Consolidated income statement

for the year ended 31 December 2006 (Expressed in Renminbi)	Note	2006 RMB million	2005 RMB million (restated – Note 1)
Revenues			
Coal revenue		**45,948**	39,926
Power revenue		**16,628**	10,879
Other revenues	5	**1,664**	1,437
Total operating revenues	4	**64,240**	52,242
Cost of revenues			
Coal purchased from third parties		**(6,935)**	(4,339)
Materials, fuel and power		**(3,236)**	(2,545)
Personnel expenses		**(2,441)**	(2,046)
Depreciation and amortisation		**(6,346)**	(5,182)
Repairs and maintenance		**(3,142)**	(2,660)
Transportation charges		**(6,246)**	(5,152)
Others	6	**(4,114)**	(3,195)
Total cost of revenues		**(32,460)**	(25,119)
Selling, general and administrative expenses		**(4,166)**	(3,311)
Other operating expense, net		**(318)**	(150)
Total operating expenses	7	**(36,944)**	(28,580)
Profit from operations		**27,296**	23,662
Finance income	8	**508**	885
Finance expenses	8	**(2,608)**	(2,945)
Net finance costs		**(2,100)**	(2,060)
Investment (loss)/income		**(1)**	10
Share of profits less losses of associates		**478**	461
Profit before income tax		**25,673**	22,073
Income tax	9	**(5,388)**	(4,080)
Profit for the year		**20,285**	17,993
Attributable to:			
Equity shareholders of the Company		**17,460**	15,619
Minority interests		**2,825**	2,374
Profit for the year		**20,285**	17,993
Dividends payable to equity shareholders of the Company attributable to the year			
Dividends resolved and proposed after the balance sheet date	13	**6,150**	7,404
Earnings per share (RMB)	14		
- Basic		**0.965**	0.937
- Diluted		**0.965**	0.937

The notes on pages 116 to 175 form part of these financial statements.

Consolidated balance sheet

at 31 December 2006 (Expressed in Renminbi)	Note	2006 RMB million	2005 RMB million (restated – Note 1)
Non-current assets			
Property, plant and equipment, net	15	**107,859**	82,530
Construction in progress	16	**14,115**	21,910
Intangible assets	17	**1,133**	1,293
Interest in associates	19	**2,369**	3,686
Other investments	20	**1,066**	74
Lease prepayments		**4,848**	3,857
Deferred tax assets	27	**1,569**	1,435
Total non-current assets		**132,959**	114,785
Current assets			
Inventories	22	**4,761**	3,572
Available-for-sale investments	23	**2,000**	–
Accounts and bills receivable, net	24	**4,860**	2,682
Prepaid expenses and other current assets	25	**3,059**	1,301
Time deposits with original maturity over three months	26	**8**	66
Cash and cash equivalents	26	**15,501**	19,863
Total current assets		**30,189**	27,484
Total assets		**163,148**	142,269
Current liabilities			
Short-term borrowings and current portion of long-term borrowings	28	**14,842**	9,645
Current portion of long-term payable	32	**88**	72
Accounts and bills payable	29	**9,133**	6,834
Income tax payable		**2,193**	1,124
Accrued expenses and other payables	30	**6,977**	6,813
Total current liabilities		**33,233**	24,488
Net current (liabilities)/assets		**(3,044)**	2,996
Total assets less current liabilities		**129,915**	117,781
Non-current liabilities			
Long-term borrowings, less current portion	28	**40,840**	40,793
Long-term payable, less current portion	32	**2,426**	2,405
Accrued reclamation obligations	31	**942**	852
Deferred tax liabilities	27	**1,006**	744
Total non-current liabilities		**45,214**	44,794
		84,701	72,987
Equity			
Share capital	33	**18,090**	18,090
Reserves		**48,681**	39,787
Equity attributable to equity shareholders of the Company		**66,771**	57,877
Minority interests		**17,930**	15,110
Total equity		**84,701**	72,987

Approved and authorised for issue by the board of directors on 23 March 2007.

Chen Biting
Chairman

Ling Wen
Director and President

The notes on pages 116 to 175 form part of these financial statements.

Balance sheet

at 31 December 2006 (Expressed in Renminbi)	Note	2006 RMB million	2005 RMB million (restated – Note 1)
Non-current assets			
Property, plant and equipment, net	15	**30,899**	27,170
Construction in progress	16	**3,664**	1,680
Intangible assets	17	**324**	344
Investments in subsidiaries	18	**19,687**	18,119
Interest in associates	19	**1,480**	2,982
Other investments	20	**1,002**	10
Other non-current financial assets	21	**377**	–
Lease prepayments		**566**	598
Deferred tax assets	27	**886**	774
Total non-current assets		**58,885**	51,677
Current assets			
Inventories	22	**2,670**	1,964
Available-for-sale investments	23	**2,000**	–
Accounts and bills receivable, net	24	**1,457**	1,324
Prepaid expenses and other current assets	25	**11,218**	9,317
Cash and cash equivalents	26	**13,937**	18,716
Total current assets		**31,282**	31,321
Total assets		**90,167**	82,998
Current liabilities			
Short-term borrowings and current portion of long-term borrowings	28	**5,101**	3,480
Current portion of long-term payable	32	**88**	72
Accounts and bills payable	29	**3,512**	2,596
Income tax payable		**1,227**	564
Accrued expenses and other payables	30	**4,474**	3,829
Total current liabilities		**14,402**	10,541
Net current assets		**16,880**	20,780
Total assets less current liabilities		**75,765**	72,457
Non-current liabilities			
Long-term borrowings, less current portion	28	**11,544**	14,868
Long-term payable, less current portion	32	**2,426**	2,405
Accrued reclamation obligations	31	**568**	497
Deferred tax liabilities	27	**491**	244
Total non-current liabilities		**15,029**	18,014
		60,736	54,443
Equity			
Share capital	33	**18,090**	18,090
Reserves		**42,646**	36,353
Total equity		**60,736**	54,443

Approved and authorised for issue by the board of directors on 23 March 2007.

Chen Biting
Chairman

Ling Wen
Director and President

The notes on pages 116 to 175 form part of these financial statements.

Consolidated statement of changes in equity

for the year ended 31 December 2006
(Expressed in Renminbi)

	Equity attributable to equity shareholders of the Company										
	Share capital RMB million (Note 33)	Share premium RMB million (Note i)	Capital reserve RMB million (Note ii)	Revaluation reserve RMB million (Note iii)	Future development fund RMB million (Note iv)	Statutory reserves RMB million (Note v)	Other reserves RMB million (Note vi)	Retained earnings RMB million	Total RMB million	Minority interests RMB million	Total equity RMB million
At 1 January 2005 (as previously reported)	15,000	–	(6,591)	7,186	338	230	849	8,384	25,396	13,085	38,481
Adjusted for acquisition of Jinjie Energy (Note 1)	–	–	–	–	–	–	20	(1)	19	9	28
At 1 January 2005 (as restated)	15,000	–	(6,591)	7,186	338	230	869	8,383	25,415	13,094	38,509
Issuance of shares upon public offering	3,090	21,568	–	–	–	–	–	–	24,658	–	24,658
Shares issue expenses	–	(755)	–	–	–	–	–	–	(755)	–	(755)
Profit for the year	–	–	–	–	–	–	–	15,619	15,619	2,374	17,993
Appropriations	–	–	–	–	543	2,898	–	(3,441)	–	–	–
Revaluation surplus realised	–	–	–	(2)	–	–	–	2	–	–	–
Realisation of deferred tax	–	–	–	–	–	–	(10)	10	–	–	–
Dividend for 2004 (Note 13)	–	–	–	–	–	–	–	(7,549)	(7,549)	–	(7,549)
Adjusted for acquisition of Jinjie Energy (Note 1)	–	–	–	–	–	–	489	–	489	–	489
Capital contributions from minority interests	–	–	–	–	–	–	–	–	–	830	830
Distributions to minority interests	–	–	–	–	–	–	–	–	–	(1,188)	(1,188)
At 31 December 2005	18,090	20,813	(6,591)	7,184	881	3,128	1,348	13,024	57,877	15,110	72,987
At 1 January 2006	**18,090**	**20,813**	**(6,591)**	**7,184**	**881**	**3,128**	**1,348**	**13,024**	**57,877**	**15,110**	**72,987**
Profit for the year	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**17,460**	**17,460**	**2,825**	**20,285**
Appropriations	**–**	**–**	**–**	**–**	**697**	**1,614**	**–**	**(2,311)**	**–**	**–**	**–**
Revaluation surplus realised	**–**	**–**	**–**	**(4)**	**–**	**–**	**–**	**4**	**–**	**–**	**–**
Realisation of deferred tax	**–**	**–**	**–**	**–**	**–**	**–**	**(17)**	**17**	**–**	**–**	**–**
Dividend for 2005 (Note 13)	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**(7,404)**	**(7,404)**	**–**	**(7,404)**
Capital contributions from minority interests	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**1,173**	**1,173**
Distributions to minority interests	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**(1,178)**	**(1,178)**
Consideration of the Acquisition (Note 1)	**–**	**–**	**–**	**–**	**–**	**–**	**(1,162)**	**–**	**(1,162)**	**–**	**(1,162)**
At 31 December 2006	**18,090**	**20,813**	**(6,591)**	**7,180**	**1,578**	**4,742**	**169**	**20,790**	**66,771**	**17,930**	**84,701**

The notes on pages 116 to 175 form part of these financial statements.

Notes:

(i) The share premium represents the difference between the total amount of the par value of shares issued and the amount of the net proceeds received upon the global initial public offering.

(ii) The capital reserve represents the difference between the total amount of the par value of shares issued and the amount of the net assets, net of revaluation and other reserves, transferred from Shenhua in connection with the Restructuring (as defined in Note 1).

(iii) As required by the relevant PRC rules and regulations with respect to the Restructuring (as defined in Note 1), the property, plant and equipment of the Group as at 31 December 2003 were revalued by China Enterprise Appraisal Co., Ltd., independent valuers registered in the PRC, on a depreciated replacement cost basis.

(iv) Pursuant to the relevant PRC regulations, the Company and its subsidiaries are required to make a transfer to future development fund based on RMB7.00 to RMB8.00 (2005: RMB7.00 to RMB8.00) per tonne of raw coal mined (net of usage). The fund can only be used for the future development of the coal mining business and is not available for distribution to shareholders.

(v) Statutory reserves

Statutory surplus reserve

According to the Company's Articles of Association, the Company is required to transfer 10% of its net profit as determined in accordance with the PRC Accounting Rules and Regulations to its statutory surplus reserve until the reserve balance reaches 50% of the registered capital. The transfer to this reserve must be made before distribution of a dividend to shareholders.

Statutory surplus reserve can be used to make good previous years' losses, if any, or to expand the Company's business, and may be converted into share capital by the issue of new shares to shareholders in proportion to their existing shareholdings or by increasing the par value of the shares currently held by them, provided that the balance after such issue is not less than 25% of the registered capital.

For the year ended 31 December 2006, the Company transferred RMB1,614 million (2005: RMB1,449 million), being 10% of the current year's net profit as determined in accordance with the PRC Accounting Rules and Regulations, to this reserve.

Statutory public welfare fund

The Company made an appropriation of RMB1,449 million to statutory public welfare fund in 2005. Pursuant to the revised Company Law of the PRC, the Company is not required by law to make appropriations to statutory public welfare fund with effect from 1 January 2006. The balances of the statutory public welfare fund as at 1 January 2006 of RMB1,564 million were transferred to statutory surplus reserve.

Discretionary surplus reserve

The appropriation to the discretionary surplus reserve is subject to the shareholders' approval. The utilisation of the reserve is similar to that of the statutory surplus reserve.

The directors have not proposed any appropriation to the discretionary surplus reserve in 2006 and 2005.

(vi) In connection with the Restructuring (as defined in Note 1), the land use rights of the Group were revalued as required by the relevant PRC rules and regulations as at 31 December 2003. The revalued amount will serve as the tax base for future years. The land use rights were not revalued for financial reporting purpose and accordingly, a deferred tax asset was created with an increase in shareholders' equity, net of minority interests. The amount also includes the difference between the considerations paid over the amount of the underlying net assets of the interests acquired in Shaanxi Guohua Jinjie Energy Corporation ("Jinjie Energy"). The transaction was recorded at historical cost and was reflected as changes in other reserves in the year the acquisition occurred.

The notes on pages 116 to 175 form part of these financial statements.

Consolidated cash flow statement

for the year ended 31 December 2006 (Expressed in Renminbi)	Note	2006 RMB million	2005 RMB million (restated – Note 1)
Net cash from operating activities	(a)	**23,622**	25,831
Investing activities			
Capital expenditure		**(22,839)**	(18,578)
Lease prepayments		**(1,096)**	(198)
Purchase of investments		**(2,106)**	(750)
Proceeds from disposal of investments		**614**	58
Proceeds from disposal of property, plant and equipment and lease prepayments		**431**	132
Increase in time deposits with maturity over three months		**–**	(61)
Maturity of time deposits with maturity over three months		**58**	50
Net cash used in investing activities		**(24,938)**	(19,347)
Financing activities			
Proceeds from bank and other loans		**30,709**	37,682
Repayments of bank and other loans		**(25,184)**	(47,439)
Consideration of the Acquisition		**(1,162)**	–
Dividend paid to minority interests		**(1,178)**	(1,188)
Contributions from minority interests		**1,173**	830
Dividend paid to equity shareholders of the Company		**(7,404)**	(7,549)
Net proceeds from issuance of new shares upon listing		**–**	23,903
Net cash (used in)/from financing activities		**(3,046)**	6,239
Net (decrease)/increase in cash and cash equivalents		**(4,362)**	12,723
Cash and cash equivalents, at the beginning of the year		**19,863**	7,140
Cash and cash equivalents, at the end of the year		**15,501**	19,863

The notes on pages 116 to 175 form part of these financial statements.

Consolidated cash flow statement *(continued)*

	2006 RMB million	2005 RMB million (restated – Note 1)
(a) Reconciliation of profit for the year to net cash from operating activities		
Profit before income tax	**25,673**	22,073
Adjustments for:		
Depreciation and amortisation	**6,611**	5,377
Impairment losses on property, plant and equipment	**147**	41
Investment loss/(income)	**1**	(10)
Interest income	**(250)**	(266)
Share of profits less losses of associates	**(478)**	(461)
Net interest expense	**2,585**	2,577
Loss on remeasurement of derivative financial instruments to fair value	**23**	368
Unrealised foreign exchange gain	**(281)**	(994)
Loss on disposal of property, plant and equipment and lease prepayments	**72**	187
	34,103	28,892
(Increase)/decrease in accounts and bills receivable	**(2,178)**	231
Increase in inventories	**(1,189)**	(881)
(Increase)/decrease in prepaid expenses and other current assets	**(94)**	1,557
(Decrease)/increase in accounts and bills payable	**(678)**	986
Increase in accrued expenses and other payables	**109**	2,080
Cash generated from operations	**30,073**	32,865
Interest received	**250**	266
Interest paid	**(2,809)**	(3,105)
Dividend received from investments	**299**	143
Income tax paid	**(4,191)**	(4,338)
Net cash from operating activities	**23,622**	25,831

The notes on pages 116 to 175 form part of these financial statements.

Notes to the financial statements

for the year ended 31 December 2006
(Expressed in Renminbi)

1 Principal activities and organisation

Principal activities

China Shenhua Energy Company Limited (the "Company") and its subsidiaries (hereinafter collectively referred to as the "Group") are principally engaged in: (i) the production and sale of coal; and (ii) the generation and sale of power in the People's Republic of China (the "PRC"). The Group operates coal mines as well as an integrated railway network and seaports that are primarily used to transport the Group's coal sales. The primary customers of the Group's coal sales include power plants and metallurgical producers in the PRC. The Group also operates power plants in the PRC, which are engaged in the generation and sale of coal-based power to provincial/regional electric grid companies.

Organisation

The Company was established in the PRC on 8 November 2004 as a joint stock limited company as part of the Restructuring (as defined below) of Shenhua Group Corporation Limited ("Shenhua" or the "Parent Company"), a state-owned enterprise under the direct supervision of the State Council of the PRC. Prior to the establishment of the Company, the coal production and power generation operations were carried on by various mining companies and power plant entities wholly owned or controlled by Shenhua.

