

CORPORATE GOVERNANCE REPORT

The Board of Directors of the Company (the "Board") is pleased to present this Corporate Governance Report in the Group's annual report for the year ended 31 December 2005.

Good corporate governance has always been recognized as vital to the Group's success and to sustain development of the Group. We commit ourselves to a high standard of corporate governance as an essential component of quality and has introduced corporate governance practices appropriate to the conduct and growth of the business of the Group.

The Code on Corporate Governance Practices ("CG Code") contained in Appendix 14 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules") sets out the principles of good corporate governance (the "Principles") and two levels of corporate governance practices:

- (a) code provisions (the "Code Provisions") which listed issuers are expected to comply with or to give considered reasons for any deviation; and
- (b) recommended best practices (the "Recommended Best Practices") for guidance only, which listed issuers are encouraged to comply with or give considered reasons for deviation.

The Company has applied the Principles and the Code Provisions as set out in the CG Code and complied with all the Code Provisions. It also put in place certain Recommended Best Practices as set out in the CG Code.

The Company periodically reviews its corporate governance practices to ensure that these continue to meet the requirements of the CG Code, and acknowledges the important role of its Board in providing effective leadership and direction to the Company's business, and ensuring transparency and accountability of the Company's operations.

The key corporate governance principles and practices of the Company are summarised as follows:

THE BOARD

Responsibilities

The Board provides leadership, approves policies, strategies and plans, and oversees their implementation to further the healthy growth of the Company, in the interests of its shareholders.

The Board takes responsibility for all major matters of the Company, including: the approval and monitoring of all policy matters, overall strategies and budgets, internal control and risk management systems, financial information, appointment of Directors and other significant financial and operational matters.

All Directors have full and timely access to all relevant information as well as the advice and services of the Company Secretary, with a view to ensuring that Board procedures and all applicable rules and regulations are followed. Each Director is normally able to seek independent professional advice in appropriate circumstances at the Company's expense, upon making request to the Board.

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The day-to-day management, administration and operation of the Company are delegated to the Managing Director, Executive Director and the senior management. The delegated functions and work tasks are periodically reviewed by the Board. Approval has to be obtained from the Board prior to any significant transactions entered into by the abovementioned officers.

The Board has the full support of the Managing Director, Executive Director and the senior management to discharge its responsibilities.

Composition

The composition of the Board reflects the necessary balance of skills and experience desirable for effective leadership of the Company and independence in decision making. During the year, the Board comprises ten members, consisting of three executive Directors, four non-executive Directors and three independent non-executive Directors.

The Board of the Company comprises the following Directors:

Executive Directors:

ZHANG Guotong *(Vice-Chairman, Managing Director, member of Remuneration Committee and Nomination Committee)*

WANG Hongxin

WU Chun Wah, Michael*

LI Tiefeng*

Non-executive Directors:

MA Zhengwu *(Chairman, Chairman of Nomination Committee and member of Remuneration Committee)*

HONG Shuikun *(member of Audit Committee)*

XU Zhen *(member of Audit Committee)*

GU Laiyun

CHEN Shengjie*

Independent non-executive Directors:

KWONG Che Keung, Gordon *(Chairman of Audit Committee, member of Remuneration Committee and member of Nomination Committee)*

TSUI Yiu Wa, Alec *(Chairman of Remuneration Committee, member of Audit Committee and member of Nomination Committee)*

LAO Youan *(member of Audit Committee, member of Remuneration Committee and member of Nomination Committee)*

* Mr. Wu Chun Wah, Michael and Mr. Li Tiefeng resigned from the office as Executive Directors on 10 February 2006 and 29 March 2005 respectively. Mr. Chen Shengjie resigned from the office of Non-executive Director on 29 March 2005.

The list of Directors (by category) is also disclosed in all corporate communications issued by the Company pursuant to the Listing Rules from time to time.

During the year ended 31 December 2005, the Board at all times met the requirements of the Listing Rules relating to the appointment of at least three independent non-executive Directors with at least one independent non-executive Director possessing appropriate professional qualifications, or accounting or related financial management expertise. The Company has received written annual confirmation from each independent non-executive Director of his independence pursuant to the requirements of the Listing Rules. The Company considers all independent non-executive Directors to be independent in accordance with the independence guidelines set out in the Listing Rules.

The non-executive Directors bring a wide range of business and financial expertise, experiences and independent judgement to the Board. Through active participation in Board meetings, taking the lead in managing issues involving potential conflict of interests and serving on Board committees, all non-executive Directors make various contributions to the effective direction of the Company.

