

## CORPORATE GOVERNANCE

### CORPORATE GOVERNANCE REPORT

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#### CORPORATE GOVERNANCE PRACTICES

The board of directors (the “Board”) of Tristate Holdings Limited (the “Company”) believes in the importance of effective corporate governance, both internally and externally. Internally, it improves the Company’s internal communications, enhances departments’ efficiency and speeds up management’s decision making process. Externally, it strengthens the Company’s competitiveness and increases confidence among shareholders, investors, customers and other stakeholders.

Throughout the year ended 31 December 2005, the Company has complied with code provisions set out in the Code on Corporate Governance Practices (the “Code”) contained in Appendix 14 of the Rules Governing the Listing of Securities (the “Listing Rules”) on The Stock Exchange of Hong Kong Limited (the “Hong Kong Stock Exchange”), except for the deviations from code provisions A.2.1, A.4.1 and A.4.2 of the Code. Actions for compliance with code provisions A.4.1 and A.4.2 of the Code were taken during the year resulting in compliance with code provision A.4.1 in 2005 and code provision A.4.2 in 2006. Details of the deviations are explained in the following relevant paragraphs.

Included in this report is the information relating to corporate governance practices of the Company during the year ended 31 December 2005 and significant events after that date and up to the date of this report.

#### BOARD OF DIRECTORS

In January 2005, the Company formalised in writing the functions and responsibilities reserved to the Board and those delegated to the management. It is clearly set out that the Board is mainly responsible for setting and approving the Company’s strategic direction and planning and all important matters including the preparation of interim and annual results (including the determination of dividends) annual financial budget and business and operation plans. In addition, each member of the Board is expected to make a full and active contribution to the Board’s affairs and ensure that the Board acts in the best interests of the Company and its shareholders as a whole.

Matters explicitly reserved for the Board’s decision include, amongst other things, (i) the size, composition, structure and role of the Board and the Board committees, (ii) the suitability of any individual as a member of the Board or the Board committee, (iii) the appointment and removal of the Chief Executive Officer (“CEO”), and (iv) monitoring the performance of the CEO to ensure the Company and its subsidiaries (collectively the “Group”) are in alignment with the Group’s strategic direction. Responsibility for delivering the Company’s objectives and running the business on a day-to-day basis is delegated to the senior management.

As at the date of this report, the Board comprises of one executive Director, Mr. WANG Kin Chung, Peter, who is also the Chairman and the CEO, four non-executive Directors, Ms. WANG KOO Yik Chun, Ms. Leslie TANG SCHILLING, Ms. MAK WANG Wing Yee, Winnie and Dr. WANG Shui Chung, Patrick and three independent non-executive Directors, Mr. YUAN Ching Man, James, Mr. LO Kai Yiu, Anthony and Mr. James Christopher KRALIK. Biographies of the Directors are set out in the “Directors’ and Senior Management’s Profile” section of the Annual Report.

The Company has been maintaining the number of independent non-executive Directors at not less than one-third of the number of the Board members since September 2004. The independent non-executive Directors are explicitly identified in all corporate communications.

Ms. WANG KOO Yik Chun, the Honorary Chairlady of the Company and a non-executive Director, is the mother of Mr. WANG Kin Chung, Peter (the Chairman and the CEO), Ms. MAK WANG Wing Yee, Winnie (non-executive Director) and Dr. WANG Shui Chung, Patrick (non-executive Director).

During the year ended 31 December 2005 and up to the date of this report, the Board includes three independent non-executive Directors. Mr. LO Kai Yiu, Anthony, one of the independent non-executive Directors, is qualified as a chartered accountant with the Canadian Institute of Chartered Accountants and is a member of the Hong Kong Institute of Certified Public Accountants. In addition to his professional accounting experience of more than eight years, he has over 25 years of experience in investment banking and other financial services.

The Company has received annual confirmations from all independent non-executive Directors that they did not have any business or financial interest with the Group and were independent as at 31 December 2005 in accordance with rule 3.13 of the Listing Rules. The Company considers that all the existing independent non-executive Directors are independent.

