

The Directors have pleasure in submitting to shareholders their annual report and the audited financial statements for the year ended 31 December 2006.

### Principal Activities

The Company acts as an investment holding company. Its subsidiaries are principally engaged in the investment in, and the operation and management of, gas pipeline infrastructure and the sale and distribution of piped and bottled gas in the People's Republic of China (the "PRC").

### Results and Appropriations

The results of the Group for the year ended 31 December 2006 are set out in the Consolidated Income Statement on page 70.

The Directors recommend the payment of a final dividend of HK\$7.75 cents (equivalent to approximately RMB7.79 cents) per share to the shareholders on the register of members on 29 May 2007. The total dividend amount is approximately RMB75,923,000, and the retention of the remaining profit for the year is approximately RMB303,694,000.

### Financial Summary

Details of the summary of the published financial information of the Group for the past eight years are set out on pages 18–19.

### Property, Plant and Equipment

During the year, the Group continued to expand its pipeline infrastructure and other related facilities. An aggregate of RMB1,859,561,000 has been incurred in acquiring property, plant and equipment.

During the year, the Group revaluated its properties, resulting in a revaluation surplus amounting to RMB4,023,000. This has been credited directly to the revaluation reserve.

Details of the movements during the year in property, plant and equipment of the Group are set out in Note 15 to the Financial Statements.

### Share Capital and Bonds

Details of movements during the year in the share capital and bonds of the Company are set out in Notes 34 and 37 to the Financial Statements respectively.

### Reserves

Details of movements during the year in the reserves of the Group are set out in Consolidated Statement of Changes in Equity on pages 73–74.

### Bank and Other Loans

Details of bank and other loans of the Group are set out in Note 33 to the Financial Statements.

### Charitable Donations

Charitable donations by the Group for 2006 amounted to RMB5,084,000 (2005: RMB698,000).

### Directors' Emoluments

Details of Directors' emoluments are set out in Note 11 to the Financial Statements.



## Directors

The Directors of the Company during the year and up to the date of this report are:

### Executive Directors:

Wang Yusuo (Chairman)  
Yang Yu (Chief Executive Officer)  
Chen Jiacheng  
Zhao Jinfeng  
Qiao Limin  
Yu Jianchao  
Cheung Yip Sang  
Cheng Chak Ngok

### Non-executive Directors:

Zhao Baoju  
Jin Yongsheng (re-designated as Non-executive Director on 5 June 2006)

### Independent non-executive Directors:

Wang Guangtian  
Yien Yu Yu, Catherine  
Kong Chung Kau

In accordance with Articles 116 of the Company's Articles of Association, Mr. Wang Yusuo, Mr. Qiao Limin, Mr. Cheng Chak Ngok, Ms. Zhao Baoju and Mr. Wang Guangtian retire by rotation and, being eligible, offer themselves for re-election.

As of 31 December 2006, none of the Directors had entered, or proposed to enter, into any service contract with any member of the Group which does not expire or is not determinable by the relevant member of the Group within one year without compensation (other than statutory compensation).

The Company has received an annual confirmation from each of the independent non-executive Directors as regards their independence to the Company, and each of the independent non-executive Directors is considered independent to the Company.

## Disclosure of Interests

### Directors' interests or short positions in shares and in share options

As at 31 December 2006, the interests and short positions of each Director of the Company in the shares, underlying shares and debentures of the Company and its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance ("SFO")) as recorded in the register required to be kept under section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange of Hong Kong Limited (the "Stock Exchange") pursuant to the Model Code for Securities Transactions by Directors of Listed Companies ("Model Code"), Appendix 10 to the Rules Governing the Listing of Securities ("Listing Rules") on the Stock Exchange, were as follows:

Name of Director	Capacity	Interests in shares			Total interests in shares	Interests in underlying shares pursuant to share options	Total aggregate interests in shares and underlying shares	Approximate percentage of the Company's total issued share capital
		Personal interests	Corporate interests	Family interests				
Mr. Wang Yusuo ("Mr. Wang")	Beneficial owner and interest of controlled corporation	2,594,000 (Note 2)	339,275,000 (Note 1)	–	341,869,000	700,000 (Note 3)	342,569,000	35.17%
Ms. Zhao Baoju ("Ms. Zhao")	Interest of spouse and interest of controlled corporation	–	339,275,000 (Note 1)	2,594,000 (Note 2)	341,869,000	700,000 (Note 3)	342,569,000	35.17%
Mr. Yang Yu	Beneficial owner	–	–	–	–	8,000,000	8,000,000	0.82%
Mr. Chen Jiacheng	Beneficial owner	–	–	–	–	6,500,000	6,500,000	0.67%
Mr. Zhao Jinfeng	Beneficial owner	–	–	–	–	6,500,000	6,500,000	0.67%
Mr. Qiao Limin	Beneficial owner	–	–	–	–	6,500,000	6,500,000	0.67%
Mr. Yu Jianchao	Beneficial owner	–	–	–	–	6,500,000	6,500,000	0.67%
Mr. Cheung Yip Sang	Beneficial owner	–	–	–	–	5,700,000	5,700,000	0.59%
Mr. Cheng Chak Ngok	Beneficial owner	–	–	–	–	800,000	800,000	0.08%

#### Notes:

- The two references to 339,275,000 shares relate to the same block of shares. Such shares are held by Xinao Group International Investment Limited ("XGII"), which is beneficially owned as to 50% by Mr. Wang and 50% by Ms. Zhao, the spouse of Mr. Wang.
- Ms. Zhao, being the spouse of Mr. Wang, is deemed to be interested in these shares held by Mr. Wang.
- Ms. Zhao, being the spouse of Mr. Wang, is deemed to be interested in these share options which were granted by the Company to Mr. Wang.

Details of the Directors' interests in share options granted by the Company are set out under the heading "Directors' rights to acquire shares".

Save as disclosed above, as at 31 December 2006, the register maintained by the Company pursuant to section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code recorded no other interests or short positions of the Directors in any shares, underlying shares or debentures of the Company or any associated corporation (within the meaning of Part XV of the SFO).



### Disclosure of Interests (continued)

#### Directors' rights to acquire shares

Pursuant to the Company's share option schemes, the Company has granted options on the Company's ordinary shares in favour of certain Directors, the details of which are as follows:

Name of Director	Date of grant	Exercise period (Note 1)	Exercise price (HK\$) (Note 2)	Number of shares subject to outstanding options as at 1 January 2006	Number of options granted during the year	Number of shares subject to outstanding options as at 31 December 2006	Approximate percentage of the Company's total issued share capital
Mr. Wang	14.02.2003	15.02.2005 – 14.02.2013	2.265	700,000 (Note 3)	–	700,000	0.07%
Ms. Zhao	14.02.2003	15.02.2005 – 14.02.2013	2.265	700,000 (Note 3)	–	700,000	0.07%
Mr. Yang Yu	14.02.2003	15.02.2005 – 14.02.2013	2.265	1,000,000		8,000,000	0.82%
	15.03.2006	16.09.2006 – 15.03.2016	6.650		3,500,000		
	15.03.2006	16.03.2008 – 15.03.2016	6.650		3,500,000		
Mr. Chen Jiacheng	15.03.2006	16.09.2006 – 15.03.2016	6.650	–	3,250,000	6,500,000	0.67%
	15.03.2006	16.03.2008 – 15.03.2016	6.650		3,250,000		
Mr. Zhao Jinfeng	15.03.2006	16.09.2006 – 15.03.2016	6.650	–	3,250,000	6,500,000	0.67%
	15.03.2006	16.03.2008 – 15.03.2016	6.650		3,250,000		
Mr. Qiao Limin	15.03.2006	16.09.2006 – 15.03.2016	6.650	–	3,250,000	6,500,000	0.67%
	15.03.2006	16.03.2008 – 15.03.2016	6.650		3,250,000		
Mr. Yu Jianchao	15.03.2006	16.09.2006 – 15.03.2016	6.650	–	3,250,000	6,500,000	0.67%
	15.03.2006	16.03.2008 – 15.03.2016	6.650		3,250,000		
Mr. Cheung Yip Sang	15.03.2006	16.09.2006 – 15.03.2016	6.650	–	2,850,000	5,700,000	0.59%
	15.03.2006	16.03.2008 – 15.03.2016	6.650		2,850,000		
Mr. Cheng Chak Ngok	15.03.2006	16.09.2006 – 15.03.2016	6.650	–	400,000	800,000	0.08%
	15.03.2006	16.03.2008 – 15.03.2016	6.650		400,000		
Total				1,700,000	39,500,000	41,200,000	

