

Corporate Governance

Governance Culture

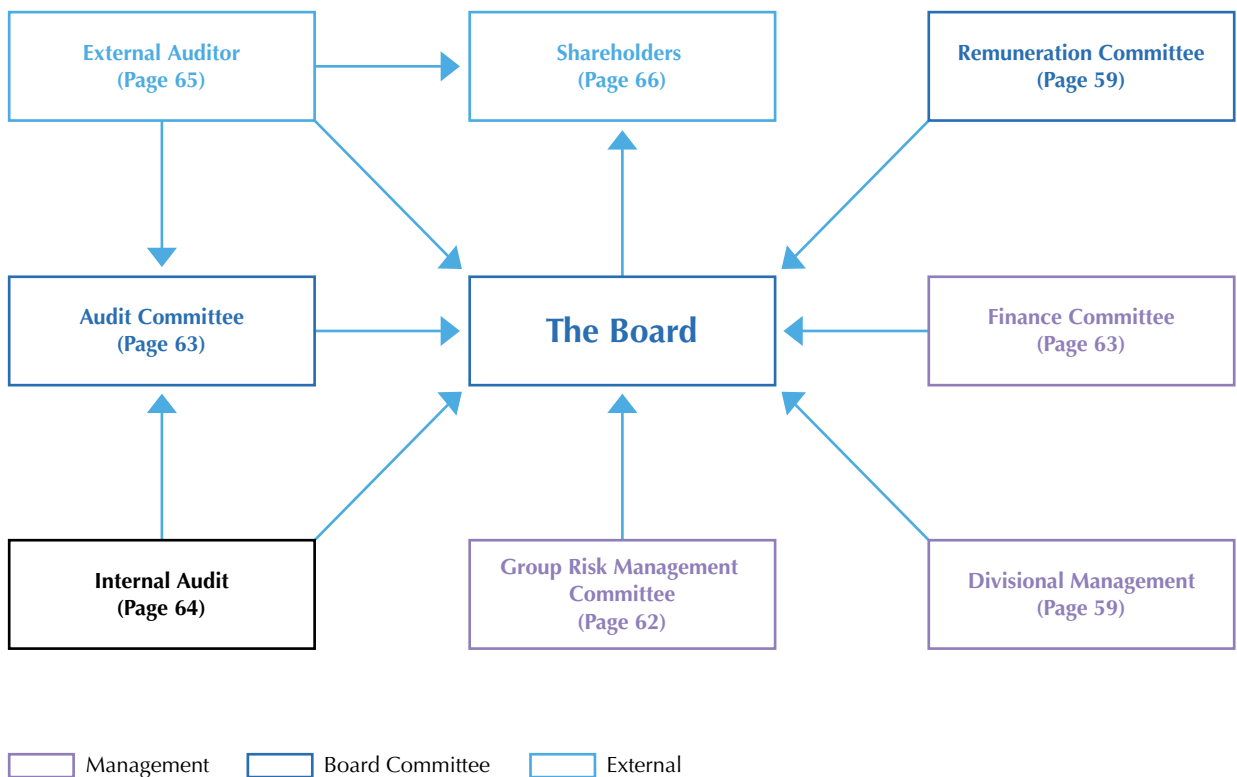
Swire Pacific is committed to ensure that its affairs are conducted in accordance with high ethical standards, something which we believe is a key component of our long-term success. This reflects our belief that in achieving our business objectives it is imperative that we act with high standards of probity, transparency and accountability.

By following this ethos we believe that shareholder wealth will be maximised in the long term and employees, business partners, and the communities in which we operate will all benefit.

Corporate governance is the process by which the Board instructs the group to conduct its affairs to ensure its strategies are fulfilled. The Board is committed to maintaining and developing robust corporate governance practices that help to ensure:

- satisfactory and sustainable returns to shareholders
- the interests of stakeholders are safeguarded
- overall business risk is understood and managed appropriately
- delivery of high-quality products and services to the satisfaction of customers
- high standards of ethics are maintained

The group's governance structure is outlined below:



Corporate Governance Statement

The Code on Corporate Governance Practices (“the CG Code”) as promulgated by The Stock Exchange of Hong Kong Limited sets out the principles of good corporate governance and provides two levels of recommendations:

- Code Provisions, with which issuers are expected to comply, but may choose to deviate from, provided they give considered reasons for non-compliance
- Recommended Best Practices, with which issuers are encouraged to comply, but which are provided for guidance only

Swire Pacific supports the principles-based approach of the CG Code and the flexibility this provides for the adoption of corporate policies and procedures in recognition of the individuality of companies, provided this is clearly explained. Swire Pacific has adopted its own code on corporate governance practices which is available from the group’s website www.swirepacific.com.

