

As an important member of automotive industry in the PRC, Denway Motors Limited (the “Company”) endeavors to maintain its high standard of corporate governance, and continues to review and reinforce its corporate governance measures.

Denway Code on Corporate Governance

Code on Corporate Governance Practices (the “CG Code”) in Appendix 14 of the Rules Governing the Listing of Securities (the “Listing Rules”) on The Stock Exchange of Hong Kong Limited (the “Stock Exchange”) sets out the principles of good corporate governance, and two levels of recommendations: (a) code provisions; and (b) recommended best practices. A listed company may devise its own code on corporate governance practices on the terms it considers to be appropriate.

Model Code for Securities Transactions by Directors of Listed Issuers (the “Model Code”) in Appendix 10 of the Listing Rules sets a required standard against which directors must measure their conduct regarding transactions in securities of their listed companies. A listed company may adopt its own code on terms no less exacting than those set out in the Model Code.

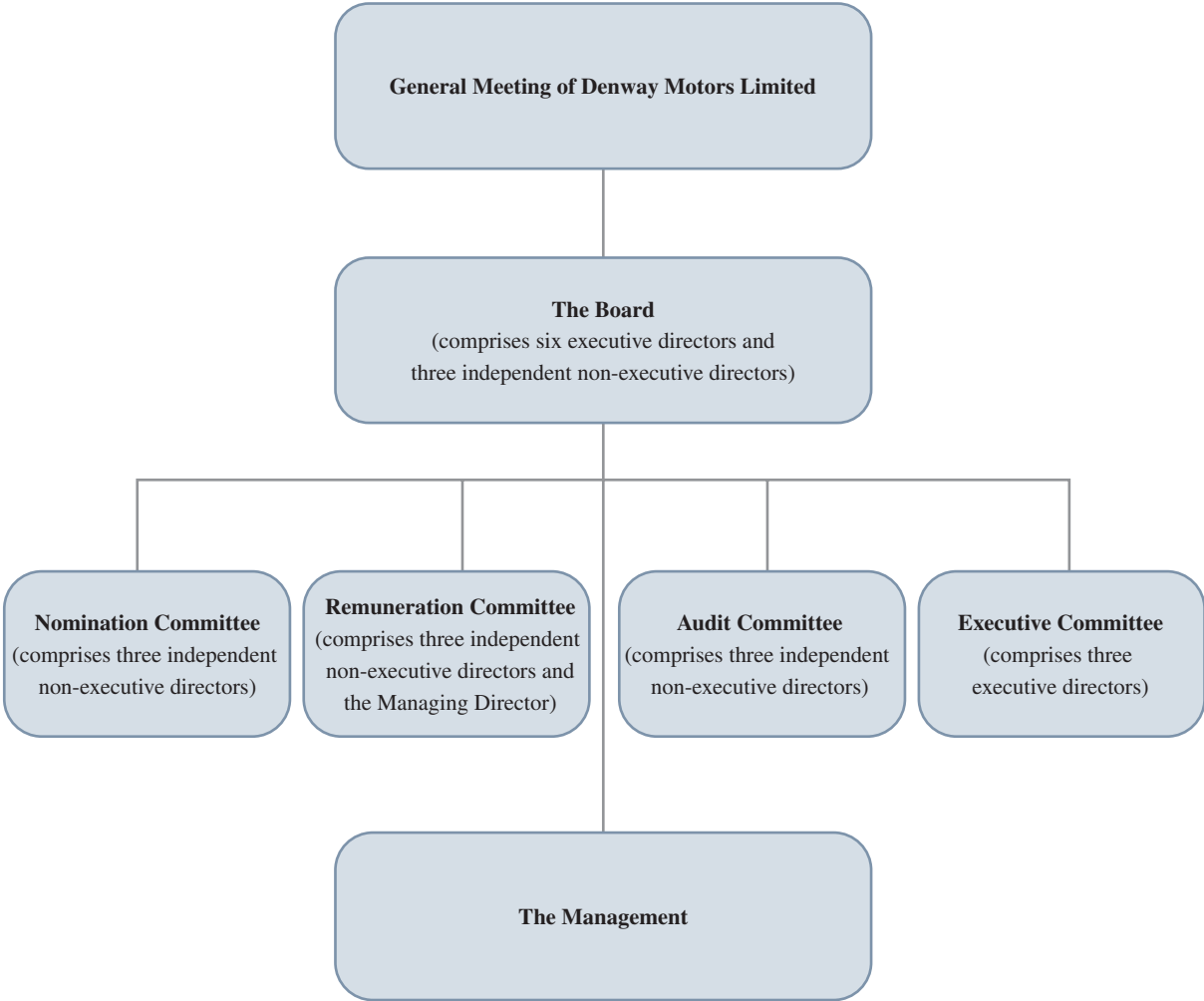
Since 2005, the Company has adopted its own Code on Corporate Governance (the “Denway Code”), which covers all mandatory code provisions of the CG Code and recommended best practices considered by the Board of Directors (the “Board”) as reasonable and appropriate as well as a set of model code for securities transactions by directors on term no less exacting than those set out in the Model Code. In fact, while implementing the Denway Code, the Company has exceeded the requirements of the CG Code in various aspects, which include:

- (1) Clearly establishing a corporate governance framework, which covers the relationship and responsibilities of external and internal relevant parties;
- (2) Including shareholders’ rights that set out in the Principles of Corporate Governance published by the highly regarded Organisation for Economic Co-operation and Development;
- (3) Consistently complying with Denway Motors Limited’s Code of Conduct;
- (4) The Audit Committee and the Nomination Committee comprising only independent non-executive directors; and
- (5) Taking the lead to disclose the financial information of the jointly controlled entities held by the Group in the preliminary announcement of the result for the accounting year and the preliminary announcement of the interim result.

During 2006, the Company complied with all code provisions as set out in the CG Code except for a single deviation. According to code provision E.1.2 of the CG Code, the Chairman of the Board should attend the annual general meeting. Due to an unexpected business commitment, Mr. Zhang Fangyou, the Chairman of the Board, was unable to attend the annual general meeting of the Company (the “AGM”) held on 6 June 2006. Mr. Lu Zhifeng, the Vice Chairman of the Board, was elected in accordance with the Company’s Articles of Association, to act as the chairman of the AGM and answered questions raised by shareholders together with the chairman of the Audit Committee, the Remuneration Committee and the Nomination Committee and other directors.

Denway Corporate Governance Structure

The Company’s corporate governance structure is as follows:



The Company is led by an efficient, high-caliber and responsible Board which ensures the Company and its subsidiaries (together the “Group”) maintain its high standard in corporate governance complemented by comprehensive internal control systems, so as to meet the requirements of the Group’s overall business development and enhance shareholder value.

Shareholders

Directors recognise that they are collectively responsible for the management and operations of the Company. By fulfilling their fiduciary duties and duties of skill, care and diligence, they represent the interests of the shareholders and enhance shareholder value.

Shareholders have the basic rights to:

- (1) Secure methods of ownership registration;
- (2) Convey or transfer shares;
- (3) Obtain relevant and important information of the Company in a timely manner and on a regular basis;
- (4) Participate and vote in general meetings;
- (5) Elect and remove directors; and
- (6) Share in the profits of the Company.

The Company has a policy of open communication and fair disclosure. Disclosure is a key mean to enhance corporate governance standards, in that it provides shareholders and other stakeholders with information necessary for them to form their own judgement and to provide feedback to the Company. Information relating to the Group's business review, future prospects and financial summary, are disclosed in the 2006 Annual Report and the Company's website at www.denway-motors.com.

The AGM is considered an annual precious event of the Company. The AGM provides an important opportunity for constructive communication between the Board and shareholders. Directors and senior management attend the AGM and answer questions raised by shareholders.

In 2006, in respect of each substantially separate issue at all general meetings, a separate resolution was proposed for the approval of shareholders.