**Disclosure of Interests** (continued)**Directors' rights to acquire shares** (continued)

Notes:

1. The vesting period of the share options is from the date of the grant until the commencement of the exercise period.
2. The closing price of the shares immediately before the date on which the options were granted during the year was HK\$6.200.
3. Ms. Zhao, being the spouse of Mr. Wang, is deemed to be interested in these share options which were granted by the Company to Mr. Wang.

The fair value per share option is provided in Note 39 to the Financial Statements.

Save as disclosed above, at no time during the year was the Company or its subsidiaries a party to any arrangements to enable the Directors, their respective spouse or children under 18 years of age to acquire benefits by means of the acquisition of shares in, or debentures of the Company or any other body corporate.

**Substantial Shareholders**

As at 31 December 2006, the interests and short positions of every person, other than Directors of the Company, in the shares and underlying shares of the Company as recorded in the register required to be kept under section 336 of the SFO were as follows:

Name of shareholder	Capacity	Interests in shares			Total interests in shares	Interests in underlying shares pursuant to share options	Total aggregate interests in shares and underlying shares	Approximate percentage of the Company's total issued share capital
		Personal interests	Corporate interests	Family interests				
Mr. Wang	Beneficial owner and interest of controlled corporation	2,594,000 (Note 2)	339,275,000 (Note 1)	-	341,869,000	700,000 (Note 3)	342,569,000 <sup>(L)</sup>	35.17%
Ms. Zhao	Interest of spouse and interest of controlled corporation	-	339,275,000 (Note 1)	2,594,000 (Note 2)	341,869,000	700,000 (Note 3)	342,569,000 <sup>(L)</sup>	35.17%
Xinao Group International Investment Limited ("XGII")	Beneficial owner	-	339,275,000 (Note 1)	-	339,275,000	-	339,275,000 <sup>(L)</sup>	34.83%
Capital Research and Management Company	Investment manager	-	91,587,000	-	91,587,000	-	91,587,000 <sup>(L)</sup>	9.40%
Penta Investment Advisers Ltd.	Investment manager	-	56,451,768 (Note 4)	-	56,451,768	-	56,451,768 <sup>(L)</sup>	5.80%
Mr. John Zwaanstra	Interest of controlled corporation	-	56,451,768 (Note 4)	-	56,451,768	-	56,451,768 <sup>(L)</sup>	5.80%

Notes:

1. The three references to 339,275,000 shares relate to the same block of shares. Such shares are held by XGII, which is beneficially owned as to 50% by Mr. Wang and 50% by Ms. Zhao, the spouse of Mr. Wang.
2. Ms. Zhao, being the spouse of Mr. Wang, is deemed to be interested in these shares held by Mr. Wang.
3. Ms. Zhao, being the spouse of Mr. Wang, is deemed to be interested in these share options which were granted by the Company to Mr. Wang.
4. The two references to 56,451,768 shares relate to the same block of shares. Such shares are held by Penta Investment Advisers Ltd., which is 100% owned by Mr. John Zwaanstra, in the capacity of an investment manager.
5. (L) represents Long Position.

### Substantial Shareholders (continued)

Save as disclosed above, as at 31 December 2006, the register maintained by the Company pursuant to section 336 of the SFO recorded no other interests or short positions in shares and underlying shares of the Company. Save for the shareholders as disclosed herein, the Directors are not aware of any persons who, as at 31 December 2006, were entitled to exercise or control the exercise of 5% or more of the voting power at general meetings of the Company and were also, as a practicable matter, able to direct or influence the management of the Company.

### Share Option Scheme

The Company has adopted a share option scheme (the "2002 Scheme") pursuant to an ordinary resolution passed at an extraordinary general meeting of the Company held on 21 May 2002.