Corporate governance does not stand still; it evolves with our businesses and their operating environments. We are always open to learn and adopt best practices. As part of its commitment to enhance corporate governance standards within the region, Swire Pacific is a member of the Asian Corporate Governance Association.

Swire Pacific has complied throughout the year with all the Provisions of the CG Code as set out in Appendix 14 to the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited (“Listing Rules”). Additionally we have considered the recommended best practices and complied with all such points with the following exceptions which we believe do not benefit our stakeholders:

- **Section C.1.4 of the CG Code recommending the production of quarterly statements.** The Company has chosen not to comply with this recommended reporting practice because it is its judgement that, as a matter of principle and practice, quarterly reports would not bring significant overall benefits to our shareholders.

- **Section A.4.4 of the CG Code recommending the establishment of a nomination committee.** The Board has considered the merits of establishing a nomination committee as recommended but has concluded that it is most efficient and in the best interests of the Company, and potential new appointees, that they collectively review and approve the appointment of any new Director as this allows a more informed and balanced decision on suitability to be made by both the potential Director and the Board.

The Board of Directors

Role of the Board

Swire Pacific is governed by a Board of Directors, which has responsibility for the strategic leadership and control of the group to maximise shareholder value, whilst balancing the broad range of stakeholder interests. Directors are collectively responsible for promoting, and are committed to the success of, Swire Pacific by directing and supervising the group’s affairs.

Responsibility for delivering Swire Pacific’s objectives and running the business on a day-to-day basis is delegated to divisional management. The Board exercises a number of reserved powers which include:

- maintaining and promoting the culture of the Company
- formulation of long-term strategy
- approving public announcements including accounts
- committing to major acquisitions, divestments and capital projects
- authorising significant change of capital structure, material borrowings, such as all issues of Medium Term Notes and repurchase of the Perpetual instruments during the year, and any issue, or buy-back, of equity securities
- approving treasury policy
- setting the dividend policy
- approving appointments to the Board
- ensuring that appropriate management development and succession plans are in place
- setting the group remuneration policy
- approving the annual budget and forecasts
- reviewing operational and financial performance
- reviewing the effectiveness of internal control and risk management

To assist in fulfilling its duties, the Board has established two primary committees, the Audit Committee (see page 63) and the Remuneration Committee (see page 59).

Chairman and Chief Executive

The CG Code requires that the roles of Chairman and Chief Executive be separate and not performed by the same individual to ensure there is clear division of responsibilities between the running of the Board and the executives who run the business.

The Chairman is responsible for:

- leadership of the Board
- setting its agenda and taking into account any matters proposed by other Directors for inclusion in the agenda
- facilitating effective contribution and dialogue from all Directors and constructive relations between them
- ensuring all Directors are properly briefed on issues arising at Board meetings and that they receive accurate, timely and clear information
- obtaining consensus amongst the directors
- ensuring, through the Board, that good corporate governance practices and procedures are followed

Up to 31st January 2006, the Chairman of Swire Pacific was D M Turnbull who, following his resignation, was succeeded by C D Pratt on 1st February 2006.

Each division, or company therein, of the group has an Executive Director or Officer who is responsible for implementing the policies and strategies set by the Board in order to ensure the successful day-to-day management of the group's individual businesses. These executives are: K G Kerr (Properties), P N L Chen (Aviation), J R Slosar (Beverages), G L Cundle (Trading & Industrial, and Marine Services) and D Ho (Marine Services).

Throughout the year there was a clear division of responsibilities between the Chairman and management executives.

Board Composition

The Board is structured to ensure it is of a high calibre and has a balance of key skills and knowledge so that it works effectively as a team and precludes individuals or groups from dominating decisions.

The Board currently comprises the Chairman, five Executive Directors, and nine Non-Executive Directors. Their biographical details are set out on pages 67 to 68 of this report and are posted on the group's website www.swirepacific.com.

The Board considers that five of the nine Non-Executive Directors – being one third of the Board – are independent in character and judgement and fulfil the independence guidelines set out in Rule 3.13 of the Listing Rules. Confirmation has been received from each Independent Non-Executive Director that they are independent as set out in Rule 3.13 of the Listing Rules.

The Non-Executive Directors bring independent advice, judgement and, through constructive challenge, scrutiny of executives and review of performance, risks and people. Committees of the Board are made up only of Non-Executives.

