

## CORPORATE GOVERNANCE PRACTICES

The Company is committed to the overall standard of corporate governance. During the year ended 31 December 2005 (“the Year”), the Company had complied with the code provisions and certain recommended best practices of the Code on Corporate Governance Practices (the “Code”) as set out in Appendix 14 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the “Listing Rules”) except for the deviation from provision A.2.1 of the Code in respect of segregation of the roles of chairman and chief executive officer.

## DIRECTORS’ SECURITIES TRANSACTIONS

The Company has adopted the Model Code for Securities Transactions by Directors of Listed Issuers (the “Model Code”) as set out in Appendix 10 of the Listing Rules for securities transactions by directors of the Company. All the members of the board have confirmed, following specific enquiry by the Company, that they have complied with the required standard as set out in the Model Code throughout the year ended 31 December 2005.

## BOARD OF DIRECTORS

### COMPOSITION OF THE BOARD

The Board of Directors comprises:

*Executive Directors:* Zhang Shuyang, *Chairman*  
Tung Chi Wai, Terrence  
Kazunori Watanabe

*Independent Non-Executive Directors:* Ede Hao Xi, Ronald  
Ts’o Shun, Roy  
Li Yueh Chen

### INDEPENDENCE OF THE INDEPENDENT NON-EXECUTIVE DIRECTORS

The Board comprises of three executive directors (with Mr. Zhang Shuyang being the Chairman) and three independent non-executive directors. The independent non-executive directors represent more than one third of the Board. In addition, one of the independent non-executive directors, Mr. Ede Hao Xi, Ronald possesses accounting and related financial management expertise.

### CHAIRMAN AND CHIEF EXECUTIVE OFFICER

The Chairman of the Board is Mr. Zhang Shuyang. Officially, there is no such role as chief executive officer of the Company. Mr. Zhang Shuyang however, is also responsible for the day-to-day operation of the Company. This kind of arrangement deviates from A.2.1 of the Code which stipulates that the roles of chairman and chief executive officer should be separated and should not be performed by the same individual.

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Mr. Zhang Shuyang, being the Chairman of the Board, is primarily responsible for the leadership of the Board and formulating long-term plans and strategies for the Company. The Company considers that the arrangement of Mr. Zhang Shuyang being the Chairman and also the person responsible for the day-to-day operation achieves maximum efficiency and effectiveness in the planning and execution of the Group's long-term strategies and policies. This arrangement would not impair the balance of power and authority between the Board and the management because half of the Board is constituted by independent non-executive directors. The interests of the shareholders as a whole would be adequately and fairly protected through the supervision by the independent non-executive directors.

## BOARD MEETINGS AND INDIVIDUAL ATTENDANCE

During the year, five Board meetings were held and the individual attendance of each Director is set out below:

Name of Director	Number of Board meetings attended	Attendance rate
Zhang Shuyang	5/5	100%
Tung Chi Wai, Terrence	5/5	100%
Kazunori Watanabe	5/5	100%
Ede Hao Xi, Ronald	4/5	80%
Ts'o Shun, Roy	5/5	100%
Li Yueh Chen	5/5	100%
<b>Average attendance rate</b>		<b>96.67%</b>

## HOW THE BOARD OPERATES

The Board is primarily responsible for formulating plans and strategies for the Company. The implementation of those plans and strategies is carried out by the management. A more detailed division of responsibilities is set out as follows.

The Board is primarily responsible for determining the following:

- (1) the operation plans and investment plans;
- (2) the annual financial budget and final accounts;
- (3) the profit distribution and loss recovery plans;
- (4) whether to increase or reduce the capital of the Company and whether to issue corporate bonds;
- (5) the plans for merger, split-up, dissolution or change of the company form;
- (6) the establishment of internal management departments;
- (7) determining the appointment and dismissal of the managers of the Company and fixing their remuneration, and determining, with due consideration to the nomination proposed by the managers, the appointment and dismissal of the vice managers and the financial managers and fixing their remuneration; and
- (8) the basic management framework.