During the year ended 31 December 2005, four regular and one special Board meetings have been held. In addition, a board committee ("Project Board Committee") and an independent board committee ("Project Independent Board Committee") were formed in August 2005 for the purposes of the major and connected transaction relating to the acquisitions of additional interest in Hua Thai Manufacturing Public Company Limited ("Hua Thai") (the "Acquisitions"). The Project Board Committee comprised Mr. WANG Kin Chung, Peter, the executive Director; Mr. YUAN Ching Man, James, Mr. LO Kai Yiu, Anthony and Mr. James Christopher KRALIK, the independent non-executive Directors; and Ms. Eleni WANG, the President and Chief Operating Officer who is also the Chairlady of the Project Board Committee. The Project Independent Board Committee comprised Mr. LO Kai Yiu, Anthony, the Chairman of such committee, Mr. YUAN Ching Man, James and Mr. James Christopher KRALIK, all being the independent non-executive Directors. Terms of reference of the Project Board Committee and the Project Independent Board Committee were approved by the Board in August 2005. Project Board Committee held five Board committee meetings and Project Independent Board Committee held four Board committee meetings during the year of 2005.

The attendance of each Director during the year at Board meetings and Board committee meetings, the annual general meeting (“2005 AGM”) and the special general meeting for approving the Acquisition (“SGM”) is set out below: —

	Meetings attended/held						2005 AGM	SGM
	Board	Audit Committee (as defined below)	Remuneration Committee (as defined below)	Project Board Committee	Project Independent Board Committee			
<b>Executive Director:</b>								
WANG Kin Chung, Peter	5/5	N/A	2/2	1/5	N/A	1/1	1/1	
— Chairman and CEO						Note 1		
— member of Remuneration Committee								
— member of Project Board Committee								
WU Ching Her (resigned on 26 January 2005)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
<b>Non-executive Directors:</b>								
WANG KOO Yik Chun	4/5	N/A	N/A	N/A	N/A	1/1	1/1	
— Honorary Chairlady								
Leslie TANG SCHILLING	4/5	N/A	N/A	N/A	N/A	0/1	1/1	
MAK WANG Wing Yee, Winnie	5/5	4/4	2/2	N/A	N/A	0/1	0/1	
— Chairlady of Remuneration Committee						Note 1		
— member of Audit Committee								
WANG Shui Chung, Patrick	3/5	N/A	N/A	N/A	N/A	0/1	0/1	
<b>Independent Non-executive Directors:</b>								
YUAN Ching Man, James	5/5	4/4	2/2	5/5	4/4	0/1	1/1	
— member of Audit Committee								
— member of Remuneration Committee								
— member of Project Board Committee								
— member of Project Independent Board Committee								
LO Kai Yiu, Anthony	5/5	4/4	2/2	5/5	4/4	1/1	0/1	
— Chairman of Audit Committee							Note 2	
— member of Remuneration Committee								
— member of Project Board Committee								
— Chairman of Project Independent Board Committee								
James Christopher KRALIK	5/5	N/A	2/2	5/5	4/4	0/1	1/1	
— member of Remuneration Committee								
— member of Project Board Committee								
— member of Project Independent Board Committee								

N/A: Not applicable

Notes:

1. Mr. WANG Kin Chung, Peter also acted as the delegate of Ms. MAK WANG Wing Yee, Winnie, the Chairlady of Remuneration Committee.
2. Conference telephone arrangement was made for the Chairman of Project Independent Board Committee to answer any questions raised by the shareholders at the SGM.

The Board has scheduled four regular board meetings for 2006 and additional Board meetings will be arranged, if and when required. Board/committee meeting schedules for each year are normally made available to all Directors/committee members before the beginning of the year. Directors can attend meetings in person or via conference telephone facility pursuant to Bye-Law 94. The Company Secretary assists the Chairman in establishing the meeting agenda and each Director/committee member may request the inclusion of items in the agenda. Information packages containing analysis and background materials for the Board/committee meetings are despatched at least three days in advance of the respective meetings to the Directors/committee members. Ms. Eleni WANG, the President and Chief Operating Officer, and Mr. LI Kwan In, the Chief Financial Officer and the qualified accountant under the requirements of the Listing Rules, are invited to attend Board meetings, and other senior executives will be invited to attend Board meetings, as appropriate.