The Independent Non-Executive Directors:

- provide open and objective challenge of management and Board members
- raise intelligent questions and challenge constructively and with vigour
- bring outside knowledge of the businesses and markets in which we operate, providing informed insight and responses to management

Although one of the Independent Non-Executive Directors, C Lee, has served in this capacity for more than nine years, the Directors are of the opinion that he remains independent, notwithstanding his length of tenure. C Lee continues to demonstrate the attributes of an Independent Non-Executive Director noted above and there is no evidence that his tenure has had any impact on his independence. The Board believes his detailed knowledge and experience of the group's business and his external experience continue to be of significant benefit to the Company, and that he maintains an independent view of its affairs.

Appointments, Re-election and Removal

Potential new Directors are identified and considered for appointment by the Board. A Director appointed by the Board is subject to election by shareholders at the first annual general meeting after his appointment and all Directors are subject to re-election by shareholders every three years.

Potential new Board members are identified based on skills and experience that, in the opinion of the Directors, will enable them to make a positive contribution to the performance of the Board.

The Board has considered the merits of establishing a nomination committee and concluded that it is most efficient and in the best interests of the Company and potential new appointees that the Board collectively reviews and approves the appointment of any new director as this allows a more informed and balanced decision on suitability to be made by both the potential director and the Board.

Full details of changes in the Board during the year are provided in the Directors' Report on page 70.

Responsibilities of Directors

On appointment, Directors undertake an induction programme at which time they receive information about the group including:

- the role of the Board and the matters reserved for its attention
- the role and terms of Board Committees
- the group's corporate governance practices and procedures
- the powers delegated to management
- the latest financial information

Directors update their skills, knowledge and familiarity with the group through their ongoing participation at meetings of the Board and its committees and through regular meetings with management at Head Office and in the divisions. Directors are regularly updated by the Company Secretary on their legal and other duties as Directors of a listed company.

Through the Company Secretary, Directors are able to obtain appropriate professional training or advice should this be required.

Each Director ensures that he or she can give sufficient time and attention to the affairs of the group. All Directors disclose to the Board on their first appointment their interests as a director or otherwise in other companies or organisations and such declarations of interests are updated annually.

Details of Directors' other appointments are shown in their biographies on page 67.

Board Processes

All committees of the Board follow the same processes as the full Board.

The dates of the 2006 Board meetings were determined in 2005 and any amendments to this schedule were notified to Directors at least 14 days before regular meetings. Suitable arrangements are in place to allow Directors to include items in the agenda for regular Board meetings.

The Board met six times in 2006. The attendance of individual Directors at meetings of the Board and its committees is set out in the table on page 58. Average attendance at Board meetings was 90%. All Directors attended Board meetings in person during the year.

Agendas and accompanying Board papers are circulated with sufficient time to allow the Directors to prepare before the Board or committee meeting.

The Chairman takes the lead to ensure that the Board acts in the best interests of Swire Pacific, that there is effective communication with the shareholders and that their views are communicated to the Board as a whole.

Board consents are given by vote at the Board meeting and supplemented via the circulation of written resolutions between Board meetings.

Minutes of Board meetings are taken by the Company Secretary and, together with any supporting papers, are available to all Directors. These record the matters considered by the Board, the decisions reached, and any concerns raised or dissenting views expressed by Directors. Draft and final versions of the minutes are sent to all Directors for their comment and record respectively.

Board meetings are structured to encourage open discussion and frank debate to ensure Directors actively participate in each meeting.

A typical Board meeting would consist of:

- review of a report by each Executive Director or Officer of the results since the last meeting and explanation of changes in the business environment and their impact on budgets and the longer-term plan. New initiatives and ideas are raised for open discussion
- presentation of papers to support decisions requiring Board approval
- an update of legal and compliance matters for Directors' consideration
- any declarations of interest

The executive management of individual businesses within the group provides the Board with such information and explanations necessary to enable them to make an informed assessment of the financial and other information put before the Board for approval. Queries raised by Directors are answered fully and promptly.

When necessary, the Independent Non-Executive Directors meet privately to discuss matters which are their specific responsibility. One such meeting was held in 2006.

The Chairman meets at least annually with the Non-Executive Directors without the Executive Directors being present.

Directors and Officers Insurance

Swire Pacific has arranged appropriate insurance cover in respect of potential legal actions against its Directors and Officers.

Conflict of Interest

If a substantial shareholder or a Director has a conflict of interest in a transaction or proposal to be considered by the Board and the Board has determined this interest to be material, the individual is required to declare his interest and to abstain from voting. The matter is considered at a Board meeting attended by Independent Non-Executive Directors who have no material interest in the transaction.