All registered shareholders receive by notice of the AGM and special general meetings (together the “General Meetings”) by post. The notice of the General Meetings contains an agenda, resolutions proposed and a voting form. All registered shareholders, whose shares are registered in the register of members, are entitled to attend the General Meetings. Shareholders who cannot attend the General Meetings can appoint their proxies or the chairman of the General Meetings as their proxies by completing the proxy form enclosed with the notice of the General Meetings and returning it to the Company’s share registrar. Pursuant to the Company’s Articles of Association, every resolution shall be decided on a show of hands unless a poll is demanded in accordance with the Listing Rules, or by the Chairman or shareholders in accordance with the Listing Rules. Procedures for demanding a vote by poll have been set out in circulars dispatched to shareholders together with the notice of the General Meetings. The procedures are read out at the General Meetings by the chairman of the General Meetings.

The Company appoints the representative of its share registrar as scrutineer, ensuring that votes cast are properly counted and recorded. The chairman of the General Meetings declares to the meeting numbers of votes cast by attending shareholders and proxies in favour or against each resolution.

The Board

1. Board Composition

The Board comprises six executive directors, who possess rich experience in the PRC automotive industry, and three independent non-executive directors who possess appropriate professional qualifications. The names of the directors are as follows:

Executive directors

Mr. ZHANG Fangyou (*Chairman*)

Mr. LU Zhifeng (*Vice Chairman*)

Mr. YANG Dadong

Mr. ZENG Qinghong

Mr. ZHANG Baoqing (*Managing Director*)

Mr. DING Baoshan

Independent non-executive directors

Mr. CHEUNG Doi Shu

Mr. LEE Ka Lun

Mr. FUNG Ka Pun

Biographies for all directors (including the number and nature of their posts in public companies and other information related to material commitment information) are set out in the section headed “Directors and Senior Management’s Profiles” in this Annual Report.

There are no relationship, whether financial, business, family or other material/relevant aspects, between the directors.

During 2006, all corporate correspondences which set out the names of the directors expressly identified the identities of all independent non-executive directors. The independent non-executive directors possess appropriate professional qualifications, of which two have accounting and related financial management expertise. Each independent non-executive director confirmed to the Stock Exchange his independence in accordance with the requirements of the Listing Rules, and also submitted an annual confirmation to the Company confirming his independence during 2006.

2. The Operation of the Board

The Board assumes responsibility for leadership and control of the Company and is responsible for promoting the success of the Company by directing and supervising the Company’s affairs. All directors take decisions objectively in the interests of the Company and fulfill fiduciary duties.

The responsibilities of the Board include:

- (1) Establishing the strategic direction of the Company;
- (2) Setting the objectives of management;
- (3) Monitoring the performance of management;
- (4) Overseeing the management of the Company’s relationships with stakeholders;
- (5) Ensuring that a framework of prudent and effective controls is in place to enable risk to be assessed and managed; and
- (6) Setting the Company’s values and standards.

The Board establishes written procedures determining which issues require a decision of the full Board and which may be delegated to the board committee or management and the Company reviews such arrangements on a periodic basis.

Matters reserved to the full Board for decision include the setting of the strategic direction of the Group, any matters involving a conflict of interest for a substantial shareholder or a director, material acquisition and disposals of assets, investments, capital projects, authority levels, major treasury policies, risk management policies and key human resources issues.

When the Board delegates management and administrative functions to management, it gives clear directions on the powers of management with respect to the circumstances where management is to report back and obtain prior approval from the Board before making decisions or entering into any commitment on behalf of the Company.

The task of management and staff is the successful implementation of the strategies and directions as determined by the Board. In doing so, they apply business principles and ethics, which are consistent with those expected by shareholders, the Board and other stakeholders.

All directors actively participate in the Board meetings to discuss the overall strategies and business directions of the Group. During 2006, the Company held four regular and thirteen non-regular Board meetings. In each of the regular Board meetings, most of the directors who were entitled to attend the meetings attended in person.