Minutes of Board/committee meetings are maintained, and draft minutes are circulated to all Directors/committee members for comments before being approved by the Chairman/committee chairman. Minutes of the Board/committee meetings are kept by the Company Secretary and are open for inspection by the Directors. Where any Director has a material or conflict of interest in any transaction discussed in the Board/committee meetings, this would not be dealt with by way of written resolutions. The Director or Directors concerned could express views but would not be counted as part of the quorum and shall abstain from voting on the relevant resolutions.

All Directors have access to the Company Secretary who is responsible for ensuring that the Board/committee procedures are complied with and for advising the Board/committee on compliance matters.

The Company has arranged directors' and officers' liability insurance in respect of any legal action against the Directors.

## CHAIRMAN AND CEO

The Chairman of the Board is responsible for ensuring the Board works effectively and discharges its responsibilities and addresses all key and appropriate issues in a timely manner. He is responsible for encouraging all Directors to make a full and active contribution to the Board's affairs and taking the lead to ensure that the Board acts in the best interests of the Company and its shareholders as a whole.

Other than the decisions reserved to the Board, the Board delegates to the CEO full authority to achieve the corporate goals of the Company in collaboration with other members of the management. The CEO assumes the responsibility for the day-to-day management of the Group and exercises his judgement in the best interests of the Company and its shareholders as a whole.

Under code provision A.2.1 of the Code, the roles of Chairman and CEO should be separate and should not be performed by the same individual. The division of responsibilities between the Chairman and CEO should be clearly established and set out in writing.

During the year 2005 and up to the date of this report, Mr. WANG Kin Chung, Peter has been the Chairman and CEO of the Company, and that the functions of the Chairman and CEO in the Company's strategic planning and development process overlap. These constitute deviations from code provision A.2.1 of the Code. However, the Board considered that it is beneficial to the Company that the Chairman and the CEO both take part in the Company's strategic planning and development process. The Board also considers that it might not be beneficial to the Company and its shareholders as a whole to have separate individuals occupying the offices of Chairman and CEO given the current size of the Group and its stage of development.

### **NON-EXECUTIVE DIRECTORS**

Under code provision A.4.1 of the Code, non-executive Directors should be appointed for a specific term, subject to re-election.

In order to comply with code provision A.4.1 of the Code, the term of the non-executive Directors (including independent non-executive Directors) has been fixed for a period of three years commencing on 1 January 2005, subject to earlier determination in accordance with the Bye-Laws and/or applicable laws and regulations. In addition, amendments to the Bye-Laws of the Company (the "Amendments") were made in the 2005 AGM to provide, among other things, that all Directors of the Company (save for any executive chairman and any managing director) shall be subject to retirement by rotation at least once every three years according to the provisions in the Company's Bye-Laws, and that a Director may voluntarily retire. A retiring Director shall be eligible for re-election.

### **REMUNERATION OF DIRECTORS**

In September 1998, the Company formed an executive personnel and compensation committee ("EPC Committee"), which is charged with the responsibility for recommending compensation packages of Directors and advising on the succession planning and development of Directors.

In January 2005, the Board resolved to change the name of the EPC Committee to remuneration committee (the "Remuneration Committee") and adopted a new set of terms of reference for the Remuneration Committee in alignment with the Code. The full text of those terms of reference is set out on the Company's website and is also available in writing upon request to the Company Secretary.

During the year 2005 and up to the date of this report, the members of the Remuneration Committee are: —

*Executive Director:*

Mr. WANG Kin Chung, Peter

*Non-executive Director:*

Ms. MAK WANG Wing Yee, Winnie

*Independent non-executive Directors:*

Mr. LO Kai Yiu, Anthony

Mr. James Christopher KRALIK

Mr. YUAN Ching Man, James (appointed on 26 January 2005)

Ms. MAK WANG Wing Yee, Winnie is the Chairlady of the Remuneration Committee.

The attendance by each committee member at each Remuneration Committee meeting during the year is set out in the "Board of Directors" section of this report.

The responsibilities of the Remuneration Committee pursuant to the new terms of reference include, amongst other things, the review of the Company's policy, structure and basis for the determination of the remuneration of the Directors and senior management, the review of the remuneration packages of all Directors and senior management, and the review and approval of the compensation payable to executive Directors and senior management in connection with any loss or termination of their office.

