The consolidated financial statements of the Company and its subsidiaries prepared under IFRS differ in certain respects from those prepared under generally accepted accounting principles in the United States of America ("US GAAP"). Significant differences between IFRS and US GAAP, which affect the equity and net profit of the Company and its subsidiaries, are summarised below:

(a) Effect of the Acquisition of Entities under Common Control

Under IFRS, the Company and its subsidiaries adopted the acquisition method to account for the acquisition of 70% equity interest in Shidongkou I Power Plant, 70% equity interest in Taicang Power Company and all of the assets and liabilities of Changxing Power Plant in July, 2002 and the acquisition of 55% equity interest in Qinbei Power Company, 60% equity interest in Yushe Power Company and all of the assets and liabilities of Xindian Power Plant in October, 2003. Under the acquisition method, the results of the acquired businesses are included in the results of operations of the Company and its subsidiaries from the date of the acquisition. The difference between the purchase consideration and the fair value of the underlying net assets acquired is treated as goodwill and amortized on a systematic basis to the income statement over its useful economic life, being the remaining weighted average useful life of the acquired depreciable or amortizable assets.

As the Company and its subsidiaries, Shidongkou I Power Plant, Taicang Power Company, Changxing Power Plant, Qinbei Power Company, Yushe Power Company, and Xindian Power Plant were under the common control of the Huaneng Group prior to the acquisition, under US GAAP, the acquisition is considered to be a transfer of businesses under common control and the acquired assets and liabilities are accounted for at historical cost in a manner similar to the pooling of interests method. Accordingly, the consolidated financial statements for all periods presented have been retroactively restated as if the current structure and operations resulting from the acquisition had been in existence since the beginning of the earliest period presented, with financial data of previously separate entities combined. The cash consideration paid by the Company is treated as an equity transaction in the year of the acquisition for US GAAP purposes. Accordingly, the resulting impact of depreciation and amortization expenses on income is also different.

(b) Effect of Acquisition of 30% Additional Equity Interests in Shidongkou I Power Plant, 5% Additional Equity Interests in Taicang Power Company and 44.16% Equity Interests in Huaiyin Power Company.

On 1st July, 2002, the Company acquired 44.16% equity interests of Huaiyin Power Company from Huaneng Group. In addition, the Company also acquired 30% additional equity interests of Shidongkou I Power Plant and 5% additional equity interests of Taicang Power Company from Huaneng Group on 31st December 2002.

Under IFRS, upon the completion of the above acquisitions, the relevant equity interests of net assets of Shidongkou I Power Plant, Taicang Power Company and Huaiyin Power Company are recorded at fair value. The excess of the total cost of the acquisition over the fair value of the relevant portion of net assets of power plant acquired is recorded as goodwill. Such goodwill is amortized on a systematic basis to the income statement over its useful economic life, being the remaining weighted average useful life of the acquired depreciable or amortizable assets. Under US GAAP, upon completion of the above acquisitions, Huaneng Group's proportionate share in the net assets of Shidongkou I Power Plant, Taicang Power Company and Huaiyin Power Company being sold to the Company was recorded at the historical carrying value. The excess of the total cost of acquisition over the net assets acquired was recorded as a reduction of deemed capital contribution to the Company. Accordingly, the resulting impact of depreciation and amortization expenses on income is also different.

(c) Housing Benefits Provided by HIPDC

HIPDC sold to certain qualified employees of the Company living quarters owned by HIPDC at preferential prices. The difference between the cost of living quarters and the sales proceeds received from the employees is considered to be housing benefits. Under IFRS, such housing benefits provided by HIPDC are not reflected in the financial statements of the Company. Under US GAAP, the amount of housing benefits provided by HIPDC to the employees of the Company are recognized as the Company's operating expenses on a straight-line basis over the estimated remaining average service life of the employees. The corresponding amount is recorded as an addition of capital contribution from HIPDC.

