group's net debt-to-equity ratios over the past years have been trending downward in general, from approximately 60% at 31 December 2002 to 36% at 31 December 2006. Owing to the increase in borrowings to finance payments for the Rail Merger and the incorporation of the obligations under service concession as a component of debt, the ratio rose to 49% at 31 December 2007 and reverted to a downward trend to 42% at 31 December 2008, 26% at 31 December 2009 and 13% at 31 December 2010.

Octopus Cards Limited is subject to a prescribed ratio of total capital to total risk-weighted assets as required by the Hong Kong Monetary Authority. MTR Corporation (Shenzhen) Limited is subject to minimum capital requirement at 40% of the total investment for the Shenzhen Metro Line 4 project in accordance with the concession agreement. Metro Trains Melbourne Pty. Ltd. is required to maintain total shareholders' funds at a specified amount in accordance with the franchise agreement. MTR Stockholm AB is required to maintain total shareholders' fund at or above 50% of its registered share capital based on the Swedish Companies Act. As at 31 December 2010, these capital requirements were met. Apart from these, neither the Company nor any of its other subsidiaries are subject to externally imposed capital requirements.

51 Other Reserves

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

in HK$ million	Fixed assets revaluation reserve	Hedging reserve	Employee share-based capital reserve	Retained profits	Total other reserves
2010					
Balance as at 1 January 2010	**1,132**	**(52)**	**52**	**61,920**	**63,052**
2009 final dividend	**–**	**–**	**–**	**(2,177)**	**(2,177)**
2010 interim dividend	**–**	**–**	**–**	**(807)**	**(807)**
Employee share-based payments	**–**	**–**	**57**	**–**	**57**
Employee share options exercised	**–**	**–**	**(6)**	**–**	**(6)**
Employee share options lapsed	**–**	**–**	**(1)**	**1**	**–**
Total comprehensive income for the year	**285**	**(26)**	**–**	**11,878**	**12,137**
Balance as at 31 December 2010	**1,417**	**(78)**	**102**	**70,815**	**72,256**
2009					
Balance as at 1 January 2009	960	(154)	25	54,979	55,810
2008 final dividend	–	–	–	(1,925)	(1,925)
2009 interim dividend	–	–	–	(800)	(800)
Employee share-based payments	–	–	32	–	32
Employee share options exercised	–	–	(2)	–	(2)
Employee share options lapsed	–	–	(3)	3	–
Total comprehensive income for the year	172	102	–	9,663	9,937
Balance as at 31 December 2009	1,132	(52)	52	61,920	63,052

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

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

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

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

Apart from retained profits, the other reserves are not available for distribution to shareholders because they do not constitute realised profits. In addition, the Company considers the cumulative surpluses on revaluation of investment properties, net of tax of HK$24,143 million (2009: HK$20,755 million) included in retained profits are non-distributable as they also do not constitute realised profits. As at 31 December 2010, the Company considers that the total amount of reserves available for distribution to equity shareholders amounted to HK$46,672 million (2009: HK$41,165 million).

Included in the Group's retained profits as at 31 December 2010 is an amount of HK$512 million (2009: HK$448 million), being the retained profits attributable to the non-controlled subsidiaries and associates.

52 Share-based Payments

A Equity-settled Share-based Payments

The Group granted equity-settled share options to its Members of the Executive Directorate and certain employees under three share option schemes namely, the Pre-Global Offering Share Option Scheme, the New Joiners Share Option Scheme and the 2007 Share Option Scheme. Details of the schemes are as follows:

(i) Pre-Global Offering Share Option Scheme

In connection with the Initial Public Offering ("IPO") and Stock Exchange listing of the Company's shares in October 2000, a Pre-Global Offering Share Option Scheme ("Pre-IPO Option Scheme") was established. Under the Pre-IPO Option Scheme, a total of 769 employees including all the Members of the Executive Directorate, except C K Chow, Lincoln K K Leong and T C Chew who joined the Company on 1 December 2003, 1 February 2002 and 11 May 2009 respectively, were granted on 20 September 2000 options to purchase an aggregate of 48,338,000 shares, representing 0.8% of the issued share capital of the Company as at 31 December 2010. The options carry an exercise price of HK$8.44 per share, which was equivalent to 90% of the IPO offer price of HK$9.38 per share. The options may be exercised prior to 11 September 2010, subject to the vesting provisions under the Scheme. As at 31 December 2010, all options granted under the Pre-IPO Option Scheme were vested and lapsed upon expiry of the Scheme on 11 September 2010.

During the year ended 31 December 2010, a total of 2,922,500 previously vested share options have been exercised. The weighted average closing price in respect of the share options exercised during the year was HK$27.993 per share. In addition, 25,500 share options lapsed as a result of expiring of the Scheme during the year.

(ii) New Joiners Share Option Scheme

In May 2002, the New Joiners Share Option Scheme (the "New Option Scheme") was adopted at the 2002 Annual General Meeting to provide share options to new members of the top and senior management of the Company who did not participate in the Pre-IPO Option Scheme. Under the Rules of the New Option Scheme, a maximum of 5,056,431 shares, which represent 0.1% of the issued share capital of the Company as at 31 December 2010, may be issued pursuant to the exercise of options granted under the New Option Scheme. Options granted will be evenly vested in respect of their underlying shares over a period of three years from the date on which the relevant option is offered. The exercise price of any option granted under the New Option Scheme is to be determined by the Company upon the offer of grant of the option and which should not be less than the greatest of (i) the average closing price of an MTR share for the five business days immediately preceding the day of offer of such option; (ii) the closing price of an MTR share on the day of offer of such option, which must be a business day; and (iii) the nominal value of an MTR share. The New Option Scheme expired on 16 May 2007 and no options can be granted under this Scheme on or after that date.

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

Date of grant	Number of share options	Exercise price HK$	Exercisable period
1 August 2003	525,700	9.75	on or prior to 14 July 2013
23 September 2005	213,000	15.97	on or prior to 9 September 2015
12 May 2006	266,500	20.66	on or prior to 25 April 2016
15 May 2006	22,000	20.66	on or prior to 25 April 2016
5 October 2006	94,000	19.732	on or prior to 29 September 2016

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

	2010		2009	
	Number of share options	Weighted average exercise price HK$	Number of share options	Weighted average exercise price HK$
Outstanding at 1 January	**1,316,200**	**15.038**	2,500,200	14.426
Exercised during the year	**(195,000)**	**17.667**	(828,500)	11.316
Lapsed during the year	**–**	**–**	(355,500)	19.404
Outstanding at 31 December	**1,121,200**	**14.581**	1,316,200	15.038
Exercisable at 31 December	**1,121,200**	**14.576**	1,316,200	15.034

The weighted average closing price in respect of the share options exercised during the year was HK$29.104 (2009: HK$26.964).

52 Share-based Payments *(continued)*

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

Share options outstanding at 31 December 2010 had the following exercise prices and remaining contractual lives:

	2010		2009	
Exercise price	**Number of share options**	**Remaining contractual life years**	Number of share options	Remaining contractual life years
HK$9.75	**525,700**	**2.54**	556,700	3.54
HK$15.97	**213,000**	**4.69**	213,000	5.69
HK$18.05	**–**	**–**	94,000	6.22
HK$20.66	**288,500**	**5.32**	358,500	6.32
HK$19.732	**94,000**	**5.75**	94,000	6.75
	1,121,200		1,316,200	

(iii) 2007 Share Option Scheme

Following the expiry of the New Option Scheme in May 2007, the 2007 Share Option Scheme (the "2007 Option Scheme") was submitted and approved at the 2007 Annual General Meeting to enhance the Company's ability to attract the best available personnel, to retain and motivate critical and key employees, to align their interest to the long-term success of the Company and to provide them with fair and market competitive remuneration. Under the Rules of the 2007 Option Scheme, a maximum of 277,461,072 shares, which represent 4.8% of the issued share capital of the Company as at 31 December 2010, may be issued pursuant to the exercise of options granted after 7 June 2007 under all share option schemes of the Company including the 2007 Option Scheme. Options granted will be vested in respect of their underlying shares not less than 1 year from the date on which the relevant option is offered. The exercise price of any option granted under the 2007 Option Scheme is to be determined by the Company upon the offer of grant of the option and which should not be less than the greatest of (i) the average closing price of an MTR share for the five business days immediately preceding the day of offer of such option; (ii) the closing price of an MTR share on the day of offer of such option, which must be a business day; and (iii) the nominal value of an MTR share.

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

On 10 December 2007, share options in respect of 8,273,000 shares were offered to Members of the Executive Directorate and selected employees of the Company as the first tranche of the share option awards for 2008 (the "First 2008 Award"). For the First 2008 Award, share options in respect of 7,968,000 shares were accepted by the grantees during the period from 11 December 2007 to 31 December 2007 and share options in respect of 305,000 shares were accepted by the grantees during the period from 2 January 2008 to 7 January 2008. On 26 March 2008, share options in respect of 2,749,000 shares were offered to selected employees of the Company and were accepted by the grantees during the period from 28 March 2008 to 23 April 2008, as the second tranche of the share option awards for 2008. This award, together with the First 2008 Award, forms the "2008 Award".

