

Corporate governance report

Esprit is committed in achieving high standards of corporate governance. The Company has continued to devote considerable efforts to identify and formalize the best practices according to international standards for the financial year ended June 30, 2006. The Esprit Corporate Governance Code was adopted by the board (the “Board”) of directors (the “Director(s)”) of the Company which ensures greater transparency and quality of disclosure as well as more effective risk control. We believe our commitment in high standard practices will translate into long-term value and ultimately maximizing returns to shareholders and stakeholders. Management’s commitment in building long term interests for shareholders and in conducting business in a socially responsible and professional manner has earned the Company widespread market recognitions. During the financial year, Esprit received, amongst others, the “Top 50 Management Teams in Asia” award from CFO Asia and being ranked number 10 of “Top 25 CG Companies of Asia-Pacific Large Caps” by CLSA.

The Company has applied the principles and complied with 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 throughout the year ended June 30, 2006, except that Non-executive Directors of the Company do not have a specific term of appointment as detailed below.

The Board

The Board’s primary role is to protect and enhance long-term shareholder value. It focuses on the Group’s overall strategic policy, monitors performance and provides proper supervision to ensure proper business conducts and effective management of the highest quality. The Board views that the collective and individual responsibilities of the Directors to all shareholders for the manner in which the affairs of the Company are managed, controlled and operated are important.

The Board has delegated the authority and responsibility for implementing business strategies and management of the daily operations of the Group’s business to the management. While allowing management substantial autonomy to run and develop the business, the Board plays a key role in structuring and monitoring the reporting systems and internal controls.

Decisions reserved for the Board are mainly related to:

- * The long term objectives and strategy of the Group;
- * Monitoring the performance of management;
- * Ensuring that a framework of prudent and effective internal controls is in place to enable risks to be assessed and managed;
- * Monitoring the quality and timeliness of external reporting;
- * Monitoring the compliance with applicable laws and regulations, and also with corporate governance policies.

The posts of the Chairman and Group CEO are held separately to reinforce their respective independence, accountability and responsibility. Mr. Michael YING Lee Yuen is the Chairman of the Company and Mr. Heinz Jürgen KROGNER-KORNALIK is the Group CEO. This segregation ensures clearly defined roles with the Chairman having responsibility to monitor the Group’s business strategies and the Group CEO having responsibility to manage the day-to-day business. The respective responsibilities of the Chairman and the Group CEO are set out in the Esprit Corporate Governance handbook.

The Board comprises ten Directors, including the Chairman of the Board. Five of them are Executive Directors. The remaining are Non-executive Directors of whom three are independent. The Non-executive Directors have no fixed term of service with the Company and are subject to the requirement of retirement by rotation and re-election by shareholders at annual general meeting ("AGM") in accordance with the Company's Bye-laws. The Non-executive Directors come from diverse business and professional backgrounds, bringing in valuable expertise and experience that promotes the best interests of the Group and its shareholders. Independent Non-executive Directors ensure the Board accounts for the interests of all shareholders and subject matters are considered in an objective manner. The Company has received confirmation from each Independent Non-executive Director about his independence as set out in Rule 3.13 of the Listing Rules and continues to consider each of them to be independent.

The Board conducts at least four regular Board meetings a year and additional meetings are held as and when required to discuss significant events or important issues. Sufficient notice is given for regular Board meetings to all Directors enabling them to attend and reasonable notice will be given in case of special Board meetings. The Group ensures that appropriate and sufficient information is provided to Board members in a timely manner to keep them abreast of the Group's latest developments thereby assisting them in the discharge of their duties. Minutes of the Board, the Audit Committee, the Remuneration Committee, the Nomination Committee and the General Committee are kept by the Company Secretary, which are open for inspection following reasonable notice by any Director.

Minutes of the Board meetings and Board Committee meetings recorded in sufficient detail matters considered in the meetings, decisions reached, including any concerns or queries raised by the Directors or dissenting views expressed. Draft and final versions of minutes of the Board and other Board committees are sent to all Directors or committee members for comments and records respectively within a reasonable time after the meeting.

The Company has established a policy enabling all Directors to seek independent professional advice in appropriate circumstances, at the Company's expense. The Board provides separate independent professional advice to Directors to assist the relevant Director or Directors to discharge his/her duties to the Company as and when requested or necessary.