(d) Acquisition of Shandong Huaneng

Huaneng Group is the controlling parent company of HIPDC, which in turn is the controlling parent of the Company. Huaneng Group used to be one of the substantial shareholders of Shandong Huaneng, holding 33.09% equity interest in it before the Company's acquisition of Shandong Huaneng. Under IFRS, upon the completion of the acquisition of Shandong Huaneng, the entire net assets of Shandong Huaneng were recorded at fair value. The excess of the fair value of the entire net assets acquired over the total cost of the acquisition was recorded as negative goodwill. Under US GAAP, upon completion of the acquisition of Shandong Huaneng, Huaneng Group's proportionate share of 33.09% in the net assets of Shandong Huaneng being transferred to the Company was recorded at the historical carrying value. The excess of the proportionate share in the book value of the net assets acquired over the relevant portion of the cash consideration was recorded as a capital contribution to the Company. The book value of the remaining 66.91% of the net assets continues to be part of the recoverable rate base under the cost recovery formula of the tariff setting mechanism. Under US GAAP, the difference between these net asset values and the cash consideration was recorded as a reduction to the property, plant and equipment value of the respective power plants.

As the amount of negative goodwill under IFRS is different from the amount of the reduction to property, plant and equipment under US GAAP due to the 33.09% portion of the net assets previously owned by Huaneng Group as described above and also that the negative goodwill under IFRS is recognized as income over the remaining weighted average useful life of the acquired depreciable or amortizable assets whereas, for US GAAP purpose, the property, plant and equipment, after the reduction described above, are depreciated over the respective assets' useful life, the net income under IFRS and US GAAP is different.

(e) Accounting Treatment of Convertible Notes

Under IFRS, the proceeds received on the issue of the convertible notes were allocated into liability and equity components. Upon initial recognition, the liability component represented the present value, at the issuance date, of the contractually determined stream of cash flows discounted at the market interest rate for instruments of comparable credit status providing substantially the same cash flows, on the same terms, but without the conversion option. The equity component was then determined by deducting the liability component from the proceeds received on the issue of the notes. Under US GAAP, the entire proceeds of the issue of convertible notes were recorded as a liabilities without distinguishing between the equity and liability components.

In accordance with IAS 39, the put option of the convertible notes, which allowed the noteholders to redeem the convertible notes at a premium, was separated from the host contract and accounted for as an embedded derivative. This put option was recorded as a liability and measured at its fair value. When IAS 39 was initially applied in 2001, the difference between the previous carrying amount and the fair value of the put option was recognised as an adjustment to the opening retained earnings as at 1st January, 2001. In addition, the liability component was measured at amortized cost and the resulting difference with the previous carrying amount was recognized as an adjustment to the opening retained earnings as at 1st January, 2001. After initial recognition, subsequent changes in the value of the put option and the amortized cost of the liability component were charged or credited to the income statements.

Under US GAAP, it is permitted not to measure the put option separately at its fair value, as it represents a derivative embedded in a pre-1998 hybrid instrument. The Company continued to accrue for the put premium liability together with the interest payable on the notes using effective interest rate of 6.66% up to the redemption date of 21st May, 2002. On 21st May, 2002, a portion of the convertible notes was not redeemed by the noteholders. Under US GAAP, the relevant portion of the accrued put premium attributable to the remaining convertible notes not redeemed was amortized as a yield adjustment over the remaining term of the convertible notes because the put price exceeded the market value of the ordinary shares of the Company at the time of the redemption.

(f) Capitalization of Borrowing Costs

In accordance with IAS 23, the Company capitalized interests on general borrowings used for the purpose of obtaining a qualifying asset in addition to the capitalization of interest on specific borrowings.

Under US regulatory accounting requirements, interest on funds borrowed generally and used for the purpose of obtaining a qualifying assets are not capitalized if such interests cannot be taken into consideration when determining the recoverable rate base for tariff setting purposes. Consequently, under US GAAP, the Company did not capitalize interest on general borrowings.

(g) Reversal of goodwill amortization

Under IFRS, goodwill is amortized using the straight-line method over its estimated useful life and recognized in the income statement as other operating expenses. Under US GAAP, in accordance with Statement of Financial Accounting Standard Number 142 “Goodwill and Other Intangible Assets”, goodwill is not amortized but tested for impairment on an annual basis and between annual tests in certain circumstances.

(h) Deferred Tax Impact

This represents deferred tax effect on the above GAAP differences where applicable.