On 8 December 2008, share options in respect of 12,712,000 shares were offered to Members of the Executive Directorate and other selected employees of the Company as the first tranche of the share option awards for 2009 (the "First 2009 Award"). Share options of the First 2009 Award were accepted by the grantees during the period from 8 December 2008 to 30 December 2008. On 12 June 2009, share options in respect of 345,000 shares were offered to selected employees of the Company and were accepted by the grantees during the period from 18 June 2009 to 9 July 2009, as the second tranche of the share option awards for 2009. This award, together with the First 2009 Award, forms the "2009 Award".

On 8 December 2009, share options in respect of 15,718,000 shares were offered to Members of the Executive Directorate and other selected employees of the Company and were accepted by the grantees during the period from 9 December 2009 to 22 December 2009, as share options award for 2010 (the "First 2010 Award"). On 28 June 2010, share options in respect of 355,000 shares were offered to selected employees of the Company and were accepted by the grantees on 21 July 2010, as the second tranche of the share option awards for 2010. This award, together with the First 2010 Award, forms the "2010 Award".

On 16 December 2010, share options in respect of 15,546,000 shares were offered to Members of the Executive Directorate and other selected employees of the Company and were accepted by the grantees during the period from 16 December 2010 to 23 December 2010, as share options award for 2011 (the "2011 Award").

52 Share-based Payments *(continued)*

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

The following table summarises the outstanding share options granted under the 2007 Option Scheme since inception.

Date of grant	Number of share options	Exercise price HK$	Exercisable period
2008 Award			
11 December 2007	45,000	27.60	on or prior to 10 December 2014
12 December 2007	2,288,000	27.60	on or prior to 10 December 2014
13 December 2007	1,805,000	27.60	on or prior to 10 December 2014
14 December 2007	872,000	27.60	on or prior to 10 December 2014
15 December 2007	343,000	27.60	on or prior to 10 December 2014
17 December 2007	751,000	27.60	on or prior to 10 December 2014
18 December 2007	288,000	27.60	on or prior to 10 December 2014
19 December 2007	80,000	27.60	on or prior to 10 December 2014
20 December 2007	190,000	27.60	on or prior to 10 December 2014
21 December 2007	15,000	27.60	on or prior to 10 December 2014
22 December 2007	35,000	27.60	on or prior to 10 December 2014
24 December 2007	118,000	27.60	on or prior to 10 December 2014
28 December 2007	35,000	27.60	on or prior to 10 December 2014
31 December 2007	130,000	27.60	on or prior to 10 December 2014
2 January 2008	48,000	27.60	on or prior to 10 December 2014
3 January 2008	40,000	27.60	on or prior to 10 December 2014
7 January 2008	125,000	27.60	on or prior to 10 December 2014
28 March 2008	204,000	26.52	on or prior to 26 March 2015
31 March 2008	349,000	26.52	on or prior to 26 March 2015
1 April 2008	249,000	26.52	on or prior to 26 March 2015
2 April 2008	276,000	26.52	on or prior to 26 March 2015
3 April 2008	159,000	26.52	on or prior to 26 March 2015
4 April 2008	23,000	26.52	on or prior to 26 March 2015
5 April 2008	17,000	26.52	on or prior to 26 March 2015
7 April 2008	342,000	26.52	on or prior to 26 March 2015
8 April 2008	116,000	26.52	on or prior to 26 March 2015
9 April 2008	85,000	26.52	on or prior to 26 March 2015
10 April 2008	58,000	26.52	on or prior to 26 March 2015
11 April 2008	117,000	26.52	on or prior to 26 March 2015
12 April 2008	48,000	26.52	on or prior to 26 March 2015
14 April 2008	40,000	26.52	on or prior to 26 March 2015
15 April 2008	34,000	26.52	on or prior to 26 March 2015
16 April 2008	40,000	26.52	on or prior to 26 March 2015
17 April 2008	124,000	26.52	on or prior to 26 March 2015
18 April 2008	15,000	26.52	on or prior to 26 March 2015
19 April 2008	25,000	26.52	on or prior to 26 March 2015
21 April 2008	66,000	26.52	on or prior to 26 March 2015
23 April 2008	19,000	26.52	on or prior to 26 March 2015
2009 Award			
8 December 2008	110,000	18.30	on or prior to 8 December 2015
9 December 2008	1,433,000	18.30	on or prior to 8 December 2015
10 December 2008	2,040,900	18.30	on or prior to 8 December 2015
11 December 2008	2,291,200	18.30	on or prior to 8 December 2015
12 December 2008	1,292,000	18.30	on or prior to 8 December 2015
13 December 2008	84,500	18.30	on or prior to 8 December 2015
14 December 2008	79,700	18.30	on or prior to 8 December 2015
15 December 2008	930,200	18.30	on or prior to 8 December 2015
16 December 2008	487,500	18.30	on or prior to 8 December 2015
17 December 2008	485,500	18.30	on or prior to 8 December 2015
18 December 2008	483,000	18.30	on or prior to 8 December 2015
19 December 2008	198,000	18.30	on or prior to 8 December 2015
20 December 2008	19,000	18.30	on or prior to 8 December 2015
22 December 2008	689,500	18.30	on or prior to 8 December 2015
23 December 2008	246,500	18.30	on or prior to 8 December 2015
24 December 2008	455,500	18.30	on or prior to 8 December 2015
25 December 2008	45,000	18.30	on or prior to 8 December 2015
29 December 2008	133,000	18.30	on or prior to 8 December 2015
30 December 2008	19,000	18.30	on or prior to 8 December 2015
18 June 2009	175,000	24.50	on or prior to 12 June 2016
6 July 2009	45,000	24.50	on or prior to 12 June 2016
9 July 2009	30,000	24.50	on or prior to 12 June 2016

52 Share-based Payments *(continued)*

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

Date of grant	Number of share options	Exercise price HK$	Exercisable period
2010 Award			
9 December 2009	585,000	26.85	on or prior to 8 December 2016
10 December 2009	2,754,000	26.85	on or prior to 8 December 2016
11 December 2009	2,322,000	26.85	on or prior to 8 December 2016
12 December 2009	610,000	26.85	on or prior to 8 December 2016
13 December 2009	12,500	26.85	on or prior to 8 December 2016
14 December 2009	2,444,000	26.85	on or prior to 8 December 2016
15 December 2009	2,804,000	26.85	on or prior to 8 December 2016
16 December 2009	1,491,000	26.85	on or prior to 8 December 2016
17 December 2009	975,000	26.85	on or prior to 8 December 2016
18 December 2009	380,500	26.85	on or prior to 8 December 2016
19 December 2009	70,000	26.85	on or prior to 8 December 2016
20 December 2009	75,000	26.85	on or prior to 8 December 2016
21 December 2009	520,000	26.85	on or prior to 8 December 2016
22 December 2009	237,000	26.85	on or prior to 8 December 2016
21 July 2010	355,000	27.73	on or prior to 28 June 2017
2011 Award			
16 December 2010	194,000	28.84	on or prior to 16 December 2017
17 December 2010	5,467,000	28.84	on or prior to 16 December 2017
18 December 2010	673,000	28.84	on or prior to 16 December 2017
19 December 2010	174,000	28.84	on or prior to 16 December 2017
20 December 2010	4,854,500	28.84	on or prior to 16 December 2017
21 December 2010	3,020,000	28.84	on or prior to 16 December 2017
22 December 2010	975,000	28.84	on or prior to 16 December 2017
23 December 2010	189,000	28.84	on or prior to 16 December 2017

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

	2010		2009	
	Number of share options	Weighted average exercise price HK$	Number of share options	Weighted average exercise price HK$
Outstanding at 1 January	**38,929,500**	**24.185**	23,393,000	22.425
Granted during the year	**15,901,500**	**28.815**	16,063,000	26.800
Exercised during the year	**(1,573,500)**	**21.840**	(56,500)	18.300
Lapsed during the year	**(689,000)**	**24.888**	(470,000)	26.618
Outstanding at 31 December	**52,568,500**	**25.646**	38,929,500	24.185
Exercisable at 31 December	**21,495,500**	**24.095**	10,253,500	23.684

Share options outstanding at 31 December 2010 had the following exercise prices and remaining contractual lives:

	2010		2009	
Exercise price	Number of share options	Remaining contractual life years	Number of share options	Remaining contractual life years
HK$27.60	**7,208,000**	**4**	7,670,000	5
HK$26.52	**2,406,000**	**4**	2,586,000	5
HK$18.30	**11,523,000**	**5**	12,610,500	6
HK$24.50	**250,000**	**5**	345,000	6
HK$26.85	**15,280,000**	**6**	15,718,000	7
HK$27.73	**355,000**	**6**	–	–
HK$28.84	**15,546,500**	**7**	–	–
	52,568,500		38,929,500	

52 Share-based Payments *(continued)*

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

According to the Black-Scholes pricing model, the fair values of options granted during the year ended 31 December 2010 were as follows:

Date of grant	Fair value of options granted HK$	Inputs into the Black-Scholes pricing model: Share price immediately before grant date HK$	Exercise price HK$	Expected volatility	Expected life years	Risk-free interest rate %	Expected dividend per share HK$
21 July 2010	**5.53**	**27.35**	**27.73**	**0.32**	**3.5**	**0.89**	**0.52**
16 December 2010	**5.86**	**28.55**	**28.84**	**0.32**	**3.5**	**1.21**	**0.52**
17 December 2010	**5.77**	**28.35**	**28.84**	**0.32**	**3.5**	**1.28**	**0.52**
18 December 2010	**5.83**	**28.45**	**28.84**	**0.32**	**3.5**	**1.28**	**0.52**
19 December 2010	**5.83**	**28.45**	**28.84**	**0.32**	**3.5**	**1.28**	**0.52**
20 December 2010	**5.79**	**28.45**	**28.84**	**0.32**	**3.5**	**1.20**	**0.52**
21 December 2010	**5.56**	**28.05**	**28.84**	**0.32**	**3.5**	**1.21**	**0.52**
22 December 2010	**5.76**	**28.40**	**28.84**	**0.32**	**3.5**	**1.20**	**0.52**
23 December 2010	**5.81**	**28.50**	**28.84**	**0.32**	**3.5**	**1.20**	**0.52**

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

(iv) During the year, the equity-settled share-based payments recognised in respect of the above share option schemes were as follows:

in HK$ million	2010	2009
Equity-settled share-based payments in respect of:		
– New Option Scheme	**–**	1
– 2007 Option Scheme	**57**	31
	57	32

B Cash-settled Share-based Payments

(i) C K Chow did not participate in the Company's Pre-Global Offering Share Option Scheme and New Joiners Share Option Scheme. Pursuant to the completion of his three-year contract expiring on 30 November 2009, he was paid on 1 December 2009 an equivalent value in cash of 418,017 shares in the Company, amounting to HK$11.3 million (calculated at a price of HK$27.0075 per share derived in accordance with the terms of the grant by reference to the average closing price of the Company's shares on the 20 business days immediately preceding 30 November 2009).

Following renewal of C K Chow's contract with effect from 1 December 2009, he is entitled to receive an equivalent value in cash of 222,161 shares in the Company on completion of this contract on 31 December 2011. For the year ended 31 December 2010, HK$3.0 million (2009: HK$6.3 million) was recorded as share-based payment expense. Fair value of the outstanding entitlement is calculated based on the closing price of the Company's shares at year-end date. As at 31 December 2010, the fair value of these shares was HK$28.30 per share (2009: HK$26.80).

(ii) Lincoln K K Leong was entitled to a derivative interest in the Company's shares and was paid on 12 April 2010 an equivalent value in cash of 160,000 shares in the Company, amounting to HK$4.6 million (calculated at a price of HK$28.785 per share derived in accordance with the terms of the grant by reference to the average closing price of the Company's shares on the 20 business days immediately preceding 9 April 2010). For the year ended 31 December 2010, HK$0.7 million (2009: HK$2.2 million) was recorded as share-based payment expense, measured on the same basis as described in note 52B(i) above.

53 Retirement Schemes

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

A Retirement Schemes Operated by the Company in Hong Kong

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

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

(i) MTR Retirement Scheme

The MTR Retirement Scheme was established under trust at the beginning of 1977 containing both defined benefit and defined contribution elements. The MTR Retirement Scheme was registered under the Occupational Retirement Schemes Ordinance (Chapter 426 of the Laws of Hong Kong) ("ORSO") with effect from 31 October 1994. On 3 July 2000, exemption was granted by the Mandatory Provident Fund Schemes Authority to maintain the MTR Retirement Scheme and offer it as an alternative to the MTR MPF Scheme.

The MTR Retirement Scheme offers benefits on retirement, permanent disability, death and leaving service to its members. It originally contained both a hybrid benefit section and a defined contribution section. The hybrid benefit section provides benefits based on the greater of a multiple of final salary and accumulated contributions with investment returns and has been closed to new entrants since 31 March 1999. The defined contribution section provided benefits based on accumulated contributions and investment returns only. Employees who were hired after the closure of the hybrid benefit section would be eligible to join the defined contribution section of the MTR Retirement Scheme or, commencing on 1 December 2000, the MTR MPF Scheme.

Following the Rail Merger and with the approval of the scheme's trustees, effective on 1 March 2008, the defined contribution section of the MTR Retirement Scheme was transferred to the MTR Provident Fund Scheme. Since then, the MTR Retirement Scheme only contains a hybrid section. Given the transfer, commencing on 1 March 2008 (note 53A(iii)), employees who are eligible to join the MTR Provident Fund Scheme, can choose between the MTR Provident Fund Scheme and the MTR MPF Scheme, except where they were previously members of the KCRC MPF Scheme where upon they may choose between the MTR Provident Fund Scheme and the KCRC MPF Scheme.

Members' contributions to the MTR Retirement Scheme are based on a fixed percentage of basic salary. The Company's contributions are determined by the Executive Directorate with reference to an actuarial valuation. As at 31 December 2010, the total membership was 5,127 (2009: 5,282). In 2010, members contributed HK$70 million (2009: HK$70 million) and the Company contributed HK$120 million (2009: HK$198 million) to the MTR Retirement Scheme. The net asset value of the MTR Retirement Scheme as at 31 December 2010 was HK$8,200 million (2009: HK$7,542 million).

According to the terms of the trust deed, forfeitures were transferred to the reserve account to be utilised at the discretion of the Company.

Actuarial valuations are carried out annually by an independent firm of consulting actuaries using the Projected Unit Credit Method to determine the accounting obligations in accordance with HKAS 19, *Employee Benefits,* and the results of the valuations as at 31 December 2009 and 2010 carried out by Towers Watson are shown in note 54.

A full actuarial valuation of the MTR Retirement Scheme using the Attained Age Method to determine the cash funding requirements was also carried out as at 31 December 2010 by Towers Watson. The principal actuarial assumptions used included a long-term rate of investment return net of salary increases of 2.0% (2009: 2.4%) per annum, together with appropriate allowances for expected rates of mortality, turnover, redundancy and retirement. The actuary confirmed that, as at the valuation date:

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

(b) on the assumption that the MTR Retirement Scheme continued in force, the value of assets was more than sufficient to cover the aggregate past service liability, with a funding level of 112.6%.

(ii) MTR RBS

The MTR RBS was established under trust as of 1 January 1995. It is a defined benefit scheme and applies to all employees classified by the Company as staff working on designated projects and who are not on gratuity terms. The MTR RBS provides for benefits to be payable only in the event of redundancy for accrued service accrued up to 31 December 2002. The MTR RBS was registered under the ORSO with effect from 1 December 1995. As at 31 December 2010, there were 307 members (2009: 318).

53 Retirement Schemes *(continued)*

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

The MTR RBS is non-contributory for members. The Company's contributions are determined by the Executive Directorate with reference to an actuarial valuation and are charged as part of the staff costs to various projects on the basis of the amount contributed. During 2009 and 2010, the Company was not required to make any contribution to the MTR RBS. The net asset value of the MTR RBS as at 31 December 2010 was HK$12 million (2009: HK$12 million).

Actuarial valuations are carried out annually by an independent firm of consulting actuaries using the Projected Unit Credit Method to determine the accounting obligations in accordance with HKAS 19, *Employee Benefits*. The valuations as at 31 December 2009 and 2010 were carried out by Towers Watson and the results are shown in note 54.

A full actuarial valuation of the MTR RBS was also carried out as at 31 December 2010 by Towers Watson using the Attained Age Method to determine the cash funding requirements. The principal actuarial assumptions used included an expected weighted rate of investment return net of salary increases, of approximately -2.5% (2009: -1.6%) per annum, together with appropriate allowance for expected rates of redundancy. The actuary confirmed that, as at the valuation date:

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

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

(iii) MTR Provident Fund Scheme

The MTR Provident Fund Scheme was renamed from the KCRC Retirement Benefit Scheme following its incorporation of the defined contribution section of the MTR Retirement Scheme on 1 March 2008. It was established on 1 February 1983 under trust and was registered under the ORSO with effect from 16 November 1994. It contains three sections, all of which are defined contribution schemes. One section consists of the members of the KCRC Retirement Benefit Scheme prior to 1 March 2008, one section consists of the members of the defined contribution section of the MTR Retirement Scheme prior to 1 March 2008 and the final section consists of those appointees eligible to join the MTR Provident Fund Scheme on or after 1 March 2008.

All benefits payable under the MTR Provident Fund Scheme are calculated by reference to the employer's contributions and members' own contributions, based on fixed percentages of members' basic salaries, together with investment returns on these contributions.

As at 31 December 2010, the total number of employees participating in the MTR Provident Fund Scheme was 6,276 (2009: 5,954). In 2010, total members' contributions were HK$52 million (2009: HK$52 million) and total contribution from the Company was HK$159 million (2009: HK$152 million). The net asset value as at 31 December 2010 was HK$3,588 million (2009: HK$3,160 million).

(iv) MTR MPF Scheme

Effective from the MPF commencement date of 1 December 2000, the Company joined The Bank Consortium MPF Plan which has been registered with the Mandatory Provident Fund Schemes Authority and authorised by the Securities and Futures Commission. The MTR MPF Scheme covers those employees who did not opt for or who are not eligible to join the MTR Retirement Scheme or the MTR Provident Fund Scheme. Both members and the Company each contribute to the MTR MPF Scheme at the mandatory levels as required by the MPF Ordinance.