Details of the share option scheme are set out in Note 39 to the Financial Statements and the section headed "Directors' rights to acquire shares" in this report.

The following tables disclose details of the Company's share options held by the employees (including Directors) and movements in such holdings under the 2002 Scheme during the year:

Grantee	Date of grant	Exercise period (Note 1)	Exercise price (HK\$) (Note 2)	Number of shares subject to outstanding options as at 1 January 2006	Number of options granted during the year	Number of shares subject to outstanding options as at 31 December 2006	Approximate percentage of the Company's total issued share capital
Directors	14.02.2003	15.02.2005 – 14.02.2013	2.265	1,700,000		41,200,000	4.23%
	15.03.2006	16.09.2006 – 15.03.2016	6.650		19,750,000		
	15.03.2006	16.03.2008 – 15.03.2016	6.650		19,750,000		
Employees	15.03.2006	16.09.2006 – 15.03.2016	6.650		9,100,000	18,200,000	1.87%
	15.03.2006	16.03.2008 – 15.03.2016	6.650		9,100,000		
Total				1,700,000	57,700,000	59,400,000	6.10%

Notes:

- The vesting period of the share options is from the date of the grant until the commencement of the exercise period.
- The closing price of the shares immediately before the date on which the options were granted during the year was HK\$6.200.

No share option was lapsed or cancelled during the year.

The fair value per share option is provided in Note 39 to the Financial Statements.

### Directors' and Controlling Shareholders' Interests in Contracts and Connected Transactions

During the year, the Group has entered into the transactions and arrangements as described below with persons who are "connected" for the purposes of the Listing Rules:

#### Non-Exempt Continuing Connected Transactions

On 31 January 2005, those Wang Family Companies (note 1) being property management companies have entered into an agreement with the Group to provide the Group with property management services to the properties situated in the PRC occupied by the Group.

On 31 January and 1 April 2005, Langfang Xinao Gas Company Limited ("Langfang Xinao"), an indirect wholly-owned subsidiary of the Company, entered into a contract for a term of one year commencing from 1 January 2005 with Langfang Xinao Property Management Company Limited ("Langfang Property Management") (note 1), and two other contracts for a term of 2.75 years and 3 years, both commencing from 1 April 2005 with Xinao Group Elephant Club Hotel Company Limited ("Elephant Club") (note 1) respectively, which provide property management services to Langfang Xinao for three office buildings situated in Langfang City with service fees of RMB208,000, RMB1,167,000 and RMB300,000 per annum respectively.

On 30 September 2005, Langfang Xinao Gas Equipment Company Limited ("Langfang Equipment"), an indirect wholly-owned subsidiary of the Company, entered into a contract for a term of one year commencing from 1 October 2005 with Elephant Club, and a contract for a term of six months commencing from 1 October 2006 with Xinao Gaoke Services Management Company Limited ("Gaoke Services") (note 1). The annual service fee for each contract was RMB120,000, where property management service would be provided by Elephant Club and Gaoke Services respectively for Langfang Equipment's factory and office building situated in Langfang City.

On 31 January 2005, the Group and the Wang Family Companies entered into an agreement, whereby each of the Group and the Wang Family Companies has agreed to lease to each other certain properties owned by the Group and the Wang Family Companies respectively.

On 31 January 2005, Langfang Xinao leased a staff quarter situated in Langfang City to Xinao Group Company Limited ("XGCL") (note 1) and entered into a contract commencing from 1 January 2005 with an annual rental of RMB436,000.

On 31 January 2005, Langfang Xinao entered into a property leasing agreement with XGCL in relation to the leasing of the office building situated in Langfang City to XGCL. The annual rental is RMB1,039,000 plus a reimbursement of management fee of RMB363,000 per annum. The contract term is for three years commencing from 1 January 2005.

On 7 February 2005, Xinao Gas Investment Group Limited, a direct wholly-owned subsidiary of the Company, entered into a property leasing agreement with Enric Investment Group Limited ("Enric Investment") (note 1) in relation to the leasing of the office building situated in Hong Kong to Enric Investment. The annual rental is HK\$456,000 (RMB471,000) plus a reimbursement of management fee and other expenses of RMB98,000 in 2006. The contract term is for three years commencing from 1 February 2005.