In 2006, directors' attendance was as follows:

	No. of attendance <i>(Note)</i>
<i>Executive directors</i>	
Mr. ZHANG Fangyou (<i>Chairman</i>)	4
Mr. LU Zhifeng (<i>Vice Chairman</i>)	4
Mr. YANG Dadong	3
Mr. ZENG Qinghong	2
Mr. ZHANG Baoqing (<i>Managing Director</i>)	4
Mr. DING Baoshan	4
<i>Independent non-executive directors</i>	
Mr. CHEUNG Doi Shu	3
Mr. LEE Ka Lun	4
Mr. FUNG Ka Pun	3

Note: The above figures do not take into account of non-regular Board meetings. Directors who attended such meetings included Mr. Zhang Fangyou (10), Mr. Lu Zhifeng (5), Mr. Yang Dadong (6), Mr. Zeng Qinghong (9), Mr. Zhang Baoqing (13), Mr. Ding Baoshan (7), Mr. Cheung Doi Shu (3), Mr. Lee Ka Lun (3) and Mr. Fung Ka Pun (3).

The Board makes arrangements to provide opportunities for all directors to include proposed discussion issued in the agenda of regular Board meetings.

At least 14 days notice are given in respect of regular Board meetings. For all other Board meetings, reasonable notice are given.

Full agendas and accompanying Board papers are circulated to all directors at least 3 days before regular Board meetings. Draft versions of minutes are sent to all directors after regular Board meetings. After expressing opinions on the draft versions of minutes, final versions of minutes are sent to all directors for their records. The delivery of agendas and accompanying Board papers of other Board meetings complies with the above arrangement on a best effort basis.

Management provides the Board and Board committees with sufficient, adequate and timely information which are complete and reliable and which enable directors to make informed decisions on matters placed before them, and perform their duties and responsibilities as the Company's directors. Management provides adequate explanations and information to the Board as enable directors to make an informed assessment of the financial and other information put before them for approval. In addition, the Board and each director have separate and independent access to the Company's senior management.

Minutes of each Board meeting and Board committee meeting are kept by the company secretary (the "Company Secretary") and are available for inspection by any director. Minutes record in sufficient detail the matters considered by the Board and the decisions reached.

All directors have free access to the advice and services of the Company Secretary with a view to ensuring that Board procedures are followed and that applicable laws and regulations, including obligations on directors relating to disclosure of interests in securities, disclosure of any conflict of interest in a transaction involving the Company, prohibitions on dealing in securities and restrictions on disclosure of price-sensitive information, are complied with and on any matter relating to the application and implementation of Denway Code.

The Board adopts a system whereby the directors may seek independent professional advice in appropriate circumstances in the furtherance of their duties and for the associated fees to be borne by the Company.

If a substantial shareholder or a director has a conflict of interest in a matter to be considered by the Board which the Board has determined to be material, the matter will be dealt with by holding a Board meeting or a Board committee meeting set up for that purpose pursuant to a resolution passed in a Board meeting. In addition, only independent non-executive directors who, and whose associates, have no material interest in the transaction concerned will be present at such meeting. Any director concerned should declare his/her interest at or prior to the Board meeting or the Board committee meeting in question and consider withdrawal from the meeting when the matter is discussed. Directors concerned must abstain from voting on any Board resolution or Board committee resolution and will not be counted in the quorum.

The Company maintains a directors' and officers' liability insurance.

3. Responsibilities of directors

Directors recognise that they are collectively and individually responsible to all shareholders, as well as to the operations, business activities and developments of the Company, and they perform their duties in accordance with Denway Code. Independent non-executive directors have the same duties of care and fiduciary duties as executive directors.

Directors acknowledge their responsibility for preparing the accounts. Directors do not aware of material uncertainties relating to events or conditions that may cast significant doubt upon the Company's ability to continue as a going concern and present the accounts on a going concern basis. The relevant statement by the auditors about their reporting responsibilities set out in the section headed "Independent Auditor's Report" in this Annual Report.

In 2006, all directors gave sufficient time and attention to the affairs of the Company.

Although the Company did not appoint any new directors in 2006, it set out guidelines for newly appointed directors. Every newly appointed director of the Company should receive a comprehensive, formal and tailored induction on the first occasion of his/her appointment, to ensure that he/she has a proper understanding of the operations and business of the Company and that he/she is fully aware of his/her responsibilities under statute and common law, the Listing Rules, applicable legal requirements and other regulatory requirements and the business and governance policies of the Company.