At the 2005 AGM, the shareholders approved the authorisation of the Directors to fix their remuneration. The Remuneration Committee considered the remuneration of the non-executive Directors and determined to revise their remuneration in view of the increasing accountability, time and effort spent on Board and Board committee matters since 2005. The new policy of remuneration of the non-executive Directors for the three years commencing from 1 January 2005 is as follows: —

- (i) Annual director's fee for each non-executive Director HK\$20,000
- (ii) Meeting attendance fees for each non-executive Director

	<b>Column A (Acting as Chairman/ Chairlady) (Note 1)</b>	<b>Column B (As participating member) (Note 2)</b>
Fee for attending each Board meeting	HK\$10,000	HK\$10,000
Fee for attending each Audit Committee meeting	HK\$20,000	HK\$10,000
Fee for attending each Remuneration Committee meeting	HK\$5,000	HK\$5,000
Fee for attending each Board Committee meeting	HK\$20,000	HK\$10,000
Fee for attending each Independent Board Committee meeting	HK\$20,000	HK\$10,000

Notes:

1. If a Director acts as the Chairman/Chairlady at the relevant meeting, he/she will be entitled to the fee set out under column A only.
2. If a Director participates in the relevant meeting as a participating member (but he/she does not act as the Chairman/Chairlady), he/she will be entitled to the fee set out in column B only.

## NOMINATION, RETIREMENT AND RE-ELECTION OF DIRECTORS

The Board is responsible for considering the suitability of individuals to act as Director, and approving or terminating the appointments. The Company has not established any nomination committee and would not consider establishing a nomination committee owing to the small size of the Board of the Company.

The Chairman of the Board is mainly responsible for identifying suitable candidates to fill Board membership whenever a vacancy arises or as an additional Director. He will put forward the qualified candidates to the Board for consideration. The Board will approve the appointment based on the candidate's qualification, business experience and suitability to the Company. Pursuant to the Bye-Laws, any Director newly appointed by the Board during the year shall hold office until the next annual general meeting and shall then be eligible for re-election at that annual general meeting.

Under code provision A.4.2 of the Code, all Directors appointed to fill a casual vacancy should be subject to election by shareholders at the first general meeting after their appointment. Every Director, including those appointed for a specific term, should be subject to retirement by rotation at least once every three years.

Pursuant to the Bye-Laws of the Company prior to the 2005 AGM, Mr. WANG Kin Chung, Peter and Ms. WANG KOO Yik Chun, being the Directors, were not subject to retirement by rotation and they had been in office for over three years. As a result, the Company deviated from code provision A.4.2 of the Code. However, after the Amendments, all Directors of the Company (save for any executive chairman and any managing director) shall be subject to the retirement by rotation at least once every three years according to the provisions in the Company's Bye-Laws, and that a Director may voluntarily retire.

Mr. WANG Kin Chung, Peter will voluntarily retire and Ms. WANG KOO Yik Chun, Ms. Leslie TANG SCHILLING, Dr. WANG Shui Chung, Patrick and Mr. LO Kai Yiu, Anthony will retire by rotation at the 2006 AGM (as defined below) and, being eligible, offer themselves for re-election. In consideration of their qualifications, experience and contributions to the Company, the Board recommended the shareholders of the Company to vote for the re-election of the aforesaid five Directors at the 2006 AGM.

In accordance with Bye-Law 90, a shareholder of the Company may recommend a person for election as a Director by lodging at the office of the Company notice in writing signed by the shareholder (other than the person to be proposed) the day after the despatch of the notice of general meeting appointed for such election and no later than seven days prior to the date of such general meeting. Upon receipt of such notice, the Board will consider the suitability of the said candidate as a Director and will make recommendation to the shareholders of the Company for their consideration.

## **DIRECTORS' SECURITIES TRANSACTIONS**

The Company has adopted a code of conduct regarding securities transactions by Directors on terms no less exacting than the required standard set out in the Model Code for Securities Transactions by Directors of Listed Issuers set out in Appendix 10 of the Listing Rules ("Model Code"). By responding to specific enquiries from the Company, the Directors have confirmed that they complied with the required standard set out in the Model Code and the Company's code of conduct regarding securities transaction by Directors throughout the year 2005.