On 31 January 2005, the Group and the Wang Family Companies entered into an agreement, whereby the Group has agreed to purchase and the Wang Family Companies have agreed to sell, in the ordinary course of its business, gas-related machinery and equipment manufactured by the Wang Family Companies (including but not limited to gas refuelling stations, gas refuelling daughter station trailers, storage tanks, compressed natural gas ("CNG") and liquefied natural gas ("LNG") trucks and compressors).

During the year, the subsidiaries of the Company, including Bengbu Xinao Gas Company Limited, Yantai Xinao Industry Company Limited, Zhuzhou Xinao Gas Company Limited ("Zhuzhou Xinao"), Lianyungang Xinao Gas Company Limited, Yantai Xinao Gas Company Limited, Yongkang Xinao Gas Company Limited, Haining Xinao Gas Development Company Limited ("Haining Gas Development"), Xiangtan Xinao Gas Company Limited, Xinao Gas Development Company Limited ("Xinao Gas Development"), Xinao Energy Logistics Company Limited, Kaifeng Xinao Gas Company Limited, Guigang Xinao Gas Company Limited, Rizhao Xinao Gas Company Limited ("Rizhao Xinao"), Chaohu Xinao Gas Development Company Limited, Yancheng Xinao Gas Company Limited, Shangqiu Xinao Gas Company Limited, Chuzhou Xinao Gas Company Limited, Changzhou Xinao Gas Engineering Company Limited, Hangzhou Xiaoshan Piped Gas Development Company Limited, Shijiazhuang Xinao Vehicle Gas Company Limited, Huaian Xinao Gas Company Limited ("Huaian Xinao"), Bengbu Xinao Gas Development Company Limited ("Benghu Gas Development"), Langfang Xinao, Xinxiang Xinao Gas Company Limited and Tongliao Xinao Gas Company Limited, purchased natural gas track trucks, pressure regulating and gas equipments from Shijiazhuang Enric Gas Machinery Company Limited ("Shijiazhuang Enric") (note 1), Enric (Bengbu) Compressor Company Limited ("Enric Bengbu") (note 1) and Enric (Langfang) Energy Equipment Integration Company Limited ("Enric Langfang") (note 1) in order to operate the distribution of natural gas and CNG vehicle refuelling station business. The total considerations of the contracts are RMB129,948,000.



## Directors' and Controlling Shareholders' Interests in Contracts and Connected Transactions *(continued)*

### Non-Exempt Continuing Connected Transactions *(continued)*

Pursuant to Rule 14A.38 of the Listing Rules, the board of Directors engaged the auditors of the Company to perform certain agreed upon procedures in respect of the continuing connected transactions of the Group. The auditors have reported their factual findings on these procedures to the board of Directors. The independent non-executive Directors have reviewed the continuing connected transactions and the report of the auditors and confirmed that, in their opinion:

1. The transactions have been entered into by the Group in the ordinary and usual course of business of the Group;
2. The transactions have been entered into on normal commercial terms, or where there are not sufficient comparable transactions to judge whether they are on normal commercial terms, on terms no less favourable to the Company than those available to or from independent third parties; and
3. The transactions have been entered into in accordance with the terms of the agreements governing such transactions and on terms that are fair and reasonable and in the interests of the shareholders of the Company as a whole.

### Non-Exempt Connected Transactions

On 15 February 2006, Xinao (China) Gas Investment Company Limited ("Xinao China") (a wholly-owned subsidiary of the Company) entered into a joint venture contract with XGCL and XGII (note 1) for the establishment of Xinneng Chemical Company Limited ("Xinneng Chemical"), a Sino-foreign equity joint venture company, in Erdos, Inner Mongolia, the PRC. Upon establishment, Xinneng Chemical would be owned by XGCL, XGII and Xinao China as to 45%, 40% and 15%, respectively. Both of the total investment and the registered capital of Xinneng Chemical would amount to US\$99,000,000 (equivalent to approximately HK\$772,200,000). The total commitment of the Group in Xinneng Chemical would amount to US\$14,850,000 (equivalent to approximately HK\$115,830,000), representing Xinao China's proportionate interest in the registered capital of Xinneng Chemical. The investment in Xinneng Chemical provides an opportunity for the Group to invest in the energy chemical industry, which is closely related to the existing business of the Group, and, more importantly, such investment enables the Group to secure a stable supply of an alternative and backup energy source which can substitute natural gas as an alternative supply to its customers without any impact on the Group's existing customers. Details of the transaction were disclosed in the Company's announcement dated 15 February 2006.