As at 31 December 2010, the total number of employees of the Company participating in the MTR MPF Scheme was 2,540 (2009: 1,875). In 2010, total members' contributions were HK$14 million (2009: HK$9 million) and total contribution from the Company was HK$16 million (2009: HK$10 million).

(v) KCRC MPF Scheme

The KCRC MPF Scheme was introduced on 1 April 2000 and registered with the Hong Kong Mandatory Provident Fund Schemes Authority. It covers those former KCRC employees who did not opt for or who were not eligible to join the former KCRC Retirement Benefit Scheme, now known as MTR Provident Fund Scheme, and those employees who, on or after 1 March 2008, were previously members of the KCRC MPF Scheme and are eligible to join the MTR Provident Fund Scheme but opt to re-join the KCRC MPF Scheme. It is a defined contribution retirement plan administered by independent trustees with both members and the Company each contributing to the KCRC MPF Scheme at the mandatory levels as required by the MPF Ordinance.

As at 31 December 2010, the total number of employees of the Company participating in the KCRC MPF Scheme was 903 (2009: 953). In 2010, total members' contributions were HK$6 million (2009: HK$7 million) and total contribution from the Company was HK$7 million (2009: HK$7 million).

B Retirement Schemes for Employees of Overseas Offices and Subsidiaries

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

(i) Defined Benefit Plan

Certain number of employees of the Group's Australian subsidiary are entitled to receive retirement benefits from the Emergency Services Superannuation Scheme operated in Australia. The benefit amounts are calculated based on the member's years of service and final average salary. The Group does not recognise any defined benefit liability in respect of this scheme because the Group has no legal or constructive obligation to pay future benefits relating to its employees; its only obligation is to pay contributions as they fall due. As at 31 December 2010, total number of the Group's employees participating in this scheme was 894 (2009: 1,029). In 2010, total members' contributions were HK$31 million (2009: HK$3 million) and total contribution from the Group was HK$44 million (2009: HK$5 million).

53 Retirement Schemes *(continued)*

B Retirement Schemes for Employees of Overseas Offices and Subsidiaries *(continued)*

(ii) Defined Contribution Plans

Except for the defined benefit plan stated in note 53B(i), all other retirement schemes to cover employees in overseas offices or in subsidiaries in Hong Kong, Mainland of China or overseas are defined contribution schemes. For Hong Kong employees, these schemes are registered under the MPF Ordinance in Hong Kong. For the Mainland of China or overseas employees, these schemes are operated in accordance with the respective local laws and regulations. As at 31 December 2010, the total number of employees of the Group participating in these schemes was 7,074 (2009: 6,081). In 2010, total members' contributions were HK$77 million (2009: HK$9 million) and total contribution from the Group was HK$180 million (2009: HK$22 million).

54 Defined Benefit Retirement Plan Obligations

The Company makes contributions to and recognises defined benefit liabilities in respect of two defined benefit plans that provide benefits for employees upon retirement or termination of services for other reasons (note 53). The movements in respect of these defined benefit plans during the year are summarised as follows.

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

The Group and The Company

	2010			2009		
in HK$ million	MTR Retirement Scheme	MTR RBS	Total	MTR Retirement Scheme	MTR RBS	Total
Present value of funded obligations	**(9,342)**	**–**	**(9,342)**	(8,959)	–	(8,959)
Fair value of plan assets	**8,200**	**12**	**8,212**	7,542	12	7,554
Net unrecognised actuarial losses/(gains)	**1,302**	**(3)**	**1,299**	1,587	(4)	1,583
Net asset	**160**	**9**	**169**	170	8	178

A portion of the above asset is expected to be recovered after more than one year. However, it is not practicable to segregate this amount from the amounts to be recovered in the next twelve months, as future contributions will also relate to future services rendered and future changes in actuarial assumptions and market conditions. The Company expects to pay HK$119 million in contribution to the MTR Retirement Scheme in 2011.

B Plan assets consist of the following:

The Group and The Company

	2010			2009		
in HK$ million	MTR Retirement Scheme	MTR RBS	Total	MTR Retirement Scheme	MTR RBS	Total
Equity securities	**4,423**	**–**	**4,423**	3,871	–	3,871
Bonds	**3,602**	**–**	**3,602**	3,681	–	3,681
Cash	**250**	**12**	**262**	53	12	65
	8,275	**12**	**8,287**	7,605	12	7,617
Voluntary units	**(75)**	**–**	**(75)**	(63)	–	(63)
	8,200	**12**	**8,212**	7,542	12	7,554

The plan assets include no investment in the Company's ordinary shares and the Company's debt securities in 2009 and 2010.

54 Defined Benefit Retirement Plan Obligations *(continued)*

C Movements in the Present Value of the Defined Benefit Obligations

The Group and The Company

	2010			2009		
in HK$ million	MTR Retirement Scheme	MTR RBS	Total	MTR Retirement Scheme	MTR RBS	Total
At 1 January	**8,959**	**–**	**8,959**	9,064	1	9,065
Members' contributions paid to the Schemes	**70**	**–**	**70**	70	–	70
Benefits paid by the Schemes	**(311)**	**–**	**(311)**	(212)	–	(212)
Current service cost	**293**	**–**	**293**	337	–	337
Interest cost	**227**	**–**	**227**	174	–	174
Actuarial losses/(gains)	**104**	**–**	**104**	(474)	(1)	(475)
At 31 December	**9,342**	**–**	**9,342**	8,959	–	8,959

D Movements in Plan Assets

The Group and The Company

	2010			2009		
in HK$ million	MTR Retirement Scheme	MTR RBS	Total	MTR Retirement Scheme	MTR RBS	Total
At 1 January	**7,542**	**12**	**7,554**	6,162	12	6,174
Group's contributions paid to the Schemes	**120**	**–**	**120**	198	–	198
Members' contributions paid to the Schemes	**70**	**–**	**70**	70	–	70
Benefits paid by the Schemes	**(311)**	**–**	**(311)**	(212)	–	(212)
Expected return on plan assets	**448**	**–**	**448**	383	–	383
Actuarial gains	**331**	**–**	**331**	941	–	941
At 31 December	**8,200**	**12**	**8,212**	7,542	12	7,554

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

	2010			2009		
in HK$ million	MTR Retirement Scheme	MTR RBS	Total	MTR Retirement Scheme	MTR RBS	Total
Current service cost	**293**	**–**	**293**	337	–	337
Interest cost	**227**	**–**	**227**	174	–	174
Expected return on plan assets	**(448)**	**–**	**(448)**	(383)	–	(383)
Net actuarial losses/(gains) recognised	**58**	**(1)**	**57**	109	(1)	108
Expense recognised	**130**	**(1)**	**129**	237	(1)	236
Less: Amount capitalised	**(21)**	**–**	**(21)**	(27)	–	(27)
	109	**(1)**	**108**	210	(1)	209

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

54 Defined Benefit Retirement Plan Obligations *(continued)*

F Actual Return on Plan Assets

in HK$ million	**2010**	2009
MTR Retirement Scheme	**779**	1,324
MTR RBS	**–**	–

G The principal actuarial assumptions used as at 31 December 2010 (expressed as weighted average) are as follows:

	2010		2009	
	MTR Retirement Scheme	MTR RBS	MTR Retirement Scheme	MTR RBS
Discount rate at 31 December	**2.9%**	**1.9%**	2.6%	2.0%
Expected rate of return on plan assets	**6.0%**	**1.5%**	6.0%	1.5%
Future salary increases	**4.0%**	**4.0%**	3.6%	3.1%

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

H Historical Information

The Group and The Company

	MTR Retirement Scheme				
in HK$ million	**2010**	2009	2008	2007	2006
Present value of funded obligations	**(9,342)**	(8,959)	(9,064)	(8,577)	(7,311)
Fair value of plan assets	**8,200**	7,542	6,162	7,929	6,906
Deficit in the Scheme	**(1,142)**	(1,417)	(2,902)	(648)	(405)
Experience adjustments arising on plan liabilities – (loss)/gain	**(357)**	(785)	1,391	(556)	(464)
Experience adjustments arising on plan assets – gain/(loss)	**331**	941	(1,997)	514	510

	MTR RBS				
in HK$ million	**2010**	2009	2008	2007	2006
Present value of funded obligations	**–**	–	(1)	(1)	(3)
Fair value of plan assets	**12**	12	12	12	12
Surplus in the Scheme	**12**	12	11	11	9
Experience adjustments arising on plan liabilities – gain/(loss)	**–**	1	–	1	3
Experience adjustments arising on plan assets – gain/(loss)	**–**	–	–	–	–

55 Interests in Jointly Controlled Operations

The Group has the following jointly controlled operations in respect of its awarded property development projects as at 31 December 2010:

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

* Completion based on issuance of occupation permit

The Group's assets held in relation to these joint venture operations include various site foundation works and related staff and overhead costs, land costs, acquisition cost of development rights and interest expense. These are set off against any payments received from developers in relation to that development package, and the balance is shown on the balance sheet either as property development in progress or deferred income (note 28) as the case may be. As at 31 December 2010, total property development in progress in respect of these jointly controlled operations was HK$6,863 million (2009: HK$3,094 million) and total deferred income was HK$81 million (2009: HK$124 million).

