Notes to the Financial Statements

(Expressed in Hong Kong Dollars)

1. General Information

Hongkong Electric Holdings Limited (the "Company") is a limited company incorporated and domiciled in Hong Kong. The address of its registered office is 44 Kennedy Road, Hong Kong.

2. Significant Accounting Policies

(a) Statement of Compliance

These financial statements have been prepared in accordance with all applicable Hong Kong Financial Reporting Standards ("HKFRSs"), which collective term includes all applicable individual Hong Kong Financial Reporting Standards, Hong Kong Accounting Standards ("HKASs") and Interpretations issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA"), accounting principles generally accepted in Hong Kong and the requirements of the Hong Kong Companies Ordinance. These financial statements also comply with the applicable disclosure provisions of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited. A summary of the significant accounting policies adopted by the Group is set out below.

(b) Basis of Preparation of the Financial Statements

The consolidated financial statements for the year ended 31st December 2008 comprise the Company and its subsidiaries (together referred to as the "Group") and the Group's interest in associates and jointly controlled entities.

The measurement basis used in the preparation of the financial statements is the historical cost basis except as explained in the accounting policies set out below.

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

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

Judgements made by management in the application of HKFRSs that have significant effect on the financial statements and estimates with a significant risk of material adjustment in the next year are discussed in note 38.

(c) Basis of Consolidation

The Group financial statements incorporate the financial statements of Hongkong Electric Holdings Limited and all its subsidiaries made up to 31st December each year, together with the Group's share of the results for the year and the Group's share of the net assets at the balance sheet date of its associates and jointly controlled entities.

(d) Subsidiaries

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

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

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

(e) Associates and Jointly Controlled Entities

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

A jointly controlled entity is an entity which operates under a contractual arrangement between the Group or Company and other parties, where the contractual arrangement establishes that the Group or Company and one or more of the other parties share joint control over the economic activity of the entity.

An investment in an associate or a jointly controlled entity is accounted for in the consolidated financial statements under the equity method and is initially recorded at cost and adjusted thereafter for the post acquisition change in the Group's share of the associate's or the jointly controlled entity's net assets. The consolidated profit and loss account includes the Group's share of the post-acquisition, post-tax results of the associates and jointly controlled entities for the year, including any impairment loss on goodwill relating to the investments in associates and jointly controlled entities recognised for the year (see notes 2(f) and 2(l)).

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

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

Notes to the Financial Statements

(Expressed in Hong Kong Dollars)

2. Significant Accounting Policies (continued)

(f) Goodwill

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

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

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

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

(g) Other Investments in Debt and Equity Securities

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

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

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

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

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

(h) Derivative Financial Instruments

Derivative financial instruments are recognised initially at fair value. At each balance sheet date the fair value is remeasured. The gain or loss on remeasurement to fair value is charged immediately to profit or loss, except where the derivatives qualify for cash flow hedge accounting, in which case recognition of any resultant gain or loss depends on the nature of the item being hedged (see note 2(i)).

(i) Hedging

(i) Fair Value Hedges

Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recognised in profit or loss, along with any changes in the fair value of the hedged assets or liabilities that are attributable to the hedged risk.

(ii) Cash Flow Hedges

Where a derivative financial instrument is designated as a hedge of the variability in cash flows of a recognised asset or liability or a highly probable forecast transaction or the foreign currency risk of a committed future transaction, the effective portion of any gain or loss on remeasurement of the derivative financial instrument to fair value is recognised directly in equity. The ineffective portion of any gain or loss is recognised immediately in profit or loss.

If a hedge of a forecast transaction subsequently results in the recognition of a non-financial asset or non-financial liability, the associated gain or loss is removed from equity and included in the initial cost or other carrying amount of the non-financial asset or liability.

If a hedge of a forecast transaction subsequently results in the recognition of a financial asset or a financial liability, the associated gain or loss is removed from equity and recognised in profit or loss in the same period or periods during which the asset acquired or liability assumed affects profit or loss (such as when interest income or expense is recognised).

For cash flow hedges, other than those covered by the preceding two policy statements, the associated gain or loss is removed from equity and recognised in profit or loss in the same period or periods during which the hedged forecast transaction affects profit or loss.