	Meetings Attended/Held			2006 Annual General Meeting
	Board	Audit Committee	Remuneration Committee	
Directors				
Executive Directors				
C D Pratt – Chairman (from 1st February 2006)	5/5			•
D M Turnbull – Chairman (up to 31st January 2006)	1/1			–
P N L Chen	6/6			•
M Cubbon	6/6			•
D Ho	6/6			•
K G Kerr	6/6			•
J R Slosar (from 12th May 2006)	3/3			–
Non-Executive Directors				
The Baroness Dunn	4/6			•
J W J Hughes-Hallett	6/6			•
P A Johansen	6/6	4/4	3/3	•
Sir Adrian Swire	4/6			•
Independent Non-Executive Directors				
V H C Cheng	4/6			•
C K M Kwok	5/6	4/4	3/3	•
C Lee	5/6	4/4	3/3	•
M C C Sze	6/6			•
M M T Yang	5/6			
Average attendance	90%	100%	100%	93%

Delegation by the Board

Responsibility for delivering Swire Pacific's strategies and objectives, established by the Board, and running each business on a day-to-day basis is delegated to management headed by an Executive Director or Officer. These individuals have been given clear guidelines and directions as to their powers and, in particular, the circumstances under which they should report back to the Board and obtain prior approval from the Board before making any commitments on behalf of Swire Pacific.

The Board monitors management's performance against the achievement of financial and non-financial measures, the principal measures being:

- monthly review of detailed management accounts consisting of profit and loss, balance sheets and cash flows compared against budget and forecast
- the output of both internal and external audit reports
- the occurrence of significant control breakdowns
- feedback from external parties such as customers, business partners, trade associations and other service providers

Securities Transactions

The Company has adopted a code of conduct ("the Securities Code") regarding securities transactions by Directors and Officers on terms no less exacting than the required standard set out in the Model Code for Securities Transactions by Directors of Listed Issuers contained in Appendix 10 of the Listing Rules. These rules are available on the group's website www.swirepacific.com.

A copy of the Securities Code is sent to each Director of the Company first on his appointment and thereafter twice annually, one month before the date of the Board meetings to approve the group's half-year and annual results, with a reminder that the Director cannot deal in the securities and derivatives of the Company until after such results have been published, and that all their dealings must be conducted in accordance with the Securities Code.

Under the Securities Code, Directors and Senior Executives of the Company are required to notify the Chairman and receive a dated written acknowledgement before dealing in the securities and derivatives of the Company, and, in the case of the Chairman himself, he must notify the Chairman of the Audit Committee and receive a dated written acknowledgement before any dealing.

All the Directors of the Company have confirmed that they have complied with the required standard set out in the Securities Code.

Directors' interests as at 31st December 2006 in the shares of the Company and its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance) are set out on page 71.

Remuneration of Directors and Executive Officers

Full details of Directors and Executive Officers remuneration are provided in note 8 of the accounts.

The Remuneration Committee comprises three Non-Executive Directors, two of whom – C K M Kwok and C Lee – are Independent Non-Executive Directors. The committee is chaired by P A Johansen.

The terms of reference of the Remuneration Committee have been reviewed with reference to the CG Code and are posted on the group's website www.swirepacific.com.

A Services Agreement exists between the Company and John Swire & Sons (H.K.) Limited ("Swire"), which has been considered in detail and approved by the Independent Non-Executive Directors of the Company. Under the terms of this agreement, staff at various levels, including Executive Directors, are seconded to the Company. These staff report to and take instructions from the Board of the Company but remain employees of the Swire group.

In order to be able to attract and retain international staff of suitable calibre, the Swire group provides a competitive remuneration package. This typically comprises salary, housing, provident fund, leave-passages and education allowances and, after three years' service, a bonus related to the profit of the overall Swire group. The provision of housing allowances affords ease of relocation, and payment of bonuses on a Swire group-wide basis enables postings to be made to group companies with different profitability profiles. Whilst bonuses are calculated by reference to the profits of the Swire group overall, the predominant part of such profits is derived from the Swire Pacific group.

Although the remuneration of these executives is not entirely linked to the profits of the business in which they are working, it is considered that, given the different profitability profiles of businesses within the Swire Pacific group, this has contributed considerably to the maintenance of a stable, motivated and high-calibre senior management team within the Company. Furthermore, as a substantial shareholder of Swire Pacific, it is in the best interest of Swire to see that executives of high quality are seconded to and retained within the Company.