During the year ended 31 December 2010, profits of HK$4,034 million (2009: HK$3,554 million) were recognised (note 10).

55 Interests in Jointly Controlled Operations *(continued)*

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

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

* Completion based on issuance of occupation permit

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

56 Material Related Party Transactions

The Financial Secretary Incorporated, which holds approximately 76.8% of the Company's issued share capital on trust for the Government of the Hong Kong SAR, is the majority shareholder of the Company. Transactions between the Group and Government departments, agencies or Government controlled entities, other than those transactions such as the payment of fees, taxes, leases and rates, etc. that arise in the normal dealings between the Government and the Group, are considered to be related party transactions pursuant to HKAS 24, *Related party disclosures,* and are identified separately in these accounts.

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

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

A The Company entered into the Airport Railway Agreement with the Government on 5 July 1995 for the construction of the Airport Railway. In addition to specifying the parameters for the design, construction and operation of the Tung Chung and Airport Express Lines, the Agreement also included provisions for the granting of land to the Company for property development (note 28).

B The Company entered into the TKE Project Agreement with the Government on 4 November 1998 for the design, construction, financing and operation of the Tseung Kwan O Extension and the granting of land for commercial and residential property developments along the railway extension.

C On 30 June 2000, the Company was granted a franchise, for an initial period of 50 years, to operate the existing mass transit railway, and to operate and construct any extension to the railway. On the same day, the Company entered into an Operating Agreement ("OA") with the Government which detailed provisions for the design, construction, maintenance and operation of the railway under the franchise. Pursuant to the terms of the OA, the Company's franchise will be extended for further periods of 50 years upon satisfying certain capital expenditure requirements at no payment and without any change in the terms of the franchise. The OA also provides that upon extension of the franchise and subject to the Government's prevailing land policy on the date on which the franchise is extended, certain consequential amendments will be made to agreements between the Government and the Company in relation to the mass transit railway, including the renewal of various railway running line leases and land leases at nominal cost. With effect from 2 December 2007, the OA was replaced by a new operating agreement, details of which are set out in note 56I below.

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

E On 24 July 2002, the Company entered into an agreement with the Government specifying the parameters for the design, construction, financing and operation of the Disneyland Resort Line ("DRL"). In connection with the financing of the DRL Project, the Government agreed to provide financial support through the Government waivers of its entitlement to cash dividends in respect of its shareholding. Such committed financial support has been met in 2004. The DRL was completed in June 2005 and commenced operation on 1 August 2005.

F On 19 November 2003, the Company entered into a formal project agreement with the Government to develop, on a build, operate and transfer basis, the Tung Chung Cable Car System together with a Theme Village at Ngong Ping on the Lantau Island under a franchise granted by the Government for a period of 30 years commencing on 24 December 2003. The project was completed with operation commenced on 18 September 2006.

G On 24 January 2005, the Company accepted an offer from the Government to allow the Company to proceed with the proposed development on Site F of Tseung Kwan O Town Lot No. 70, Area 86, at an assessed land premium of HK$2,319 million together with other ancillary terms and conditions as specified in the modification letter to be entered into between the Company and the Government. Upon award of the development package on 8 February 2005, the agreed land premium, of which one-half or HK$1,160 million was paid by the Company, was settled.

56 Material Related Party Transactions *(continued)*

H On 18 July 2005, the Company entered into a project agreement with the Airport Authority for the procurement of MTR station extension works and related railway facilities to serve the SkyPlaza at the Hong Kong International Airport. The project was completed with the facilities opened on 28 February 2007.

I In connection with the Rail Merger (note 3), on 9 August 2007, the Company entered into a new operating agreement with the Government ("new OA"), which is based on the existing OA referred to in note 56C above. On the Appointed Day, the Company's existing franchise under the Mass Transit Railway Ordinance was expanded to cover railways other than the existing MTR railway for an initial period of 50 years from the Appointed Day ("expanded franchise"). The new OA detailed the design, construction, maintenance and operation of the railways under the expanded franchise. Pursuant to the terms of the new OA (and the MTR Ordinance), the Company's franchise may be extended for further periods of 50 years (from the date of the extension) upon satisfying certain capital expenditure requirements at no payment and without any change in the terms of the franchise. The new OA includes terms relating to the Company's obligations in relation to electrical power supply, control centres, the monitoring of environmental conditions, the provision of accommodation for the Hong Kong Police Force, the notification of certain events to the Commissioner for Transport, hours of operation and service capacity, performance requirements, customer service pledges and safety management. The new OA also sets out a framework for the award of new railway projects in Hong Kong and introduces a fare adjustment mechanism. A detailed description of the new OA is contained in the circular to shareholders in respect of the Extraordinary General Meeting convened to approve the Rail Merger.

J Other than the new OA described in note 56I above, the Company also entered into the following principal agreements with KCRC and the Government in connection with the Rail Merger on 9 August 2007:

(i) Merger Framework Agreement, which contains provisions for the overall structure and certain specific aspects of the rail merger, including the seamless interchange programme, corporate governance, certain employee arrangements, implementation of certain fare reductions, the payments for property package, arrangements relating to flat production and land premium, the treatment of KCRC's cross border leases, Shatin to Central Link arrangements and the allocation of liabilities for certain pre and post merger claims by third parties;

(ii) Service Concession Agreement, which contains provisions in relation to the grant of the right to access, use and operate the concession property and a licence to access and use certain KCRC land; the term of the service concession; the arrangements for the redelivery of the KCRC system upon concession expiry; the provision of ex-KCRC services by the Company to specified standards; the obligation to pay upfront and annual payments; the legal and beneficial ownership of future concession property (Additional Concession Property); and the regime for compensation payable by KCRC upon return of the Additional Concession Property;

(iii) Sale and Purchase Agreement, which sets out the terms pursuant to which the Company acquired certain assets and contracts from KCRC;

(iv) Kowloon Southern Link ("KSL") Project Management Agreement, which sets out the terms on which the Company was appointed by KCRC to project manage the design and construction of the KSL in return for a management fee of approximately HK$710.8 million and an incentive payment of up to HK$110 million if the construction of the KSL is completed ahead of time and under budget. The Company itself will not construct, nor be responsible for the costs of the KSL works. Upon commencement of service on 16 August 2009, the KSL formed part of the service concession;

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

(vi) Outsourcing Agreement, which sets out the terms on which the Company is to provide certain financial and administrative services to KCRC after the Rail Merger for two years, in return for an annual fee of HK$19.8 million; and

(vii) Property Package Agreements, which set out the arrangements in respect of the acquisition of the property package. These arrangements include the assignment of certain properties by KCRC to the Company, the acquisition of certain properties by the Company through its acquisition of certain KCRC subsidiaries under the Sale and Purchase Agreement, the granting of leases on certain properties by the Government to the Company and the relating interim arrangements before such granting is effective, the management of certain development sites by the Company in return for a fee substantially equal to the profits from the developments, and the granting of certain potential development sites to the Company.

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

K Also in connection with the Rail Merger, the Company entered into US Cross Border Lease ("CBL") Assumption Agreements with KCRC on 30 November 2007 and US CBL Allocation Agreement with KCRC and KCRC's subsidiaries on 2 December 2007. The agreements set out the terms on which the Company has undertaken to perform, on a joint and several basis with KCRC, the obligations of KCRC under the respective CBLs, and delineate and allocate the obligations and responsibility for risks relating to the CBLs. Details of the commitment of the Company in connection with these agreements are specified in note 57E and a detailed description of these agreements are contained under the paragraph "Connected Transactions" of the Report of the Members of the Board.

L On 6 February 2008, the Company entered into a preliminary project agreement with the Government for the undertaking of the pre-authorisation activities of the West Island Line. Pursuant to the agreement, the Company received HK$400 million from the Government to undertake the detailed design of the railway works, carry out all necessary ground investigations, invite and assess tenders for the railway works construction contracts, and carry out ancillary and other support services.

56 Material Related Party Transactions *(continued)*

M On 21 August 2008, the Company entered into a maintenance agreement with the Hong Kong Airport Authority for the renewal of an expired maintenance agreement for the automatic people mover system serving the Hong Kong International Airport including the Sky Plaza and Sky Pier terminal buildings. The renewed agreement has a duration of five years effective from 6 July 2008 and widens the scope to cover the operation and maintenance of eight new vehicles and one new line, both of which were ready for passenger service starting from the fourth quarter of 2009. During 2010, HK$40 million (2009: HK$34 million) was recognised as consultancy income in respect of the maintenance agreements.

N On 24 November 2008, the Company entered into an Entrustment Agreement with the Government for the design of and site investigation and procurement activities in relation to the Shatin to Central Link (note 27B). During 2010, expenditure of HK$376 million (2009: HK$267 million) was incurred relating to these activities.

O On 24 November 2008, the Company entered into an Entrustment Agreement with the Government for the design of and site investigation and procurement activities in relation to the Hong Kong Section of the Guangzhou-Shenzhen-Hong Kong Express Rail Link ("XRL") (note 27C). During 2010, total expenditure of HK$44 million (2009: HK$280 million) was incurred under the Entrustment Agreement.