In connection with the Restructuring (as defined below), Shenhua's principal coal production and power generation operations together with the related assets and liabilities that were transferred to the Company were segregated and separately managed effective on 31 December 2003 (the "Restructuring"). Pursuant to the Restructuring, property, plant and equipment related to the operations and businesses that were transferred to the Company were revalued as at 31 December 2003 as required by the PRC rules and regulations.

On 8 November 2004, in consideration for Shenhua transferring the coal mining and power generating assets and liabilities to the Company, the Company issued 15 billion domestic state-owned ordinary shares with a par value of RMB1.00 each to Shenhua. The shares issued to Shenhua represented the entire registered and paid-up share capital of the Company at that date.

In June 2005, the Company issued 2,785,000,000 H shares with a par value of RMB1.00 each, at a price of HK$7.50 per H share by way of a global initial public offering to Hong Kong and overseas investors. As part of the global initial public offering, 278,500,000 domestic state-owned ordinary shares of RMB1.00 each owned by Shenhua were converted into H shares and sold to Hong Kong and overseas investors. The Company was listed on the Stock Exchange of Hong Kong Limited ("the Stock Exchange") on 15 June 2005. In July 2005, the Company issued 304,620,455 H shares with a par value of RMB1.00 each, at a price of HK$7.50 per H share upon the exercise of the over-allotment option in connection with the global initial public offering. As part of the exercise of the over-allotment option, 30,462,045 domestic state-owned ordinary shares of RMB1.00 each owned by Shenhua were converted into H shares and sold to Hong Kong and overseas investors. A total of 3,398,582,500 H shares were listed on the Stock Exchange.

Pursuant to a resolution passed at the Directors' meeting on 10 March 2006, the Company acquired a 70% stake in Shaanxi Guohua Jinjie Energy Corporation ("Jinjie Energy") (the "Acquisition") from Beijing Guohua Power Company Limited ("Beijing Guohua Power"), a subsidiary of Shenhua, at a consideration of RMB1,162 million. The Acquisition was completed in August 2006.

1 Principal activities and organisation *(continued)*

Restatement

As the Company and Jinjie Energy were under common control of Shenhua, the Acquisition has been reflected as a combination of entities under common control and accounted for in a manner similar to a pooling-of-interests. Accordingly, the assets and liabilities of Jinjie Energy have been accounted for at historical costs and the financial statements of the Company prior to the Acquisition have been restated to include the results of operations of Jinjie Energy on a combined basis. The consideration paid by the Company for the Acquisition of Jinjie Energy has been accounted for as an equity transaction in the consolidated statement of changes in equity.

The results of operations for the year ended 31 December 2005, the financial conditions as at 31 December 2005 and the equity attributable to equity shareholders of the Company as at 31 December 2005 and 1 January 2005 previously reported by the Group and Jinjie Energy and the combined amounts presented in the accompanying consolidated financial statements are set out below:

	The Group (as previously reported) RMB million	**Jinjie Energy** RMB million	**Combined** RMB million
Results of operations for the year ended 31 December 2005:			
Revenues	52,242	–	52,242
Profit/(loss) from operations	23,684	(22)	23,662
Profit/(loss) for the year	18,012	(19)	17,993
Basic earnings per share (RMB)	0.937	–	0.937
Financial conditions as at 31 December 2005:			
Current assets	27,419	65	27,484
Total assets	139,260	3,009	142,269
Current liabilities	22,837	1,651	24,488
Total liabilities	66,771	2,511	69,282
Minority interests	15,107	3	15,110
Equity attributable to equity shareholders of the Company	57,382	495	57,877
Equity attributable to equity shareholders of the Company as at 1 January 2005	25,396	19	25,415

2 Significant accounting policies

(a) Statement of compliance

The financial statements have been prepared in accordance with all applicable International Financial Reporting Standards ("IFRSs") promulgated by the International Accounting Standards Board ("IASB"). IFRSs include International Accounting Standards ("IAS") and interpretations. These financial statements also comply with the disclosure requirements of the Hong Kong Companies Ordinance and the applicable disclosure provisions of the Rules Governing the Listing of Securities on the Stock Exchange.

The IASB has issued certain new and revised IFRSs that are first effective or available for early adoption for the current accounting period of the Group and the Company. Note 3 provides information on the changes in accounting policies resulting from initial application of these developments to the extent that they are relevant to the Group and the Company for the current and prior accounting periods reflected in these financial statements.

2 Significant accounting policies *(continued)*

(b) Basis of preparation of the financial statements

The consolidated financial statements for the year ended 31 December 2006 comprise the Company and its subsidiaries and the Group's interest in associates.

These financial statements are prepared on the historical cost basis as modified by the revaluation of certain property, plant and equipment (see Note 2(i)); and that financial instruments classified as available-for-sale or trading (see Note 2(f)) and derivative financial instruments (see Note 2(g)) are stated at fair value.

The preparation of financial statements in conformity with IFRSs requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgments about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Judgements made by management in the application of IFRSs that have significant effect on the financial statements and estimates with a significant risk of material adjustment in the next financial year are disclosed in Note 40.

(c) Subsidiaries and minority interests

Subsidiaries are entities controlled by the Group. Control exists when the Group has the power to govern the financial and operating policies of an entity, so as to obtain benefits from its activities. In assessing control, potential voting rights that presently are exercisable are taken into account.

An investment in a subsidiary is consolidated into the consolidated financial statements from the date that control commences until the date that control ceases. Intra-group balances and transactions and any unrealised profits arising from intra-group transactions are eliminated in full in preparing the consolidated financial statements. Unrealised losses resulting from intra-group transactions are eliminated in the same way as unrealised gains but only to the extent that there is no evidence of impairment.

Minority interests represent the portion of the net assets of subsidiaries attributable to interests that are not owned by the Company, whether directly or indirectly through subsidiaries, and in respect of which the Group has not agreed any additional terms with the holders of those interests which would result in the Group as a whole having a contractual obligation in respect of those interests that meets the definition of a financial liability. Minority interests are presented in the consolidated balance sheet within equity, separately from equity attributable to the equity shareholders of the Company. Minority interests in the results of the Group are presented on the face of the consolidated income statement as an allocation of the total profit or loss for the year between minority interests and the equity shareholders of the Company.

Where losses applicable to the minority exceed the minority's interest in the equity of a subsidiary, the excess, and any further losses applicable to the minority, are charged against the Group's interest except to the extent that the minority has a binding obligation to, and is able to, make additional investment to cover the losses. If the subsidiary subsequently reports profits, the Group's interest is allocated all such profits until the minority's share of losses previously absorbed by the Group has been recovered.

Loans from holders of minority interests and other contractual obligations towards these holders are presented as financial liabilities in the consolidated balance sheet in accordance with Notes 2(o) or 2(p) depending on the nature of the liability.

In the Company's balance sheet, an investment in a subsidiary is stated at cost less impairment losses (see Note 2(m)).

2 Significant accounting policies *(continued)*

(d) Associates

An associate is an entity in which the Group or the Company has significant influence, but not control or joint control, over its management, including participation in the financial and operating policy decisions.

An investment in an associate is accounted for in the consolidated financial statements under the equity method and is initially recorded at cost and adjusted thereafter for the post acquisition change in the Group's share of the associate's net assets. The consolidated income statement includes the Group's share of the post-acquisition, post-tax results of the associates for the year, including any impairment loss on goodwill relating to the investment in associates recognised for the year (see Notes 2(e) and 2(m)).

When the Group's share of losses exceeds its interest in the associate, the Group's interest is reduced to nil and recognition of further losses is discontinued except to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of the associate. For this purpose, the Group's interest in the associate is the carrying amount of the investment under the equity method together with the Group's long-term interests that in substance form part of the Group's net investment in the associate.

Unrealised profits and losses resulting from transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associate, except where unrealised losses provide evidence of an impairment of the asset transferred, in which case they are recognised immediately in profit or loss.

In the Company's balance sheet, its investments in associates are stated at cost less impairment losses (see Note 2(m)).

(e) Goodwill

Goodwill represents the excess of the cost of a business combination or an investment in an associate over the Group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities.

Goodwill is stated at cost less accumulated impairment losses. Goodwill is allocated to cash-generating units and is tested annually for impairment (see Note 2(m)). In respect of associates, the carrying amount of goodwill is included in the carrying amount of the interest in the associate.

Any excess of the Group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities over the cost of a business combination or an investment in an associate is recognised immediately in profit or loss.

On disposal of a cash-generating unit of an associate during the year, any attributable amount of purchased goodwill is included in the calculation of the profit or loss on disposal.

(f) Other investments in debt and equity securities

The Group's and the Company's policies for investments in debt and equity securities, other than investments in subsidiaries and associates, are as follows:

Investments in debt and equity securities are initially stated at cost, which is their transaction price unless fair value can be more reliably estimated using valuation techniques whose variables include only data from observable markets. Cost includes attributable transaction costs, except where indicated otherwise below. These investments are subsequently accounted for as follows, depending on their classification:

Investments in securities held for trading are classified as current assets. Any attributable transaction costs are recognised in profit or loss as incurred. At each balance sheet date the fair value is remeasured, with any resultant gain or loss being recognised in profit or loss.

2 Significant accounting policies *(continued)*

(f) Other investments in debt and equity securities *(continued)*

Dated debt securities that the Group and/or the Company have the positive ability and intention to hold to maturity are classified as held-to-maturity securities. Held-to-maturity securities are stated in the balance sheet at amortised cost less impairment losses (see Note 2(m)).

Investments in equity securities that do not have a quoted market price in an active market and whose fair value cannot be reliably measured are recognised in the balance sheet at cost less impairment losses (see Note 2(m)).

Investments in securities which do not fall into any of the above categories are classified as available-for-sale securities. At each balance sheet date the fair value is remeasured, with any resultant gain or loss being recognised directly in equity, except foreign exchange gains and losses in respect of monetary items such as debt securities which are recognised directly in profit or loss. Where these investments are interest-bearing, interest calculated using the effective interest method is recognised in profit or loss. When these investments are derecognised or impaired (see Note 2(m)), the cumulative gain or loss previously recognised directly in equity is recognised in profit or loss.

Investments are recognised/derecognised on the date the Group commits to purchase/sell the investments or they expire.

(g) Derivative financial instruments

Derivative financial instruments are recognised initially at fair value. At each balance sheet date the fair value is remeasured. The gain or loss on remeasurement to fair value is charged immediately to profit or loss, except where the derivatives qualify for cash flow hedge accounting or hedge the net investment in a foreign operation, in which case recognition of any resultant gain or loss depends on the nature of the item being hedged.

(h) Cash and cash equivalents

Cash and cash equivalents comprise cash at bank and on hand, demand deposits with banks and other financial institutions, and short-term, highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value, having been within three months of maturity at acquisition. Bank overdrafts that are repayable on demand and form an integral part of the Group's cash management are also included as a component of cash and cash equivalents for the purpose of the consolidated cash flow statement.

(i) Property, plant and equipment

Property, plant and equipment, which consist of buildings, mining structures and mining rights, mining related machinery and equipment, generators and related machinery and equipment, railway and port transportation structures and furniture, fixtures, motor vehicles and other equipment, are initially stated at cost less accumulated depreciation and impairment losses (see Note 2(m)). The cost of an asset comprises its purchase price, any directly attributable costs of bringing the asset to its present working condition and location for its intended use, the cost of borrowed funds used during the period of construction and, when relevant, the costs of dismantling and removing the items and restoring the site on which they are located, and changes in the measurement of existing liabilities recognised for these costs resulting from changes in the timing or outflow of resources required to settle the obligation or from changes in the discount rate.

The Group recognises in the carrying amount of an item of property, plant and equipment the cost of replacing part of such an item when that cost is incurred if it is probable that the future economic benefits embodied with the item will flow to the Group and the cost of the item can be measured reliably. All other cost is recognised as an expense in the income statement in the period in which it is incurred.

2 Significant accounting policies *(continued)*

(i) Property, plant and equipment *(continued)*

When proved and probable coal reserves have been determined, costs incurred to develop coal mines are capitalised as part of the cost of the mining structures. All other expenditures, including the cost of repairs and maintenance and major overhaul, are expensed as they are incurred. Mining exploration costs, such as expenditures related to locating coal deposits and determining the economic feasibility, and the costs of removing waste materials or "stripping costs" are expensed as incurred.

Subsequent to the revaluation which was required by the PRC rules and regulations in connection with the Restructuring and which was based on depreciated replacement costs, property, plant and equipment are carried at revalued amount, being the fair value at the date of the revaluation, less subsequent accumulated depreciation and impairment losses (see Note 2(m)).

When an item of property, plant and equipment is revalued, any accumulated depreciation at the date of the revaluation is restated proportionately with the change in the gross carrying amount of the asset so that the carrying amount of the asset after revaluation equals its revalued amount. When an item of property, plant and equipment is revalued, the entire class of property, plant and equipment to which that asset belongs is revalued simultaneously. When an asset's carrying amount is increased as a result of a revaluation, the increase is credited directly to shareholder's equity as a component of revaluation reserve. However, a revaluation increase is recognised as income to the extent that it reverses a revaluation decrease of the same asset previously recognised as an expense. When an asset's carrying amount is decreased as a result of a revaluation, the decrease is recognised as an expense in the income statement. However, a revaluation decrease is charged directly against any related revaluation surplus to the extent that the decrease does not exceed the amount held in the revaluation reserve in respect of that same asset. Revaluations are to be performed with sufficient regularity such that the carrying amount does not differ materially from that which would be determined using fair value at the balance sheet date.

Gains or losses arising from the retirement or disposal of property, plant and equipment are determined as the difference between the net disposal proceeds and the carrying amount of the asset and are recognised as income or expense in the income statement on the date of disposal. On disposal of a revalued asset, the related revaluation surplus is transferred from revaluation reserve to retained earnings.

Depreciation is provided to write off the cost/revalued amount of each part of an item of property, plant and equipment, other than mining structures and mining rights, over its estimated useful life on a straight-line basis, after taking into account its estimated residual value. The estimated useful lives of property, plant and equipment are as follows:

	Depreciable life
Buildings	20-50 years
Mining related machinery and equipment	5-18 years
Generators and related machinery and equipment	20-30 years
Railway and port transportation structures	30-45 years
Furniture, fixtures, motor vehicles and other equipment	5-10 years

Mining structures and mining rights are depreciated on a units-of-production method utilising only proved and probable coal reserves in the depletion base.

The Group's mining rights are of sufficient duration (or convey a legal right to renew for sufficient duration) to enable all reserves to be mined in accordance with current production schedules.

2 Significant accounting policies *(continued)*

(j) Lease prepayments

Lease prepayments represent land use rights paid to the PRC's governmental authorities. Land use rights are carried at cost less impairment losses (see Note 2(m)) and are charged to the income statement on a straight-line basis over the respective periods of the rights which range from 30 years to 50 years.

(k) Construction in progress

Construction in progress is stated at cost less impairment losses (see Note 2(m)). Cost comprises direct costs of construction, borrowing costs and foreign exchange differences on related borrowed funds to the extent that they are regarded as an adjustment to interest charges, during the period of construction.

Capitalisation of these costs ceases and the construction in progress is transferred to property, plant and equipment when substantially all the activities necessary to prepare the asset for its intended use are completed. No depreciation is provided in respect of construction in progress until it is completed and ready for its intended use.

(l) Intangible assets (other than goodwill)

Intangible assets that are acquired by the Group are stated at cost less accumulated amortisation and impairment losses (see Note 2(m)) and are charged to the income statement on a straight-line basis over the estimated useful life of 20-45 years.

(m) Impairment losses

(i) Impairment of investments in debt and equity securities and other receivables

Investments in debt and equity securities and other current and non-current receivables that are stated at cost or amortised cost or are classified as available-for-sale securities are reviewed at each balance sheet date to determine whether there is objective evidence of impairment. If any such evidence exists, any impairment loss is determined and recognised as follows:

— For unquoted equity securities carried at cost, the impairment loss is measured as the difference between the carrying amount of the financial asset and the estimated future cash flows, discounted at the current market rate of return for a similar financial asset where the effect of discounting is material. Impairment losses for equity securities are not reversed.

— For trade and other current receivables and other financial assets carried at amortised cost, the impairment loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition of these assets), where the effect of discounting is material.

If in a subsequent period the amount of an impairment loss decreases and the decrease can be linked objectively to an event occurring after the impairment loss was recognised, the impairment loss is reversed through profit or loss. A reversal of an impairment loss shall not result in the asset's carrying amount exceeding that which would have been determined had no impairment loss been recognised in prior years.