(i) US Regulatory Accounting

Under US GAAP, Statement of Financial Accounting Standard Number 71 "Accounting for the Effects of Certain Types of Regulation" ("SFAS 71") is applicable to utilities in the United States whose regulators have the power to approve and/or regulate rates that may be charged to customers. SFAS 71 recognizes that the regulatory process produces economic effects which should be reflected in the financial statements. Because revenues are based on costs, SFAS 71 governs the period in which various costs are included in the income statements with the objective of matching costs with revenues. Provided that, through the rate setting process, the utility is substantially assured of recovering its allowable costs by the collection of revenue from its customers, such costs not yet recovered are deferred as regulatory assets. The regulatory process may also impose a liability on a rate-regulated enterprise, usually representing obligations to the enterprise's customers, which should be recognized as a regulatory liability.

In order to apply SFAS 71, three criteria must be met. These criteria require that a) the power rates for regulated services or products provided to customers be established by or are subject to approval by an independent, third-party regulator or by an entity's own governing board empowered by statute or contract to establish power rates that bind customers; b) the regulated power rates are designed to recover the costs of providing the regulated services or products; and c) in view of the demand for the regulated services or products and the level of competition, direct and indirect, it is reasonable to assume that power rates, which are set at levels that will recover costs, can be charged to and collected from customers; this criterion requires consideration of anticipated changes in levels of demand or competition during the recovery period for any capitalized costs.

The Company and its subsidiaries believe that all of their power plants meet these specific criteria of SFAS 71 with the exception of the Shidongkou I Power Plant, the Taicang Power Company, the Huaiyin Power Company, the Changxing Power Plant, the Qinbei Power Company, Yushe Power Company and Xindian Power Plant acquired in 2002 and 2003 (the "power plants acquired in 2002 and 2003"). Firstly, the power rates are established by an independent regulator, the provincial or local price bureau. Secondly, the pricing policy applicable to the power plants provides for rate-setting based on the specific costs of the power plants. This process has operated historically and will continue under the pricing policy. Finally, based on the significant demand for electricity in the Company and its subsidiaries' service territory, it is reasonable to assume that the authorized power rates will be collected from customers.

With respect to the power plants acquired in 2002 and 2003, these criteria mentioned above are not met and, therefore, SFAS71 cannot be applied. Consequently, the power plants acquired in 2002 and 2003 have adopted US GAAP without specific reference to the regulatory basis of accounting provided for under SFAS71.

Under IFRS, as there is no equivalent regulatory accounting standard, the Company's and its subsidiaries' policy is to recognize regulatory assets established under SFAS 71 only where they comprise rights or other access to future economic benefits as a result of past events; or to recognize regulatory liabilities only where they comprise a present obligation the settlement of which is expected to result in an outflow of resources embodying economic benefits.

For the year ended 31st December, 2003, there was no material difference in the recognition of both regulatory and non-regulatory assets and liabilities between IFRS and US GAAP.

Differences between IFRS and US GAAP which affect the net assets and net profit of the Company and its subsidiaries are summarized below:

	Note	Net Assets As at December 31, 2003 Rmb'000	As at December 31, 2002 Rmb'000
Net assets under IFRS		**33,955,355**	30,416,060
Impact of US GAAP adjustments *Note i:*			
Effect of acquisition of Qinbei Power Company, Yushe Power Company and Xindian Power Plant	*(a)*	**(417,368)**	97,690
Effect of acquisition of Shidongkou I Power Plant, Taicang Power Company and Changxing Power Plant	*(a)*	**(886,116)**	(998,752)
Effect of acquisition of 30% additional equity interests in Shidongkou I Power Plant, 5% additional equity interests in Taicang Power Company and 44.16% equity interests in Huaiyin Power Company	*(b)*	**(296,717)**	(313,859)
Recording of capital contribution arising from acquisition of Shandong Huaneng	*(d)*	**862,922**	862,922
Difference in accounting treatment for acquisition of Shandong Huaneng	*(d)*	**(261,273)**	(174,182)
Adjustments on convertible notes			
- Reversal of equity component of the convertible notes	*(e)*	**(510,506)**	(510,506)
- Reversal of adjustment relating to the convertible notes arising form the initial adoption of IAS 39	*(e)*	**463,921**	463,921
- Difference in accounting treatment of convertible notes	*(e)*	**37,933**	5,246
Difference in capitalization of borrowing costs	*(f)*	**(93,890)**	(88,412)
Reversal of goodwill amortization			
- Reversal of goodwill amortization of equity investment in SEG	*(g)*	**54,639**	—
- Reversal of goodwill amortization of investment in Huaiyin Power Company	*(g)*	**17,370**	—
Applicable deferred tax impact of the above GAAP differences	*(h)*	**200,674**	261,147
Net assets under US GAAP *Note i*		**33,126,944**	30,021,275