Appointment and Succession Planning of Directors

The Company has established a Nomination Committee and formal, considered and transparent procedures for the appointment and succession planning of Directors.

In accordance with the Company's Articles of Association, one third of the Directors are subject to retirement by rotation every year and any new Director appointed to fill a causal vacancy or as an addition to the Board shall be eligible for re-election by shareholders at the first general meeting after appointment.

Code Provision A.4.1 of Appendix 14 to the Listing Rules requires that non-executive directors should be appointed for a specific term and should be subject to re-election. With respect to Code Provision A.4.1, the non-executive directors of the Company have not been appointed for any specific terms since they are subject to retirement by rotation and re-election at the annual general meeting of the Company in accordance with the Memorandum and Articles of Association of the Company. As such, the Company considers that sufficient measures have been taken to serve the purpose of this Code Provision.

The Board and Nomination Committee as a whole is responsible for reviewing the Board composition, developing and formulating the relevant procedures for nomination and appointment of Directors, monitoring the appointment and succession planning of Directors and assessing the independence of independent non-executive Directors. The Board reviewed its own structure, size and composition regularly to ensure that it has a balance of expertise, skills and experience appropriate to the requirements of the business of the Company.

Where vacancies on the Board exist, the Board will carry out the selection process by making reference to the skills, experience, professional knowledge, personal integrity and time commitments of the candidates proposed by the Nomination Committee, the Company's needs and other relevant statutory requirements and regulations. An external recruitment agency may be engaged to carry out the recruitment and selection process when necessary.

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In accordance with the Company's Articles of Association, Mr. Kwong Che Keung, Gordon, Mr. Tsui Yiu Wa, Alec and Mr. Lao Youan shall retire by rotation and being eligible, offer themselves for re-election at the Annual General Meeting ("AGM") of the Company to be held on 23 June 2006.

The Board recommended the re-appointment of the Directors standing for re-election at the forthcoming annual general meeting of the Company.

The Company's circular in relation to the forthcoming annual general meeting contains detailed information of the Directors standing for re-election.

Training for Directors

There were two Directors newly appointed during the year ended 31 December 2005, including Mr. Wang Hongxin, an executive director and Mr. Xu Zhen, a non-executive director. In case there is any newly appointed Director, he/she will be provided an induction so as to ensure that he/she has appropriate understanding of the business and operations of the Company and that he/she is fully aware of his/her responsibilities and obligations under the Listing Rules and the relevant regulatory requirements.

There are also arrangements in place for providing continuing briefing and professional development to Directors whenever necessary.

Board Meetings

Number of Meetings and Directors' Attendance

Regular Board meetings are held at least four times a year at approximately quarterly intervals for reviewing and approving the financial and operating performance, and considering and approving the overall strategies and policies of the Company.

During the year ended 31 December 2005, five Board meetings were held and four of which were regular Board meetings.

The individual attendance record of each Director at the meetings of the Board, Audit Committee and Remuneration Committee during the year ended 31 December 2005 is set out below:

Name of Directors	Attendance/Number of Meetings		
	Board	Audit Committee	Remuneration Committee
MA Zhengwu	5/5	Not applicable	–/–
ZHANG Guotong	5/5	Not applicable	–/–
WANG Hongxin	5/5	Not applicable	Not applicable
WU Chun Wah, Michael*	5/5	Not applicable	Not applicable
HONG Shuikun	5/5	2/2	Not applicable
XU Zhen	5/5	2/2	Not applicable
GU Laiyun	4/5	Not applicable	Not applicable
KWONG Che Keung, Gordon	5/5	2/2	–/–
TSUI Yiu Wa, Ales	5/5	2/2	–/–
LAO Youan	4/5	2/2	–/–
LI Tiefeng*	Not applicable	Not applicable	Not applicable
CHEN Shengjie*	Not applicable	Not applicable	Not applicable

* Mr. Wu Chun Wah, Michael and Mr. Li Tiefeng resigned from the office as Executive Directors on 10 February 2006 and 29 March 2005 respectively. Mr. Chen Shengjie resigned from the office of Non-executive Director on 29 March 2005. During the period from 1 January 2005 to 29 March 2005, one meetings of the Board was held. And no meeting of Remuneration Committee was held for the year ended 31 December 2005, however, a meeting of Remuneration Committee was held on 21 March 2006.

Practices and Conduct of Meetings

Annual meeting schedules and draft agenda of each meeting are normally made available to Directors in advance. Notices of regular Board meetings are served to all Directors at least 14 days before the meetings. For other Board and committee meetings, reasonable notice is generally given.