2 Significant accounting policies *(continued)*

(m) Impairment losses *(continued)*

(i) Impairment of investments in debt and equity securities and other receivables *(continued)*

— For available-for-sale securities, the cumulative loss that has been recognised directly in equity is removed from equity and is recognised in profit or loss. The amount of the cumulative loss that is recognised in profit or loss is the difference between the acquisition cost (net of any principal repayment and amortisation) and current fair value, less any impairment loss on that asset previously recognised in profit or loss.

Impairment losses recognised in profit or loss in respect of available-for-sale equity securities are not reversed through profit or loss. Any subsequent increase in the fair value of such assets is recognised directly in equity.

Impairment losses in respect of available-for-sale debt securities are reversed if the subsequent increase in fair value can be objectively related to an event occurring after the impairment loss was recognised. Reversals of impairment losses in such circumstances are recognised in profit or loss.

(ii) Impairment of other assets

Internal and external sources of information are reviewed at each balance sheet date to identify indications that the following assets may be impaired or, except in the case of goodwill, an impairment loss previously recognised no longer exists or may have decreased:

— property, plant and equipment;

— construction in progress;

— intangible assets;

— investments in subsidiaries and associates; and

— goodwill.

If any such indication exists, the asset's recoverable amount is estimated. In addition, for goodwill, intangible assets that are not yet available for use and intangible assets that have indefinite useful lives, the recoverable amount is estimated annually whether or not there is any indication of impairment.

— Calculation of recoverable amount

The recoverable amount of an asset is the greater of its net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of time value of money and the risks specific to the asset. Where an asset does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the smallest group of assets that generates cash inflows independently (i.e. a cash-generating unit).

2 Significant accounting policies *(continued)*

(m) Impairment losses *(continued)*

(ii) Impairment of other assets *(continued)*

— Recognition of impairment losses

An impairment loss is recognised in profit or loss whenever the carrying amount of an asset, or the cash-generating unit to which it belongs, exceeds its recoverable amount. Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the cash-generating unit (or group of units) and then, to reduce the carrying amount of the other assets in the unit (or group of units) on a pro-rata basis, except that the carrying value of an asset will not be reduced below its individual fair value less costs to sell, or value in use, if determinable.

— Reversals of impairment losses

In respect of assets other than goodwill, an impairment loss is reversed if there has been a favourable change in the estimates used to determine the recoverable amount. An impairment loss in respect of goodwill is not reversed.

A reversal of an impairment loss is limited to the asset's carrying amount that would have been determined had no impairment loss been recognised in prior years. Reversals of impairment losses are credited to profit or loss in the year in which the reversals are recognised.

(n) Inventories

Coal inventories are stated at the lower of weighted average cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

When coal inventories are sold, the carrying amount of those inventories is recognised as an expense in the period in which the related revenue is recognised. The amount of any write-down of inventories to net realisable value and all losses of inventories are recognised as an expense in the period the write-down or loss occurs. The amount of any reversal of any write-down of inventories is recognised as a reduction in the amount of inventories recognised as an expense in the period in which the reversal occurs.

Inventories of ancillary materials, spare parts and small tools used in production are stated at cost less impairment losses for obsolescence.

(o) Interest-bearing borrowings

Interest-bearing borrowings are recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition, interest-bearing borrowings are stated at amortised cost with any difference between the amount initially recognised and redemption value being recognised in profit or loss over the period of the borrowings, together with any interest and fees payable, using the effective interest method.

(p) Trade and other payables

Trade and other payables are initially recognised at fair value and are subsequently stated at amortised cost unless the effect of discounting would be immaterial, in which case they are stated at cost.

(q) Trade and other receivables

Trade and other receivables are initially recognised at fair value and thereafter stated at amortised cost less impairment losses for bad and doubtful debts (see Note 2(m)), except where the receivables are interest-free loans made to related parties without any fixed repayment terms or the effect of discounting would be immaterial. In such cases, the receivables are stated at cost less impairment losses for bad and doubtful debts (see Note 2(m)).

2 Significant accounting policies *(continued)*

(r) Financial guarantees issued, provisions and contingent liabilities

(i) Financial guarantees issued

Where the Group issues a financial guarantee, the fair value of the guarantee (being the transaction price, unless the fair value can otherwise be reliably estimated) is initially recognised as deferred income within trade and other payables.

The amount of the guarantee initially recognised as deferred income is amortised in profit or loss over the term of the guarantee as income from financial guarantees issued. In addition, provisions are recognised in accordance with Note 2(r)(ii) if and when (i) it becomes probable that the holder of the guarantee will call upon the Group under the guarantee, and (ii) the amount of that claim on the Group is expected to exceed the amount currently carried in trade and other payables in respect of that guarantee i.e. the amount initially recognised, less accumulated amortisation.

(ii) Provisions and contingent liabilities

Provisions are recognised for liabilities of uncertain timing or amount when the Group or the Company has a legal or constructive obligation arising as a result of a past event, it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made. Where the time value of money is material, provisions are stated at the present value of the expenditure expected to settle the obligation.

Where it is not probable that an outflow of economic benefits will be required, or the amount cannot be estimated reliably, the obligation is disclosed as a contingent liability, unless the probability of outflow of economic benefits is remote. Possible obligations, whose existence will only be confirmed by the occurrence or non-occurrence of one or more future events are also disclosed as contingent liabilities unless the probability of outflow of economic benefits is remote.

(s) Revenue recognition

Provided it is probable that the economic benefits will flow to the Group and the revenue and costs, if applicable, can be measured reliably, revenue is recognised in profit or loss as follows:

(i) Revenues associated with the sale of coal and other goods are recognised when the title to the goods has been passed to the customer which is at the date that the customer receives and accepts the goods. Acceptance occurs when the customer agrees to the amount and quality of the delivered goods. Export coal sales are recognised as revenues when the customers receive and accept the goods at the port and pay for freight costs.

(ii) Revenue from sale of power is recognised upon the transmission of electric power to the power grid companies, as determined based on the volume of electric power transmitted and the applicable fixed tariff rates agreed with the respective electric power grid companies annually.

(iii) Revenue from the rendering of transportation and other services is recognised upon the delivery or performance of the services.

(t) Borrowing costs

Borrowing costs are expensed in profit or loss in the period in which they are incurred, except to the extent that they are capitalised as being directly attributable to the acquisition, construction or production of an asset which necessarily takes a substantial period of time to get ready for its intended use or sale.

The capitalisation of borrowing costs as part of the cost of a qualifying asset commences when expenditure for the asset is being incurred, borrowing costs are being incurred and activities that are necessary to prepare the asset for its intended use or sale are in progress. Capitalisation of borrowing costs is suspended or ceases when substantially all the activities necessary to prepare the qualifying asset for its intended use or sale are interrupted or complete.

2 Significant accounting policies *(continued)*

(u) Translation of foreign currencies

The Group's functional and presentation currency is Renminbi ("RMB"). Foreign currency transactions during the year are translated into RMB at the applicable rates of exchange quoted by the People's Bank of China ("PBOC") prevailing on the transaction dates. Monetary assets and liabilities denominated in foreign currencies are translated into RMB at the applicable PBOC rates ruling at the balance sheet date. Foreign currency differences, other than those capitalised as construction in progress, are recognised as income or expense in the income statement.

(v) Obligations for land reclamation

The Group's obligations for land reclamation consist of spending estimates at both surface and underground mines in accordance with the PRC rules and regulations. The Group estimates its liabilities for final reclamation and mine closure based upon detailed calculations of the amount and timing of the future cash spending for a third party to perform the required work. Spending estimates are escalated for inflation, then discounted at a discount rate that reflects current market assessments of the time value of money and the risks specific to the liability such that the amount of provision reflects the present value of the expenditures expected to be required to settle the obligation. The Group records a corresponding asset associated with the liability for final reclamation and mine closure. The obligation and corresponding asset are recognised in the period in which the liability is incurred. The asset is depreciated on the units-of-production method over its expected life and the liability is accreted to the projected spending date. As changes in estimates occur (such as mine plan revisions, changes in estimated costs, or changes in timing of the performance of reclamation activities), the revisions to the obligation and asset are recognised at the appropriate discount rate.

(w) Operating leases

Operating lease payments are charged to the income statement on a straight-line basis over the period of the respective leases.

(x) Employee benefits

(i) Short-term employee benefits and contributions to defined contribution retirement plans

Salaries, annual bonuses, paid annual leave, contributions to defined contribution retirement plans and the cost of non-monetary benefits are accrued in the years in which the associated services are rendered by employees. Where payment or settlement is deferred and the effect would be material, these accounts are stated at their present value.

(ii) Defined contribution retirement plans

Obligations for contributions to defined contribution retirement plans are recognised as an expense in profit or loss when they are due.

The Group's contributions to defined contribution retirement plans administered by the PRC government are recognised as an expense when incurred according to the contribution determined by the plans.

(iii) Share appreciation rights

Share appreciation rights ("SARs") are granted to employees of the Company. The fair value of the amount payable to the employee is recognised as an expense with a corresponding increase in liabilities. The fair value initially is measured at grant date and spread over the period during which the employees become unconditionally entitled to payment. The fair value of the SARs is measured based on the binomial option pricing model, taking into account the terms and conditions upon which the instruments were granted. The liability is remeasured at each balance sheet date and at settlement date. Any changes in the fair value of the liability are recognised in the income statement.

2 Significant accounting policies *(continued)*

(x) Employee benefits *(continued)*

(iv) Termination benefits

Termination benefits are recognised when, and only when, the Group demonstrably commits itself to terminate employment or to provide benefits as a result of voluntary redundancy by having a detailed formal plan which is without realistic possibility of withdrawal.

(y) Income tax

Income tax for the year comprises current tax and movements in deferred tax assets and liabilities. Current tax and movements in deferred tax assets and liabilities are recognised in profit or loss except to the extent that they relate to items recognised directly in equity, in which case they are recognised in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax assets and liabilities arise from deductible and taxable temporary differences respectively, being the differences between the carrying amounts of assets and liabilities for financial reporting purposes and their tax bases. Deferred tax assets also arise from unused tax losses and unused tax credits.

Apart from certain limited exceptions, all deferred tax liabilities, and all deferred tax assets to the extent that it is probable that future taxable profits will be available against which the asset can be utilised, are recognised. Future taxable profits that may support the recognition of deferred tax assets arising from deductible temporary differences include those that will arise from the reversal of existing taxable temporary differences, provided those differences relate to the same taxation authority and the same taxable entity, and are expected to reverse either in the same period as the expected reversal of the deductible temporary difference or in periods into which a tax loss arising from the deferred tax asset can be carried back or forward. The same criteria are adopted when determining whether existing taxable temporary differences support the recognition of deferred tax assets arising from unused tax losses and credits, that is, those differences are taken into account if they relate to the same taxation authority and the same taxable entity, and are expected to reverse in a period, or periods, in which the tax loss or credit can be utilised.

The limited exceptions to recognition of deferred tax assets and liabilities are those temporary differences arising from goodwill not deductible for tax purposes and the initial recognition of assets or liabilities that affect neither accounting nor taxable profit (provided they are not part of a business combination). For temporary differences relating to investments in subsidiaries, they are recognised except to the extent that, in the case of taxable differences, the Group controls the timing of the reversal and it is probable that the differences will not reverse in the foreseeable future, or in the case of deductible differences, they are recognised only to the extent that it is probable that they will reverse in the future.

The amount of deferred tax recognised is measured based on the expected manner of realisation or settlement of the carrying amount of the assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date. Deferred tax assets and liabilities are not discounted.

The carrying amount of a deferred tax asset is reviewed at each balance sheet date and is reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow the related tax benefit to be utilised. Any such reduction is reversed to the extent that it becomes probable that sufficient taxable profits will be available.

Additional income taxes that arise from the distribution of dividends are recognised when the liability to pay the related dividends is recognised.

2 Significant accounting policies *(continued)*

(y) Income tax *(continued)*

Current tax balances and deferred tax balances, and movements therein, are presented separately from each other and are not offset. Current tax assets are offset against current tax liabilities, and deferred tax assets against deferred tax liabilities, if the Company or the Group has the legally enforceable right to set off current tax assets against current tax liabilities and the following additional conditions are met:

— in the case of current tax assets and liabilities, the Company or the Group intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously; or

— in the case of deferred tax assets and liabilities, if they relate to income taxes levied by the same taxation authority on either:

  — the same taxable entity; or

  — different taxable entities, which, in each future period in which significant amounts of deferred tax liabilities or assets are expected to be settled or recovered, intend to realise the current tax assets and settle the current tax liabilities on a net basis or realise and settle simultaneously.

(z) Research and development costs

Expenditure on research activities is recognised as an expense in the period in which it is incurred. Expenditure on development activities is capitalised if the product or process is technically and commercially feasible and the Group has sufficient resources and the intention to complete development. The expenditure capitalised includes the costs of materials, direct labour and an appropriate proportion of overheads. Capitalised development costs are stated at cost less accumulated amortisation and impairment losses (see Note 2(m)). Other development expenditure is recognised as an expense in the period in which it is incurred.

(aa) Dividends

Dividends are recognised as a liability in the period in which they are declared.

(ab) Related parties

For the purposes of these financial statements, a party is considered to be related to the Group if:

(i) the party has the ability, directly or indirectly through one or more intermediaries, to control the Group or exercise significant influence over the Group in making financial and operating policy decisions, or has joint control over the Group;

(ii) the Group and the party are subject to common control;

(iii) the party is an associate of the Group or a joint venture in which the Group is a venturer;

(iv) the party is a member of key management personnel of the Group or the Group's parent, or a close family member of such an individual, or is an entity under the control, joint control or significant influence of such individuals;

(v) the party is a close family member of a party referred to in (i) or is an entity under the control, joint control or significant influence of such individuals; or

(vi) the party is a post-employment benefit plan which is for the benefit of employees of the Group or of any entity that is a related party of the Group.

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Group, directly or indirectly, including any director (whether executive or otherwise) of the Group.

Close family members of an individual are those family members who may be expected to influence, or be influenced by, that individual in their dealings with the entity.

2 Significant accounting policies *(continued)*

(ac) Earnings per share

The Group presents basic and diluted earnings per share ("EPS") data for its ordinary shares. Basic EPS is calculated by dividing the profit or loss attributable to equity shareholders of the Company by the weighted average number of ordinary shares outstanding during the period. Diluted EPS is determined by adjusting the profit or loss attributable to equity shareholders of the Company and the weighted average number of ordinary shares outstanding for the effects of all dilutive potential ordinary shares, which comprise convertible notes and share options granted to employees.

(ad) Segment reporting

A segment is a distinguishable component of the Group that is engaged either in providing products or services (business segment), or in providing products or services within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those of other segments.

In accordance with the Group's internal financial reporting system, the Group has chosen business segment information as the primary reporting format and geographical segment information as the secondary reporting format for the purposes of these financial statements. The Group has two reportable business segments which are (i) coal operations; and (ii) power operations, and three reportable geographical segments which are (i) the PRC domestic markets; (ii) Asia Pacific markets-export sales; and (iii) other markets-export sales.

Segment revenue, expenses, results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis to that segment. For example, segment assets may include inventories, trade receivables and property, plant and equipment. Segment revenue, expenses, assets, and liabilities are determined before intra-group balances and intra-group transactions are eliminated as part of the consolidation process, except to the extent that such intra-group balances and transactions are between group entities within a single segment. Inter-segment pricing is based on similar terms as those available to other external parties.

Segment capital expenditure is the total cost incurred during the period to acquire segment assets (both tangible and intangible) that are expected to be used for more than one period.

Unallocated items mainly comprise financial and corporate assets, interest-bearing loans, borrowings, tax balances, corporate and financing expenses.

2 Significant accounting policies *(continued)*

(ae) Determination of fair values

A number of the Group's accounting policies and disclosures require the determination of fair value, for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and/or disclosure purposes based on the following methods. Where applicable, further information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability.

(i) Trade and other receivables

The fair value of trade and other receivables, excluding construction work in progress, is estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date.

(ii) Derivatives

The fair value of interest rate swaps is based on broker quotes. Those quotes are tested for reasonableness by discounting estimated future cash flows based on the terms and maturity of each contract and using market interest rates for a similar instrument at the measurement date.

(iii) Non-derivative financial liabilities

Fair value of non-derivative financial liabilities, which is determined for disclosure purposes, is calculated based on the present value of future principal and interest cash flows, discounted at the market rate of interest at the reporting date. In respect of the liability component of convertible notes, the market rate of interest is determined by reference to similar liabilities that do not have a conversion option.