Independent non-executive directors of the Company give the Board and other Board committees they are serving the benefit of their skills, expertise, varied backgrounds and qualifications through attending regular Board meetings and other Board committee meetings. The responsibilities of independent non-executive directors include:

- (1) Participating in Board meetings to bring an independent judgement on issues of strategy, policy, performance, accountability, resources, key appointments and standards of conduct;
- (2) Taking the lead where potential conflicts of interests are;
- (3) Serving on the Audit Committee, the Remuneration Committee, the Nomination Committee and other Board committees; and
- (4) Scrutinising the Company's performance in achieving agreed corporate goals and objectives, and monitoring the reporting of performance.

All independent non-executive directors attend Board meetings regularly and serve in the Audit Committee, the Remuneration Committee and the Nomination Committee.

In 2006, the Company arranged independent non-executive directors to visit the jointly controlled entities of the Company so that they gained insight into the latest development of the Company's business and formed an important component of a programme of continuous professional development.

Denway Code covers model code for securities transactions by directors on terms no less exacting than those set out in Appendix 10 "Model Code" of the Listing Rules on the Stock Exchange. Having made specific enquiries, all directors confirmed that they strictly complied with the Model Code and the model code for securities transactions by the directors stated in Denway Code throughout 2006. Relevant employees of the Company also complied with the relevant code throughout 2006.

The Company adopt a new staff handbook which, among other things, states clearly that, other than under specific circumstances, employees of the Company are prohibited to deal in stocks and related derivatives of the Company.

Directors' interests in the shares of the Company as at 31 December 2006 are disclosed in the section headed "Report of the Directors" in this Annual Report.

Directors' interests as at 31 December 2006 in any business that could or may compete with the business of the Group are disclosed in the section headed "Report of the Directors" in this Annual Report.

4. Appointment, re-election and removal of directors

The Company has a formal, considered and transparent procedure for the appointment of new directors to the board and has plans in place for orderly succession for appointments to the board.

The Company has the Nomination Committee. For further details, please refer to the section headed “Nomination Committee” in this report. The appointment of a new director is a matter for consideration by the Nomination Committee and decision by the full Board.

All directors appointed to fill a casual vacancy are subject to election by shareholders at the first general meeting after their appointment.

Every director is subject to retirement by rotation at least once every 3 years and is eligible for re-election. The names and biographical details of the directors who offer themselves for re-election in 2006 are contained in a circular to shareholders to assist them in making an informed decision on their election.

The term of service of all independent non-executive directors is one year (subject to renewal every year). They are also subject to retirement by rotation and re-election at least once every 3 years in accordance with the Company’s Articles of Association.

5. Chairman and Managing Director

The Chairman and the Managing Director (for the purpose of this report, the “Managing Director” has the same capacity as the “Chief Executive Officer” referred to in Appendix 23 of the Listing Rules) are two separate roles and are not performed by the same individual. Mr. ZHANG Fangyou, the Chairman, is responsible for managing the Board and Mr. ZHANG Baoqing, the Managing Director, is responsible for managing the Company’s business. The division of responsibilities between the Chairman and Managing Director is clearly established and set out in writing in Denway Code.

The responsibilities of the Chairman of the Board include:

- (1) Providing leadership for the Board;
- (2) Ensuring all directors are properly briefed on matters to be discussed at Board meetings;
- (3) Ensuring all directors receive adequate, complete and reliable information in a timely manner;
- (4) Ensuring that the Board works effectively, discharges its responsibilities and discusses all key issues in a timely manner;

- (5) Ensuring that, the Company Secretary settles and approves the agenda for Board meetings on Chairman's behalf, taking into account any matters proposed by the other directors for inclusion in the agenda;
- (6) Providing effective communication with shareholders and ensuring that views of shareholders are communicated to the Board as a whole;
- (7) Ensuring good corporate governance practices and procedures are in place;
- (8) Giving each director an opportunity to express his/her views at Board meetings, encouraging all directors to fully contribute to the Board's affairs and ensuring that the Board acts in the best interests of the Company; and
- (9) Facilitating the effective contribution of all directors, in particular independent non-executive directors, and building constructive relations between executive and independent non-executive directors.