The Remuneration Committee has reviewed this policy and the levels of remuneration paid to Executive Directors of the Company. At its meeting in November, the Committee considered a report prepared for it by Mercer Human Resource Consulting Limited, an independent firm of consultants, which confirmed that the remuneration of the Company's Executive Directors was in line with comparators in peer group companies. The Committee approved individual Directors' remuneration packages to be paid in respect of 2007.

No Director takes part in any discussion about his or her own remuneration.

The fees received by the Independent Non-Executive Directors were reviewed by the Remuneration Committee at its November meeting and compared to the fees paid at 32 other Hong Kong listed companies. The Committee proposed to increase the fees payable to the Chairmen of the Audit Committee and the

Remuneration Committee in recognition of their additional workload as committee chairmen. On the Committee's recommendation, the Board approved the following fee levels:

Fee	2006 HK\$	2007 HK\$
Director's Fee	200,000	200,000
Fee for Audit Committee Chairman	150,000	200,000
Fee for Audit Committee Member	150,000	150,000
Fee for Remuneration Committee Chairman	50,000	65,000
Fee for Remuneration Committee Member	50,000	50,000

Accountability and Audit

Financial Reporting

The Board acknowledges its responsibility for:

- the proper stewardship of Swire Pacific's affairs, to ensure the integrity of financial information
- preparing annual and interim accounts and other related information that give a true and fair view of the group's affairs and of the results and cash flows for the period, in accordance with Hong Kong Financial Reporting Standards and the Hong Kong Companies Ordinance
- selecting appropriate accounting policies and ensuring that these are consistently applied
- making judgements and estimates that are prudent and reasonable
- ensuring that the application of the going concern assumption is appropriate

Internal Controls

The Board acknowledges its responsibility to establish, maintain and review the effectiveness of the group's system of internal controls to ensure that shareholders' investments and Swire Pacific's assets are safeguarded. This responsibility is primarily fulfilled on its behalf by the Audit Committee as discussed on page 63.

The foundation for a strong system of internal control is a solid control environment. This is dependent on the ethics of the organisation, the quality and competence of its personnel, the direction provided by the Board, and the effectiveness of management.

Since profits are, in part, the reward for successful risk taking in business, the purpose of internal controls is to help manage and control, rather than eliminate, risk. Consequently internal controls can only provide reasonable, and not absolute, assurance against misstatement or loss.

The key components of the group's control structure are as follows:

Culture: The Board believes that good governance is fundamentally about the culture of an organisation which is more significant than any written procedures.

We aim at all times to act ethically and with integrity and to install this behaviour in all our employees by example from the Board down. During the year we introduced training courses on our Code of Conduct to emphasise its importance across the group.

Swire Pacific has a commitment to competence which is reflected in the rigorous selection process and career development plans for all employees. The organisation prides itself on being a long-term employer which instils in individuals, as they progress through the group, a thorough understanding of Swire Pacific's corporate philosophy.

Our channels of communication are open, allowing employees a means of communicating significant information upstream with a willingness on the part of more senior personnel to listen. Employees are aware that, whenever the unexpected occurs, attention should be given not only to the event itself, but also in determining the cause.

Through our Code of Conduct employees are encouraged and instructed on how to report control deficiencies or suspicion of impropriety to those who are in a position to take necessary action.

Risk assessment: The Board of Directors and the management each have responsibility to identify and analyse the risks underlying the achievement of business objectives, and to determine a basis for how such risks should be managed and mitigated.

There are two key management committees which monitor risk processes throughout the group; the Group Risk Management Committee ("GRMC") and the Finance Committee. These are primarily made up of senior management and both are chaired by the Group Finance Director who reports to the Board on matters of significance that arise.

The GRMC, discussed further on page 62, focuses on business, operational safety, security and reputational risks. The Finance Committee, discussed further on page 63, focuses on broad financial and treasury risk.

Management structure: The group has a clear organisational structure, that, to the extent required, delegates authority to manage the day-to-day responsibility for the design, documentation and implementation of procedures and ongoing monitoring of risk. Individuals appreciate where they will be held accountable in this process.

A Control Self Assessment process requires the management in each material business unit to assess, through use of detailed questionnaires, the adequacy and effectiveness of controls over the reliability of financial reporting, the effectiveness and efficiency of operations and compliance with applicable laws and regulations. This process and its results are reviewed by Internal Audit and form part of the Audit Committee's annual assessment of control effectiveness.