(iv) Share appreciation rights ("SARs")

The fair value of SARs is measured based on the binomial option pricing model. Measurement inputs include share price on measurement date, exercise price of the instrument, expected volatility (based on weighted average historic volatility adjusted for changes expected due to publicly available information), weighted average expected life of the instruments (based on historical experience and general option holder behaviour), expected dividends, and the risk-free interest rate (based on government bonds). Service and non-market performance conditions attached to the transactions are not taken into account in determining fair value.

3 Adoption of new/revised IFRSs

The Group has adopted the amendments to IAS 39, *Financial instruments: Recognition and measurement: Financial Guarantee Contracts*, with effective from 1 January 2006.

In prior years, financial guarantees issued by the Group were disclosed as contingent liabilities. No provisions were made in respect of these guarantees unless it was more likely than not that the guarantee would be called upon.

Under the new policy, financial guarantees issued are measured initially at fair value and recognised as deferred income within trade and other payables. The deferred income is amortised in profit and loss over the term of the guarantee as income from financial guarantees issued. In addition, provisions are recognised in accordance with IAS 37. Further details of the new policy are set out in Note 2(r)(i).

The adoption of the above new policy did not have any financial impact on the Group's and the Company's financial statements for the years presented.

The Group has not applied any new standard or interpretation that is not yet effective for the current accounting period (see Note 43).

4 Revenues

The Group is principally engaged in the production and sale of coal, generation and sale of power and the provision of transportation services in the PRC. Revenues represent the aggregate of the invoiced value of goods sold and services provided, net of sales taxes.

5 Other revenues

	2006 RMB million	2005 RMB million
Rendering of transportation and other services	**1,536**	1,357
Sale of ancillary materials and other goods	**45**	57
Others	**83**	23
	1,664	1,437

6 Cost of revenues – others

	2006 RMB million	2005 RMB million
Coal selection and minery fees	**830**	557
Coal extraction service costs	**573**	544
Sales taxes and surcharges	**456**	404
Dredging expenses	**379**	294
Relocation compensation expenses	**192**	203
Operating lease charges	**190**	222
Environmental protection costs	**153**	121
Resources compensation fees	**147**	100
Public utilities expenses	**127**	75
Cost of sale of ancillary materials and other goods	**63**	53
Others	**1,004**	622
	4,114	3,195

7 Total operating expenses

	2006 RMB million	2005 RMB million (restated – Note 1)
Personnel expenses	**3,772**	3,112
– including contribution to retirement plans	**353**	348
– share appreciation rights expense	**22**	1
Depreciation and amortisation	**6,611**	5,377
Net loss on disposal of property, plant and equipment and lease prepayments	**72**	187
Cost of inventories (Note)	**26,985**	20,719
Research and development costs	**66**	24
Auditors' remuneration	**35**	27
– audit services	**33**	25
– tax services	**2**	2
Operating lease charges on properties	**250**	285
Provisions for accounts receivable, other receivables and inventories	**58**	32
Impairment losses on property, plant and equipment	**147**	41

Note:

Cost of inventories includes RMB5,707 million (2005: RMB4,929 million) for the year ended 31 December 2006, relating to personnel expenses, depreciation and amortisation and operating lease charges, which amounts are also included in the respective amounts disclosed separately above for each of these types of expenses.

8 Finance income / (expenses)

	2006 RMB million	2005 RMB million (restated – Note 1)
Interest income	**250**	266
Foreign exchange gain	**258**	619
Finance income	**508**	885
Interest on loans from banks and other financial institutions, and other borrowings wholly repayable within five years	**(3,013)**	(3,255)
Less: Interest expense capitalised*	**428**	678
Net interest expense	**(2,585)**	(2,577)
Loss on remeasurement of derivative financial instruments to fair value	**(23)**	(368)
Finance expenses	**(2,608)**	(2,945)
Net finance costs	**(2,100)**	(2,060)
* Interest expense was capitalised in construction in progress at the following rates per annum	**1.8%-6.156%**	1.8%-5.508%

9 Income tax

Income tax in the consolidated income statement represents:

	2006 RMB million	2005 RMB million (restated – Note 1)
Provision for PRC income tax	**5,260**	3,987
Deferred taxation (Note 27)	**128**	93
	5,388	4,080

A reconciliation of the expected tax with the actual tax expense is as follows:

	2006 RMB million	2005 RMB million (restated – Note 1)
Profit before income tax	**25,673**	22,073
Expected PRC income tax expense at a statutory tax rate of 33% (Note i)	**8,472**	7,284
Differential tax rate on subsidiaries' income (Note i)	**(2,924)**	(3,060)
Non-deductible expenses (Note ii)	**126**	209
Tax effect in respect of associates' income	**(158)**	(152)
Other non-taxable income	**–**	(2)
Tax credit of domestic equipment purchases	**(169)**	(12)
Tax losses not recognised	**140**	–
Others	**(99)**	(187)
	5,388	4,080

Notes:

(i) The provision for PRC current income tax is based on a statutory rate of 33% of the assessable profit of the entities comprising the Group as determined in accordance with the relevant income tax rules and regulations of the PRC, except for certain branches, subsidiaries and associates of the Company, which are exempted or taxed at preferential rates of 7.5% or 15%.

(ii) Non-deductible expenses mainly represent personnel and other miscellaneous expenses in excess of statutory deductible limits for tax purposes.

10 Directors' and supervisors' emoluments

The amounts of emoluments paid and payable to the directors and supervisors of the Company by the Group for the years are as follows:

	2006					
	Fees RMB million	Basic salaries, housing and other allowances and benefits in kind RMB million	Discretionary bonuses RMB million	Share appreciation rights (Note) RMB million	Retirement scheme contributions RMB million	Total RMB million
Executive directors						
Chen Biting	–	–	–	2.26	–	2.26
Wu Yuan (retired from the office on 25 August 2006)	–	0.25	0.57	1.80	0.13	2.75
Ling Wen	–	0.28	0.60	1.54	0.14	2.56
Non-executive directors						
Zhang Xiwu	–	–	–	2.04	–	2.04
Zhang Yuzhuo	–	–	–	1.54	–	1.54
Han Jianguo	–	–	–	1.54	–	1.54
Independent non-executive directors						
Huang Yicheng	0.43	–	–	–	–	0.43
Anthony Francis Neoh	0.43	–	–	–	–	0.43
Chen Xiaoyue	0.43	–	–	–	–	0.43
Supervisors						
Xu Zufa	–	–	–	1.35	–	1.35
Wu Gaoqian	–	0.21	0.16	–	0.10	0.47
Li Jianshe	–	0.10	0.21	–	0.10	0.41
	1.29	0.84	1.54	12.07	0.47	16.21

10 Directors' and supervisors' emoluments *(continued)*

	2005					
	Fees RMB million	Basic salaries, housing and other allowances and benefits in kind RMB million	Discretionary bonuses RMB million	Share appreciation rights (Note) RMB million	Retirement scheme contributions RMB million	Total RMB million
Executive directors						
Chen Biting	–	0.23	0.56	0.16	0.10	1.05
Wu Yuan	–	0.19	0.44	0.13	0.09	0.85
Ling Wen	–	0.18	0.40	0.11	0.08	0.77
Non-executive directors						
Zhang Xiwu	–	–	–	0.14	–	0.14
Zhang Yuzhuo	–	–	–	0.11	–	0.11
Han Jianguo	–	–	–	0.11	–	0.11
Independent non-executive directors						
Huang Yicheng	0.40	–	–	–	–	0.40
Anthony Francis Neoh	0.40	–	–	–	–	0.40
Chen Xiaoyue	0.40	–	–	–	–	0.40
Supervisors						
Xu Zufa	–	0.18	0.40	0.11	0.08	0.77
Wu Gaoqian	–	0.13	0.20	—	0.05	0.38
Li Jianshe	–	0.09	0.21	—	0.05	0.35
	1.20	1.00	2.21	0.87	0.45	5.73

Note: Please refer to Note 36 for details of the share appreciation rights.

11 Individuals with highest emoluments

Of the five highest paid individuals of the Group, four (2005: four) are directors of the Company for the year ended 31 December 2006 whose emoluments are included in Note 10 above.

The following table sets out the emoluments of the Group's remaining one (2005: one) highest paid individual for the year ended 31 December 2006 who is not a director nor a supervisor of the Company:

	2006 RMB million	2005 RMB million
Basic salaries, housing and other allowances and benefits in kind	**0.25**	0.16
Discretionary bonuses	**0.29**	0.34
Share appreciation rights	**1.16**	0.08
Retirement scheme contributions	**0.12**	0.07
	1.82	0.65

11 Individuals with highest emoluments *(continued)*

The emoluments of this individual is within the following band:

	Number of individual 2006	2005
Nil – RMB1,005,000 (equivalent to HK$1,000,000)	**–**	1
RMB1,507,001 – RMB2,009,000 (equivalent to HK$1,500,001 to HK$2,000,000)	**1**	–
	1	1

12 Profit attributable to equity shareholders of the Company

The consolidated profit attributable to equity shareholders of the Company includes a profit of RMB12,519 million (2005: RMB11,928 million) which has been dealt with in the financial statements of the Company.

13 Dividends

(a) Dividends payable to equity shareholders of the Company attributable to the year

	2006 RMB million	2005 RMB million
Special dividend to Shenhua resolved after the balance sheet date	**–**	5,143
Final dividend proposed after the balance sheet date of RMB0.34 (2005: RMB0.125) per ordinary share	**6,150**	2,261
	6,150	7,404

On 23 March 2007, the directors proposed a final dividend of RMB0.34 per share totalling RMB6,150 million to all equity shareholders of the Company for shareholders' approval at the forthcoming annual general meeting.

The dividends resolved and proposed after the balance sheet date have not been recognised as a liability at the balance sheet date.

13 Dividends *(continued)*

(b) Dividends payable to equity shareholders of the Company attributable to the previous financial year, approved and paid during the year

	2006 RMB million	2005 RMB million
Special dividend to Shenhua in respect of previous financial year, resolved and paid during the year	**5,143**	–
Final dividend in respect of the previous financial year, approved and paid during the year	**2,261**	7,549
	7,404	7,549

On 27 March 2005, the directors proposed and the sole shareholder approved that the distributable profit of the Group for the period from 1 January 2005 to the date immediately preceding the date of its listing on the Stock Exchange (i.e. 14 June 2005) be entirely distributed to Shenhua. Pursuant to a resolution passed at the directors' meeting on 10 March 2006, the directors resolved to pay a special dividend to Shenhua amounting to RMB5,143 million (being the distributable profit of the Group for the period from 1 January 2005 to 14 June 2005). The special dividend was paid on 18 May 2006.

A final dividend of RMB0.125 per share totalling RMB2,261 million in respect of the year ended 31 December 2005 was approved at the annual general meeting held on 12 May 2006 and was subsequently paid on 29 May 2006.

On 27 March 2005, a final dividend of RMB7,549 million in respect of the year ended 31 December 2004 was approved for distribution to Shenhua and was subsequently paid on 26 May 2005.

14 Earnings per share

The calculation of basic earnings per share for the year ended 31 December 2006 was based on the profit attributable to equity shareholders of the Company for the year of RMB17,460 million (2005: RMB15,619 million as restated) and the weighted average number of shares in issue during the year ended 31 December 2006 of 18,090 million (2005: 16,678 million).

Weighted average number of ordinary shares

	2006 million	2005 million
Ordinary shares issued at 1 January	**18,090**	15,000
Effect of shares issued in June 2005 (Note 1)	**–**	1,534
Effect of shares issued in July 2005 (Note 1)	**–**	144
Weighted average number of ordinary shares at 31 December	**18,090**	16,678

The Company had no dilutive potential shares outstanding for both years presented.

15 Property, plant and equipment, net

The Group

	Buildings RMB million	Mining structures and mining rights RMB million	Mining related machinery and equipment RMB million	Generators and related machinery and equipment RMB million	Railway and port transportation structures RMB million	Furniture, fixtures, motor vehicles and other equipment RMB million	Total RMB million
Cost/valuation:							
At 1 January 2005 (restated)	9,447	7,334	11,614	23,608	36,194	2,766	90,963
Additions	7	3,132	253	18	576	278	4,264
Transferred from construction in progress	1,160	179	3,035	3,365	2,783	172	10,694
Disposals	(46)	(33)	(239)	(23)	(92)	(156)	(589)
At 31 December 2005 (restated)	10,568	10,612	14,663	26,968	39,461	3,060	105,332
Representing:							
Cost (restated)	2,377	3,659	5,879	4,759	8,705	786	26,165
Valuation – 2003 (Note (b))	8,191	6,953	8,784	22,209	30,756	2,274	79,167
	10,568	10,612	14,663	26,968	39,461	3,060	105,332
Accumulated depreciation and impairment losses:							
At 1 January 2005 (restated)	1,860	606	3,667	5,157	5,326	1,315	17,931
Charge for the year	459	288	1,182	1,296	1,594	281	5,100
Impairment losses (Note (e))	1	–	–	–	10	30	41
Written back on disposals	(2)	(5)	(97)	(13)	(31)	(122)	(270)
At 31 December 2005 (restated)	2,318	889	4,752	6,440	6,899	1,504	22,802
Net book value:							
At 31 December 2005 (restated)	8,250	9,723	9,911	20,528	32,562	1,556	82,530
Cost/valuation:							
At 1 January 2006	**10,568**	**10,612**	**14,663**	**26,968**	**39,461**	**3,060**	**105,332**
Additions	**22**	**93**	**556**	**48**	**1,173**	**298**	**2,190**
Transferred from construction in progress	**3,743**	**762**	**4,702**	**15,049**	**5,319**	**525**	**30,100**
Disposals	**(86)**	**(220)**	**(573)**	**(45)**	**(119)**	**(147)**	**(1,190)**
At 31 December 2006	**14,247**	**11,247**	**19,348**	**42,020**	**45,834**	**3,736**	**136,432**
Representing:							
Cost	**6,142**	**4,514**	**11,137**	**19,856**	**15,197**	**1,609**	**58,455**
Valuation – 2003 (Note (b))	**8,105**	**6,733**	**8,211**	**22,164**	**30,637**	**2,127**	**77,977**
	14,247	**11,247**	**19,348**	**42,020**	**45,834**	**3,736**	**136,432**
Accumulated depreciation and impairment losses:							
At 1 January 2006	**2,318**	**889**	**4,752**	**6,440**	**6,899**	**1,504**	**22,802**
Charge for the year	**656**	**389**	**1,438**	**1,790**	**1,700**	**338**	**6,311**
Impairment losses (Note (e))	**–**	**–**	**147**	**–**	**–**	**–**	**147**
Written back on disposals	**(19)**	**(28)**	**(467)**	**(25)**	**(38)**	**(110)**	**(687)**
At 31 December 2006	**2,955**	**1,250**	**5,870**	**8,205**	**8,561**	**1,732**	**28,573**
Net book value:							
At 31 December 2006	**11,292**	**9,997**	**13,478**	**33,815**	**37,273**	**2,004**	**107,859**

15 Property, plant and equipment, net *(continued)*

The Company

	Buildings RMB million	Mining structures and mining rights RMB million	Mining related machinery and equipment RMB million	Generators and related machinery and equipment RMB million	Railway and port transportation structures RMB million	Furniture, fixtures, motor vehicles and other equipment RMB million	Total RMB million
Cost/valuation:							
At 1 January 2005	1,989	6,078	8,005	6	10,169	696	26,943
Additions	6	2,951	169	–	393	91	3,610
Transferred from construction in progress	108	156	2,984	–	516	83	3,847
Disposals	(43)	(33)	(170)	(1)	(3)	(45)	(295)
At 31 December 2005	2,060	9,152	10,988	5	11,075	825	34,105
Representing:							
Cost	317	3,275	5,532	1	2,092	316	11,533
Valuation – 2003 (Note (b))	1,743	5,877	5,456	4	8,983	509	22,572
	2,060	9,152	10,988	5	11,075	825	34,105
Accumulated depreciation:							
At 1 January 2005	366	518	1,728	4	2,103	330	5,049
Charge for the year	80	283	1,003	2	554	75	1,997
Written back on disposals	(2)	(5)	(83)	(1)	(2)	(18)	(111)
At 31 December 2005	444	796	2,648	5	2,655	387	6,935
Net book value:							
At 31 December 2005	1,616	8,356	8,340	–	8,420	438	27,170
Cost/valuation:							
At 1 January 2006	**2,060**	**9,152**	**10,988**	**5**	**11,075**	**825**	**34,105**
Additions	**16**	**93**	**421**	**–**	**836**	**169**	**1,535**
Transferred from construction in progress	**414**	**701**	**3,856**	**–**	**15**	**113**	**5,099**
Disposals	**(24)**	**(220)**	**(553)**	**–**	**(38)**	**(86)**	**(921)**
At 31 December 2006	**2,466**	**9,726**	**14,712**	**5**	**11,888**	**1,021**	**39,818**
Representing:							
Cost	**747**	**4,069**	**9,809**	**1**	**2,943**	**598**	**18,167**
Valuation – 2003 (Note (b))	**1,719**	**5,657**	**4,903**	**4**	**8,945**	**423**	**21,651**
	2,466	**9,726**	**14,712**	**5**	**11,888**	**1,021**	**39,818**
Accumulated depreciation and impairment losses:							
At 1 January 2006	**444**	**796**	**2,648**	**5**	**2,655**	**387**	**6,935**
Charge for the year	**73**	**358**	**1,295**	**–**	**547**	**120**	**2,393**
Impairment losses (Note (e))	**–**	**–**	**147**	**–**	**–**	**–**	**147**
Written back on disposals	**(6)**	**(28)**	**(452)**	**–**	**(7)**	**(63)**	**(556)**
At 31 December 2006	**511**	**1,126**	**3,638**	**5**	**3,195**	**444**	**8,919**
Net book value:							
At 31 December 2006	**1,955**	**8,600**	**11,074**	**–**	**8,693**	**577**	**30,899**

15 Property, plant and equipment, net *(continued)*

(a) All of the Group's buildings and plant and equipment are located in the PRC.