The Managing Director is appointed by the Board. The responsibilities of the Managing Director include:

- (1) Providing leadership for the management;
- (2) Implementing and reporting to the Board on the Company's strategy;
- (3) Overseeing the realisation by the Company of the objectives set by the Board;
- (4) Providing all such information to the Board as is necessary to enable the Board to monitor the performance of management;
- (5) Leading the management of the Company's relationship with its stakeholders;
- (6) Putting in place programmes for management development and succession;
- (7) With the financial controller, establishing and maintaining proper internal controls and systems as well as disclosure controls and procedures; and
- (8) Discharging such duties and authority as may be delegated in writing to him/her by the Board.

Nomination Committee

The objectives of the Nomination Committee are to lead the process for Board appointments and for identifying and nominating for the approval of the Board, candidates for appointment to the Board.

The Nomination Committee was set up on 2 September 2005. It comprises three independent non-executive directors. The Nomination Committee is chaired by Mr. FUNG Ka Pun. The Nomination Committee is provided with sufficient resources to discharge its duties and is authorized by the Board to obtain independent legal or other professional advices.

The Nomination Committee held one committee meeting in 2006. During the meeting, the retirement by rotation and re-election of directors was discussed.

During 2006, there was no change to the composition of the Board and no resignation or removal of a director. The Nomination Committee recommended the re-election of Mr. LU Zhifeng, Mr. YANG Dadong and Mr. DING Baoshan as the Company's executive directors at the 2006 AGM.

For the forthcoming 2007 AGM, the Nomination Committee recommended the re-election of Mr. ZHANG Fangyou and Mr. ZENG Qinghong to be re-appointed as the Company's executive directors and Mr. CHEUNG Doi Shu to be re-appointed as the Company's independent non-executive director.

The Nomination Committee reported to the Board its conclusions and recommendations following each committee meeting.

In 2006, attendance of committee members of the Nomination Committee was as follows:

Nomination Committee members	No. of attendance
Mr. CHEUNG Doi Shu (<i>Independent non-executive director</i>)	1
Mr. LEE Ka Lun (<i>Independent non-executive director</i>)	1
Mr. FUNG Ka Pun (<i>Independent non-executive director</i>) (<i>Chairman of the Nomination Committee</i>)	1

The roles and functions of the Nomination Committee include:

- (1) Reviewing the structure, size and composition of the Board on a regular basis and making recommendations to the Board regarding any proposed changes;
- (2) Identifying individuals suitably qualified to become Board members and selecting or making recommendations to the Board on the selection of, individuals nominated for directorships;
- (3) Assessing the independence of independent non-executive directors;

- (4) Making recommendations to the Board on relevant matters relating to the appointment or re-appointment of directors and succession planning for directors; and
- (5) Considering other topics, as defined by the Board.

Terms of reference of the Nomination Committee have been published on the Company's website at www.denway-motors.com.

Remuneration Committee

The objectives of the Remuneration Committee are to discharge the Board's responsibilities relating to the compensation of the Company's directors and senior management, to oversee the administration of the Company's compensation plans and to prepare any report on executive compensation required by the applicable rules and regulations.

The Remuneration Committee was set up on 3 January 2005. It comprises three independent non-executive directors and the Managing Director. The Remuneration Committee is chaired by Mr. CHEUNG Doi Shu. The Remuneration Committee is provided with sufficient resources to discharge its duties and is authorized by the Board to obtain independent legal or other professional advices.

The Remuneration Committee held one committee meeting in 2006. During the meeting, the human resource scheme and the remuneration for directors and senior management were discussed.

Directors' fees and other emoluments paid to directors are disclosed on a named basis in the section headed "Notes to the Consolidated Financial Statements" in this Annual Report in accordance with the requirements of the Listing Rules.

The Remuneration Committee reported to the Board its conclusions and recommendations following each committee meeting.