P On 13 July 2009, the Company entered into a Project Agreement with the Government for the financing, design, construction and operation of the West Island Line (note 26B).

Q On 6 November 2009, the Company renewed the Outsourcing Agreement referred to in note 56J(vi) with KCRC for a period of two years effective from 2 December 2009. The annual fee payable to KCRC under the agreement has been revised to HK$16.5 million.

During the year, the Group had the following material related party transactions:

R On 26 January 2010, the Government and the Company entered into another Entrustment Agreement for the construction and commissioning of the XRL (note 27C).

S On 12 March 2010, the Government granted Kowloon Inland Lot No. 11126 (Site C, Canton Road, Kowloon) and Kowloon Inland Lot No. 11129 (Site D, Canton Road, Kowloon) to the Company for the property development at Austin Station with a total consideration of HK$11,708 million, of which the Company contributed HK$3,900 million which has been settled in June 2010.

T In connection with the construction of various railway projects, certain essential project works are embedded within the infrastructure works to be undertaken by the Government or certain of its related parties. These works have been entrusted to the Government and its related parties and are payable on an actual cost basis according to architectural certifications. The Government and certain of its related parties, on the other hand, have entered into entrustment agreements with the Company for the construction of various other infrastructure works that are also reimbursable according to actual costs certified. Details of the amounts paid and the amounts receivable and payable as at 31 December 2010 are provided in notes 26, 40 and 45 respectively.

U The Company has business transactions with its non-controlled subsidiaries in the normal course of operations, details of which are disclosed in note 30.

V The Company has business transactions with its associates in the normal course of operations, details of which are disclosed in note 32.

W The Group has paid remuneration to the Members of the Board and Members of the Executive Directorate. Details of these transactions are described in note 9A. In addition, the Members of the Executive Directorate were granted share options under the Company's Pre-Global Offering Share Option Scheme, New Joiners Share Option Scheme and 2007 Share Option Scheme. Details of the terms of these directors' options are disclosed in note 9B and under the paragraph "Board Members' and Executive Directorate's Interests in Shares" of the Report of the Members of the Board. Their gross remuneration charged to the profit and loss account is summarised as follows:

in HK$ million	2010	2009
Short-term employee benefits	**57.1**	56.2
Post-employment benefits	**1.6**	5.4
Equity compensation benefits	**10.9**	13.1
	69.6	74.7

The above remuneration is included in staff costs and related expenses disclosed in note 8A.

X During the year, the following dividends were paid to the Government:

in HK$ million	2010	2009
Cash dividends paid	**1,302**	920
Shares allotted in respect of scrip dividends	**991**	1,171
	2,293	2,091

57 Commitments

A Capital Commitments

(i) Outstanding capital commitments as at 31 December 2010 not provided for in the accounts were as follows:

The Group

in HK$ million	Hong Kong railway operations	Hong Kong railway extension projects	Hong Kong property rental and development	Mainland of China and overseas projects	Total
2010					
Authorised but not yet contracted for	**1,575**	**–**	**142**	**–**	**1,717**
Authorised and contracted for	**986**	**7,100**	**326**	**1,340**	**9,752**
	2,561	**7,100**	**468**	**1,340**	**11,469**
2009					
Authorised but not yet contracted for	1,116	–	192	–	1,308
Authorised and contracted for	1,506	3,784	108	2,177	7,575
	2,622	3,784	300	2,177	8,883

The Company

in HK$ million	Hong Kong railway operations	Hong Kong railway extension projects	Hong Kong property rental and development	Total
2010				
Authorised but not yet contracted for	**1,561**	**–**	**140**	**1,701**
Authorised and contracted for	**986**	**7,100**	**315**	**8,401**
	2,547	**7,100**	**455**	**10,102**
2009				
Authorised but not yet contracted for	1,109	–	179	1,288
Authorised and contracted for	1,505	3,784	105	5,394
	2,614	3,784	284	6,682

Excluded from the above tables are estimated future project costs relating to WIL and SZL4 of HK$5,225 million and HK$672 million respectively as at 31 December 2010.

(ii) The commitments under Hong Kong railway operations comprise the following:

The Group and The Company

in HK$ million	Improvement and enhancement works	Acquisition of property, plant and equipment	Additional concession property	Total
2010				
Authorised but not yet contracted for	**795**	**285**	**495**	**1,575**
Authorised and contracted for	**344**	**375**	**267**	**986**
	1,139	**660**	**762**	**2,561**
2009				
Authorised but not yet contracted for	632	34	450	1,116
Authorised and contracted for	385	930	191	1,506
	1,017	964	641	2,622

57 Commitments *(continued)*

B Operating Lease Commitments

The Group had operating leases on office buildings, staff quarters, bus depot and a shopping centre in Beijing as at 31 December 2010. The total future minimum lease payments under non-cancellable operating leases are payable as follows:

	The Group		The Company	
in HK$ million	**2010**	2009	**2010**	2009
Payable within one year	**141**	77	**7**	23
Payable after one but within five years	**3**	131	**2**	4
	144	208	**9**	27

The above includes HK$4 million (2009: HK$20 million) in respect of the office accommodation and quarters for construction project staff, majority of which are subject to rent reviews.

In respect of the operating lease on the shopping centre in Beijing, the Group has the right to acquire the shopping centre in Beijing at a pre-determined price during the first five years of the lease term, which commenced from April 2006, or release its obligation as a tenant by making a compensation to the landlord upon expiry of the fifth year. The Group obtained a bank guarantee of RMB12.5 million in respect of the quarterly rental payment arrangement with the landlord. In addition, the Company provides guarantees amounting to RMB102.5 million to the landlord for the rental payments for the first five years of the lease, which was entered into by the Company's subsidiary, MTR (Beijing) Commercial Facilities Management Co. Ltd..

In addition to the above, there are future operating lease commitments of HK$6,747 million (2009: HK$10,113 million) in respect of railway subsidiaries outside of Hong Kong over the respective franchise periods, of which HK$1,024 million (2009: HK$1,305 million) is payable within one year, HK$3,944 million (2009: HK$5,144 million) is payable after one but within five years and HK$1,779 million (2009: HK$3,664 million) is payable over five years. These railway subsidiaries will generate franchise revenue receivables to the Group.

C Liabilities and Commitments in respect of Property Management Contracts

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

As at 31 December 2010, the Group had total outstanding liabilities and contractual commitments of HK$1,314 million (2009: HK$1,179 million) in respect of these works and services. Cash funds totalling HK$1,371 million (2009: HK$1,201 million) obtained through monthly payments of management service charges from the managed properties are held by the Group on behalf of those properties for settlement of works and services provided.

D Material Financial Guarantee Contracts

The Company provides guarantees to investors of debt securities issued by one of its subsidiaries, MTR Corporation (C.I.) Limited (note 42C), which amounted to approximately HK$10,644 million (in notional amount) as at 31 December 2010. Proceeds from such debts issued have been on lent to the Company. As such, the primary liabilities have already been recorded in the Company's balance sheet.

The Group provides standby letters of credit ("standby LC's") to the Investors to the lease out/lease back transaction ("Lease Transaction") (note 23E) to cover additional amounts payable by the Group in the event the transactions are terminated prior to the expiry of the lease terms, and such standby LC's amounted to US$108 million (HK$838 million) as at 31 December 2010. The Group also provides standby LC's to certain of the Investors under the Lease Transaction (note 23E) to replace some of the Defeasance Securities previously used to support the corresponding long-term lease payments as a result of credit rating downgrades of these securities, and such standby LC's amounted to US$36 million (HK$283 million) as at 31 December 2010.

E US Cross Border Lease ("CBL") Agreements

In connection with the Rail Merger in December 2007, the Company entered into a number of agreements ("US CBL Assumption Agreements") with respect to the CBLs that KCRC had entered into with its CBL counterparties in relation to certain of its property and equipment ("CBL Property") between 1998 and 2003. Pursuant to the US CBL Assumption Agreements, the Company has undertaken to perform, on a joint and several basis with KCRC, the obligations of KCRC under the respective CBLs.

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

57 Commitments *(continued)*

E US Cross Border Lease ("CBL") Agreements *(continued)*

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

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

F Service Concession in respect of the Rail Merger

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

G Investments in Mainland of China

(i) Investment in Line 4 of Shenzhen Metro System ("Shenzhen Line 4")

In March 2009, the Group and the Shenzhen Municipal People's Government signed the Project Concession Agreement to build Phase 2 of Shenzhen Line 4 and to operate both Phases 1 and 2 of Shenzhen Line 4 for a period of 30 years. The estimated total investment for Shenzhen Line 4 is RMB6.0 billion, comprising equity investment of RMB2.4 billion and bank loans in Renminbi for the remaining balance. On 15 May 2009, a financing agreement with a bank in Mainland of China was signed for the provision of a financing package in the aggregate amount of RMB4.0 billion to the project. The financing package comprises a RMB3.6 billion 20-year loan and other credit facilities, and is secured by certain future revenues from and interest in insurance policies covering the project.