(b) As required by the relevant PRC rules and regulations with respect to the Restructuring, the property, plant and equipment of the Group as at 31 December 2003 were revalued for each asset class by China Enterprise Appraisal Co., Ltd. (the "PRC valuers"), independent valuers registered in the PRC, on a depreciated replacement cost basis. The value of property, plant and equipment was determined at RMB66,832 million. The net surplus on the revaluation of RMB8,260 million was incorporated in the consolidated balance sheet as at 31 December 2003.

The Group's properties were also valued separately by American Appraisal China Limited, independent qualified valuers in Hong Kong, on a depreciated replacement cost basis, as at 15 March 2005. The value arrived at by these valuers is approximately the same as that arrived at by the PRC valuers as adjusted for the depreciation for the period from 1 January 2004 to 15 March 2005.

(c) Had property, plant and equipment been carried at cost less accumulated depreciation, the historical carrying amounts as at 31 December 2006 would have been as follows:

	2006	2005
	RMB million	RMB million (restated – Note 1)
Buildings	**10,971**	7,890
Mining structures and mining rights	**5,479**	4,958
Mining related machinery and equipment	**13,038**	9,468
Generators and related machinery and equipment	**33,752**	20,449
Railway and port transportation structures	**35,321**	30,528
Furniture, fixtures, motor vehicles and other equipment	**2,160**	1,750
	100,721	75,043

(d) Up to the date of this report, the Group was in the process of applying for or changing registration of the title certificates of certain of its properties with an aggregate carrying value of approximately RMB2,977 million as at 31 December 2006 (2005: RMB875 million as restated), of which RMB2,236 million related to newly acquired properties in 2006. The directors are of the opinion that the Group is entitled to lawfully and validly occupy or use the above mentioned properties.

(e) Certain property, plant and equipment which were obsolete, damaged or that could not generate future economic benefits were provided against for impairment for the years ended 31 December 2006 and 31 December 2005 respectively.

16 Construction in progress

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB million	RMB million (restated – Note 1)	**RMB million**	RMB million
At the beginning of the year	**21,910**	13,317	**1,680**	1,649
Additions	**22,305**	19,287	**7,083**	3,878
Transferred to property, plant and equipment	**(30,100)**	(10,694)	**(5,099)**	(3,847)
At the end of the year	**14,115**	21,910	**3,664**	1,680

The construction in progress as at 31 December 2006 are mainly related to mining, generators and related machinery and equipment.

17 Intangible assets

Intangible assets mainly represent the cost of acquiring railway route access and use rights. The movement of intangible assets is as follows:

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB million	RMB million	**RMB million**	RMB million
At the beginning of the year	**1,293**	1,210	**344**	343
Additions	**140**	360	**4**	20
Amortisation	**(300)**	(277)	**(24)**	(19)
At the end of the year	**1,133**	1,293	**324**	344

The amortisation charge for the year is included in cost of revenues in the consolidated income statement.

18 Investments in subsidiaries

	The Company	
	2006	2005
	RMB million	RMB million (restated – Note 1)
Unlisted shares, at cost	**19,687**	18,119

18 Investments in subsidiaries *(continued)*

The Company's subsidiaries are unlisted and established in the PRC. Details of the Company's principal subsidiaries as at 31 December 2006 are as follows:

Name of the company	Type of legal entity	Particulars of registered capital	% held by the Company	Principal activities
Shenhua Zhunge'er Energy Co., Ltd.	Limited company	Registered capital RMB7,102 million	58%	Coal mining and development
Shuohuang Railway Development Co., Ltd.	Limited company	Registered capital RMB5,880 million	53%	Provision of transportation services
Shenhua Huanghua Harbor Administration Co., Ltd.	Limited company	Registered capital RMB1,820 million	70%	Provision of harbour and port services
Shenhua Baoshen Railway Co., Ltd.	Limited company	Registered capital RMB602 million	88%	Provision of transportation services
Guangdong Guohua Yuedian Taishan Power Co., Ltd.	Limited company	Registered capital RMB2,700 million	80%	Generation and sale of electricity
CLP Guohua Power Co., Ltd.	Limited company	Registered capital RMB1,637 million	51%	Generation and sale of electricity

19 Interest in associates

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB million	RMB million	**RMB million**	RMB million
Unlisted shares, at cost	**–**	–	**1,480**	2,982
Share of net assets	**2,369**	3,686	**–**	–
	2,369	3,686	**1,480**	2,982

19 Interest in associates *(continued)*

The Group's interest in associates are individually and in aggregate not material to the Group's financial condition or results of operations for the year. The Group's associates are unlisted and established in the PRC. Details of the Group's principal associates as at 31 December 2006 are as follows:

			Proportion of ownership interest			
Name of the Company	**Type of legal entity**	**Particulars of registered capital**	**Group's effective interest**	**% held by the Company**	**% held by the Company's subsidiaries**	**Principal activities**
Hebei Guohua Dingzhou Power Co., Ltd.	Limited company	Registered capital RMB931 million	41%	41%	–	Power generation
Zhejiang Jiahua Power Co., Ltd.	Limited company	Registered capital RMB2,055 million	20%	20%	–	Power generation
Inner-Mongolia Haibowan Power Co., Ltd.	Limited company	Registered capital RMB280 million	40%	40%	–	Power generation
Inner-Mongolia Jingda Power Co., Ltd.	Limited company	Registered capital RMB455 million	30%	30%	–	Power generation
Shenhua Finance Co., Ltd.	Limited company	Registered capital RMB700 million	33%	21%	19%	Provision of financial services

20 Other investments

Other investments comprise unlisted equity securities and certain subsidiaries which are individually and in aggregate not material to the Group's financial position and results of operations for the year. As there is no quoted market price in an active market for these investments, they are stated at cost less impairment losses.

21 Other non-current financial assets

Other non-current financial assets represent entrusted loans to a subsidiary (2005: Nil) through a PRC state-owned bank. The loans are interest bearing at rates ranging from 5.202% to 5.4315% per annum and are receivable within eight years.

22 Inventories

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB million	RMB million	**RMB million**	RMB million
Coal	**1,487**	1,140	**934**	751
Materials and supplies	**3,274**	2,432	**1,736**	1,213
	4,761	3,572	**2,670**	1,964

The analysis of the amount of inventories recognised as an expense is as follows:

	The Group	
	2006	2005
	RMB million	RMB million
Carrying amount of inventories sold	**26,953**	20,746
Write down of inventories	**36**	–
Reversal of write down of inventories	**(4)**	(27)
	26,985	20,719

The reversal of write-down of inventories made in prior years arose due to an increase in the estimated net realisable value of certain inventories.

23 Available-for-sale investments

On 29 December 2006, the Group entered into two fund management contracts with Industrial and Commercial Bank of China ("ICBC") with a total principal of RMB2,000 million. The expected return from the investments ranges from 2.4% to 2.8% per annum. The securities that ICBC could invest in may include trust funds, government bonds, financial bonds, bills, enterprise bonds, short-term financial coupons and other bonds. As at 31 December 2006, ICBC has not yet invested the fund into any securities on behalf of the Group. The maturity date of both the contracts is 28 June 2007.

24 Accounts and bills receivable, net

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB million	RMB million	**RMB million**	RMB million
Accounts receivable	**4,331**	2,531	**1,412**	1,276
Impairment losses for bad and doubtful accounts	**(20)**	(23)	**(11)**	(13)
	4,311	2,508	**1,401**	1,263
Bills receivable	**549**	174	**56**	61
	4,860	2,682	**1,457**	1,324

Credit of up to 60 days is granted to customers with established trading history, otherwise sales on cash terms are required.

The following is the ageing analysis of accounts and bills receivable, net of impairment losses for bad and doubtful accounts:

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB million	RMB million	**RMB million**	RMB million
Current	**4,803**	2,639	**1,448**	1,286
Within one year	**53**	39	**7**	35
Between one and two years	**4**	2	**2**	1
Between two and three years	**–**	2	**–**	2
	4,860	2,682	**1,457**	1,324

Included in accounts and bills receivable are the following amounts denominated in a currency other than the functional currency of the entity to which they relate:

	The Group		The Company	
	2006	2005	**2006**	2005
	million	million	**million**	million
United States Dollars	**USD89**	USD76	**USD89**	USD76

25 Prepaid expenses and other current assets

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB million	RMB million (restated – Note 1)	**RMB million**	RMB million
Amounts due from Shenhua	**52**	107	**52**	71
Prepayments in connection with construction work and equipment purchases	**2,144**	585	**2,015**	401
Prepaid expenses and deposits	**624**	394	**494**	229
Amounts due from subsidiaries	**–**	–	**8,558**	8,443
Amounts due from associates	**50**	104	**50**	100
Other receivables	**149**	80	**25**	54
Advances to staff	**40**	31	**24**	19
	3,059	1,301	**11,218**	9,317

In the Company's balance sheet, the balances with subsidiaries are unsecured, interest-free and have no fixed terms of repayment.

26 Time deposits with original maturity over three months and cash and cash equivalents

Included in time deposits with original maturity over three months and cash and cash equivalents are the following amounts denominated in a currency other than the functional currency of the entity to which they relate:

	The Group		The Company	
	2006	2005	**2006**	2005
	million	million	**million**	million
United States Dollars	**USD14**	USD9	**–**	–
Hong Kong Dollars	**HK$494**	HK$487	**HK$491**	HK$486

27 Deferred tax assets and liabilities

Deferred tax assets and deferred tax liabilities are attributable to the items set out below:

	The Group					
	Assets		Liabilities		Net balance	
	2006 RMB million	2005 RMB million (restated – Note 1)	**2006 RMB million**	2005 RMB million	**2006 RMB million**	2005 RMB million (restated – Note 1)
Current						
Allowances, primarily for receivables and inventories	**69**	64	**–**	–	**69**	64
Non-current						
Property, plant and equipment	**253**	169	**(734)**	(601)	**(481)**	(432)
Lease prepayments	**857**	877	**–**	–	**857**	877
Tax losses carried forward, net of valuation allowance	**11**	122	**–**	–	**11**	122
Tax allowable expenses not yet incurred	**–**	–	**(272)**	(143)	**(272)**	(143)
Unrealised profits from sales within the Group	**90**	70	**–**	–	**90**	70
Accrued salaries not yet paid	**90**	39	**–**	–	**90**	39
Pre-operating expenses written off	**58**	53	**–**	–	**58**	53
Others	**141**	41	**–**	–	**141**	41
Deferred tax assets/(liabilities)	**1,569**	1,435	**(1,006)**	(744)	**563**	691

	The Company					
	Assets		Liabilities		Net balance	
	2006 RMB million	2005 RMB million	**2006 RMB million**	2005 RMB million	**2006 RMB million**	2005 RMB million
Current						
Allowances, primarily for receivables and inventories	**40**	40	**–**	–	**40**	40
Non-current						
Property, plant and equipment	**106**	28	**(232)**	(123)	**(126)**	(95)
Lease prepayments	**533**	544	**–**	–	**533**	544
Tax allowable expenses not yet incurred	**–**	–	**(259)**	(121)	**(259)**	(121)
Unrealised profits from sales within the Company	**90**	70	**–**	–	**90**	70
Accrued salaries not yet paid	**35**	33	**–**	–	**35**	33
Others	**82**	59	**–**	–	**82**	59
Deferred tax assets/(liabilities)	**886**	774	**(491)**	(244)	**395**	530

27 Deferred tax assets and liabilities *(continued)*

Movements in temporary differences are as follows:

The Group

	At 1 January 2006 RMB million (restated – Note 1)	Recognised in consolidated income statement RMB million	At 31 December 2006 RMB million
Current			
Allowances, primarily for receivables and inventories	**64**	**5**	**69**
Non-current			
Property, plant and equipment	**(432)**	**(49)**	**(481)**
Lease prepayments	**877**	**(20)**	**857**
Tax losses carried forward, net of valuation allowances	**122**	**(111)**	**11**
Tax allowable expenses not yet incurred	**(143)**	**(129)**	**(272)**
Unrealised profits from sales within the Group	**70**	**20**	**90**
Accrued salaries not yet paid	**39**	**51**	**90**
Pre-operating expenses written off	**53**	**5**	**58**
Others	**41**	**100**	**141**
Net deferred tax assets	**691**	**(128)**	**563**

	At 1 January 2005 RMB million (restated – Note 1)	Recognised in consolidated income statement RMB million (restated – Note 1)	At 31 December 2005 RMB million (restated – Note 1)
Current			
Allowances, primarily for receivables and inventories	69	(5)	64
Non-current			
Property, plant and equipment	(165)	(267)	(432)
Lease prepayments	894	(17)	877
Tax losses carried forward, net of valuation allowances	23	99	122
Tax allowable expenses not yet incurred	(47)	(96)	(143)
Unrealised profits from sales within the Group	32	38	70
Accrued salaries not yet paid	15	24	39
Pre-operating expenses written off	32	21	53
Others	(69)	110	41
Net deferred tax assets	784	(93)	691

27 Deferred tax assets and liabilities *(continued)*

The Company

	At 1 January 2006 RMB million	Recognised in income statement RMB million	At 31 December 2006 RMB million
Current			
Allowances, primarily for receivables and inventories	**40**	**–**	**40**
Non-current			
Property, plant and equipment	**(95)**	**(31)**	**(126)**
Lease prepayments	**544**	**(11)**	**533**
Tax allowable expenses not yet incurred	**(121)**	**(138)**	**(259)**
Unrealised profits from sales within the Company	**70**	**20**	**90**
Accrued salaries not yet paid	**33**	**2**	**35**
Others	**59**	**23**	**82**
Net deferred tax assets	**530**	**(135)**	**395**

	At 1 January 2005 RMB million	Recognised in income statement RMB million	At 31 December 2005 RMB million
Current			
Allowances, primarily for receivables and inventories	40	–	40
Non-current			
Property, plant and equipment	(103)	8	(95)
Lease prepayments	554	(10)	544
Tax allowable expenses not yet incurred	(45)	(76)	(121)
Unrealised profits from sales within the Company	32	38	70
Accrued salaries not yet paid	13	20	33
Others	(22)	81	59
Net deferred tax assets	469	61	530

28 Borrowings

The Group's and the Company's short-term borrowings comprise:

	The Group 2006 RMB million	The Group 2005 RMB million (restated – Note 1)	The Company 2006 RMB million	The Company 2005 RMB million
Borrowings from banks and other financial institutions	**9,255**	5,951	**2,000**	2,000
Loans from subsidiaries	**–**	–	**900**	300
Current portion of long-term borrowings	**5,587**	3,694	**2,201**	1,180
	14,842	9,645	**5,101**	3,480

The Group's and the Company's interest rates per annum on short-term borrowings were:

	The Group 2006	The Group 2005 (restated – Note 1)	The Company 2006	The Company 2005
Borrowings from banks and other financial institutions	**4.185%-5.508%**	3.6%-5.508%	**4.388%-5.508%**	5.022%
Loans from subsidiaries	**–**	–	**2.277%-2.70%**	2.277%
Current portion of long-term borrowings	**2.30%-6.156% L+0.6%-1.8%**	2.30%-5.508% L+0.6%-1.35%	**2.30%-6.156% L+0.6%**	2.30%-5.508% L+0.6%

The Group's and the Company's long-term borrowings comprise:

		The Group 2006 RMB million	The Group 2005 RMB million (restated – Note 1)	The Company 2006 RMB million	The Company 2005 RMB million
Loans from banks and other financial institutions *					
Renminbi denominated	Interest rates ranging from 3.60% to 6.156% per annum with maturities through 28 December 2023	**40,286**	37,805	**8,056**	9,624
US Dollars denominated	Interest rate at L+0.6% -1% per annum with maturities through 20 June 2020	**564**	568	**276**	567
Japanese Yen denominated	Interest rates ranging from 1.80% to 4.45% or L+1.8% per annum with maturities through 20 March 2031	**5,577**	6,114	**5,413**	5,857
		46,427	44,487	**13,745**	16,048
Less: current portion of long-term borrowings		**(5,587)**	(3,694)	**(2,201)**	(1,180)
		40,840	40,793	**11,544**	14,868

* At 31 December 2006, the balance includes an entrusted loan from the Parent Company amounting to RMB1,000 million (2005: RMB1,000 million).