In 2006, attendance of committee members of the Remuneration Committee was as follows:

Remuneration Committee members	No. of attendance
Mr. CHEUNG Doi Shu (<i>Independent non-executive director</i>) (<i>Chairman of the Remuneration Committee</i>)	1
Mr. LEE Ka Lun (<i>Independent non-executive director</i>)	1
Mr. FUNG Ka Pun (<i>Independent non-executive director</i>)	1
Mr. ZHANG Boqing (<i>Executive director and Managing Director</i>)	1

The roles and functions of the Remuneration Committee include:

- (1) Making recommendations to the Board on the policy and structure for all remuneration of directors, senior management and all other employee of the corporate office and on the establishment of a formal and transparent procedure for developing policy on such remuneration;
- (2) Determining the specific remuneration packages of all executive directors and senior management, and making recommendations to the Board of the remuneration of non-executive directors;
- (3) Reviewing and approving performance-based remuneration by reference to corporate goals and objectives resolved by the Board from time to time;
- (4) Reviewing and approving the compensation payable to executive directors and senior management in connection with any loss or termination of their office or appointment to ensure that such compensation is determined in accordance with relevant contractual terms;
- (5) Reviewing and approving compensation arrangements relating to dismissal or removal of directors for misconduct to ensure that such arrangements are determined in accordance with relevant contractual terms;
- (6) Ensuring that no director or any of his associates is involved in deciding his/her own remuneration;
- (7) Consulting the Managing Director about their proposals relating to the remuneration of other executive directors; and
- (8) Considering other topics, as defined by the Board.

Terms of reference of the Remuneration Committee have been published on the Company's website at www.denway-motors.com.

Audit Committee

The objectives of the Audit Committee are to review the financial statements on behalf of the Board, to create a climate of discipline, risk management awareness and control, to enable the independent non-executive directors sitting on the Board committees to contribute an independent judgement and play a positive role, to help the financial controller by providing a forum in which he/she can raise issues, to strengthen the position of the independent auditor by providing a channel of communication and forum for issues of concern, to provide a framework within which the independent auditor can assert his/her independence in the event of a dispute with management, to increase public confidence in the credibility and objectivity of financial statements and of the Board.

The Audit Committee was set up on 30 June 1999. It comprises three independent non-executive directors. The Audit Committee is chaired by Mr. LEE Ka Lun. The Audit Committee is provided with sufficient resources to discharge its duties and is authorized by the Board to obtain independent legal or other professional advices.

The Audit Committee held two committee meetings in 2006 and the independent auditor of the Company attended the committee meetings. During the meetings, the Audit Committee reviewed 2005 annual report and accounts and 2006 interim report, and review significant financial reporting judgements contained in them. Meanwhile, the Audit Committee discussed with the independent auditor and the management and reviewed the system of internal control and financial control matters.

The Audit Committee has reviewed the results of the Group for the year ended 31 December 2006.

In addition, the Audit Committee made recommendations to the Board on the re-appointment of the independent auditor, and approved the remuneration and terms of engagement of the independent auditor. Meanwhile, the Audit Committee reviewed and monitored the independent auditor's independence and objectivity and the effectiveness of the audit process, and to develop and implement policy on the engagement of the independent auditor to supply non-audit services.

The Audit Committee reported to the Board its conclusions and recommendations following each committee meeting.

For the year ended 31 December 2006, audit fee paid by the Company to PricewaterhouseCoopers (independent auditor of the Company) was HK\$2,540,000. Non-auditing fee paid amounted to HK\$276,290, representing HK\$150,990, HK\$45,300 and HK\$80,000 for non-auditing advice on disposal of a subsidiary, taxation services and other fees, respectively.

In 2006, attendance of committee members of the Audit Committee was as follows:

Audit Committee members	No. of attendance
Mr. CHEUNG Doi Shu (<i>Independent non-executive director</i>)	2
Mr. LEE Ka Lun (<i>Independent non-executive director</i>) (<i>Chairman of the Audit Committee</i>)	2
Mr. FUNG Ka Pun (<i>Independent non-executive director</i>)	2

The roles and functions of the Audit Committee include:

Relationship with the independent auditor

- (1) Being primarily responsible for making recommendation to the Board on the appointment, re-appointment and removal of the independent auditor, and approving the remuneration and terms of engagement of the independent auditor, and any questions of resignation or dismissal of that auditor;
- (2) Reviewing and monitoring the independent auditor's independence and objectivity and the effectiveness of the audit process in accordance with applicable standard, and discussing with the independent auditor the nature and scope of the audit and reporting obligations before the audit commences;
- (3) Developing and implementing policy on the engagement of the independent auditor to supply non-audit services.