Controls & review: Control activities comprise a diverse range of policies and procedures that help to ensure that the relevant management directives are carried out and any actions that may be needed to address risks are taken. These may include approvals and verifications, reviews, safeguarding of assets and segregation of duties. Control activities can also be divided into operations, financial reporting and compliance, although there may, on occasions, be some overlap between them. The common control activities adopted by the group include the following:

- analytical reviews: for example, conducting reviews of actual performance versus budgets, forecasts, prior periods and competitors
- direct functional or activity management: reviews of performance reports, conducted by managers in charge of functions or activities
- information-processing: performing a variety of controls to check accuracy, completeness and authorisation of transactions, for example, exception reports
- physical controls: ensuring equipment, inventories, securities and other assets are safeguarded and subjected to periodic checks
- performance indicators: carrying out analyses of different sets of data, operational and financial, examining the relationships between them, and taking corrective action where necessary. By investigating unexpected results or unusual trends, management can identify circumstances where the underlying objectives are in danger of not being achieved
- segregation of duties: dividing and segregating duties amongst different people, to strengthen checks and minimise the risk of errors and abuse

Swire Pacific has in place effective processes and systems to identify, capture and report operational, financial, and compliance-related information in a form and time-frame that enables people to carry out their responsibilities.

Internal Audit: Independent of management, the Internal Audit function reports directly to the Chairman and performs regular reviews of key risk areas and monitors compliance with group accounting and financial procedures. The role of Internal Audit is discussed further on page 64.

Group Risk Management Committee

The GRMC coordinates the proper application of operational risk management procedures throughout the group.

The Committee focuses on business, operational, safety, security and reputational risks.

This Committee is chaired by the Group Finance Director and includes senior representatives from each operating division as well as the Group Risk Manager, Staff Director and Head of Internal Audit.

Two specialist sub-committees focus on insurance matters and loss prevention initiatives. The insurance sub-committee is chaired by the Group Finance Director and it reviews and approves the group's general insurance programmes. The loss prevention sub-committee is chaired by the Head of Corporate Safety, Cathay Pacific Airways Limited and its main focus is to promote effective loss prevention through the sharing of divisional best practices and regular reviews of the root causes of losses. The same sub-committee also oversees risk surveys conducted by third parties and closely monitors the implementation of risk mitigation recommendations derived from such surveys. Both sub-committees work closely with the group's risk management consultants and with the group's lead insurers and reinsurers.

In 2006, the GRMC and its sub-committees met five times.

Objectives

The Committee's aim is to continually strengthen the risk management culture throughout the group, by overseeing the development of risk management processes, identifying and sharing divisional best practices, monitoring divisional performance, promoting education and using group leverage to reduce the overall cost of risk.

During the year the key activities of GRMC were:

- overseeing the completion of an Enterprise Risk Management project to standardise the identification and assessment of the major risks facing the group's business units. This process has been undertaken at the operating unit level and was conducted with assistance from risk management consultants. Updated divisional and group-wide risk registers have been produced as a result of this project and these will be used to monitor risk profiles on an ongoing basis

- arranging 38 risk surveys at various locations in Hong Kong, Mainland China and the United States, with a focus on key operational risk exposures including employee safety, property, general liability, motor and legal risk management
- conducting a review of the group's Occupational Health and Safety policies in preparation for the implementation of enhanced and consistent safety standards across the group
- reviewing claims performance and the adoption of proactive claims management strategies, including an increased focus on the rehabilitation of injured staff
- developing an emergency portal and the testing of divisional response plans so as to enhance business continuity preparedness and mitigate the potential impact of infectious diseases and pandemics on the group's activities

Finance Committee

The Finance Committee consists of the Group Finance Director, four Divisional Finance Directors, the General Manager Corporate Finance, Treasurer and Group Finance Manager. It meets at least twice annually and additionally as specific matters arise, for example on issuing new debt securities.

Objective

Its aim is to develop company policy on all areas of finance, including financial risk and management of invested funds, and to develop the group's treasury policies. The group's approach to treasury risk is discussed on page 88.

Audit Committee

The Audit Committee, consisting of three Non-Executive Directors, C K M Kwok, C Lee and P A Johansen, assists the Board in discharging its responsibilities for corporate governance and financial reporting. Two of the committee are Independent Directors, one of whom, C K M Kwok, is Chairman. All the members served for the whole of 2006.

The terms of reference of the Audit Committee follow the guidelines set out by the Hong Kong Institute of Certified Public Accountants, and comply with the CG Code and are available on the group's website www.swirepacific.com.