Board papers together with all appropriate, complete and reliable information are sent to all Directors at least 3 days before each Board meeting or committee meeting to keep the Directors apprised of the latest developments and financial position of the Company and to enable them to make informed decisions. The Board and each Director also have separate and independent access to the senior management whenever necessary.

The Company Secretary of the Company is responsible for keeping minutes of all Board meetings and committee meetings. Draft minutes are normally circulated to Directors for comment within a reasonable time after each meeting and the final version is open for Directors' inspection.

According to current Board practice, any material transaction, which involves a conflict of interests for a substantial shareholder or a Director, will be considered and dealt with by the Board at a duly convened Board meeting. The Company's Articles of Association also contains provisions requiring Directors to abstain from voting and not to be counted in the quorum at meetings for approving transactions in which such Directors or any of their associates have a material interest.

CHAIRMAN AND MANAGING DIRECTOR

The Company fully supports the division of responsibility between the Chairman of the Board and the Managing Director to ensure a balance of power and authority. The positions of the Chairman and Managing Director are held by Mr. MA Zhengwu and Mr. ZHANG Guotong respectively. Their respective responsibilities are clearly defined and set out in writing.

The Chairman provides leadership and is responsible for the effective functioning of the Board in accordance with good corporate governance practice. With the support of the senior management, the Chairman is also responsible for ensuring that the Directors receive adequate, complete and reliable information in a timely manner and appropriate briefing on issues arising at Board meetings.

The Managing Director focuses on implementing objectives, policies and strategies approved and delegated by the Board. He is in charge of the Company's day-to-day management and operations. He is also responsible for developing strategic plans and formulating the company practices and procedures, business objectives, and risk assessment for the Board's approval.

BOARD COMMITTEES

The Board has established three committees, namely, the Audit Committee, Remuneration Committee and Nomination Committee, for overseeing particular aspects of the Company's affairs. All Board committees of the Company are established with defined written terms of reference. The terms of reference of the Board committees kept in the Company and are available to shareholders upon request. The majority of the members of each Board committees are independent non-executive Directors and the list of the Chairman and members of each Board committee is set out in this report on page 12.

The Board committees are provided with sufficient resources to discharge their duties and, upon reasonable request, are able to seek independent professional advice in appropriate circumstances, at the Company's expenses.

Remuneration Committee

The primary objectives of the Remuneration Committee include making recommendations on and approving the remuneration policy and structure and remuneration packages of the Directors and the senior management. The Remuneration Committee is also responsible for establishing transparent procedures for developing such remuneration policy and structure to ensure that no Director or any of his/her associates will participate in deciding his/her own remuneration, which remuneration will be determined by reference to the performance of the individual and the Company as well as market practice and conditions.

The Remuneration Committee normally meets for reviewing the remuneration policy and structure and determination of the annual remuneration packages of the members of the Board and the senior management and other related matters. The human resources department is responsible for collection and administration of the human resources data and making recommendations to the Remuneration Committee for consideration. The Remuneration Committee shall consult the Chairman and/or the Managing Director of the Company about these recommendations on remuneration policy and structure and remuneration packages.

The Remuneration Committee did not meet during the year ended 31 December 2005 and the Board reviewed the existing remuneration policy and structure of the Company and remuneration packages of the Directors and the senior management. The Remuneration Committee subsequently met on 21 March 2006.

Audit Committee

The Audit Committee comprises three independent non-executive Directors (including one independent non-executive Director who possesses the appropriate professional qualifications or accounting or related financial management expertise) and two Non-executive Directors. None of the members of the Audit Committee is a former partner of the Company's existing external auditors.

The main duties of the Audit Committee include the following:

- (a) To review the financial statements and reports and consider any significant or unusual items raised by the qualified accountant, compliance officer, internal auditor or external auditors before submission to the Board.
- (b) To review the relationship with the external auditors by reference to the work performed by the auditors, their fees and terms of engagement, and make recommendation to the Board on the appointment, re-appointment and removal of external auditors.
- (c) To review the adequacy and effectiveness of the Company's financial reporting system, internal control system and risk management system and associated procedures.

The Audit Committee held two meetings during the year ended 31 December 2005 to review the financial results and reports, financial reporting and compliance procedures and the re-appointment of the external auditors.

There are no material uncertainties relating to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern.

The Audit Committee has not taken a different view from the Board regarding the selection, appointment, resignation or dismissal of external auditors.

The Company's annual results for the year ended 31 December 2005 have been reviewed by the Audit Committee.