On 6 November 2006, Bengbu Gas Development, a 70%-owned subsidiary of the Company, as vendor entered into a disposal agreement with Xinneng Energy Limited ("Xinneng Energy") (note 1) as purchaser pursuant to which Bengbu Gas Development agreed to sell and Xinneng Energy agreed to purchase the dimethyl ether ("DME") business for consideration of RMB14,864,864 (equivalent to approximately HK\$14,293,000). After disposal, more capital and expertise would be injected for the expansions and developments of the DME business in order to render it more competitive. Considering that the principal businesses of Bengbu Gas Development are the sales of piped gas and bottled liquefied petroleum gas but not in DME-related business, and that Xinneng Energy has rich raw materials and technological expertise on DME production and already possesses a license to establish an annual 300,000-ton DME production project in Bengbu City, the management of the Group decided that in order to utilise its assets more efficiently, the DME Business should be transferred to Xinneng Energy, which is currently 15% indirectly owned by the Company, thereby still enabling the Group to retain part of the future earnings generated by the DME business, if any. Details of the transaction were disclosed in the Company's announcement dated 6 November 2006.

On 6 November 2006, Xinao China, a wholly-owned subsidiary of the Company, as purchaser entered into an acquisition agreement with Huaian City Urban Asset Operation Company Limited ("Huaian Asset") (note 2) as vendor pursuant to which Xinao China conditionally agreed to purchase and Huaian Asset conditionally agreed to sell the 20% equity interest in Huaian Xinao beneficially owned by Huaian Asset, being the entire equity interest held by Huaian Asset in Huaian Xinao for consideration of RMB27,800,600 (equivalent to approximately HK\$26,731,000). As at 6 November 2006, Huaian Xinao was an 80%-owned subsidiary of the Company. Upon the completion of the acquisition, the Group would consolidate and gain full control on Huaian Xinao and the Group's equity interests in Huaian Xinao would be increased from 80% to 100%, thereby increasing the Group's share of profit (if any) in Huaian Xinao by 20%. Huaian Xinao is now undergoing steady growth. Its piped natural gas source has commenced supply, which should bring in long term returns to Huaian Xinao. Details of the transactions were disclosed in the Company's announcement dated 6 November 2006.



## Directors' and Controlling Shareholders' Interests in Contracts and Connected Transactions (continued)

### Exempted Connected Transactions

During the year, Xinao Gas Development provided gas connection services to XGCL, Bengbu Xinao Property Company Limited ("Bengbu Property") (note 1), Langfang Xinao Property Development Company Limited ("Langfang Property") (note 1) and Langfang Xincheng Property Development Company Limited ("Langfang Xincheng Property") (note 1), with the contract sum of RMB413,000, RMB1,351,000, RMB711,000 and RMB7,000 respectively.

During the year, Zhuzhou Xinao paid rentals of properties to Zhuzhou City Urban Construction Investment and Operation Company Limited ("Zhuzhou Construction") (note 2) with the amount of RMB12,000, whilst Haining Xinao paid rentals of properties to Haining City Wantong Gas Company Limited ("Haining Wantong") (note 2) and Haining City Mintai Coal Gas Company Limited ("Haining Mintai") (note 2), with the amount of RMB50,000 and RMB120,000 respectively.

During the year, Xinao Gas Development purchased decoration service for a training centre from Langfang Xinao Construction and Installation Engineering Company Limited ("Langfang Construction") (note 1) for a consideration of RMB3,240,000.

During the year, the Group made a donation of RMB4,200,000 to Xinao Charity Fund (note 3).