Interest rates comprise fixed rates and floating rates based on the London Interbank Offered Rate ("LIBOR"/"L").

The above borrowings are unsecured.

28 Borrowings *(continued)*

The long-term borrowings were repayable as follows:

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB million	RMB million (restated – Note 1)	**RMB million**	RMB million
Within one year or on demand	**5,587**	3,694	**2,201**	1,180
After one year but within two years	**6,298**	6,214	**2,028**	2,921
After two years but within five years	**13,738**	14,849	**2,635**	3,809
After five years	**20,804**	19,730	**6,881**	8,138
	46,427	44,487	**13,745**	16,048

Included in borrowings are the following amounts denominated in a currency other than the functional currency of the entity to which they relate:

	The Group		The Company	
	2006	2005	**2006**	2005
	million	million	**million**	million
United States Dollars	**USD72**	USD82	**USD35**	USD70
Japanese Yen	**JPY84,979**	JPY88,980	**JPY82,481**	JPY85,231

The Group had unsecured banking facilities amounting to RMB8,072 million as at 31 December 2006 (2005: RMB4,350 million). As at 31 December 2006, the unutilised banking facilities amounted to RMB4,789 million (2005: RMB3,919 million). Such banking facilities would be drawn down in accordance with the level of working capital and planned capital expenditure of the Company and its subsidiaries.

29 Accounts and bills payable

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB million	RMB million (restated – Note 1)	**RMB million**	RMB million
Accounts payable	**8,465**	5,458	**3,511**	2,596
Bills payable	**668**	1,376	**1**	–
	9,133	6,834	**3,512**	2,596

The following is the ageing analysis of accounts and bills payable:

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB million	RMB million (restated – Note 1)	**RMB million**	RMB million
Within one year	**8,705**	6,422	**3,332**	2,274
One to two years	**262**	368	**43**	315
Two to three years	**139**	24	**134**	7
Over three years	**27**	20	**3**	–
	9,133	6,834	**3,512**	2,596

29 Accounts and bills payable *(continued)*

Included in accounts and bills payable are the following amounts denominated in a currency other than the functional currency of the entity to which they relate:

	The Group		The Company	
	2006	2005	**2006**	2005
	million	million	**million**	million
United States Dollars	**USD21**	USD69	**USD16**	USD52
Hong Kong Dollars	**HK$84**	–	**–**	–
Euros	**EUR11**	–	**EUR11**	–

RMB101 million (2005: RMB463 million) of the accounts and bills payable are expected to be settled after more than one year.

30 Accrued expenses and other payables

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB million	RMB million	**RMB million**	RMB million
		(restated – Note 1)		
Accrued staff wages and welfare benefits	**1,364**	1,202	**843**	696
Accrued interest payable	**73**	46	**50**	32
Accrued taxes other than income tax	**1,555**	1,204	**1,083**	958
Other accrued expenses and payables	**2,191**	3,069	**1,273**	1,160
Fair value of derivative financial instruments	**246**	223	**246**	223
Customer deposits and receipts in advances	**1,548**	1,069	**979**	760
	6,977	6,813	**4,474**	3,829

At 31 December 2006, the Group had amounts payable to related parties amounting to RMB211 million (2005: RMB1,283 million as restated). The Company had amounts payable to related parties amounting to RMB200 million as at 31 December 2006 (2005: RMB126 million).

Accrued expenses and payables with an amount of RMB241 million (2005: RMB117 million) are expected to be settled after more than one year.

31 Accrued reclamation obligations

The accrual for reclamation costs has been determined based on management's best estimates. However, so far as the effect on the land from current mining activities becomes apparent in future periods, the estimate of the associated costs may be subject to change in the near term. The Group believes that the accrued reclamation obligations at 31 December 2006 are adequate. The accrual is necessarily based on estimates and therefore, the ultimate liability may exceed or be less than such estimates.

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB million	RMB million	**RMB million**	RMB million
At the beginning of the year	**852**	650	**497**	470
Addition	**40**	172	**40**	–
Accretion expense	**50**	30	**31**	27
At the end of the year	**942**	852	**568**	497

32 Long-term payable

Long-term payable represents payable for acquisition of mining rights which is to be settled over the period of production on an annual basis. The annual payment is determined by fixed rates on a per tonne basis with reference to the annual production volume of the acquired mines.

33 Share capital

	2006 RMB million	2005 RMB million
Registered, issued and fully paid:		
14,691,037,955 domestic state-owned ordinary shares of RMB1.00 each	**14,691**	14,691
3,398,582,500 H shares of RMB1.00 each	**3,399**	3,399
	18,090	18,090

	2006 No. of shares million	2005 No. of shares million
At 1 January	**18,090**	15,000
Conversion of domestic state-owned shares into H shares	**–**	(309)
Issue of H shares	**–**	3,399
At 31 December	**18,090**	18,090

The Company was incorporated on 8 November 2004 with a registered share capital of 15,000,000,000 domestic state-owned ordinary shares with a par value of RMB1.00 each. Such shares were issued to Shenhua in consideration for the assets and liabilities transferred from Shenhua (Note 1).

In 2005, the Company issued 3,398,582,500 H shares with a par value of RMB1.00 each, at a price of HK$7.50 per H share by way of a global initial public offering to Hong Kong and overseas investors. The H shares were listed on the Stock Exchange.

34 Commitments and contingent liabilities

(a) Capital commitments

As at 31 December 2006, the Group had capital commitments for acquisition and construction of land and buildings and equipment, and for the acquisition of investments and associates as follows:

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB million	RMB million (restated – Note 1)	**RMB million**	RMB million
Authorised and contracted for				
- Land and buildings	**4,333**	4,911	**863**	200
- Equipment	**9,542**	6,686	**1,540**	1,973
- Investments and associates	**–**	450	**–**	450
	13,875	12,047	**2,403**	2,623
Authorised but not contracted for				
- Land and buildings	**12,639**	11,990	**3,573**	2,794
- Equipment	**12,550**	20,764	**7,859**	8,485
	25,189	32,754	**11,432**	11,279

(b) Operating lease commitments

The Group leases business premises through non-cancellable operating leases. These operating leases do not contain provisions for contingent lease rentals. None of the rental agreements contain escalation provisions that may require higher future rental payments nor impose restrictions on dividends, additional debt and/or further leasing. As at 31 December 2006, future minimum lease payments under non-cancellable operating leases on business premises having initial or remaining lease terms of more than one year are payable as follows:

	The Group		The Company	
	2006	2005	**2006**	2005
	RMB million	RMB million (restated – Note 1)	**RMB million**	RMB million
Within one year	**43**	48	**25**	37
After one year but within five years	**152**	185	**82**	141
After five years	**109**	178	**58**	137
	304	411	**165**	315

34 Commitments and contingent liabilities *(continued)*

(c) Financial guarantees issued

As at the balance sheet date, the Group issued the following guarantees:

(i) a guarantee in respect of a banking facility made by Shenhua Finance Company Limited ("Shenhua Finance") to an associate of the Company; and

(ii) guarantees to banks in respect of banking facilities granted to subsidiaries.

As at the balance sheet date, the directors do not consider it probable that a claim will be made against the Group under any of the guarantees. The maximum liability of the Group at the balance sheet date under the single guarantee issued is the outstanding amount of the banking facility to an associate of RMB310 million (2005: RMB310 million). The maximum liability of the Company at the balance sheet date under the guarantee is RMB1,966 million (2005: RMB2,478 million).

(d) Legal contingencies

The Group is a defendant in certain lawsuits as well as the plaintiff in other proceedings arising in the ordinary course of business. While the outcomes of such contingencies, lawsuits or other proceedings cannot be determined at present, management believes that any resulting liabilities will not have a material adverse effect on the financial position or operating results of the Group.

(e) Environmental contingencies

To date, the Group has not incurred any significant expenditures for environmental remediation, is currently not involved in any environmental remediation, and apart from the provision for land reclamation costs, has not accrued any further amounts for environmental remediation relating to its operations. Under the existing legislation, management believes that there are no probable liabilities that will have a material adverse effect on the financial position or operating results of the Group. The PRC government, however, has moved, and may move further towards the adoption of more stringent environmental standards. Environmental liabilities are subject to considerable uncertainties which affect the Group's ability to estimate the ultimate cost of remediation efforts. These uncertainties include (i) the exact nature and extent of the contamination at various sites including, but not limited to coal mines and land development areas, whether operating, closed or sold; (ii) the extent of required cleanup efforts; (iii) varying costs of alternative remediation strategies; (iv) changes in environmental remediation requirements; and (v) the identification of new remediation sites. The amount of such future cost is indeterminable due to such factors as the unknown magnitude of possible contamination and the unknown timing and extent of the corrective actions that may be required. Accordingly, the outcome of environmental liabilities under future environmental legislation cannot reasonably be estimated at present, and could be material.

35 Related party transactions

(a) Transactions with Shenhua and its affiliates ("Shenhua Group") and the associates of the Company

The Group is controlled by the Parent Company and has significant transactions and relationships with the Parent Company and its affiliates. Related parties refer to enterprises over which the Parent Company is able to exercise significant influence or control. The Company also has entered into transactions with its associates, over which the Company can exercise significant influence. Because of the above relationships, it is possible that the terms of these transactions are not the same as those that would result from transactions among wholly unrelated parties.

The Group had the following transactions with Shenhua Group and the associates of the Company that were carried out in the normal course of business:

		2006 RMB million	2005 RMB million (restated – Note 1)
Interest income	(i)	**9**	10
Purchases of ancillary materials and spare parts	(ii)	**(509)**	(423)
Ancillary and social services	(iii)	**(438)**	(305)
Transportation services income	(iv)	**71**	78
Interest expense	(v)	**(50)**	(98)
Purchase of coal	(vi)	**(1,421)**	(927)
Sale of coal	(vii)	**1,730**	1,133
Property leasing	(viii)	**(41)**	(49)
Transportation services expense	(ix)	**(272)**	(175)
Net deposits (placed with)/withdrawn from related party		**(1,469)**	3,728
Net loans repaid to related party		**–**	(2,822)
Repairs and maintenance services expense	(x)	**(3)**	(31)
Coal export agency expense	(xi)	**(67)**	(70)
Entrusted loan from a related party		**–**	1,000
Entrusted loan repaid by/(to) a related party		**50**	(100)
Income from equipment installation and construction work	(xii)	**32**	–
Purchase of equipment and construction work	(xiii)	**(124)**	(171)
(Repaid to)/advance from a related party		**(1,200)**	1,200
Other income	(xiv)	**58**	60

35 Related party transactions *(continued)*

(a) Transactions with Shenhua and its affiliates ("Shenhua Group") and the associates of the Company *(continued)*

(i) Interest income represents interest earned from deposits placed with its associate. The applicable interest rate is determined in accordance with the prevailing savings deposit rate.

(ii) Purchases of ancillary materials and spare parts represent purchase of materials and utility supplies from Shenhua Group related to the Group's operations.

(iii) Ancillary and social services represent expenditures for social welfare and support services such as property management, water and electricity supply, and canteen paid to Shenhua Group.

(iv) Transportation services income represents income earned from its associate and Shenhua Group in respect of coal transportation services.

(v) Interest expense represents interest incurred in respect of borrowings from Shenhua Group. The applicable interest rate is determined in accordance with the prevailing borrowing rate.

(vi) Purchase of coal represents coal purchased from Shenhua Group.

(vii) Sale of coal represents income from sale of coal to its associates and Shenhua Group.

(viii) Property leasing represents rental charge in respect of properties leased from Shenhua Group.

(ix) Transportation services expense represents expense related to coal transportation services provided by its associates.

(x) Repairs and maintenance services expense represents expense related to machinery repairs and maintenance services provided by Shenhua Group.

(xi) Coal export agency expense represents expense related to coal export agency services provided by Shenhua Group.

(xii) Income from equipment installation and construction work represents equipment installation and construction service provided to related parties.

(xiii) Purchase of equipment and construction work represents expense related to purchase of equipment and construction work from related parties.

(xiv) Other income includes agency income, repairs and maintenance service income, sales of ancillary materials and spare parts, management fee income and sales of electricity, etc.

The directors of the Company are of the opinion that the above transactions with related parties were conducted in the ordinary course of business, on normal commercial terms and in accordance with the agreements governing such transactions.

35 Related party transactions *(continued)*

(a) Transactions with Shenhua and its affiliates ("Shenhua Group") and the associates of the Company *(continued)*

In connection with the Restructuring, the Company and Shenhua Group entered into a number of agreements effective as at 1 January 2004, which were subsequently revised as stated below. The terms of the principal agreements impacting the results of operations of the Company are summarised as follows:

(a) The Company entered into a three-year mutual supply agreement expiring 31 December 2006 which was subsequently extended to 31 December 2007 in the revised agreement with the Parent Company for the mutual provision of production supplies and ancillary services. Pursuant to the agreements, Shenhua Group provides the Company with the production supplies, such as explosives, fuses, oil products, and other related or similar production supplies and services; ancillary production services including security, logistics and support services, tendering services, other related or similar services and use of the information network system; and ancillary administrative services, such as social security and pension management service and staff data recording services. On the other hand, the Company provides Shenhua Group with water supplies, rolling stock management, rail transportation and other related or similar production supplies or services and use of the information network system.

The products and services provided under the agreement, other than the social security, pension management services, and staff data recording services which are provided by Shenhua Group free of charge and the sharing of use of the information network system, are provided in accordance with the following pricing policy:

- price prescribed by the state (including any price prescribed by any relevant local government), if applicable;
- where there is no state-prescribed price but where there is a state-guidance price, then the state-guidance price;
- where there is neither a state-prescribed price nor a state-guidance price, the market price; or
- where none of the above is applicable or where it is not practical to apply the above pricing policies in reality, the price agreed between the relevant parties shall be the reasonable costs incurred in providing the goods or services plus a profit margin of 5% of such costs.

Each party may terminate the provision of production supplies and ancillary services on six months' prior written notice unless the other party is unable to obtain similar production supplies and ancillary services from third parties.

(b) The Company entered into a three-year coal supply agreement expiring 31 December 2006 which was subsequently extended to 31 December 2007 in the revised agreement with the Parent Company. Pursuant to the agreements, the Group and Shenhua Group supply coal to each other in accordance with their needs. The coal supplied is charged at the prevailing market price. Each party is entitled to purchase coal from any independent third party if such a third party is able to provide coal to it on better terms and conditions than those offered by the other party.

Each party may terminate the supply of coal by giving six months' prior written notice to the other party. However, if the Company cannot conveniently purchase coal from a third party, Shenhua Group may not terminate the supply of coal under any circumstances.