When a hedging instrument expires or is sold, terminated or exercised, or the Group revokes designation of the hedge relationship but the hedge forecast transaction is still expected to occur, the cumulative gain or loss at that point remains in equity and is recognised in accordance with the above policy when the transaction occurs. If the hedged transaction is no longer expected to take place, the cumulative unrealised gain or loss recognised in equity is recognised immediately in profit or loss.

(j) Fixed Assets, Depreciation and Amortisation

(i) Fixed assets are stated in the balance sheet at cost less accumulated depreciation (see note 2(j)(vi)), amortisation (see note 2(k)) and impairment losses (see note 2(l)).

(ii) The cost of self-constructed items of property, plant and equipment includes the cost of materials, direct labour, the initial estimate, where relevant, of the costs of dismantling and removing the items and restoring the site on which they are located, and an appropriate proportion of production overheads and borrowing costs (see note 2(w)).

(iii) Subsequent expenditure relating to a fixed asset that has already been recognised is added to the carrying amount of the asset when it is probable that future economic benefits, in excess of the originally assessed standard of performance of the existing asset, will flow to the enterprise.
All other subsequent expenditure is recognised as an expense in the period in which it is incurred.

Notes to the Financial Statements

(Expressed in Hong Kong Dollars)

2. Significant Accounting Policies (continued)

(j) Fixed Assets, Depreciation and Amortisation (continued)

(iv) Gains or losses arising from the retirement or disposal of an item of fixed asset are determined as the difference between the net disposal proceeds and the carrying amount of the item and are recognised in profit or loss on the date of retirement or disposal.

(v) Leasehold land held for own use under operating leases is stated in the balance sheet at cost less accumulated amortisation (see note 2(k)) and impairment losses (see note 2(l)).

(vi) Depreciation is calculated to write off the cost of fixed assets less their estimated residual value, if any, using the straight-line method over their estimated useful lives as follows:

	Years
Cable tunnels	100
Buildings	60
Ash lagoon and gas pipeline	60
Transmission and distribution equipment, overhead lines and cables	60
Generating plant and machinery	35
Gas turbines and gas turbine combined cycle	30
Mechanical meters	30
Wind turbines	20
Electronic meters, microwave and optical fibre equipment and trunk radio system	15
Furniture and fixtures, sundry plant and equipment	10
Computers	5 to 10
Motor vehicles and marine craft	5 to 6
Workshop tools and office equipment	5

Both the useful life of an asset and its residual value, if any, are reviewed annually.

During the year, the expected useful lives of certain fixed assets were extended as a result of the annual review of estimated useful lives (see note 38(a)).

(k) Leased Assets and Operating Lease Charges

An arrangement, comprising a transaction or a series of transactions, is or contains a lease if the Group determines that the arrangement conveys a right to use a specific asset or assets for an agreed period of time in return for a payment or a series of payments. Such a determination is made based on an evaluation of the substance of the arrangement and is regardless of whether the arrangement takes the legal form of a lease.

Where the Group has the use of assets held under operating leases, payments made under the leases are charged to profit or loss in equal instalments over the accounting periods covered by the lease term, except where an alternative basis is more representative of the pattern of benefits to be derived from the leased asset.

The cost of acquiring land held under an operating lease is amortised on a straight-line basis over the period of the lease term.

(l) Impairment of Assets

(i) Impairment of Investments in Debt and Equity Securities and Other Receivables

Investments in debt and equity securities (other than investments in subsidiaries, associates and jointly controlled entities: see note 2(l)(ii)) and other current and non-current receivables that are stated at cost or amortised cost are reviewed at each balance sheet date to determine whether there is objective evidence of impairment. Objective evidence of impairment includes observable data that comes to the attention of the Group about one or more of the following loss events:

– significant financial difficulty of the debtor;

– a breach of contract, such as a default or delinquency in interest or principal payments;

– it becoming probable that the debtor will enter bankruptcy or other financial reorganisation;

– significant changes in the technological, market, economic or legal environment that have an adverse effect on the debtor; and

– a significant or prolonged decline in the fair value of an investment in an equity instrument below its cost.

If any such evidence exists, any impairment loss is determined and recognised as follows:

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

– For trade and other current receivables and other financial assets carried at amortised cost, the impairment loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition of the asset), where the effect of discounting is material. This assessment is made collectively where financial assets carried at amortised cost share similar risk characteristics, such as similar past due status, and have not been individually assessed as impaired. Future cash flows for financial assets which are assessed for impairment collectively are based on historical loss experience for assets with credit risk characteristics similar to the collective group.