In addition, in January 2005 the Board formally adopted the Model Code as guidelines for relevant employees in respect of their dealings in the securities of the Company.

## **AUDIT COMMITTEE**

An audit committee of the Company (the "Audit Committee") was formed in September 1998. During the year ended 31 December 2005, four Audit Committee meetings were held. The attendance of each Audit Committee member at Audit Committee meetings during the year is set out in the "Board of Directors" section of this report.

During the year 2005 and up to the date of this report, the members of the Audit Committee are: —

### *Non-executive Director:*

Ms. MAK WANG Wing Yee, Winnie

### *Independent non-executive Directors:*

Mr. LO Kai Yiu, Anthony

Mr. YUAN Ching Man, James

Mr. LO Kai Yiu, Anthony is the Chairman of the Audit Committee and has the professional qualifications and accounting and related financial management expertise as required under rule 3.10(2) of the Listing Rules.

In January 2005, the Board adopted a new set of terms of reference for the Audit Committee in alignment with the Code. The main duties of the Audit Committee are set out below: —

- (a) to make recommendations to the Board on the appointment, re-appointment and removal of the external auditors, and any questions of resignation or dismissal of the auditors;
- (b) to review and monitor the external auditors' independence and the objectivity and the effectiveness of the audit process in accordance with applicable standards;
- (c) to develop and implement policy on the engagement of external auditors to supply non-audit services;
- (d) to monitor the integrity of the financial statements of the Company and the Company's annual and interim reports and accounts, and to review significant financial reporting judgements contained in such reports;
- (e) to review the Company's financial controls, internal controls and risk management systems; and
- (f) to review the Group's financial and accounting policies and practices.

The terms of reference of the Audit Committee are set out in full on the Company's website and are also available in writing upon request to the Company Secretary.

The Audit Committee held a meeting in April 2005 to review the annual report and audited accounts for the year ended 31 December 2004. Another meeting was held in September 2005 to review the interim report and unaudited accounts for the six months ended 30 June 2005 and such report was then recommended to the Board for approval. The Audit Committee held two additional meetings during the year to consider and discuss the matters relating to nature and scope of the audit, the remuneration and terms of engagement of the auditors, accounting and financial procedures, management information system and internal controls of the Group.

The Audit Committee has reviewed the Company's annual report and audited accounts for the year ended 31 December 2005 with the auditors and the management of the Company and recommended them to the Board for approval.

## FINANCIAL REPORTING

The Directors acknowledge that they are responsible for the preparation of the Company's accounts which give a true and fair view of the financial position of the Company as of 31 December 2005 and of the results of its operations and cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards and for ensuring that appropriate accounting policies are selected and applied consistently.

To the best of the knowledge of the Directors, there is no uncertainty relating to events or conditions that may cast significant doubt upon the Company's ability to continue as a going concern.

## INTERNAL CONTROL

The Board acknowledges its responsibility for maintaining an effective system of internal controls to safeguard the investment of the Company's shareholders and the Group's assets at all times. The primary purpose of such system is to provide reasonable assurance regarding the achievement of the Group's objectives in relation to the reliability of financial reporting and the effectiveness and efficiency of operations.



During the year, the management conducted a review of the Group's key internal controls in all major activities including budgeting, sales orders management, factory loading, purchases, inventory, accounts receivables, accounts payable, periodical financial reporting, etc. This review indicates that key internal controls are in place to facilitate business operations and financial reporting. It has also identified areas within the system for further improvement. Resources have been allocated to continuously improve the system of internal controls and management information system, and the progress of such work is reported to the Audit Committee on a periodical basis.

As part of the internal controls system, internal audit functions have been established within the Group in late 2005 and they report to the Audit Committee on a periodical basis.

### **AUDITORS' REMUNERATION**

The external auditors of the Company for the two years ended 31 December 2004 and 2005 were PricewaterhouseCoopers ("PwC"). In January 2005, the Audit Committee adopted a written policy which clearly sets out the procedure for the appointment of external auditors to supply non-audit services to the Group.