During the year, Shantou Xinao Gas Company Limited and Zhanjiang Xinao paid pipeline construction fee to Shantou City Chenghai Gas Construction Company Limited ("Shantou Chenghai") (note 2) with amount of RMB329,000 and RMB649,000 respectively.

During the year, Xinao China, a wholly-owned subsidiary of the Company, as purchaser entered into an acquisition agreement with Rizhao Finance Bureau as vendor pursuant to which Xinao China conditionally agreed to purchase and Rizhao Finance Bureau conditionally agreed to sell the 100% equity interest in Rizhao Coal Gas Company ("Rizhao Coal Gas") (note 2) (which held 20% of Rizhao Xinao) beneficially owned by Rizhao Finance Bureau for consideration of RMB7,483,000 (equivalent to approximately HK\$7,518,000). Before the acquisition, Rizhao Xinao was an 80%-owned subsidiary of the Company. Upon the completion of the acquisition, the Group would consolidate and gain full control on Rizhao Xinao and the Group's equity interests in Rizhao Xinao would be increased from 80% to 100%, thereby increasing the Group's share of profit (if any) in Rizhao Xinao by 20%. Rizhao Xinao is now undergoing steady growth which should bring in long term returns to the Group.

#### Notes:

1. Wang Family Companies, including, among others, Langfang Property Management, Elephant Club, Gaoke Services, XGCL, Enric Investment, Shijiazhuang Enric, Enric Bengbu, Enric Langfang, XGII, Xinneng Energy, Bengbu Property, Langfang Property, Langfang Xincheng Property and Langfang Construction, are companies controlled (entitled to exercise, or control the exercise of 30% or more of the voting power at the general meeting of the relevant company) by Mr. Wang, the Chairman, an executive Director and a controlling shareholder of the Company, and/or his associates (including Ms. Zhao, a non-executive Director and a controlling shareholder of the Company and the spouse of Mr. Wang), thereby being connected persons of the Company.
2. Huaian Asset, Zhuzhou Construction, Haining Wantong, Haining Mintai, Shantou Chenghai and Rizhao Coal Gas, are each a minority equity interest holder of one or more non-wholly-owned subsidiary(ies) of the Company who is entitled to exercise, or control the exercise of, 10% or more of the voting power at any general meeting of such non wholly-owned subsidiary, thereby being connected persons of the Company.
3. Xinao Charity Fund is a non-profit-making organization, of which Mr. Wang is the legal representative and he has no beneficial interests on the donation.
4. Most subsidiaries, jointly-controlled entities and associates of the Company in the PRC, minority equity interest holders and related parties mentioned above have names in Chinese only, and the English names used here are for reference only.

In the opinion of the independent non-executive Directors, these transactions were carried out in the ordinary course of business of the Group and on normal commercial terms.

Other than as disclosed above, no other contracts of significance to which the Company, its ultimate holding company or its subsidiaries was a party and in which a Director or a controlling shareholder of the Company had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year.

### Post Balance Sheet Events

Details of significant events occurring after the balance sheet date are set out in Note 49 to the Financial Statements.



### Convertible Securities, Options, Warrants or Similar Rights

Other than the share options as set out in Directors' rights to acquire shares and Note 39 to the Financial Statements, the Company issued five-year convertible bonds ("CB" or "CBs") in an aggregate principal amount of HK\$550,000,000 on 15 November 2004. The CBs are zero coupon bonds; the issue price is 100% whereas the redemption price is 106.43%, which means that the effective interest rate is 1.25% per annum. The bondholders have the option to require the Company to redeem the CBs 2.5 years after the issue date. If the bondholders do not exercise the option of redemption, then they have to hold the CBs to maturity or exercise the conversion right during the conversion period. Bondholders can exercise the conversion right between 15 December 2004 and 15 November 2009 and convert the CBs into ordinary shares of HK\$0.10 each of the Company, and the Company has the option to issue share or pay cash in lieu of shares to such bondholders. The conversion price for each ordinary share at the issue date of the CBs was HK\$5.4375, which is subject to adjustment for events, if any, which may have diluting effects after the issue. If all the CBs are converted into shares, 101,145,000 ordinary shares of the Company will be issued. During the year, HK\$379,130,000 of CBs, representing 68.93% of the CBs issued, was converted into 69,725,039 ordinary shares of the Company. As of 31 December 2006, the accumulated CBs being converted were HK\$458,700,000, representing 83.40% of the CBs. If all the outstanding CBs are converted into shares, 16,790,804 ordinary shares of the Company will be issued, equivalent to 1.72% of the total issued share capital of the Company as at 31 December 2006.