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

Impairment losses are written off against the corresponding assets directly.

Notes to the Financial Statements

(Expressed in Hong Kong Dollars)

2. Significant Accounting Policies (continued)

(l) Impairment of Assets (continued)

(ii) Impairment of Other Assets

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

- fixed assets;
- pre-paid interests in leasehold land classified as being held under an operating lease;
- investments in subsidiaries, associates and jointly controlled entities; and
- goodwill.

If any such indication exists, the asset's recoverable amount is estimated. In addition, for goodwill, the recoverable amount is estimated annually whether or not there is any indication of impairment.

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

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

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

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

(iii) Interim Financial Reporting and Impairment

Under the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited, the Group is required to prepare an interim financial report in compliance with HKAS 34, Interim Financial Reporting, in respect of the first six months of the financial year. At the end of the interim period, the Group applies the same impairment testing, recognition and reversal criteria as it would at the end of the financial year (see notes 2(l)(i) and (ii)).

Impairment losses recognised in an interim period in respect of goodwill and available-for-sale equity securities carried at cost are not reversed in a subsequent period. This is the case even if no loss, or a smaller loss, would have been recognised had the impairment been assessed only at the end of the financial year to which the interim period relates.

(m) Inventories

Coal, stores, fuel oil and liquefied natural gas are valued at cost on a weighted average basis.

Cost comprises all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition. Cost of inventories recognised as an expense includes the write-off and all losses of inventories.

(n) Trade and Other Receivables

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

(o) Interest-bearing Borrowings

Interest-bearing borrowings are recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition, with the exception of fixed interest borrowings that are designated as hedged items in fair value hedges (see note 2(i)(i)), interest-bearing borrowings are stated at amortised cost with any difference between the amount initially recognised and redemption value being recognised in profit or loss over the period of the borrowings, together with any interest and fees payable, using the effective interest method.

For interest-bearing borrowings that are designated as hedged items in fair value hedges, fair value changes that are attributable to the hedged risk are recognised in profit or loss (see note 2(i)(i)).

(p) Trade and Other Payables

Trade and other payables are initially recognised at fair value. Except for financial guarantee liabilities measured in accordance with note 2(t)(i), trade and other payables are subsequently stated at amortised cost unless the effect of discounting would be immaterial, in which case they are stated at cost.

Notes to the Financial Statements

(Expressed in Hong Kong Dollars)

2. Significant Accounting Policies (continued)

(q) Cash and Cash Equivalents

Cash and cash equivalents comprise cash at bank and on hand, demand deposits with banks and other financial institutions and short-term, highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value, having been within three months of maturity at acquisition.

(r) Employee Benefits

(i) Short Term Employee Benefits

Salaries, annual bonuses, paid annual leave and the cost of non-monetary benefits are accrued in the year in which the associated services are rendered by employees. Where payment or settlement is deferred and the effect would be material, these amounts are stated at their present values.

(ii) Defined Benefit Retirement Schemes Obligations

The Group's net obligation in respect of defined benefit retirement schemes is calculated separately for each scheme by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods; that benefit is discounted to determine the present value and the fair value of any scheme assets is deducted. The discount rate is the yield at the balance sheet date of high quality corporate bonds that have maturity dates approximating the terms of the Group's obligations. The calculation is performed by a qualified actuary using the "Projected Unit Credit Method".

Where the calculation of the Group's net obligation results in a negative amount, the asset recognised is limited to the net total of any cumulative unrecognised past service costs and the present value of any future refunds from or reductions in future contributions to the defined benefit retirement schemes.

Any cumulative unrecognised actuarial gains or losses in respect of the defined benefit retirement schemes are recognised in full in the period in which they occur, outside profit or loss, in equity.

(iii) Contributions to Defined Contribution Retirement Schemes

Obligations for contributions to defined contribution retirement schemes, including contributions payable under the Hong Kong Mandatory Provident Fund Schemes Ordinance, are recognised as an expense in profit or loss as incurred.

(s) Income Tax

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

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

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

Apart from certain limited exceptions, all deferred tax liabilities and all deferred tax assets, to the extent that it is probable that future taxable profits will be available against which the asset can be utilised, are recognised.

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

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

Current tax balances and deferred tax balances, and movements therein, are presented separately from each other and are not offset.