Review of financial information

- (1) Monitoring integrity of financial statements of the Company and the Company's annual report and accounts, interim report, and reviewing significant financial reporting judgements contained in them;
- (2) Liaising with the Board, senior management and the Company's qualified accountant, and meeting, at least once a year, with the independent auditor; and
- (3) Considering any significant or unusual items that are, or may need to be, reflected in such reports and accounts and giving due consideration to any matters that have been raised by the Company's qualified accountant and the independent auditor.

Oversight of financial reporting system and internal control procedures

- (1) Reviewing the Company's financial controls, internal control and risk management systems;
- (2) Discussing with the management the system of internal control and ensuring that management has discharged its duty to have an effective internal control system;
- (3) Considering any findings of major investigations of internal control matters and management's response as delegated by the Board or on its own initiative;
- (4) Reviewing the Group's financial and accounting policies and practices;
- (5) Reviewing the independent auditor's management letter;

- (6) Ensuring that the Board will provide a timely response to the issues raised in the independent auditor's management letter;
- (7) Reporting to the Board on the matters set out in CG Code as required by the Stock Exchange; and
- (8) Considering other topics, as defined by the Board.

Terms of reference of the Audit Committee have been published on the Company's website at www.denway-motors.com.

Executive Committee

The objective of the Executive Committee is to oversee the day-to-day management of the Group, its jointly controlled entities and associates.

The Executive Committee was set up on 2 September 2005. It comprises three executive directors. The Executive Committee is provided with sufficient resources to discharge its duties and is authorized by the Board to obtain independent legal or other professional advices.

Internal Control

The Board is responsible for maintaining a sound and effective internal control system for the Group. The system is for the interests of the shareholders by protecting the shareholders' investment and the assets of the Group.

The Company's internal control system, which is based on the "Basic Structure for Internal Control and Risk Management" issued by the Hong Kong Institute of Certified Public Accountants in June 2005, is a set of procedures for providing reasonable guarantee, in a view to meet the following objectives:

- (1) Effectiveness and efficiencies of operations;
- (2) Reliability of financial reporting; and
- (3) Compliance with the applicable laws and regulations.

In 2006, the comprehensive internal control review activities for the Group undertaken by the Company include:

(1) Control Environment

Confirmed the Group has active and involved Board and other Board committees, high ethical values and strict staff conduct standards, effective human resources policies, as well as a sound organisational structure that has provided solid foundations, discipline and structure for the Company's control environment.

(2) Risk Assessment

Pursuant to the Group's development strategies and corporate goals, the Company identified and conducted a thorough risk assessment affecting the Group, including business risks, financial risks, compliance risks and operational and other risks. Based on the results of the risk assessment, the Company employed an independent adviser to conduct a detailed review in respect of areas of concern of the Group, so as to minimise the original risk to a level acceptable to and controllable by the Group. The Company is actively responding to the opinion of the independent adviser and carrying out follow-up actions and will furnish a detailed report to the Board.

(3) Control Activities

The Group carried out control activities comprising a diverse range of policies and procedures, include conducting reviews of actual performance versus budgets, reviewing of performance reports, checking information processing in transactions, performing physical controls, analysing performance indicators and dividing and segregating duties amongst different people.

(4) Information and Communication

Monitored and confirmed the Group establishes sound channels and communication systems for internal and external flows of information, which are effectively used, wherever appropriate, to identify, access and report relevant information on operational, financial and regulatory compliance. The Group's procedures and internal controls for the handling and dissemination of price sensitive information are in accordance with the Guide on Disclosure of Price-Sensitive Information published by the Stock Exchange in January 2002.

(5) Monitoring

The Company monitored the implementation of the Group's internal control system regularly and evaluated its performance quality on an ongoing basis to ensure the effective operation of internal controls.

In 2006, the Board conducted a review of the effectiveness of the system of internal control of the Group based on reports of the management and independent advisers. The review covered all material controls, including financial, operational and compliance controls and risk management functions.