	Note	Net profit For the year ended December 31, 2003 Rmb'000	2002 Rmb'000	2001 Rmb'000
Net profit under IFRS		**5,430,408**	3,921,004	3,450,658
Impact of US GAAP adjustments *Note i*:				
Effect of acquisition of Qinbei Power Company, Yushe Power Company and Xindian Power Plant	*(a)*	**13,109**	56,919	(42,789)
Effect of acquisition of Shidongkou I Power Plant, Taicang Power Company and Changxing Power Plant	*(a)*	**112,636**	126,498	234,127
Effect of acquisition of 30% additional equity interests in Shidongkou I Power Plant, 5% additional equity interests in Taicang Power Company and 44.16% equity interests in Huaiyin Power Company	*(b)*	**19,347**	10,556	—
Recording housing benefits provided by HIPDC	*(c)*	**(26,152)**	(26,152)	(26,152)
Difference in accounting treatment for acquisition of Shandong Huaneng	*(d)*	**(87,091)**	(87,091)	(87,091)
Difference in accounting treatment of convertible notes	*(e)*	**25,434**	5,116	—
Difference in capitalization of borrowing costs	*(f)*	**(5,478)**	(88,412)	—
Reversal of goodwill amortization				
- Reversal of goodwill amortization of equity investment in SEG	*(g)*	**54,639**	—	—
- Reversal of goodwill amortization of investment in Huaiyin Power Company	*(g)*	**17,370**	—	—
Applicable deferred tax impact of the above GAAP differences	*(h)*	**(84,181)**	33,674	—
Net profit under US GAAP *Note i*		**5,470,041**	3,952,112	3,528,753
Basic earnings per ordinary share under US GAAP (Rmb) *Note ii*		**0.91**	0.66	0.62
Basic earnings per ADS under US GAAP (Rmb) *Note ii*		**36.35**	26.35	24.79
Diluted earnings per ordinary share under US GAAP (Rmb) *Note ii*		**0.90**	0.65	0.61
Diluted earnings per ADS under US GAAP (Rmb) *Note ii*		**36.18**	25.99	24.32

(Note i) Consistent with applying the accounting treatment under US GAAP as described in Note (a) above, the consolidated financial statements under US GAAP for prior periods presented have been retroactively restated as if the current structure and operations resulted from the acquisition of the Qinbei Power Company, the Yushe Power Company and the Xindian Power Plant had been in existence since the beginning of the earliest period presented.

(Note ii) Earning per ordinary shares and per equivalent ADS were calculated by dividing the net profit for the financial year under US GAAP by the weighted average number of ordinary shares and ADS in issue during the financial year. On a diluted basis, both net profit for the financial year and the weighted average number of ordinary shares and ADS outstanding for the financial year were adjusted on the assumption that the convertible notes had been fully converted at the beginning of the year.

In preparing the summary of difference between IFRS and US GAAP, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Accounting estimates have been employed in these financial statements to determine reported amounts, including realizability, useful lives of assets and other areas. Actual results could differ from those estimates.

The following are condensed consolidated balance sheets of the Company and its subsidiaries as at 31st December, 2002 and 2003, and the related condensed consolidated statements of income, changes in shareholders' equity and cash flows for each of the years in the three-year period ended 31st December, 2003, restated to reflect the impact of the effect of the acquisition of entities under common control which is accounted for at historical cost in a manner similar to the pooling of interests method, with financial data of previously separate entities combined, under US GAAP and other differences between IFRS and US GAAP.

