

# CORPORATE GOVERNANCE REPORT

The Company is dedicated to ensure high standards of corporate governance with an emphasis on a diligent board of directors (the “Board”), sound internal control, and increasing transparency and accountability to shareholders. The Board acknowledges that good corporate governance practices and procedures are beneficial to the Group and its shareholders. The Company is committed to improve those practices and maintain its ethical corporate culture.

The Company has adopted the code provisions set out in the Code of Corporate Governance Practices (the “Code”) contained in Appendix 14 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the “Listing Rules”) which became effective on 1 January 2005 as its own code of corporate governance practices.

Subject to the deviation disclosed in this report, the Company has complied with the code provisions set out in the Code.

## The Board

The Board is responsible for the leadership and management of the Company. Key responsibilities of the Board comprise formulation of the Group’s overall strategies and policies, setting of performance and management targets, evaluation of business performance and supervision of management’s performance. The management was delegated the authority and responsibility by the Board for the management and operations of the Group. In addition, the Board has also delegated various responsibilities to the Board committees as detailed in this report.

The Board meets at least four times a year and additional operational meetings are also held, when required. The company secretary is responsible for preparing agenda and notices for the meetings. Senior management of the Group also provides the directors with relevant information on a timely basis regarding key business developments of the Group and issues affecting the Group. Agenda and other information package are normally delivered to the directors before the meetings. The directors also have independent access to the senior management in respect of operating issues. The directors may take independent professional advice where appropriate to discharge their duties, at the Company’s expenses.

During the year ended 31 December 2005, the Board held eight meetings. The attendance of each of the directors at the Board meetings is as follows:

<b>Directors</b>	<b>Attendance of Board meetings in 2005</b>
Niu Gensheng (i)	4/8
Lu Jun (i)	6/8
Yang Wenjun (i)	4/8
Sun Yubin	6/8
Jiao Shuge (alias Jiao Zhen) (i)	3/8
Liu Haifeng, David (i)	3/8
Jin Yujuan, Lily	5/8
Wang Huaibao	4/8
Zhang Julin	4/8
Li Jianxin	4/8

- (i) During the year, a number of directors opted for not attending certain Board meetings to avoid conflict of interest. The number of meetings in which each of these directors was absent with apologies was: three for Mr Niu Gensheng, two for Ms Lu Jun, Mr Yang Wenjun and Mr Jiao Shuge and one for Mr Liu Haifeng, David.
- (ii) During the year, three Board meetings were convened to handle operational-level matters such as the opening or operation of bank accounts.

Minutes of meetings of the Board and Board committees are kept by the company secretary of the Company and are not only open for inspection by the directors but also sent to the directors for records. All directors have access to the company secretary of the Company, who is responsible for ensuring that the Board procedures are complied with and advising the Board on compliance matters.

### **Chairman and Chief Executive Officer**

The role of the chairman of the Board (the "Chairman") is separate from that of the chief executive officer to ensure a balance of power and authority. The Chairman is responsible for overseeing the functioning of the Board while the chief executive officer is responsible for managing the Group's business.

The Chairman shall ensure that Board meetings are planned and conducted effectively and all directors are properly briefed on issues arising at Board meetings. He is also responsible for ensuring that the directors receive in a timely manner adequate information, which must be complete and reliable.

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## Board Composition

As at 31 December 2005, the Board comprises ten directors, including four executive directors (Mr Niu Gensheng, Ms Lu Jun, Mr Yang Wenjun and Mr Sun Yubin), three non-executive directors (Mr Jiao Shuge (alias Jiao Zhen), Mr Liu Haifeng, David<sup>1</sup> and Ms Jin Yujuan, Lily<sup>2</sup>) and three independent non-executive directors (Mr Wang Huaibao, Mr Zhang Julin and Mr Li Jianxin). The chairman of the Company is Mr Jiao Shuge and the chief executive officer of the Company is Mr Niu Gensheng.

The Company has received annual confirmation of independence from the three independent non-executive directors in accordance with Rule 3.13 of the Listing Rules. The Board has assessed their independence and concluded that all the independent non-executive directors are independent within the definition of the Listing Rules. The independent non-executive directors possess appropriate professional qualifications, or accounting or related financial management expertise.