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The management is primarily responsible for the following:

- (1) being in charge of the Company's production, operation and management and implementing the resolutions of the Board;
- (2) implementing the Company's business plan and investment plan;
- (3) devising the plan for internal management structure;
- (4) devising the basic management framework;
- (5) formulating rules for the operation of the Company;
- (6) nominating the appointment or dismissal of the Company's vice managers and financial managers;
- (7) determining the appointment and dismissal of management officers other than those required to be appointed or dismissed by the Board; and
- (8) other responsibilities delegated by the Board or conferred to by the Company's articles of associations.

### **NON-EXECUTIVE DIRECTORS**

Each of the non-executive directors has signed a letter of appointment with the Company for a term of two years. However, such term is subject to re-appointment at general meeting upon retirement by rotation at least once every three years.

### **REMUNERATION OF DIRECTORS**

The Remuneration Committee was established on 12 December 2005. The Remuneration Committee comprises:

Ts'o Shun, Roy, *Chairman*  
Ede Hao Xi, Ronald  
Li Yueh Chen  
Tung Chi Wai, Terrence

The Remuneration Committee comprises mainly of independent non-executive directors.

### **FUNCTIONS OF THE REMUNERATION COMMITTEE**

The functions of the Remuneration Committee include those set out in B.1.3 (a)-(f) of the Code. They include, among others, making recommendations to the Board on the Company's policy and structure for all remuneration of directors and senior management and on the establishment of a formal and transparent procedure for developing policy on such remuneration. The Remuneration Committee also reviews and approves the compensation arrangements relating to dismissal or removal of directors to ensure that such arrangements are in accordance with the relevant contractual terms or are otherwise reasonable and appropriate.



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During the Year, the Board held one meeting for determining remuneration. All six directors attended the meeting and approved the directors' remuneration in accordance with each director's service contract.

## **NOMINATION OF DIRECTORS**

The Nomination Committee was established on 12 December 2005. The Nomination Committee comprises:

Li Yueh Chen, *Chairman*

Ede Hao Xi, Ronald

Ts'o Shun, Roy

Zhang Shuyang

## **FUNCTIONS OF THE NOMINATION COMMITTEE**

The functions of the Nomination Committee are as set out in A.4.5 of the Code. They include, among others, reviewing the composition of the Board, selecting suitably qualified individuals for directorship, assessing the independence of independent non-executive directors and making recommendations to the Board on the appointment of directors.

Before the Nomination Committee was established, the Board was responsible for the selection and recommendation of candidates suitable for directorship. The Board adopted the nomination procedures set out in A.4.5 of the Code. The Board would review the candidates' resumes, consider their qualifications and experiences, and select the most suitable person for directorship.

During the Year, the Board held one meeting to determine the directors' performance. All six directors attended the meeting. At the meeting, the Board reviewed the qualifications and the performance of the existing directors during the Year and the composition of the Board. The Board ensured the independence of the independent non-executive directors and that a sufficient number of independent directors had been in place to balance the power and authority of the Board and the management.

## **AUDITORS' REMUNERATION**

For the year ended 31 December 2005, the auditors of the Company, Ernst & Young, only provided audit services to the Company.

## **AUDIT COMMITTEE**

### **COMPOSITION OF THE AUDIT COMMITTEE**

The Audit Committee was established on 22 June 2004. The Audit Committee comprises:

Ede Hao Xi, Ronald, *Chairman*

Ts'o Shun, Roy

Li Yueh Chen

The Audit Committee comprises of independent non-executive directors. Mr. Ede Hao Xi, Ronald has professional qualification and accounting and related financial management expertise and is the chairman of the committee. The composition of the Audit Committee complies with the requirements under Rule 3.21 of the Listing Rules.

## FUNCTIONS OF THE AUDIT COMMITTEE

The functions of the Audit Committee are as set out in C.3.3(a)-(n) of the Code. They include, among others, making recommendations to the Board on the appointment and removal of auditors, reviewing the Company's financial statements, reviewing the Company's financial controls, internal controls, and risk management system.