The Audit Committee met four times in 2006. Regular attendees at the Audit Committee meetings are the Group Finance Director, the Head of Internal Audit and the external auditors. The Committee meets regularly with the external auditors without the presence of Company management. Each meeting receives written reports from the Group Risk Management Committee, external and internal auditors. Other attendees during the year included the independent property valuers and the Group Taxation Manager.

The work of the Committee during 2006 included review of the following matters:

- the completeness, accuracy and integrity of formal announcements relating to the group's performance including the 2005 annual and 2006 interim accounts and announcements, with recommendations to the Board for approval
- the group's compliance with regulatory and statutory requirements
- the group's internal controls and risk management systems and its compliance with the CG Code
- the group's risk management processes
- consideration of the adequacy of the group's procedures for staff to raise concerns where fraud is suspected
- the approval of the 2007 annual Internal Audit programme and review of progress on the 2006 programme
- periodic reports from Internal Audit and progress in resolving any matters identified therein
- significant accounting and audit issues
- Swire Pacific's policy regarding connected party transactions and the nature of such transactions
- overseeing and managing the relationship with external auditors as discussed on page 65

In 2007, the Committee has reviewed, and recommended to the Board for approval, the 2006 accounts.

Assessing the Effectiveness of Internal Controls

On behalf of the Board, the Audit Committee reviews annually the continued effectiveness of the group's assessment of risk and systems of internal controls over financial accounting and reporting, the effectiveness and efficiency of operations, and compliance with laws and regulations. This assessment considers:

- the scope and quality of management's ongoing monitoring of risks and of the systems of internal control, the work of its Internal Audit Function, and the assurances provided by the Group Finance Director
- the changes in the nature and extent of significant risks since the previous review and the group's ability to respond to changes in its business and external environment
- the extent and frequency with which the results of monitoring are communicated, enabling the Committee to build up a cumulative assessment of the state of control in the Company and the effectiveness with which risk is being managed
- the incidence of any significant control failings or weaknesses that have been identified at any time during the period and the extent to which they have resulted in unforeseen outcomes or contingencies that have had, could have had, or may in the future have, a material impact on the Company's financial performance or condition
- the effectiveness of the Company's processes in relation to financial reporting and statutory and regulatory compliance

The process used by the Audit Committee to review the effectiveness of the system of internal control includes:

- discussions with management on areas of risk identified
- the review of significant risks reported by the Internal Audit Department and Group Risk Management Committee
- the review of internal and external audit plans

- the review of significant issues arising from internal and external auditor reports
- the review of the results of management's Control Self Assessment exercise

As a result of the above review the Board confirms that the group's internal control systems are adequate and effective and have complied with the provisions of the CG Code through the year 2006 and to the date of this annual report.

Internal Audit Department

Swire Pacific has had an Internal Audit (IA) Department in place for many years which plays a critical role in monitoring the governance of the group. The department is staffed by 11 qualified audit professionals and conducts audits of Swire Pacific, its subsidiaries and certain associates.

IA has primary reporting lines to the Chairman of the Board and, without the need to consult with management, to the Chairman of the Audit Committee and via him to the Board. IA has unrestricted access to all areas of the group's business units, assets, records and personnel in the course of conducting its work.

The annual IA work plan and resources are reviewed and agreed with the Audit Committee.

Scope of Work

Business unit audits are designed to provide assurance that the internal control systems of Swire Pacific are designed and operating effectively, and that the risks associated with the achievement of business objectives are being managed properly.

The frequency of each audit is determined by IA using its own risk assessment methodology, considering such factors as recognised risks, overall materiality of each unit, previous IA results, external auditor comments, organisational change, output from the work of the Group Risk Management Committee and management's view. In any event each business would typically be audited at least every three years. New businesses in the group would be audited within six months of acquisition. 39 assignments were conducted in 2006.

IA specifically assists the Audit Committee in assessing the effectiveness of the group's internal controls through its review of the process by which management have completed the annual Control Self Assessment and the results thereof.

The department also conducts ad hoc projects and investigative work as may be required by management or the Audit Committee.

Audit Conclusion and Response

Copies of IA reports are sent to the Chairman, the Group Finance Director, and the external auditor. The results of each review are also presented to the Audit Committee.

Management is called upon to present action plans which are agreed in response to the department's recommendations and these are followed up to ensure that they are satisfactory resolved.

External Auditor

The Audit Committee acts as a point of independent contact, from management, with the external auditor ("the auditor"). The auditor has direct access to the Chairman of the Audit Committee, who meets with them periodically without management present.