The attendance of individual members of the Board and other Board Committees meetings during the financial year ended June 30, 2006 is set out in the table on page 48:

Directors	Board	Meetings attended/Held		
		Audit Committee	Nomination Committee	Remuneration Committee
Executive Directors				
Michael YING Lee Yuen, Chairman	4/4			3/3
Heinz Jürgen KROGNER-KORNALIK, Deputy Chairman	4/4			
John POON Cho Ming, Deputy Chairman	4/4		1/1	
Thomas Johannes GROTE	4/4			
Jerome Squire GRIFFITH	4/4			
Non-executive Directors				
Jürgen Alfred Rudolf FRIEDRICH	4/4	4/4		
Simon LAI Sau Cheong	3/4		1/1	
Independent Non-executive Directors				
Paul CHENG Ming Fun	4/4	4/4	1/1	
Alexander Reid HAMILTON	4/4	4/4		3/3
Raymond OR Ching Fai	3/4	4/4		3/3

The Company has complied with the Code on Corporate Governance Practices (the “Code”) as set out in Appendix 14 of the Listing Rules throughout the year ended June 30, 2006, only with deviation from code provision A.4.1 of the Code.

Under the code provision A.4.1 of the Code, Non-executive Directors should be appointed for a specific term, subject to re-election. However, Non-executive Directors of the Company do not have a specific term of appointment.

To comply with the code provision A.4.2 of the Code, relevant amendment was made to Bye-law 87 of the Company’s Bye-laws with the approval of the shareholders to the effect that all Directors including Non-executive Directors of the Company are subject to retirement by rotation in the annual general meeting of the Company and each Director is effectively appointed under an average term of 3 years.

Under the Company’s Bye-laws, one-third of the Directors must retire, thus becoming eligible for re-election at each annual general meeting. This year, Messrs. Heinz Jürgen KROGNER-KORNALIK, Jürgen Alfred Rudolf FRIEDRICH and Paul CHENG Ming Fun will retire at the forthcoming AGM of the Company and all being eligible to offer themselves for re-election. Their biographical details will be set out in the circular to shareholders to assist shareholders in making an informed decision on their elections. None of the Directors for re-election at the forthcoming AGM has a service contract with any member of the Group which is not determinable by the relevant employer within one year without payment of compensation (other than statutory compensation).

Mr. Heinz Jürgen KROGNER-KORNALIK has entered into service contract with a member of the Group that does not provide for a fixed period of service and can be terminated by the Company by giving four months’ notice.

Both Mr. Jürgen Alfred Rudolf FRIEDRICH and Mr. Paul CHENG Ming Fun do not have a service contract with the Company. They have no fixed term of service with the Company and are subject to retirement by rotation and re-election in accordance with the Bye-laws of the Company.

Auditors’ Remuneration

A summary of fees for audit and non-audit services for the financial year ended June 30, 2006 is as follows:

Nature of the Services	2006 HK\$’000	2005 HK\$’000
Audit services		
– Current year	11,250	8,376
– Underprovision in prior year	802	–
Other services	5,958	5,561
	18,010	13,937

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To oversee particular aspects of the Company's affairs and to assist in the execution of its responsibilities, the Board has established four Board Committees, namely Audit Committee, Nomination Committee, Remuneration Committee and General Committee. Non-executive Directors play an important role in these committees to ensure independent and objective views are expressed and to promote critical review and control.

Audit Committee

The Audit Committee was established to assist the Board in safeguarding the Company's assets by providing an independent review of the effectiveness of the financial reporting process and the internal control and risk management systems of the Company. The committee also oversees the audit process and performs other duties as assigned by the Board. The Terms of Reference of the Audit Committee that have been adopted by the Audit Committee are posted on the Company's website. All the members of our Audit Committee are Non-executive Directors, with a majority (including the chairman of the Audit Committee) being Independent Non-executive Directors. The committee met 4 times in FY2005/2006.

The Members of the Audit Committee are:

Jürgen Alfred Rudolf FRIEDRICH
Paul CHENG Ming Fun
Alexander Reid HAMILTON (Chairman)
Raymond OR Ching Fai

The Audit Committee is provided with sufficient resources to discharge its duties and meets regularly with management, internal auditors and external auditors and reviews their reports. During the financial year, the Audit Committee reviewed the interim results and the annual results of the Group for the year ended June 30, 2006 as well as the accounting principles and practices adopted by the Group, reviewed the nature, scope and findings of internal and external audits in addition to reviewing the Company's treasury activities, liquidity and risk management. Our Group CFO, the external auditors, internal auditors and senior management attended the meetings to answer any questions raised by the Audit Committee.