NOMINATION COMMITTEE

The Company has established a Nomination Committee and was chaired by the Chairman of the Board, members of the Nomination Committee including the managing director and all of the three Independent Non-executive Directors. Nomination Committee responsible for nominating potential candidates for directorship appointment and succession, regular review on the composition and structure of the Board and making appropriate recommendation to the Board in order to ensure the balance of expertise, skills and experience among the members of the Board. Nomination will be made reference to the skill, experience, professional knowledge, personal integrity and time commitment.

MODEL CODE FOR SECURITIES TRANSACTIONS

In the year ended 31 December 2005, the Company has adopted its own code of conduct regarding Directors' securities transactions (the "Code of Conduct") on terms no less exacting than the required standard set out in the Model Code for Securities Transactions by Directors of Listed Issuers (the "Model Code") as set out in Appendix 10 to the Listing Rules. Specific enquiry has been made of all the Directors and the Directors have confirmed that they have complied with the requirements of the Code of Conduct and the Model Code throughout the year ended 31 December 2005.

The Company also has established written guidelines on no less exacting than the Model Code (the "Written Guidelines") for securities transactions by the employees who are likely to be in possession of unpublished price-sensitive information of the Company. No incident of non-compliance of the Written Guidelines by the employees was noted by the Company.

RESPONSIBILITIES IN RESPECT OF THE FINANCIAL STATEMENTS AND AUDITORS' REMUNERATION

The Board is responsible for presenting a balanced, clear and understandable assessment of annual and interim reports, price-sensitive announcements and other disclosures required under the Listing Rules and other regulatory requirements. The Directors acknowledge their responsibility for preparing the financial statements of the Company for the year ended 31 December 2005.

The statement of the external auditors of the Company about their reporting responsibilities on the financial statements is set out in the Auditors' Report on page 26.

The remuneration paid to the external auditors of the Company in respect of audit services and non-audit services for the year ended 31 December 2005 amounted to HK\$1,280,000 and HK\$283,000 respectively. An analysis of the remuneration paid to the external auditors of the Company is set out below:

	Amount of Fee Payable/Paid (HK\$'000)
Audit Services	1,280
Review on interim results	242
Other non-audit services	41
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Total	<u>1,563</u>

INTERNAL CONTROLS

The Board has full responsibility for the Group's internal control system, which includes the establishment of a defined management structure with specified limited of authority. The system is designed to help the achievement of business objectives of the Group, safeguard assets against unauthorized use or disposition, ensure the maintenance of proper accounting records for the provision of reliable financial information for internal use or for publication and ensure compliance with relevant legislation and regulation. The internal control system is designed to provide reasonable, but not absolute, assurance against material misstatement or loss. In 2005, the management of the Company reported an incident of a short term loan made without the prior approval of the Board.

The key procedures that the Board established to provide a more effective internal controls are as follows:

– Organizational Structure

An appropriate organizational structure is in place with defined operating policies and procedures as well as responsibility and lines of authority.

– Authority and Control

The Executive Directors and senior management are delegated with respective levels of authorities to carry out the corporate strategies and policies and the related matters formulated by the Board.

– Budgetary Control and Financial Reporting

The Group implements budget management, and financial budget is executed upon approval by the Board. Relevant procedures have been established to assess, review and approve major capital and recurrent expenditures, and regular review and comparison between operating results and the budget are made.

The Group has established appropriate internal control procedures to ensure the keeping of accurate and complete accounting and management records on a timely basis. Examination and review are carried out regularly to ensure that the financial statements are properly prepared in conformity with the generally accepted accounting principles, the Group's accounting policies and the applicable laws and regulations.

– Internal Auditing

The Group has regularly conducted internal audit to review whether the internal control procedures are implemented appropriately.

SHAREHOLDER RIGHTS AND INVESTOR RELATIONS

The rights of shareholders and the procedures for demanding a poll on resolutions at shareholders' meetings are contained in the Company's Articles of Association. Details of such rights to demand a poll and the poll procedures are included in all circulars to shareholders and will be explained during the proceedings of meetings. Poll results will be published in newspapers on the business day following the shareholders' meeting. The general meetings of the Company provide a forum for communication between the shareholders and the Board. The Chairman of the Board as well as chairmen of the Audit Committee and Remuneration Committee, or in their absence, other members of the respective committees, are available to answer questions at the shareholders' meetings. Separate resolutions are proposed at shareholders' meetings on each substantial issue, including the election of individual Directors.

To promote effective communication, the Company also maintains a website at <http://www.hk217.com>, where extensive information and updates on the Company's business developments and operations, financial information, corporate governance practices and other information are posted.