The Audit Committee's duties in regard to the auditor include:

- recommending to the Board, for the approval by shareholders, the auditor's appointment
- approval of the auditor's terms of engagement
- consideration of the letter of representation provided by the Board to the auditor
- review of reports and other ad hoc papers from the auditor
- assessment of auditor's independence and objectivity, including the monitoring of non-audit services provided to ensure their independence and objectivity would not be, or be seen to be compromised
- approval of audit and non-audit fees

Quality and Effectiveness

The Audit Committee annually appraises the quality and effectiveness of the auditor. Prior to recommending the appointment of the auditor at the last AGM, four audit firms were invited to tender to complete the group audit. This process took approximately seven weeks and involved giving details of the group's businesses and access to management to the audit firms to allow an informed assessment and proposal for service to be made by them. On completion of this process the Audit Committee concluded that it was in the Company's best interest to maintain PricewaterhouseCoopers ("PwC") as auditor for 2006.

Auditor Independence

Independence of the auditor is of critical importance to the Audit Committee, Board and stakeholders. The Audit Committee assesses the independence of the auditor through a series of questions including seeking confirmation of any matters known by the auditor which may impinge on this and obtaining confirmation that their proposed audit fee provides them with what they consider a fair return for this service, irrespective of any additional work that they may provide. The Board also receives from PwC, in accordance with their professional ethics, formal confirmation that they consider themselves to be independent of Swire Pacific.

Provision of Non-audit Services

In deciding on whether the auditor should provide non-audit services the following key principles are considered:

- the auditor should not audit its own firm's work
- the auditor should not make management decisions
- the auditor's independence should not be impaired
- quality of service

The prior approval of the Audit Committee is obtained for any services provided by the auditor where the fee is likely to be in excess of HK\$1 million.

In addition, any services which may be considered to be in conflict with the role of the auditor must be submitted to the Audit Committee for approval prior to engagement, regardless of the amounts involved.

Fees paid to the external auditor are disclosed in note 6 to the accounts.

Shareholders

Communication with Shareholders and Investors

The Board and Senior Management recognise their responsibility to represent the interests of all shareholders and to maximise shareholder value. Communication with shareholders and accountability to shareholders is a high priority of the Company.

The principle methods we use to communicate with our shareholders are as follows:

- The Chairman is available to meet shareholders to ensure the Board understands and takes into consideration their views
- The Group Finance Director makes himself available on a day-to-day basis for contact with major shareholders, investors and analysts over a one month period immediately after announcement of interim and annual results. In 2006 he held 24 meetings with analysts and investors in Hong Kong, conducted two analyst briefings, two investor group briefings, four overseas roadshows, spoke at four investor conferences and was interviewed by Bloomberg and CNBC on two occasions
- Through publication of annual and interim accounts
- Through our AGM as discussed below
- Through the group's website. This includes electronic copies of financial reports, webcasts of analysts presentations given at the time of the final and interim results announcements, latest news, public announcements and general information about the group's businesses
- During the current year we have introduced, as part of our stakeholder dialogue exercise, interviews with shareholders and the investment community to understand specifically what their views are of Swire Pacific

The Annual General Meeting

The Annual General Meeting is an important forum to engage with shareholders. The most recent Annual General Meeting was held on 10th May 2006 at the Pacific Place Conference Centre, Level 5, One Pacific Place, 88 Queensway, Hong Kong. The meeting was open to all shareholders and members of the press. The Directors who attended the meeting are detailed in the table on page 58.

At the Annual General Meeting, separate resolutions were proposed for each issue and were voted on by poll. The significant items discussed were:

- the report of the Directors and the audited accounts for the year ended 31st December 2005
- declaration of final dividends
- re-electing Directors
- re-appointing the auditor and authorising the Directors to fix their remuneration
- an ordinary resolution giving Directors a general mandate to make on-market share repurchases
- to give Directors a general mandate to allot and issue shares up to 20% of the then issued share capital, provided that the aggregate nominal amount of the shares of any class so allotted wholly for cash shall not exceed 5% of the aggregate nominal amount of the share class then in issue

Minutes of the meeting together with voting results are available on the group's website, www.swirepacific.com.

Other Information for Shareholders

Key shareholder dates for 2007 are set out on the inside back cover of this report and on the group's website.

A list of analysts known to cover Swire Pacific is available from the group's website. This should not be considered an endorsement of the work or recommendation of these firms' work and reports.

From information publicly available to the Company and within the knowledge of its Directors, at least 25% of the Company's total issued share capital is held by the public at all times. Details of the shareholder profile of the Company are in the Directors' Report on page 73.