Nomination Committee

The Nomination Committee was established to enhance transparency and highlight fairness in the selection and appointment of Board members. The Nomination Committee consists of three members, the majority of which are Non-executive Directors. The Terms of Reference of the Nomination Committee which have been adopted by the Board are posted on the Company's website. The committee met once during the financial year.

The Members of the Nomination Committee are:

John POON Cho Ming
Simon LAI Sau Cheong
Paul CHENG Ming Fun

In evaluating whether an appointee is suitable to act as a Director, the Board will consider the skills and expertise of the appointee; as well as personal ethics, integrity and the willingness to commit time to the affairs of the Group. Where the appointee is appointed as an Independent Non-executive Director, the Nomination Committee will also consider his/her independence. During the year, the Nomination Committee had also reviewed and made recommendations in respect of the re-appointment of retiring Directors, which were approved by the shareholders at the last AGM.

Remuneration Committee

The responsibility of the Remuneration Committee is to formulate transparent procedures for developing remuneration policies and packages for key executives. The Remuneration Committee comprises three members, the majority of whom are Independent Non-executive Directors.

The Members of the Remuneration Committee are:

Michael YING Lee Yuen
Alexander Reid HAMILTON
Raymond OR Ching Fai

The Terms of Reference of the Remuneration Committee that have been adopted by the Remuneration Committee are posted on the Company's website. The Committee met 3 times during the financial year. A summary of the work performed by the Remuneration Committee during the year is set out on page 64.

General Committee

The General Committee is established and responsible for discussion, consideration and approval of certain routine corporate administrative matters of the Company. The General Committee comprises four members, the majority of which are Executive Directors. The committee met 26 times in FY2005/2006.

The Members of the General Committee are:

Michael YING Lee Yuen
Heinz Jürgen KROGNER-KORNALIK
John POON Cho Ming
Simon LAI Sau Cheong

Model Code for Securities Transactions by Directors

The Company has adopted a code of conduct regarding Directors' securities transactions 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") contained in Appendix 10 of the Listing Rules.

The Company has made specific enquiry with all Directors and all of them confirmed that, for the financial year ended June 30, 2006 they have complied with the required standard set out in the Model Code.

Voting by Poll

The Company's shareholders are adequately informed of the procedures for and their rights to demand voting by poll in shareholders' meetings at which their approvals are sought through disclosure in the Company's circulars.

At the 2005 AGM, the Chairman of the Meeting demanded a poll on all resolutions. The procedures for demanding a poll by the shareholders were incorporated in the circular sent to the shareholders in the time stipulated. Secretaries Limited, the Company's branch share registrar in Hong Kong, was appointed as the scrutineer to ensure the votes were properly counted.

Directors' Responsibilities for the Financial Statements

The Directors are responsible for overseeing the preparation of financial statements for the year ended June 30, 2006, which give a true and fair view of the state of affairs of the Company and of the cash flows for that financial year. In preparing the financial statements for the year ended June 30, 2006, the Directors have selected appropriate accounting policies, applied them consistently in accordance with the International Financial Reporting Standards and made judgments and estimates that are prudent and reasonable, and have prepared the financial statements on the ongoing concern basis.

The Directors are responsible for keeping proper accounting records, for safeguarding the assets of the Company and for taking reasonable steps for the prevention and detection of fraud and other irregularities.

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Internal Control and Risk Management

A sound internal control system mitigates the Group's risk exposure while facilitating the effectiveness and efficiency of operations and ensuring compliance with laws and regulations. The system is independently reviewed on an ongoing basis so that practical and effective control systems are implemented to provide reasonable assurance in protecting material assets and in identifying business risks. The Group is committed to the identification, monitoring and management of risks associated with its business activities and has implemented practical and effective control systems including:

- A tailored organizational and governance structure with clearly defined lines of responsibility;
- Budgeting and forecasting systems for performance measurement and monitoring of business units;
- A quarterly review of the Group's performance by the Audit Committee and the Board;
- Protection of the Group's trademarks globally;
- Group-wide insurance programs; and
- A global cash management system deployed to enhance proper control and yield of cash assets.