Biographies of the directors are set out on pages 14 to 17 of the annual report, which demonstrates a diversity of skills, expertise, experience and qualifications.

## Appointments, Re-election and Removal of Directors

None of the Directors has entered into any service agreement with the Company or any of its subsidiaries which is not determinable by the Group within one year without payment of compensation, other than statutory compensation.

Each director has entered into a service contract with the Company for an initial term of one year and continuing thereafter for further successive period of one year, for a maximum duration of three years. The directors are subject to retirement by rotation and re-election at each annual general meeting of the Company in accordance with article 112 of the Company's articles of association. The directors appointed as an addition to the Board or to fill a casual vacancy on the Board shall be subject to re-election by the shareholders at the first general meeting after the appointment. To further align with the Code, amendments to the Company's articles of association will be proposed in the forthcoming annual general meeting to more closely reflect the provisions set out in the Code.

- 1 Mr Liu Haifeng, David, a former non-executive director of the Company resigned on 26 January 2006. Mr Julian Juul Wolhardt was appointed as a non-executive director on the same day.
- 2 Ms Jin Yujuan, Lily, a former non-executive director of the Company resigned on 7 March 2006.

## Board Committees

The Company has established three Board committees, namely the audit committee, the remuneration committee and the nomination committee, each of which is governed by specific terms of reference approved by the Board, covering its functions, duties and powers. The terms of reference of the respective Board committees have complied with the Code provisions and are available for public inspection at the Company's principal place of business in Hong Kong.

### Audit Committee

The audit committee comprises three non-executive directors, two of whom are independent (the "Audit Committee"). The committee is chaired by Mr Zhang Julin, an independent non-executive director.

The Audit Committee serves as a focal point for communication between other directors, the external auditors, and the management as their duties relate to financial and other reporting, internal controls and the auditing. The Audit Committee is to assist the Board in fulfilling its responsibilities by providing an independent review of financial reporting, be satisfying themselves as to the effectiveness of the Company's internal controls and as to the efficiency of the audits.

During the year, the Audit Committee has performed the following:

- met with the external auditors to discuss the general scope and findings of their audit and interim review works;
- reviewed external auditor's management letter and management's response;
- reviewed and recommended to the Board approval of the external auditors' remuneration;
- made recommendation to the Board on the re-appointment of the external auditors;
- reviewed the external auditors' independence, objectivity and the effectiveness of the audit process;
- reviewed and monitored the integrity of financial statements, annual and interim reports, and annual and interim announcements of the Company;
- discussed auditing, internal control, risk management and financial reporting matters before recommending them to the Board for approval;
- reviewed the connected transactions entered into by the Group; and
- revised its terms of reference to comply with the Code.

All issues raised by the external auditors and the Audit Committee have been addressed by the senior management. The work and findings of the Audit Committee have been reported to the Board. During the year, no issues brought to the attention of the senior management and the Board were of sufficient significance for disclosure in the annual report.

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The Audit Committee held two meetings in 2005 and one meeting to date in 2006. The attendance record of each member of the Audit Committee in 2005 is set out below:

<b>Directors</b>	<b>Attendance of Committee Meetings in 2005</b>
Zhang Julin (chairman)	2/2
Jiao Shuge	2/2
Li Jianxin	2/2

Other than the reporting responsibilities of the Company's auditors (please refer to the auditors' report set out on page 39), the directors acknowledge their responsibility for preparing the financial statements of the Group and the Company which give a true and fair view of the state of affairs of the Group and the Company as at 31 December 2005 and the profit and cash flows of the Group for the year then ended.

## **Remuneration Committee**

The remuneration committee comprises five members, three of whom are independent non-executive directors, one executive director and one non-executive director (the "Remuneration Committee"). The Remuneration Committee is chaired by Mr Wang Huaibao, an independent non-executive director.

The duties of the Remuneration Committee are to review annually and recommend to the Board the overall remuneration policy for the directors and senior management to ensure that the level of remuneration is linked to their level of responsibilities undertaken. The Remuneration Committee shall also evaluate annually the performance of the directors and the senior management and recommend to the Board specific adjustments in their remuneration and/or reward payments.