Condensed Combined Balance Sheets

	As at 31st December, 2003 Rmb'000	2002 Rmb'000
ASSETS		
Non-current assets		
Property, plant and equipment, net	**40,042,558**	40,207,383
Investment in associates	**2,820,669**	200,960
Deferred tax assets	**210,455**	249,804
Land use rights and other assets	**1,292,849**	1,322,828
Goodwill	**78,726**	63,754
Total non-current assets	**44,445,257**	42,044,729
Current assets		
Inventories, net	**800,281**	964,468
Other receivables and assets, net	**259,421**	269,488
Accounts receivable	**2,804,026**	2,514,975
Due from related parties	**5,862**	—
Restricted cash	**159,961**	13,259
Temporary cash investments	**144,996**	1,362,065
Cash and cash equivalents	**4,128,648**	3,145,452
Total current assets	**8,303,195**	8,269,707
Total assets	**52,748,452**	50,314,436

	As at 31st December, 2003 Rmb'000	2002 Rmb'000
EQUITY AND LIABILITIES		
Shareholders' equity	33,126,944	30,021,275
Minority interests	1,125,259	957,224
Non-current liabilities		
Convertible notes	—	166,498
Accrued put premium on convertible notes	—	30,841
Long-term loans from shareholders	—	404,891
Long-term bank loans	8,305,320	9,114,651
Other long-term loans	848,284	671,027
Other financial liabilities	—	19,397
Deferred tax liabilities	91,584	110,510
Total non-current liabilities	9,245,188	10,517,815
Current liabilities		
Accounts payable and accrued liabilities	3,342,517	4,021,982
Taxes payable	917,362	680,692
Due to HIPDC	87,508	100,475
Due to other related parties	27,338	—
Staff welfare and bonus payable	220,896	233,566
Short-term loans	1,600,000	1,266,686
Current portion of long-term loans from shareholders	388,875	404,891
Current portion of long-term bank loans	2,409,240	1,946,732
Current portion of other long-term loans	243,386	163,098
Convertible notes	952	—
Accrued put premium for convertible notes	8,636	—
Other financial liabilities	4,351	—
Total current liabilities	9,251,061	8,818,122
Total liabilities and equity	52,748,452	50,314,436

Condensed Combined Statements of Income

	Year ended 31st December, 2003 Rmb'000	2002 Rmb'000	2001 Rmb'000
Operating revenue, net	**24,142,713**	20,834,089	19,151,816
Operating expenses:			
Fuel	**(9,374,408)**	(8,007,244)	(6,639,223)
Maintenance	**(971,282)**	(746,138)	(966,985)
Depreciation	**(4,067,809)**	(3,609,605)	(3,531,839)
Labor	**(1,532,605)**	(1,267,136)	(1,135,627)
Service fees to HIPDC	**(230,792)**	(263,716)	(307,322)
Income tax	**(1,276,478)**	(1,043,675)	(882,465)
Others	**(706,802)**	(972,610)	(910,127)
Total operating expenses	**(18,160,176)**	(15,910,124)	(14,373,588)
Income before financial expenses	**5,982,537**	4,923,965	4,778,228
Interest income	**53,884**	88,157	120,146
Interest expense	**(610,278)**	(810,879)	(1,154,827)
Exchange losses, net	**(30,929)**	(33,131)	(42,578)
Total financial expenses	**(587,323)**	(755,853)	(1,077,259)
Share of profit (loss) of associates	**266,730**	(1,634)	(5,381)
Minority interests	**(191,903)**	(214,366)	(166,835)
Net profit attributable to the shareholders	**5,470,041**	3,952,112	3,528,753