In 2005, remunerations paid to PwC (including any entity that is under common control, ownership or management with PwC or any entity that a reasonable and informed third party having knowledge of all relevant information would reasonably conclude as part of PwC nationally or internationally) in respect of audit and non-audit services to the Group amounted to HK\$3,008,000 (2004: HK\$2,970,000) and HK\$2,279,000 (2004: HK\$556,000) respectively. Included in the 2005 remuneration for non-audit services was a fee of HK\$1,380,000 paid to PwC in respect of the engagement to prepare (i) an accountants' report on Hua Thai and its subsidiaries ("Hua Thai Group"), (ii) a letter on the unaudited proforma consolidated statement of assets and liabilities of the Group and Hua Thai Group after the Acquisitions (the "Enlarged Group"), and (iii) a letter on the Directors' statement on sufficiency of working capital of the Enlarged Group for the purposes of the circular to the shareholders of the Company dated 8 September 2005 relating to the Acquisitions. In support of such engagement, PwC issued a letter to the Audit Committee in August 2005 confirming that they were independent accountants with respect to the Company and Hua Thai within the meaning of the requirements of PwC and of the Code of Ethics of International Federation of Accountants. The remaining remuneration for non-audit services mainly related to tax services provided.

During 2005, the engagement partner of PwC for the Company was rotated. During 2005 and up to the date of this report, the Group has not employed any staff who was formerly involved in the Group's statutory audit.

### **SHAREHOLDERS' RIGHTS AND INVESTOR RELATIONS**

The Company values communication with shareholders and investors. Enquiries and suggestions from shareholders or investors are welcome through the following channels to the Company Secretary:

- (i) By mail to the Company's head office at 5/F., 66-72 Lei Muk Road, Kwai Chung, New Territories, Hong Kong;
- (ii) By telephone at telephone number (852) 2279 3888;
- (iii) By fax at fax number (852) 2423 5576; or
- (iv) By e-mail at cosec@tristateww.com.

At the 2005 AGM held on 22 June 2005, the Company proposed the following amendments to the Bye-Laws of the Company in order to comply with the amended Listing Rules effective on 15 February 2002, the Companies Act 1981 of the laws of Bermuda effective on 14 February 2003 and the Code which came into effect on 1 January 2005: —

- (i) that the Company be permitted to send or otherwise make available corporate communications to members by electronic means;
- (ii) that the Company be allowed to send corporate communications to members either in the English language only, or both the English and Chinese language in accordance with the wishes of their members and subject always to the Listing Rules and all applicable laws;
- (iii) that the Company be permitted to send and distribute summary financial reports in place of the long form report;
- (iv) that there be appointed non-executive directors for a specific term, subject to re-election; and
- (v) that every director, including those appointed for a specific term, should be subject to retirement by rotation at least once every three years.

The shareholders of the Company approved such amendments at the 2005 AGM.

The last shareholders' meeting of the Company was held on 6 October 2005 at Room 5A, 5/F., 66–72 Lei Muk Road, Kwai Chung, New Territories, Hong Kong at which the Acquisitions were considered and the relevant ordinary resolution was unanimously passed by the shareholders at the SGM. Details of the Acquisitions were set out in the circular of the Company dated 8 September 2005 and the voting result was set out in the announcement of the Company dated 6 October 2005.

The Board resolved that the forthcoming annual general meeting of the Company will be held at Room 5A, 5/F., 66–72 Lei Muk Road, Kwai Chung, New Territories, Hong Kong on Tuesday, 6 June 2006 at 10:00 a.m. ("2006 AGM"). The notice of the 2006 AGM will be sent to all shareholders of the Company separately. The Chairman of the Board together with the Chairman of the Audit Committee and the Chairlady of the Remuneration Committee or their delegates will attend the 2006 AGM to answer questions from the shareholders of the Company on the business to be dealt with at the 2006 AGM.

## MOVING FORWARD

As at the date of this report, the Company, upon implementing the improvements on the Company's corporate governance practices, has applied the principles and complied with all requirements of the code provisions of the Code with the only deviation being with regard to the separation of the role of the Chairman and the CEO as detailed above. The Board acknowledges its responsibility to ensure the establishment and implementation of good corporate governance practices and procedures.

On behalf of the Board

**WANG Kin Chung, Peter**

*Chairman and Chief Executive Officer*

Hong Kong, 13 April 2006