During the year, the Remuneration Committee had performed the following:

- assessed the performance of the directors and senior management;
- reviewed and approved the remuneration for the directors and senior management;
- reviewed the remuneration policy and recommended to the Board;
- approved the Company's share option plan and recommended to the Board; and
- revised its terms of reference to comply with the Code.

The Remuneration Committee held one meeting in 2005 and one meeting to date in 2006. The attendance record of each member of the Remuneration Committee in 2005 is set out below:

<b>Directors</b>	<b>Attendance of Committee Meetings in 2005</b>
Wang Huaibao (chairman)	1/1
Lu Jun	1/1
Liu Haifeng, David	1/1
Zhang Julin	1/1
Li Jianxin	1/1

#### **Nomination Committee**

The nomination committee comprises three non-executive directors, two of whom are independent (Mr Wang Huaibao and Mr Zhang Julin) (“Nomination Committee”). The Nomination Committee is chaired by Mr Jiao Shuge, a non-executive director.

The responsibilities of the Nomination Committee is to review the structure, size and composition, including the skills, knowledge and experiences of the Board compared to its current position and make recommendations to the Board regarding any proposed changes. The Nomination Committee is also responsible to identify and nominate suitable candidates qualified to become Board members and makes recommendation to the Board on relevant matters relating to the appointment or re-appointment of directors if necessary, in particular, candidates who can add value to the management through their contributions in the relevant strategic business areas and which appointments will result in the constitution of a stronger and more diverse Board. In the selection process, the Nomination Committee makes reference to criteria including, inter alia, reputation for integrity, accomplishment and experience in the dairy industry, professional and educational background, and commitment in respect of available time.

The Nomination Committee did not convene any meeting in 2005 as no director has resigned or was dismissed during the year ended 31 December 2005 and has convened one meeting in January 2006.

The Nomination Committee will meet at times as and when required to consider nomination related matters.

#### **Directors’ Securities Transactions**

The Company has adopted the Model Code for Securities Transactions by Directors of Listed Issuers set out in Appendix 10 of the Listing Rules as the Company’s code of conduct and rules governing dealings by all the directors in the securities of the Company (“Model Code”). Having made specific enquiry of all the directors, the Company confirms that, during the year, all the directors have strictly complied with the Model Code.

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## Investor Relations and Communications

The Company adopts a proactive policy in promoting investor relations and communications. Regular meetings are held with institutional investors and financial analysts to ensure two-way communications on the Company's performance and development. When the Company announced its interim and annual results, briefings are conducted to apprise investors, analysts and the press of the Group's operating results as well as business strategies and outlook. Investor relations website has been launched during the year to ensure investors is able to have access to Company's information, latest news and reports. All directors, including the Chairman, have attended the annual general meeting in June 2005 to be available to answer questions at the meeting.

Separate resolutions are proposed at general meetings for each substantially separate issue, including election of directors.

Details of voting procedures by way of a poll and rights of shareholders to demand a poll were included in the circular dispatched to the shareholders of the Company. The circular also included relevant details of proposed resolutions and biography of directors standing for re-election.

## Compliance with the Code

Save and except that one of the resolutions which was passed at the Company's annual general meeting held on 28 June 2005 by way of a show of hands rather than by poll as required by the Listing Rules, details of which had been disclosed in an announcement dated 11 July 2005, none of the directors of the Company is aware of any information that would reasonably indicate that the Company was not at any time during the year in compliance with the Code.

Subsequent to the incident, the Company has strengthened relevant internal control measures including the setting up of procedures in relation to the communications with legal and other professional advisors, more frequent review of compliance with the Listing Rules and the implementation of internal training programs to communicate updates in the Listing Rules to the relevant personnel in the Group.

## Auditors

Details of fees paid or payable to Ernst & Young for the year ended 31 December 2005 are as follows:

<b>Services rendered</b>	<i>RMB'000</i>
2005 annual audit	1,860
2005 interim review	350
Non-audit services:	
Review on connected transactions	60
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	2,270

The above fees were approved by the Audit Committee. The re-appointment of Ernst & Young as auditors of the Company has been recommended by the Audit Committee and endorsed by the Board and is subject to approval by the shareholders at the forthcoming annual general meeting.