35 Related party transactions *(continued)*

(a) Transactions with Shenhua and its affiliates ("Shenhua Group") and the associates of the Company *(continued)*

(c) The Company entered into a three-year financial services agreement expiring 31 December 2006 which was subsequently terminated on 24 May 2005 with Shenhua Finance, a subsidiary of Shenhua and an assoicate of the Company. The Company entered into a new financial services agreement which was effective from 21 July 2006 to 31 December 2007 with Shenhua Finance on 21 July 2006. Pursuant to the new agreement, Shenhua Finance provides financial services to the Group. The terms and conditions of such services should not be less favourable than the terms and conditions of financial services rendered to other members of Shenhua Group by Shenhua Finance and by other financial institutions. The interest rate for the Group's deposit with Shenhua Finance should not be lower than the lowest limit fixed by the PBOC for the same type of deposit. The interest rate for loans made by Shenhua Finance to the Company should not be higher than the highest limit fixed by PBOC for the same type of loan. The fees charged by Shenhua Finance for the provision of other financial services shall be fixed according to the rate of fees chargeable by the PBOC or the China Banking Regulatory Commission.

(d) The Company entered into a ten-year property leasing agreement expiring 31 December 2013 which was subsequently extended to 31 December 2014 in the revised agreement with the Parent Company. Pursuant to the agreements, the Group leases certain properties from Shenhua Group and vice versa. No rent is payable by the Company before Shenhua Group obtains the relevant certificate of property ownership for that piece of property. The rental charges will be based on comparable market rates. If Shenhua Group negotiates to sell a leased property to a third party, the Company has a pre-emptive right to purchase such property under terms no less favourable to the Company. The lessee may sub-let any of the properties with the consent of lessor. The Group may at any time during the term of the property leasing agreement enter into or terminate the lease of the properties under the property leasing agreement by providing three months' written notice.

(e) The Company entered into a ten-year land leasing agreement expiring 31 December 2013 which was subsequently extended to 31 December 2024 in the revised agreement with the Parent Company, which may be renewed upon request by the Company for another 20 years on the same terms (subject to the prevailing market rent) by giving one month's written notice prior to expiry of the land leasing agreement. No rent is payable before Shenhua Group has obtained the relevant land use rights certificate for that parcel of land, but thereafter, the annual rent is determined between the parties based on the relevant laws and regulations then in force and the local market rate. The rights of the Group to use land under the land leasing agreement may not be sub-let. The Group may at any time during the term of the land leasing agreement terminate the lease of any parcel of land leased under the land leasing agreement by providing three months' written notice.

(f) The Company entered into a three-year agency agreement expiring 31 December 2006 which was subsequently extended to 31 December 2007 in the revised agreement with the Parent Company for the export of coal on the Company's behalf. Shenhua Group is appointed as a non-exclusive export agent of the Company in priority over other export agencies if the terms of export services offered by it are equal or more favourable than other export agencies. Pursuant to the agreements, Shenhua Group is entitled to receive an agency fee based on the relevant market rates or lower rates. Currently, the rate is 0.7% of the free on board price of each tonne of coal exported by Shenhua Group on the Company's behalf.

35 Related party transactions *(continued)*

(a) Transactions with Shenhua and its affiliates ("Shenhua Group") and the associates of the Company *(continued)*

(g) The Company and one of its subsidiaries entered into a three-year agency agreement expiring 31 December 2006 which was subsequently extended to 31 December 2007 in the revised agreement with the Parent Company for the sale of coal by the Company's subsidiary on behalf of Shenhua Group to minimise any potential competition between Shenhua Group and the Company. The Company's subsidiary is appointed as the exclusive sales agent for Shenhua Group for thermal coal and non-exclusive sales agent for coking coal. The unit selling price for sales the Company's subsidiary makes as agent will be determined by the Company's subsidiary according to the spot market price, subject to confirmation by Shenhua Group. Pursuant to the agreements, the Company's subsidiary is entitled to receive an agency fee which is based on its related costs incurred plus a profit margin of 5% for sale of coal outside the Inner Mongolia Autonomous Region. The Company's subsidiary does not charge any fee for sales of coal within the Inner Mongolia Autonomous Region.

(h) The Company entered into a ten-year trademark license agreement expiring 31 December 2013 which was subsequently amended by a supplemental agreement with the Parent Company. Pursuant to the agreements, Shenhua Group has granted the Group a non-exclusive licence to use the registered trademarks in the PRC. The trademarks licensed under the trademark license agreement may be used by the Group on a royalty-free basis for a term of ten years, which is renewable for another term of ten years if so agreed by both parties. Shenhua Group has agreed to maintain at its own cost the registration of such trademarks during the term of the trademarks license agreement. Shenhua Group has also agreed to be responsible for the expenses for enforcement against any infringement of the licensed trademarks by third parties.

(i) A subsidiary of the Company entered into a three-year coal supply agreement expiring 31 December 2006 which was subsequently extended to 31 December 2007 in the revised agreement with Heibei Guohua Dingzhou Power Generation Co., Ltd. ("Dingzhou", an associate of the Company). Pursuant to the agreements, the Company's subsidiary supplies coal to Dingzhou. The coal supplied is determined in accordance with the prevailing market price. Each party may terminate the supply of coal at any time by providing six months' prior written notice to the other party.

(j) A subsidiary of the Company entered into a one-year maintenance agreement with effect from 1 January 2004 which was subsequently renewed for two more years to 31 December 2006 in the renewed agreement with Dingzhou. Pursuant to the agreements, the Company's subsidiary provides rail line maintenance services to Dingzhou on a daily basis.

35 Related party transactions *(continued)*

(a) Transactions with Shenhua and its affiliates ("Shenhua Group") and the associates of the Company *(continued)*

Amounts due from/to Shenhua Group and the associates of the Company:

	Note	**2006 RMB million**	2005 RMB million (restated – Note 1)
Cash and cash equivalents		**1,469**	–
Accounts receivable		**112**	48
Prepaid expenses and other current assets	25	**102**	211
Total amounts due from Shenhua Group and the associates of the Company		**1,683**	259
Accounts payable		**345**	190
Accrued expenses and other payables	30	**211**	1,283
Long-term borrowings	28	**1,000**	1,000
Total amounts due to Shenhua Group and the associates of the Company		**1,556**	2,473

The deposits placed with an associate of the Company generate interest based on prevailing bank interest rates published by PBOC. Long-term borrowings bear an interest rate at 5.25% per annum. Other than the above, amounts due from/to Shenhua Group and the associates of the Company bear no interest, are unsecured and are repayable in accordance with normal commercial terms.

Acquisition of a subsidiary

Pursuant to a resolution passed at the Directors' meeting on 10 March 2006, the Company acquired a 70% stake in Jinjie Energy from Beijing Guohua Power at a consideration of RMB1,162 million. The Acquisition was completed in August 2006.

Following the Acquisition of Jinjie Energy (see Note 1), certain transactions between Jinjie Energy and Shenhua Group and the associates of the Company in 2005 were considered as related party transactions in these financial statements and the disclosures in this regard for the year ended 31 December 2005 were restated accordingly.

(b) Key management personnel emoluments

Key management personnel receive compensation in the form of fees, salaries, housing and other allowances, benefits in kind, discretionary bonuses, share appreciation rights and retirement scheme contributions.

Key management personnel compensation of the Group's summarised as followings:

	2006 RMB million	2005 RMB million
Short-term employee benefits	**4**	4
Post-employment benefits	**1**	1
Share appreciation rights expense	**17**	1
	22	6

Total remuneration is included in "personnel expenses" as disclosed in Note 7.

(c) Contributions to post-employment benefit plans

The Group participates in various defined contribution post-employment benefit plans organised by municipal and provincial governments for its employees. Further details of the Group's post-employment benefit plans are disclosed in Note 36.

35 Related party transactions *(continued)*

(d) Transactions with other state-controlled entities in the PRC

The Company is a state-controlled entity and operates in an economic regime currently dominated by entities directly or indirectly controlled by the PRC government ("state-controlled entities") through its government authorities, agencies, affiliations and other organisations.

Other than those transactions with the Parent Company and its associates as disclosed above, the Group conducts certain business activities with other state-controlled entities which include but are not limited to the following:

- Power sales;
- Sales and purchases of coal;
- Transportation services;
- Construction work of railway;
- Purchases of ancillary materials and spare parts;
- Ancillary and social services; and
- Financial services arrangements.

These transactions are conducted in the ordinary course of the Group's business on terms comparable to those with other entities that are not state-controlled. The Group has established its buying, pricing strategy and approval process for purchases and sales of products and services. Such buying, pricing strategy and approval processes do not depend on whether the counterparties are state-controlled entities or not.

Having considered the potential for transactions to be impacted by related party relationships, the Group's pricing strategy, buying and approval processes, and what information would be necessary for an understanding of the potential effect of the relationship on the financial statements, the directors are of the opinion that the following transactions with other state-controlled entities require disclosure:

(i) Transactions with other state-controlled entities, including state-controlled banks in the PRC

	2006 RMB million	2005 RMB million
Coal revenue	**22,405**	18,495
Power revenue	**16,210**	10,616
Transportation costs	**4,799**	4,093
Interest income	**241**	256
Interest expenses	**2,789**	3,043

(ii) Balances with other state-controlled entities, including state-controlled banks in the PRC

	2006 RMB million	2005 RMB million
Accounts receivable	**3,217**	1,618
Cash and time deposits at banks	**14,039**	19,928
Short-term borrowings and current portion of long-term borrowings	**14,842**	9,645
Long-term borrowings, less current portion	**39,840**	39,793

36 Employee benefits plan

As stipulated by the regulations of the PRC, the Group participates in various defined contribution retirement plans organised by municipal and provincial governments for its employees. The Group is required to make contributions to the retirement plans at rates ranging from 17% to 20% of the salaries, bonuses and certain allowances of the employees. A member of the plan is entitled to a pension equal to a fixed proportion of the salary prevailing at the member's retirement date. The Group has no other material obligation for the payment of pension benefits associated with these plans beyond the annual contributions described above. The Group's contributions for the year ended 31 December 2006 were RMB353 million (2005: RMB348 million as restated).

On 19 November 2005, the Company's board of directors approved a scheme of share appreciation rights for the senior management of the Group with a term of 10 years with effect from 15 June 2005. No shares will be issued under this scheme. The rights will be granted in units with each unit representing one H share of the Company.

The rights to the units will have an exercise period of six years from the date of grant and can be exercised after the second, third and fourth anniversary of the date of grant and the total number of the rights exercised by an individual may not in aggregate exceed one-third, two-thirds and 100% respectively, of the total rights granted to the individual.

Upon exercise of the said rights, the exercising participant will, subject to the restrictions under the scheme, receive a payment in RMB, after deducting any applicable withholding tax, equal to the product of the number of rights exercised and the difference between the exercise price and market price of the H shares of the Company at the time of exercise.

The Company granted 3.2 million share appreciation rights during the year ended 31 December 2006 (2005: 2.8 million) and recognised a compensation expense over the applicable vesting period. The compensation expense recognised for the year ended 31 December 2006 amounted to RMB22 million (2005: RMB1 million). The exercise price of granted share appreciation rights as approved by the board of directors ranges from HK$7.90 to HK$11.80. As at 31 December 2006, 6.0 million (2005: 2.8 million) share appreciation rights were outstanding.

37 Segment information

The Group's risks and rates of return are affected predominantly by differences in the products and services it produces. The Group's primary format for reporting segment information is business segments with geographical segments as its secondary format.

Business segments:

The Group has two reportable segments as follows:

(1) Coal operations – which produces coal from surface and underground mines, and the sale and transportation of coal to external customers and the power segment. The Group primarily sells its coal under long-term coal supply contracts which typically allow the parties to make annual price adjustments.

(2) Power operations – which uses coal, sourced from coal mining segment of the Group and purchased from external suppliers, to generate the electric power for sale to external power grid companies and to the coal segment. The sales of power are not subject to long-term minimum power supply obligations. Electric power is sold to the power grid companies in accordance with planned power output at the tariff rates as approved by the relevant government authorities. Electric power produced in excess of the planned power output is sold at the tariff rate as agreed upon with the respective power grid companies which are generally lower than the tariff rates for planned power output.

The segments were determined primarily because the Group manages its coal and power generation businesses separately. The reportable segments are each managed separately due to differences in their operating, distribution and production processes and gross margin characteristics.

The Group evaluates the performance and allocates resources to its reportable segments on an income from operations basis, without considering the effects of finance costs or investment income. The accounting policies of the Group's reportable segments are the same as those described in the significant accounting policies (see Note 2). Corporate administrative costs and assets are not allocated to the operating segments; instead, operating segments are charged for direct corporate services. Inter-segment transfer pricing is based on market prices or prices pre-determined by the relevant governmental authority.

37 Segment information *(continued)*

(a) Income statement

The following table presents segmental information:

	Coal		Power		Corporate and others (Note)		Eliminations		Total	
	2006 RMB million	2005 RMB million	**2006 RMB million**	2005 RMB million (restated – Note 1)	**2006 RMB million**	2005 RMB million	**2006 RMB million**	2005 RMB million	**2006 RMB million**	2005 RMB million (restated – Note 1)
Revenues										
External sales	**47,604**	41,344	**16,636**	10,898	**–**	–	**–**	–	**64,240**	52,242
Inter-segment sales	**6,744**	4,156	**83**	53	**–**	–	**(6,827)**	(4,209)	**–**	–
Total operating revenues	**54,348**	45,500	**16,719**	10,951	**–**	–	**(6,827)**	(4,209)	**64,240**	52,242
Cost of revenues										
Coal purchased from third parties	**(6,777)**	(4,209)	**(158)**	(130)	**–**	–	**–**	–	**(6,935)**	(4,339)
Cost of coal production	**(8,964)**	(7,042)	**–**	–	**–**	–	**2,009**	1,190	**(6,955)**	(5,852)
Cost of coal transportation	**(11,306)**	(9,673)	**–**	–	**–**	–	**1,423**	804	**(9,883)**	(8,869)
Power cost	**–**	–	**(10,905)**	(7,387)	**–**	–	**3,372**	2,195	**(7,533)**	(5,192)
Others	**(1,144)**	(853)	**(10)**	(14)	**–**	–	**–**	–	**(1,154)**	(867)
Total cost of revenues	**(28,191)**	(21,777)	**(11,073)**	(7,531)	**–**	–	**6,804**	4,189	**(32,460)**	(25,119)
Selling, general and administrative expenses	**(2,611)**	(2,215)	**(1,336)**	(877)	**(219)**	(219)	**–**	–	**(4,166)**	(3,311)
Other operating (expenses)/ income , net	**(244)**	(207)	**(24)**	57	**(50)**	–	**–**	–	**(318)**	(150)
Profit/(loss) from operations	**23,302**	21,301	**4,286**	2,600	**(269)**	(219)	**(23)**	(20)	**27,296**	23,662
Reconciliation of profit from operations to profit for the year:										
Net financing costs									**(2,100)**	(2,060)
Investment (loss)/income									**(1)**	10
Share of profits less losses of associates									**478**	461
Income tax									**(5,388)**	(4,080)
Profit for the year									**20,285**	17,993

Note: "Corporate and others" represents miscellaneous expenses that are immaterial.

37 Segment information *(continued)*

(b) Balance sheet

Assets and liabilities dedicated to a particular segment's operations are included in that segment's total assets and liabilities. Assets which benefit more than one segment are considered to be corporate assets and are not allocated. "Unallocated assets" consists primarily of cash and cash equivalents, time deposits, investments and deferred tax assets. "Unallocated liabilities" consists primarily of short-term and long-term borrowings, income tax payable and deferred tax liabilities.

Interests in and earnings from associates are included in the segments in which the associates operate. Information on interest in associates is included in Note 19.

	2006 RMB million	2005 RMB million (restated – Note 1)
Assets		
Segment assets		
Coal	**82,131**	69,978
Power	**57,016**	45,647
Combined segment assets	**139,147**	115,625
Interest in associates		
Coal	**657**	544
Power	**1,712**	3,142
Total interest in associates	**2,369**	3,686
Unallocated assets	**21,632**	22,958
Total assets	**163,148**	142,269
Liabilities		
Segment liabilities		
Coal	**(12,847)**	(11,127)
Power	**(5,457)**	(4,686)
Combined segment liabilities	**(18,304)**	(15,813)
Unallocated liabilities	**(60,143)**	(53,469)
Total liabilities	**(78,447)**	(69,282)

37 Segment information *(continued)*

(c) Other segment information

	Coal		Power		Corporate and others (Note)		Total	
	2006 RMB million	2005 RMB million	**2006 RMB million**	2005 RMB million (restated – Note 1)	**2006 RMB million**	2005 RMB million	**2006 RMB million**	2005 RMB million (restated – Note 1)
Capital expenditure	**13,696**	13,609	**10,818**	10,298	**121**	4	**24,635**	23,911
Depreciation and amortisation	**4,044**	3,593	**2,565**	1,783	**2**	1	**6,611**	5,377
Share of profits less losses of associates	**94**	85	**384**	376	**–**	–	**478**	461
Impairment losses on property, plant and equipment	**147**	41	**–**	–	**–**	–	**147**	41

Segment capital expenditure is the total cost incurred during the year to acquire segment assets that are expected to be used for more than one year.