The Company has established an Internal Audit function that is responsible for performing regular and systematic reviews of internal control system so as to provide reasonable assurance that they continue to operate satisfactorily and effectively within the Group and the Company. The attainment of such objectives involves the following activities being carried out by the Internal Audit function:

- reviewing and appraising the soundness, adequacy and application of accounting, financial and other controls and promoting effective control in the Group and the Company;
- ascertaining the extent of compliance with established policies, procedures and statutory requirements;
- ascertaining the extent to which the Group's and the Company's assets are accounted for and safeguarded from losses of all kinds;
- appraising the reliability and usefulness of information for reporting to management;
- recommending improvements to the existing system of internal control; and
- carrying out investigations and special reviews requested by management and/or the Audit Committee of the Company.

To complement the in-house Internal Audit function, the Company has appointed KPMG to perform periodic internal audits. Internal auditors present the audit reports to the Audit Committee and would follow up on any action plans agreed by management.

The Code requires the Board to carry out a review on the effectiveness of the Company's system of internal control. This review is carried out by the Internal Audit function and their findings and opinion on the effectiveness of the Company's system of internal control is considered by the Audit Committee, which reports to the Board.

The Board has received a high level risk assessment from an external consultant with no material issue noted, and has reviewed the effectiveness of the internal control system of the Group.

Pro-active Investor Relations

The Board of Esprit recognizes the importance of maintaining two-way communication with its shareholders. Annual and interim reports offer comprehensive operational and financial performance information to shareholders and the annual general meeting provides a forum for shareholders to exchange views directly with the Board. Our Investor Relations Department communicates with research analysts and institutional investors in an on-going manner and provides them with up-

to-date and comprehensive information about the Company's corporate developments. To ensure our investors have a better understanding of the Company, including, among others, its performance, business activities and strategy, our management also engages in pro-active investor relations program. Both our Group CEO and Group CFO meet with research analysts and the press after our results announcements, attend major investors' conferences and participate in international non-deal roadshows to communicate the Company's financial performance and global business strategy. The Company also practises timely and non-selective dissemination of material information. Current information on the Company including interim and annual reports, announcements and press releases, presentations and webcasts can be retrieved through our investor relations website www.espritholdings.com. Information on the website is updated in a timely manner to ensure that speed, fairness and transparency remain the hallmarks of our disclosure practices. Our continuing efforts to enhance our investor relations program gained market recognition in the past years. The Company ranked, among others, number two for the "Best Investor Relations" award by FinanceAsia in April 2006 and received the "Best Investor Relations (Buy-side view)" in Hong Kong and in the Retail Sector awards from Asia Investor Relations Market Report in November 2005. The list of awards honored to the Company by different parties recently is tabled on page 54.

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Time	Award	Awarding Party
July 2006	Gold award, Best Overall Annual Report (Retail Fashion Category)	INTERNATIONAL ARC AWARDS
April 2006	Best Investor Relations (No. 2) Best CFO (No. 2) Best Commitment to Strong Dividends (No. 3) Best Managed Company (No. 4) Best Corporate Governance (No. 7)	FINANCEASIA
November 2005	Best CFO in the Retail Sector Best Investor Relations in Hong Kong (Buy-side view) Best Investor Relations in the Retail Sector (Buy-side view)	ASIA INVESTOR RELATIONS MARKET REPORT
November 2005	2005 HKMA Best Annual Reports Awards: Honourable Mention Citation for Achievement in Design	HONG KONG MANAGEMENT ASSOCIATION ("HKMA")
October 2005	Asia's Fab 50 Companies	FORBES ASIA
October 2005	Asian BusinessWeek 50	ASIAN BUSINESSWEEK
October 2005	Top 50 Management Teams in Asia	CFO ASIA
October 2005	The Top Performers - Retail	SOUTH CHINA MORNING POST
October 2005	CG Watch 2005, Corporate Governance in Asia Top 25 CG Companies of Asia-Pacific Large Caps (rank no. 10) Top CG Quartile for Hong Kong (top 15) QARP (Quality at Reasonable Price) for Asia ex-Japan Large Caps (top 20)	CLSA