As at 31 December 2010, the Group's outstanding contract commitments relating to the project were RMB1.1 billion (HK$1.3 billion) (2009: HK$2.2 billion) (note 57A). Payment guarantees and performance guarantees provided to the counterparties by a bank on the Group's behalf in respect of the construction of Phase 2 of Shenzhen Line 4 were RMB182 million (HK$215 million) and RMB85 million (HK$100 million) respectively. On 1 July 2010, the Group took over the operation of Phase 1 of Shenzhen Line 4.

(ii) Investment in Beijing Metro Line 4 Project ("Beijing Line 4")

In April 2006, the Group and the Beijng Municipal People's Government entered into the Concession Agreement for the investment, construction and operation of the Beijing Line 4 for a term of 30 years. The estimated total investment for Beijing Line 4 is RMB15.3 billion, of which 70% is borne by the Beijing Municipal People's Government to finance mainly land acquisition and civil construction while the remaining 30% is borne by Beijing MTR Corporation Limited ("Beijing MTR"), a public-private-partnership company formed by the Group and two subsidiaries of the Beijing Municipal People's Government with the Group owning 49% of equity interest, to finance mainly the electrical and mechanical systems and rolling stock as well as to operate and maintain the line. Registered capital of Beijing MTR is approximately RMB1.4 billion with the Group's contribution amounting to RMB676 million. On 28 September 2009, Beijing Line 4 was opened for operation.

Apart from Beijing Line 4, on 30 December 2009, Beijing MTR was granted an operation and maintenance concession for Beijing Daxing Line, a 22-kilometre and 11-station extension of Beijing Line 4 from Gongyixiqiao Station to Tiangongyuan Station, for a period of 10 years, renewable for further terms of 10 years until the expiry of the concession of Beijng Line 4. The Beijing Daxing Line commenced service on 30 December 2010. After the opening of Beijing Daxing Line, the extended 50-kilometre and 35-station Beijing Line 4 becomes the longest metro line in Beijing.

(iii) Investment in Shenyang Metro Lines Project

On 7 May 2009, the Group signed the Operation and Maintenance Concession Agreement with Shenyang Municipal Government for the operation and maintenance of Shenyang Metro Lines 1 and 2 for a term of 30 years. A joint venture company, Shenyang MTR Corporation Limited ("Shenyang MTR") was formed by the Group and a wholly-owned subsidiary of the Shenyang Municipal Government, with the Group owning 49% of equity interest. Total investment of Shenyang MTR is RMB400 million in which RMB200 million is registered capital. As of 31 December 2010, the Group injected equity of RMB49 million into Shenyang MTR and provided a parent company guarantee of RMB151 million (HK$178 million) to Shenyang Municipal Government for Shenyang MTR's obligations in the Concession Agreement.

Due to unforeseeable external factors, Shenyang MTR became unable to perform the operating activities under the Concession Agreement. As a result, the shareholders of Shenyang MTR resolved to reduce the registered capital from RMB200 million to RMB20 million with the equity interest remaining unchanged. Accordingly, the Group's capital contribution to Shenyang MTR will be reduced to RMB9.8 million. The reduction of capital is subject to approval by relevant authorities in the Mainland of China.

(iv) Investment in Hangzhou Metro Line 1 Project ("Hangzhou Line 1")

On 4 March 2010, the Company's wholly-owned subsidiary, MTR Hangzhou Line 1 Investment Company Limited, together with a subsidiary of Hangzhou Metro Group Company Limited, entered into a Concession Agreement with the Hangzhou Municipal Government for the investment, construction and operation of Hangzhou Line 1 for a term of 25 years. The line is expected to commence service in 2012.

57 Commitments *(continued)*

G Investments in Mainland of China *(continued)*

Total investment of the project is estimated at RMB22 billion. Project works on civil construction, representing approximately 63% of the total investment, is being undertaken by Hangzhou Metro Group Company Limited. Project works on electrical and mechanical systems, rolling stock and testing and commissioning, representing approximately 37% of the total investment, will be undertaken by a joint venture company owned by the Group and Hangzhou Metro Group Company Limited, with the Group owning 49% of equity interest. The joint venture company will be funded by a combination of debt and equity with the Group's equity investment being approximately RMB2.2 billion (HK$2.6 billion).

The Concession Agreement is subject to approval by relevant authorities in the Mainland of China.

H Investments in Europe and Australia

(i) Investment in London Overground Franchise

On 11 November 2007, London Overground Rail Operations Ltd ("LOROL"), the 50/50 partnership between the Group and DB Regio (UK) Limited, took over the operation of the new London Overground service in Greater London for a period of seven years with an option for a two-year extension.

Under the terms of the concession agreement, LOROL has provided a performance bond of GBP15 million (HK$181 million) to Transport for London ("TfL"). The performance bond is jointly and severally indemnified by the parent companies through parent company guarantees and may be called by TfL if the concession is terminated early as a result of default. As provided in the concession agreement, the bond was replaced by a new bond of GBP10.8 million (HK$130 million) in July 2010 after the successful commencement of the East London Line operations. This new bond is guaranteed by Deutsche Bahn, the ultimate parent company of DB Regio (UK) Limited, with the Company providing to Deutsche Bahn a counter indemnity that is further backed by a performance bond of GBP5.4 million (HK$65 million) for the Company's share of the guarantee.

As at 31 December 2010, an unsecured debt of GBP2 million (HK$24 million) with interest rate at 2.5% per annum above the published Bank of England base rate from time to time was provided equally by the Group and DB Regio (UK) Limited to LOROL (GBP1 million each). The final repayment date of this debt is on the date of expiry or the earlier termination of the term of the London Rail Concession under the concession agreement.

(ii) Investment in Stockholm Metro Franchise

On 2 November 2009, MTR Stockholm AB, the Company's wholly owned subsidiary in Sweden, took over the train and station operations as well as rolling stock maintenance of the Stockholm Metro in Sweden for a period of eight years with a possible extension for an additional period of six years. The servicing, maintenance and cleaning of trains are carried out by Tunnelbanan Teknik Stockholm AB, a joint venture company owned by the Group and Mantena AS with equal equity interests. MTR Stockholm AB leases the rolling stock, stations, office buildings, depots, depot equipment and other minor assets from the Stockholm transport authority ("SL"). On a back to back contract basis, MTR Stockholm AB leases the depots and depot equipment to Tunnelbanan Teknik Stockholm AB.

As at 31 December 2010, the Group's investment in MTR Stockholm AB comprised an equity investment of SEK40 million, an unsecured debt of SEK140 million (HK$162 million) at an interest rate of 3% above the 3-month Stockholm Inter Bank Offer Rate ("STIBOR") published by the Riksbank from time to time and with repayment due by 31 December 2013, and a capital contribution of SEK30 million which will be repaid if MTR Stockholm AB is able to distribute profits under the Swedish Company Act and its dividends to its shareholder(s) increase from one year to another.

In addition, MTR Stockholm AB and Mantena AS provided, based on their respective equity interest, senior debt of SEK100 million (HK$116 million) and subordinated debt of SEK30 million (HK$35 million) to Tunnelbanan Teknik Stockholm AB at an interest rate of 3% and 4% per annum respectively above the 3-month STIBOR.

Under the concession, the Group provides to SL a guarantee of SEK1,000 million (HK$1,157 million), which can be called if the concession is terminated early as a result of default by MTR Stockholm AB.

(iii) Investment in Melbourne Metropolitan Train Franchise

On 30 November 2009, Metro Trains Melbourne Pty. Ltd. ("MTM"), a company owned by the Group, United Rail Services Limited ("UGL") and John Holland Melbourne Rail Franchise Pty. Ltd. ("JHL") with the Group holding 60% of equity interest and UGL and JHL each holding 20% of interest, took over the operation and maintenance of the Melbourne metropolitan train network in Australia for an initial period of eight years with a renewal option up to an additional seven years.

Total investment in MTM is AUD65 million through a mixture of equity and shareholder loans. As at 31 December 2010, the Group's share of investment in MTM was AUD39 million, which comprised an equity investment of AUD9.75 million and a subordinated loan of AUD29.25 million (HK$232 million) at an interest rate of 7.5% per annum with final repayment at the date of expiry or the earlier termination of the concession.

The Group, UGL and JHL together provide to the State of Victoria Government a joint and several parent company guarantee of AUD125 million (HK$990 million) and a performance bond of AUD75 million (HK$594 million) for MTM's performance and other obligations under the franchise agreement, each bearing its share of liability based on its shareholdings in MTM.

58 Accounting Estimates and Judgements

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

(i) Estimated Useful Life and Depreciation of Property, Plant and Equipment

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

(ii) Impairment of Long-lived Assets

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

(iii) Pension Costs

The Group employs independent valuation professionals to conduct annual assessment of the actuarial position of the Group's retirement plans. The determination of the Group's obligation and expense for the defined benefit element of these plans is dependent on certain assumptions and factors provided by the Company, which are disclosed in notes 53A(i) and 53A(ii).

(iv) Revenue Recognition on Property Development

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

(v) Properties Held for Sale

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

(vi) Interest-free Loan to a Property Developer

The Group estimated the fair value of the interest-free loan to a developer at its present value discounted at the prevailing market rates of interest at inception.