Note: "Corporate and others" represents miscellaneous expenses that are immaterial.

Geographical segments:

The Group has three geographical segments by location of customers as follows:

(1) Domestic markets – external customers which are located in the PRC.

(2) Asia Pacific markets – export sales to customers which are located outside the PRC and primarily to customers in Korea and Japan.

(3) Other markets – export sales to customers which are located outside the PRC and the Asia Pacific region.

(i) Income statement

	2006 RMB million	2005 RMB million
Domestic markets	**55,123**	42,606
Export sales – Asia Pacific markets	**8,825**	9,351
Export sales – other markets	**292**	285
Total operating revenues	**64,240**	52,242

(ii) Balance sheet

The location of all the Group's production or service facilities and other assets is in the PRC.

38 Distributable reserves

The movement of shareholders' equity of the Company is as follows:

	Share capital RMB million (Note 33)	Share premium RMB million	Statutory reserves RMB million	Capital and other reserves RMB million	Retained earnings RMB million	Total RMB million
At 1 January 2005 (as previously reported)	15,000	–	230	1,716	6,794	23,740
Adjusted for acquisition of Jinjie Energy (Note 1)	–	–	–	20	–	20
At 1 January 2005 (as restated)	15,000	–	230	1,736	6,794	23,760
Issuance of shares upon public listing	3,090	21,568	–	–	–	24,658
Share issue expenses	–	(755)	–	–	–	(755)
Profit for the year	–	–	–	–	13,840	13,840
Appropriations	–	–	2,898	499	(3,397)	–
Dividend for 2004 (Note 13)	–	–	–	–	(7,549)	(7,549)
Adjusted for acquisition of Jinjie Energy (Note 1)	–	–	–	489	–	489
Realisation of deferred tax	–	–	–	(10)	10	–
Revaluation surplus realised	–	–	–	(2)	2	–
At 31 December 2005	18,090	20,813	3,128	2,712	9,700	54,443
At 1 January 2006	**18,090**	**20,813**	**3,128**	**2,712**	**9,700**	**54,443**
Profit for the year	**–**	**–**	**–**	**–**	**14,859**	**14,859**
Appropriations	**–**	**–**	**1,614**	**587**	**(2,201)**	**–**
Dividend for 2005 (Note 13)	**–**	**–**	**–**	**–**	**(7,404)**	**(7,404)**
Realisation of deferred tax	**–**	**–**	**–**	**(17)**	**17**	**–**
Revaluation surplus realised	**–**	**–**	**–**	**(4)**	**4**	**–**
Consideration of the acquisition (Note 1)	**–**	**–**	**–**	**(1,162)**	**–**	**(1,162)**
At 31 December 2006	**18,090**	**20,813**	**4,742**	**2,116**	**14,975**	**60,736**

According to the Company's Articles of Association, the amount of retained profits available for distribution to equity shareholders of the Company is the lower of the amount determined in accordance with the PRC Accounting Rules and Regulations and the amount determined in accordance with IFRSs after the appropriation to reserves as detailed in Note (v) to the consolidated statement of changes in equity.

At 31 December 2006, the aggregate amount of reserves available for distribution to equity shareholders of the Company was RMB14,975 million (2005: RMB9,700 million).

39 Financial instruments

Exposure to credit, liquidity, interest rate and currency risks arises in the normal course of the Group's business. These risks are limited by the Group's and the Company's financial management policies and practices described below.

(a) Credit risk

The carrying amounts of cash and cash equivalents, time deposits, investments, accounts and bills receivable, other receivables and available-for-sale investments represent the Group's and the Company's maximum exposure to credit risk in relation to these financial assets. Substantially all of the Group's and the Company's cash and cash equivalents are held in major financial institutions located in the PRC, which management believes are of high credit quality. The Group's and the Company's major customers are power plants, metallurgical companies and power grid companies, which accounted for significant amounts of the Group's and the Company's total operating revenues during the year. The Group and the Company have no significant credit risk with any of these customers since the Group and the Company maintain long-term and stable business relationships with these large customers in the coal and power industries. Accounts receivable are typically unsecured and denominated in RMB, and are derived from revenues earned from operations arising in the PRC. The Group and the Company perform ongoing credit evaluations of its customers' financial condition and generally does not require collateral on accounts receivable. The impairment losses on bad and doubtful accounts have been within management's expectations.

The maximum exposure to credit risk is represented by the carrying amount of each financial asset, including derivative financial instruments, in the balance sheet. Except for the financial guarantees given by the Group and the Company as set out in Note 34(c), the Group and the Company do not provide any other guarantees which would expose the Group or the Company to credit risk. The maximum exposure to credit risk in respect of these financial guarantees at the balance sheet date is disclosed in Note 34(c).

(b) Currency risk

Except for export sales which are transacted in US Dollars, all of the revenue-generating operations of the Group and the Company are transacted in RMB, which is not fully convertible into foreign currencies. On 1 January 1994, the PRC government abolished the dual rate system and introduced a single rate of exchange as quoted by the PBOC. However, the unification of the exchange rate does not imply convertibility of RMB into Hong Kong Dollars or other foreign currencies. All foreign exchange transactions must take place through the PBOC or other institutions authorised to buy and sell foreign exchange. Approval of foreign currency payments by the PBOC or other institutions requires submitting a payment application form together with suppliers' invoices, shipping documents and signed contracts.

In addition, the Group and the Company incur foreign currency risk on borrowings that are denominated in a currency other than RMB. The currencies giving rise to this risk are primarily US Dollars and Japanese Yen. To reduce the risk, the Group has entered into forward exchange contracts, details of which are set out in Note (d) below.

(c) Interest rate risk

The interest rates and terms of repayment of the Group's and the Company's borrowings are disclosed in Note 28. To reduce the interest rate exposure to fixed rate borrowings, the Group has entered into interest rate swaps, details of which are set out in Note (d) below.

39 Financial instruments *(continued)*

(d) Fair values

The following disclosure of the estimated fair value of financial instruments is made in accordance with the requirements of IAS 32. Fair value estimates, methods and assumptions, set forth below for the Group's financial instruments, are made solely to comply with the requirements of IAS 32 and should be read in conjunction with the financial statements. The estimated fair value amounts have been determined by the Group using market information and valuation methodologies considered appropriate. However, considerable judgement is required to interpret market data to develop the estimates of fair values. Accordingly, the estimates presented herein are not necessarily indicative of the amounts the Group and the Company could realise in a current market exchange. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts.

The following summaries the major methods and assumptions used in estimating the fair values of the Group's and the Company's financial instruments.

Long-term borrowings: The fair values of long-term borrowings are estimated by discounting future cash flows using current market interest rates offered to the Group and the Company for borrowings with substantially the same characteristics and maturities. As at 31 December 2006, the carrying amounts and fair values of the Group's and the Company's long-term borrowings are as follows:

	The Group				The Company			
	2006		2005		2006		2005	
	Carrying amount RMB million	Fair value RMB million	Carrying amount RMB million (restated – Note 1)	Fair value RMB million (restated – Note 1)	Carrying amount RMB million	Fair value RMB million	Carrying amount RMB million	Fair value RMB million
Long-term borrowings	**46,427**	**46,597**	44,487	44,835	**13,745**	**13,950**	16,048	16,400

Derivatives: Forward exchange contracts are either marked to market using listed market prices or by discounting the contractual forward price and deducting the current spot rate. For interest rate swaps broker quotes are used. Those quotes are back tested using pricing models or discounted cash flow techniques. Where discounted cash flow techniques are used, estimated future cash flows are based on management's best estimates and the discount rate is a market related rate for a similar instrument having a similar maturity at the balance sheet date. Where other pricing models are used, inputs are based on market related data at the balance sheet date.

39 Financial instruments *(continued)*

(d) Fair values *(continued)*

Derivatives outstanding at 31 December 2006 in connection with the fixed rate borrowings denominated in Japanese Yen are as follows:

Remaining term to maturity	The Group receives (notional amount Japanese Yen million)	Interest revenues	The Group pays (notional amount US Dollars million)	Interest charges
Within one year	–		–	
After one year but within five years	3,693	Fixed 2.3%	33	6 month L-1.14% to 6 month L-1.12%
After five years	25,089	Fixed 1.8% to 2.6%	216	Fixed 2.95% to 4.45% or 6 month L-2.36% to 6 month L-0.29%
	28,782		249	

Derivatives outstanding at 31 December 2005 in connection with the fixed rate borrowings denominated in Japanese Yen are as follows:

Remaining term to maturity	The Group receives (notional amount Japanese Yen million)	Interest revenues	The Group pays (notional amount US Dollars million)	Interest charges
Within one year	–		–	
After one year but within five years	8,951	Fixed 2.3%	83	Fixed 3.58% or 6 month L-1.14% to 6 month L-1.12%
After five years	11,088	Fixed 2.5% to 2.6%	99	Fixed 4.29% or 4.45% or 6 month L-0.39% to 6 month L-0.29%
	20,039		182	

39 Financial instruments *(continued)*

(d) Fair values *(continued)*

The carrying amount and the fair value of the Group's and the Company's derivative financial instruments are as follows:

	The Group and the Company			
	2006		2005	
	Carrying amount RMB million	**Fair value RMB million**	Carrying amount RMB million	Fair value RMB million
Derivative financial instruments - liabilities	**246**	**246**	223	223

Change in fair value is recognised as net financing costs in the consolidated income statement.

The fair value of interest rate swaps is the estimated amount that the Group would receive or pay to terminate the swap at the balance sheet date, taking into account current interest rates and the current creditworthiness of the swap counterparties.

The fair values of all other financial instruments approximate their carrying amounts due to the nature or short-term maturity of these instruments.

40 Accounting estimates and judgements

The Group's financial condition and results of operations are sensitive to accounting methods, assumptions and estimates that underlie the preparation of the financial statements. The Group bases the assumptions and estimates on historical experience and on various other assumptions that the Group believes to be reasonable and which form the basis for making judgements about matters that are not readily apparent from other sources. On an on-going basis, management evaluates its estimates. Actual results may differ from those estimates as facts, circumstances and conditions change.

The selection of critical accounting policies, the judgements and other uncertainties affecting application of those policies and the sensitivity of reported results to changes in conditions and assumptions are factors to be considered when reviewing the financial statements. The principal accounting policies are set forth in Note 2. The Group believes the following critical accounting policies involve the most significant judgements and estimates used in the preparation of the financial statements.

Coal reserves

Engineering estimates of the Group's coal reserves are inherently imprecise and represent only approximate amounts because of the subjective judgements involved in developing such information. There are authoritative guidelines regarding the engineering criteria that have to be met before estimated coal reserves can be designated as "proved" and "probable". Proved and probable coal reserve estimates are updated at regular basis and have taken into account recent production and technical information about each mine. In addition, as prices and cost levels change from year to year, the estimate of proved and probable coal reserves also changes. This change is considered a change in estimate for accounting purposes and is reflected on a prospective basis in related depreciation rates.

Despite the inherent imprecision in these engineering estimates, these estimates are used in determining depreciation expenses and impairment loss. Depreciation rates are determined based on estimated proved and probable coal reserve quantity (the denominator) and capitalised costs of mining structures and mining rights (the numerator). The capitalised cost of mining structures and mining rights are amortised based on the units of coal produced.

40 Accounting estimates and judgements *(continued)*

Impairments

In considering the impairment losses that may be required for certain of the Group's assets which include property, plant and equipment, construction in progress and investments in its subsidiaries and associates (Note 2(m)(ii)), recoverable amount of the asset needs to be determined. The recoverable amount is the greater of the net selling price and the value in use. It is difficult to precisely estimate selling price because quoted market prices for these assets may not be readily available. In determining the value in use, expected cash flows generated by the asset are discounted to their present value, which requires significant judgement relating to items such as level of sale volume, selling price and amount of operating costs. The Group uses all readily available information in determining an amount that is reasonable approximation of recoverable amount, including estimates based on reasonable and supportable assumptions and projections of items such as sale volume, selling price and amount of operating costs.

In considering the impairment losses that may be required for current receivables, future cashflows need to be determined. One of the key assumptions that has to be applied is about the ability of the debtors to settle the receivables. Despite that the Group has used all available information to make this estimation, inherent uncertainty exists and actual write-offs may be higher than the amount estimated.

Depreciation

Other than the mining structures and mining rights, property, plant and equipment are depreciated on a straight-line basis over the estimated useful lives of the assets, after taking into account the estimated residual value. The Group reviews the estimated useful lives of the assets regularly. The useful lives are based on the Group's historical experience with similar assets and taking into account anticipated technological changes. The depreciation expense for future periods is adjusted if there are significant changes from previous estimates.

Obligations for land reclamation

The estimation of the liabilities for final reclamation and mine closure involves the estimates of the amount and timing for the future cash spending as well as the discount rate used for reflecting current market assessments of the time value of money and the risks specific to the liability. The Group considers the factors including future production volume and development plan, the geological structure of the mining regions and reserve volume to determine the scope, amount and timing of reclamation and mine closure works to be performed. Determination of the effect of these factors involves judgements from the Group and the estimated liabilities may turn out to be different from the actual expenditure to be incurred. The discount rate used by the Group may also be altered to reflect the changes in the market assessments of the time value of money and the risks specific to the liability, such as change of the borrowing rate and inflation rate in the market. As changes in estimates occur (such as mine plan revisions, changes in estimated costs, or changes in timing of the performance of reclamation activities), the revisions to the obligation will be recognised at the appropriate discount rate.

Derivative financial instruments

In determining the fair value of the derivative financial instruments, considerable judgement is required to interpret market data used in the valuation techniques. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts.

41 Subsequent events

The following significant transactions took place subsequent to 31 December 2006:

(a) On 23 March 2007, the directors proposed a final dividend payable to all equity shareholders of the Company. Further details are disclosed in Note 13(a).

(b) On 29 December 2006, the Standing Committee of the Tenth National People's Congress ("NPC") passed a resolution to submit the draft corporate income tax law to the Tenth NPC plenary session for voting. According to the income tax law that was passed by NPC on 16 March 2007, corporate income tax rate will be revised to 25% with effect from 1 January 2008. Since implementation measure on transitional policy of preferential tax rate granted according to current tax law and administrative regulations was not yet announced, financial impact of the new tax law cannot be reasonably estimated at this stage.

42 Immediate and ultimate controlling party

At 31 December 2006, the directors consider the immediate parent and ultimate controlling party of the Group to be Shenhua Group Corporation Limited, a state-owned enterprise established in the PRC.

43 Possible impact of amendments, new standards and interpretations issued but not yet effective for the annual accounting period ended 31 December 2006

Up to the date of issue of these financial statements, the IASB has issued the following amendments, new standards and interpretations which are not yet effective for the annual accounting period ended 31 December 2006 and which have not been adopted in these financial statements:

	Effective for accounting period beginning on or after
IFRS 7, Financial Instruments: Disclosures	1 January 2007
IFRS 8, Operating Segments	1 January 2009
IFRIC 7, Applying the Restatement Approach under IAS 29, Financial Reporting in Hyperinflationary Economies	1 March 2006
IFRIC 8, Scope of IFRS 2	1 May 2006
IFRIC 9, Reassessment of Embedded Derivatives	1 June 2006
IFRIC 10, Interim financial reporting and impairment	1 November 2006
IFRIC 11, IFRS 2 – Group and Treasury Share Transactions	1 March 2007
IFRIC 12, Service Concession Agreements	1 January 2008
Amendment to IAS 1, Presentations of Financial Statements: Capital Disclosures	1 January 2007

43 Possible impact of amendments, new standards and interpretations issued but not yet effective for the annual accounting period ended 31 December 2006 *(continued)*

The Group is in the process of making an assessment of what the impact of these amendments, new standards and new interpretations is expected to be in the period of initial application. So far the Group believes that the adoption of IFRIC 7, IFRIC 8, IFRIC 9, IFRIC 11 and IFRIC 12 are not applicable to any of the Group's operations and that the adoption of the rest of the above amendments, new standards and new interpretations is unlikely to have a significant impact on the Group's results of operations and financial position.

44 Comparative figures

Certain comparative figures have been adjusted or re-classified as a result of the application of pooling-of-interests method on the acquisition of Jinjie Energy or to conform with the current year's presentation.