Condensed Combined Statements of Changes in Shareholders' Equity

	Rmb'000
Balance as at 1st January, 2001	23,991,504
Dividend relating to 2000	(1,243,000)
Net profit attributable to shareholders for the year ended 31st December, 2001	3,528,753
Capital contribution arising from acquisition of Shandong Huaneng	862,922
Capital contribution from HIPDC arising from housing benefits provided by HIPDC	26,152
Issuance and sale of 350,000,000 new Domestic Shares, net of direct issuance cost	2,770,058
Distribution to Huaneng Group	(146,546)
Balance as at 31st December, 2001	29,789,843
Dividends relating to 2001	(1,800,000)
Net profit attributable to shareholders for the year ended 31st December, 2002	3,952,112
Conversion of convertible notes to new ordinary shares	1,655
Net deemed capital distribution to Huaneng Group arising from the acquisition of the equity interests of the Shidongkou I Power Plant, Taicang Power Company, Huaiyin Power Company and Changxing Power Plant and additional interests in Shidongkou I Power Plant and Taicang Power Company	(2,034,222)
Contribution from Huaneng Group	85,735
Capital contribution from HIPDC arising from housing benefits provided by HIPDC	26,152
Balance as at 31st December, 2002	30,021,275
Dividends relating to 2002	(2,049,408)
Net profit attributable to shareholders for the year ended 31st December, 2003	5,470,041
Conversion of convertible notes to new ordinary shares	165,548
Net deemed capital distribution to Huaneng Group arising from the acquisition of the equity interests of the Qinbei Power Company, Yushe Power Company and Xindian Power Plant	(506,664)
Capital contribution from HIPDC arising from housing benefits provided by HIPDC	26,152
Balance as at 31st December, 2003	33,126,944

Condensed combined statements of cash flows

	Year ended 31st December, 2003 Rmb'000	2002 Rmb'000	2001 Rmb'000
Net cash provided by operating activities	**9,655,472**	7,820,762	6,528,209
Net cash (used in)/provided by investing activities	**(5,904,727)**	2,077,754	(5,340,464)
Net cash used in financing activities	**(2,767,549)**	(9,239,037)	(1,129,337)
Net increase in cash and cash equivalents	**983,196**	659,479	58,408
Cash and cash equivalents, beginning of year	**3,145,452**	2,485,973	2,427,565
Cash and cash equivalents, end of year	**4,128,648**	3,145,452	2,485,973

Statement of Comprehensive Income

Under US GAAP, certain items shown as components of common equity must be more prominently reported in a separate statement as components of comprehensive income. However, for each of the year in the three-year period ended 31st December, 2003, apart from the net income, there was no other comprehensive income which should be included in the statement of comprehensive income.

New Accounting Pronouncements

In 2003, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 149, Amendment of Statement 133 on Derivative Instruments and Hedging Activities ("SFAS 149"), Statement of Financial Accounting Standards No. 150, Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity ("SFAS 150") and FASB Interpretation No.46, Consolidation of Variable Interest Entities ("FIN 46").

SFAS 149 amends and clarifies financial accounting and reporting for derivative instruments, including certain derivative instruments embedded in other contracts (collectively referred to as derivatives) and for hedging activities under FASB Statement No. 133, Accounting for Derivative Instruments and Hedging Activities. SFAS 149 is effective for contracts entered into or modified after 30th June, 2003. The Company considered the effects of adoption SFAS 149 and do not expect any material impact on the financial statements.

SFAS 150 establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. It requires that an issuer classify a financial instrument that is within its scope as a liability (or an asset in some circumstances). Many of those instruments were previously classified as equity. Some of the provisions of this Statement are consistent with the current definition of liabilities in FASB Concepts Statement No. 6, Elements of Financial Statements. The remaining provisions of this Statement are consistent with the Board's proposal to revise that definition to encompass certain obligations that a reporting entity can or must settle by issuing its own equity shares, depending on the nature of the relationship established between the holder and the issuer. In addition, SFAS 150 concludes the first phase of the Board's redeliberations of the Exposure Draft, Accounting for Financial Instruments with Characteristics of Liabilities, Equity, or Both. SFAS 150 is effective for financial instruments entered into or modified after 31st May, 2003, and otherwise is effective at the beginning of the first interim period beginning after 15th June, 2003, except for mandatorily redeemable financial instruments of nonpublic entities. The Company considered the effects of adoption SFAS 150 and do not expect any material impact on the financial statements.

FIN 46 provides guidance on the identification of and financial reporting for entities over which controls is achieved through means other than voting rights. This interpretation requires existing unconsolidated variable interest entities to be consolidated by their primary beneficiaries if the entities do not effectively disperse risks among parties involved. FIN 46 applies immediately to variable interest entities created after 31st January, 2003, and to variable interest entities in which an enterprise obtains an interest after that date. It applies in the first fiscal year or interim period beginning after 15th June, 2003, to variable interest entities in which an enterprise holds a variable interest that it acquired before 1st February, 2003. The Company considered the effects of adoption FIN 46 and do not expect any material impact on the financial statements.