(vii) Valuation of Investment Properties

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

(viii) Franchise in Hong Kong

The current franchise under which the Group is operating in Hong Kong allows it to run the mass transit railway system in Hong Kong until 1 December 2057. Pursuant to the terms stipulated in the new Operating Agreement with the Government, the Company considers that it has the legal right to extend the franchise for further periods of 50 years upon expiry of each franchise term (note 56I). The Group's depreciation policies (note 2I) in respect of certain assets' lives which extend beyond 2057 are on this basis.

(ix) Income Tax

Certain treatments adopted by the Group in its tax returns in the past years are yet to be finalised with the Hong Kong Inland Revenue Department. In assessing the Group's income tax and deferred taxation in the 2010 accounts, the Company has followed the tax treatments it has adopted in those tax returns, which may be different from the final outcome in due course.

(x) Project Provisions

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

(xi) Deferred Expenditure

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

(xii) Fair Value of Derivatives and Other Financial Instruments

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

58 Accounting Estimates and Judgements *(continued)*

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

(xiii) Obligations under Service Concession

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

B Critical Accounting Judgements in Applying the Group's Accounting Policies

(i) Provisions and Contingent Liabilities

The Group recognises provisions for liabilities of uncertain timing or amount when the Group has a legal or constructive obligation arising as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made. Where it is not probable that an outflow of economic benefits will be required, or the amount cannot be estimated reliably, the obligation is disclosed as contingent liability. As at 31 December 2010, the Group considered that it had no disclosable contingent liabilities as there were neither pending litigations nor events with potential obligation which were probable to result in material outflow of economic benefits to the Group.

(ii) Non-controlled Subsidiaries

The Group regards Octopus Holdings Limited and its subsidiaries (the "OHL Group") as non-controlled subsidiaries. In determining whether the Group has control over these subsidiaries, the Group has taken into account its voting right conferred to it under the Shareholder's Agreement of OHL and the effective influence it may exercise over the decision of OHL's Board. Throughout the year ended 31 December 2010, the Group considered that its voting right in the OHL Group has been maintained at 49% despite an equity interest of 57.4%. As such, the OHL Group of companies were accounted for as non-controlled subsidiaries in the Group's accounts.

59 Possible Impact of Amendments, New Standards and Interpretations Issued but Not Yet Effective for the Annual Accounting Period Ended 31 December 2010

Up to the date of issue of these accounts, the HKICPA has issued the following amendments, new standards and interpretations which are not yet effective for the year ended 31 December 2010 and which have not been adopted in these accounts.

	Effective for accounting periods beginning on or after
Amendments to HKAS 32, *Financial instruments: Presentation – Classification of rights issues*	1 February 2010
HK(IFRIC) 19, *Extinguishing financial liabilities with equity instruments*	1 July 2010
Amendment to HKFRS 1, *First-time Adoption of Hong Kong Financial Reporting Standards – Limited exemption from comparative HKFRS 7 disclosures for first-time adopters*	1 July 2010
Improvements to HKFRSs 2010	1 July 2010 or 1 January 2011
HKAS 24 (Revised), *Related party disclosures*	1 January 2011
Amendment to HK(IFRIC) 14, HKAS 19 – *The limit on a defined benefit asset, minimum funding requirements and their interaction*	1 January 2011
Amendments to HKAS 12, *Income Taxes – Deferred tax: Recovery of underlying assets*	1 January 2012
HKFRS 9, *Financial instruments*	1 January 2013

The Group is in the process of making an assessment of what the impact of these amendments, new standards and new interpretations is expected to be in the period of initial application. HKFRS 9 addresses the classification and measurement of financial assets and liabilities and the adoption of it is expected to have impact on the Group's results of operations and financial position. Amendments to HKAS 12 introduce a rebuttable presumption on the measurement of deferred tax on investment properties carried at fair value and the adoption of it is expected to result in the retrospective derecognition of deferred tax liabilities in relation to the change in value of investment properties upon first adoption. Such derecognition, if measured at 31 December 2010, would amount to HK$4,764 million. HKAS 24 (Revised) amends the disclosure requirements applicable to government-related entities and the adoption of it is expected to result in amended disclosures. Other than these three new issue or amendments, it has concluded so far that the adoption of other new issues or amendments is unlikely to have a material impact on the Group's results of operations and financial position.

60 Approval of Accounts

The accounts were approved by the Board on 3 March 2011.

Glossary

Airport Express	Train Service provided between AsiaWorld-Expo Station and Hong Kong Station
Appointed Day or Day One or Merger Date	2 December 2007 when the Rail Merger was completed
Articles of Association	The articles of association of the Company
Board	The board of directors of the Company
Bus	Feeder bus services operated in support of West Rail Line, East Rail Line and Light Rail
Company or MTR Corporation	MTR Corporation Limited 香港鐵路有限公司, a company which was incorporated under the Companies Ordinance on 26 April 2000
Companies Ordinance	The Companies Ordinance (Chapter 32 of the Laws of Hong Kong)
Computershare	Computershare Hong Kong Investor Services Limited
Cross-boundary Service or Cross-boundary	Journeys with the destination to / commencing from Lo Wu and Lok Ma Chau stations
Customer Service Pledge	Annually published performance targets in accordance with the Operating Agreement
Director or Member of the Board	A member of the Board
Domestic Service	Collective name for Kwun Tong, Tsuen Wan, Island, Tung Chung, Tseung Kwan O, Disneyland Resort, East Rail (excluding Cross-boundary Service), West Rail and Ma On Shan lines
FSI	The Financial Secretary Incorporated, a corporation solely established under the Financial Secretary Incorporation Ordinance (Chapter 1015 of the Laws of Hong Kong)
Government	The Government of the Hong Kong SAR
Group	The Company and its subsidiaries
HKSE or Stock Exchange	The Stock Exchange of Hong Kong Limited
Hong Kong or Hong Kong SAR or HKSAR	The Hong Kong Special Administrative Region of the People's Republic of China
Intercity	Intercity passenger services operated between Hong Kong and certain major cities in the Mainland of China such as Guangzhou, Beijing and Shanghai
Interest Cover	Operating profit before depreciation, amortisation and variable annual payment arising from the Rail Merger divided by gross interest and finance charges before capitalisation and accreted interest on loan to a property developer
KCRC	Kowloon-Canton Railway Corporation
Kowloon Southern Link	Project for extension of the West Rail Line from Nam Cheong Station to East Tsim Sha Tsui Station via Austin Station, providing direct access between the East Rail Line and West Rail Line after the completion of the project
Light Rail	Light rail system serving North West New Territories
Listing Rules	The Rules Governing the Listing of Securities on the Stock Exchange
Mainland or Mainland China or Mainland of China	The People's Republic of China excluding Hong Kong SAR
MTR Ordinance	The Mass Transit Railway Ordinance (Chapter 556 of the Laws of Hong Kong)
Net Debt-to-equity Ratio	Loans and other obligations, bank overdrafts, obligations under service concession and loan from holders of non-controlling interests net of cash, bank balances and deposits, and investment in bank medium term notes in the consolidated balance sheet as a percentage of the total equity
Operating Agreement	The agreement entered into by the Company and the Government on 30 June, 2000 for the operation of our rail services before the Rail Merger and a new agreement entered on 9 August 2007 for the operation of all of our rail and bus passenger services after the Rail Merger
Operating Margin	Operating profit from railway and related businesses before depreciation, amortisation and variable annual payment arising from the Rail Merger as a percentage of turnover
Ordinary Shares	Ordinary shares of HK$1.00 each in the capital of the Company
Rail Merger or Merger	The merger of the rail operations of MTR Corporation and KCRC and the acquisition of certain property interests by MTR Corporation from KCRC, full details of which are set out in the Rail Merger Circular. The Rail Merger was completed on 2 December 2007
Rail Merger Bill or Rail Merger Ordinance	The Rail Merger Bill refers to the draft legislation on the Rail Merger which was passed by the Legislative Council of Hong Kong on 8 June 2007 and became the Rail Merger Ordinance (Ordinance No.11 of 2007)
Rail Merger Circular	Refers to the circular dated 3 September 2007 despatched to the Company's shareholders in connection with the Rail Merger
Return on Average Equity Attributable to Equity Shareholders	Profit attributable to equity shareholders of the Company as a percentage of the average of the beginning and closing total equity attributable to equity shareholders of the Company of the period
Service Concession	A contract to provide services for a particular period which is awarded by a public sector entity to an operator; in the context of concession projects in Hong Kong, service concession refers to the concession granted or to be granted by KCRC and/or Government to the Company to operate, maintain and renew certain railway lines under the Service Concession Agreement or a Supplemental Service Concession Agreement, as more particularly described in the Rail Merger Circular; in the context of concession projects in the Mainland of China and Overseas, service concession refers to the concession granted by the government or relevant public sector entity to a subsidiary or associate of the Company to provide certain specified services for a specified period under a negotiated concession agreement.
Service Quality Index	A measure of customer satisfaction for the services provided by Domestic / Cross-boundary services and Airport Express based on the service attributes (excluding fares) weighted by the corresponding importance rating from the customer research

Shareholder Services

Any matters relating to your shareholding, such as transfer of shares, change of name or address, and loss of share certificates should be addressed in writing to the Registrar:

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