## AUDIT COMMITTEE MEETINGS AND INDIVIDUAL ATTENDANCE

Name of Directors	Number of Audit Committee Meetings attended	Attendance rate
Ede Hao Xi, Ronald	2/2	100%
Ts'oo Shun, Roy	2/2	100%
Li Yueh Chen	2/2	100%
<b>Average attendance rate</b>		<b>100%</b>

During the Year, the Audit Committee reviewed the audited consolidated financial statements of the Group for the year ended 31 December 2004 and the interim report for the six months ended 30 June 2005. The Audit Committee discussed with the auditors, on Ernst & Young, the accounting principles and practices adopted by the Group and the recommendations by Ernst & Young on enhancing the management and internal controls of the Company.

## INTERNAL CONTROLS

The Board is responsible for the internal control system of the Group. The Board is committed to implementing an effective and sound internal control system to safeguard the Company's assets, ensure compliance with laws and regulations, manage business risks and protect the interest of the shareholders. Procedures have been designed for financial, operational and compliance controls and for risk management. Some of the Group's key internal control procedures are as follows:

## FINANCIAL CONTROLS

The Company has developed an expense approval system. All expenses, depending on their amount, have to be approved by either department managers, general administrative managers, general managers or directors.

The Company has a credit control system as follows:

- The finance department should analyse the payment history of each existing customers based on the information currently available, and provide the sales department with such analysis. The sales department will then make risk adjustment for the credit limit to be granted. Such amounts shall be approved by the finance department.
- The sales department assesses the risk exposure for new customers and then determines the credit limit to be granted, which is subject to the final approval by the finance department.
- The finance department should frequently assess whether the credit risk of a customer is under control.
- If a customer has a large amount or exceeds the credit limit, the sales department should set up security procedure in order to obtain approval from the finance department.



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- e) The finance department should investigate the impact of credit risks on the Group and the corresponding risk-bearing capacity of the Group, and should ensure that the credit risks which arise from new projects will not affect the operational stability of the existing subsidiaries of the Group.

### OPERATIONAL CONTROLS

Persons who manage custodian of the Company's common seal, exclusive seal, legal representative seal and various certificates shall assume the responsibility of custody and use of the chops and certificates. The transfer of custody to other person shall be subject to the authorisation by the director in charge. Material documents such as contracts and agreements shall be sealed upon authorisation by the director in charge.

The Company has a management committee, which comprises ten members. They include executive directors, general managers of the subsidiaries, the chief engineers of different product R&D departments and general managers of sales departments, all of whom have voting rights. The company secretary and secretary to the Board attend management meetings but have no voting rights. In addition, the Company has an extended management committee, which consists of these ten people and the principal officers of the other departments who however have no voting rights. The extended management committee meets once every month and the activities primarily include matters such as examining and reviewing the consolidated financial statements of the previous month, reviewing the operation of the previous month, reviewing and improving the internal controls of the Company, discussing significant events (which represent purchase projects with subject amount exceeding RMB1 million, sales projects with subject amount exceeding RMB1.5 million and other material projects), acting on appropriate resolutions and authorisations and appointing and removing the Company's senior management staff. In connection with the resolutions, decisions shall be made only by the members with voting rights.

The Company has established rules in relation to contract approval. They are: (1) contracts shall be approved by departmental managers and the Company's general manager in ordinary circumstances; and (2) purchase contracts with subject amount exceeding RMB1 million, sales contracts with subject amount exceeding RMB1.5 million and other material contracts shall be examined by the legal advisors at the Company's legal department and approved by the Company's general manager.

### COMPLIANCE CONTROLS

The Group has a legal department which is constituted by the Office of the Board. The Company also retains PRC and Hong Kong legal advisers to safeguard the Company's and shareholders' interests.

The Board and the Audit Committee have reviewed the effectiveness of the internal control system of the Group for the Year including financial, operational and compliance controls and risk management. The Board and the Audit Committee have sought to improve the system and also to remedy the deficiencies which were identified through the system.

### FINANCIAL REPORTING

The Board is responsible for preparing the accounts. The Board and the Audit Committee have reviewed the audited consolidated financial statements of the Group for the year ended 31 December 2005 and are of the views that those statements represent a true and fair view of the financial position and performance of the Group for the year.

The statement by the auditors of the Company regarding their reporting responsibilities is set out in the Report of the Auditors on page 38.