Other than disclosed above, the Company had no other outstanding convertible securities, options, warrants or other similar rights as at 31 December 2006.

### Major Customers and Suppliers

For the year ended 31 December 2006, the aggregate amount of turnover and purchases attributable to the Group's five largest customers and suppliers respectively accounted for less than 30% of the Group's total turnover and purchases.

### Pre-Emptive Rights

There are no provisions for pre-emptive rights under the Company's Articles of Association, or the laws of the Cayman Islands, which would oblige the Company to offer new shares on a pro-rata basis to existing shareholders.

### Purchase, Sale or Redemption of Listed Securities

During the year, neither the Company nor any of its subsidiaries has purchased, sold or redeemed any of the Company's listed securities.

### Audit Committee

The Company established an Audit Committee on 28 March 2001. The Audit Committee has reviewed with management the accounting principles and practices adopted by the Group and discussed auditing, internal controls and financial reporting matters. Members of the Audit Committee are Mr. Wang Guangtian, Ms. Yien Yu Yu, Catherine and Mr. Kong Chung Kau, who are all independent non-executive Directors. The Audit Committee has reviewed the unaudited interim accounts and the audited annual accounts for 2006. Three Audit Committee meetings were held during the financial year.

### Remuneration Committee

The Company's Remuneration Committee was established on 31 December 2004 and is composed of one executive Director, namely, Mr. Yang Yu, and three independent non-executive Directors, namely, Mr. Wang Guangtian, Ms. Yien Yu Yu, Catherine and Mr. Kong Chung Kau. The Remuneration Committee's responsibilities include the review of the Company's policy for remuneration of Directors and senior management and determination of the remuneration packages of executive Directors and senior management including benefits in kind, pension rights and compensation payments.

### The Code on Corporate Governance Practices

To the knowledge of the Board, the Company has complied with the Code on Corporate Governance Practices ("Code") as set out in Appendix 14 of the Listing Rules throughout the year, and there have been no material deviations from the Code. Details of compliance are set out in the Corporate Governance Report on pages 47 to 68 of the Annual Report.

### The Model Code for Securities Transactions

The Company has adopted a code of conduct regarding Directors' securities transactions on terms no less exacting than the required standards set out in the Model Code set out in Appendix 10 to the Listing Rules. Specific enquiries have been made with all Directors who have confirmed that they have complied with the required standard set out in the Model Code and the code of conduct regarding Directors' securities transactions.

### Public Float

Based on the information that is publicly available to the Company and within the knowledge of the Directors, as at the date of this report, there is sufficient public float of not less than 25% of the Company's issued shares as required under the Listing Rules.

### Loan Agreements Imposing Specific Performance Obligations on Controlling Shareholders

According to the US\$25,000,000 Loan Agreement entered into by the Company and the subsequent amendment thereto, Mr. Wang Yusuo, the controlling shareholder of the Company, is required to retain at least 27% of the total issued share capital of the Company throughout the term of the loan agreement, which is 5 years from 18 May 2004. The Company issued 7 year bonds on 5 August 2005 and the terms and conditions of the bonds require Mr. Wang Yusuo, the controlling shareholder of the Company, to retain control over the Company throughout the term of the bonds. The total amount of the loan involved is US\$200,000,000 (equivalent to RMB1,614,040,000).

### Interests in Competitors

During the year, none of the Directors or the management shareholders of the Company or their respective associates had an interest in a business which competes or may compete with the business of the Group.

### Auditors

A resolution will be submitted to the annual general meeting to re-appoint Messrs. Deloitte Touche Tohmatsu as auditors of the Company.

On behalf of the Board

**WANG Yusuo**

*Chairman*

Hong Kong, 19 April 2007