(t) Financial Guarantees Issued, Provisions and Contingent Liabilities

(i) Financial Guarantees Issued

Financial guarantees are contracts that require the issuer (i.e. the guarantor) to make specified payments to reimburse the beneficiary of the guarantee (the "holder") for a loss the holder incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument.

Where the Group issues a financial guarantee, the fair value of the guarantee (being the transaction price, unless the fair value can otherwise be reliably estimated) is initially recognised as deferred income within trade and other payables. Where consideration is received or receivable for the issuance of the guarantee, the consideration is recognised in accordance with the Group's policies applicable to that category of asset. Where no such consideration is received or receivable, an immediate expense is recognised in profit or loss on initial recognition of any deferred income.

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

Notes to the Financial Statements

(Expressed in Hong Kong Dollars)

2. Significant Accounting Policies (continued)

(t) Financial Guarantees Issued, Provisions and Contingent Liabilities (continued)

(ii) Other Provisions and Contingent Liabilities

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

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

(u) Revenue Recognition

(i) Regulation of Earnings under the Scheme of Control

The earnings of a subsidiary, The Hongkong Electric Company, Limited ("HEC") are regulated by the Hong Kong SAR Government (the "Government") under a Scheme of Control ("SOC") which provides for a permitted level of earnings based principally on a return on HEC's capital investment in electricity generation, transmission and distribution assets (the "Permitted Return"). HEC is required to submit detailed financial plans for approval by the Government which project the key determinants of the Permitted Return HEC will be entitled to over the Financial Plan period.

The Government has approved the Financial Plan covering the period from 2004 to 2008. No further Government approval is required during this period unless a need for significant rate increases, over and above those set out in the Financial Plan, is identified during the Annual Review conducted with the Government under the terms of the SOC.

(ii) Fuel Clause Account

Under the SOC, any difference between the standard cost of fuel and the actual cost of fuel consumed is debited (or credited) to the Fuel Clause Account ("Fuel Clause Transfer").

Fuel Clause Surcharges (or Rebates) are charged (or given) to customers by adding to (or deducting from) the Basic Tariff rate to produce a Net Tariff rate payable by customers and are credited (or debited) to the Fuel Clause Account.

The balance on the Fuel Clause Account at the end of a financial year represents the difference between Fuel Clause Rebates (or Surcharges) and Fuel Clause Transfers during the year, together with any balance brought forward from the prior year and interest thereon based on prevailing market interest rates. Any debit balance is carried forward as a deferred receivable to be recovered from Fuel Clause Transfers or Fuel Clause Surcharges and any credit balance is carried forward as a deferred payable to be cleared by Fuel Clause Transfers or Fuel Clause Rebates.

Fuel Clause Rebates or Surcharges are utilised to smooth increases in Net Tariffs paid by customers. The impact of tariff smoothing is to reduce the Net Tariffs payable by customers in certain years and increase the Net Tariffs in other years. However, the tariff smoothing has no impact on HEC's total earnings and the related balance on the Fuel Clause Account is expected to be recovered by Fuel Clause Surcharges in excess of Fuel Clause Transfers. It has been agreed with the Government that any deficit balance outstanding at the end of 2008 will be carried forward and recovered under the new Scheme of Control regime effective from 1st January 2009. In accounting for income, Fuel Clause Account debit balances are therefore treated as deferred receivables in the balance sheet and not accounted for in profit or loss each year.

(iii) Income Recognition

Electricity income is recognised based on units of electricity consumed by customers during the year at Basic Tariff rates, which is the unit charge agreed with the Government during the Annual Tariff Review for each financial year.

Electricity-related income and technical service fees are recognised when the related services are rendered.

Dividend income from unlisted investments is recognised when the shareholders' right to receive payment is established.

Interest income is recognised on a time apportioned basis using the effective interest method.

(v) Translation of Foreign Currencies

Foreign currency transactions during the year are translated into Hong Kong dollars at the foreign exchange rates ruling at the transaction dates, or at contract rates if foreign currencies are fixed in supplier agreements or hedged by forward foreign exchange contracts. Monetary assets and liabilities denominated in foreign currencies are translated into Hong Kong dollars at the foreign exchange rates ruling at the balance sheet date.

Exchange gains and losses in respect of fixed assets under construction are, up to the date of commissioning, incorporated in the cost of the assets. All other exchange differences are dealt with in profit or loss.

Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the foreign exchange rates ruling at the transaction dates. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated using the foreign exchange rates ruling at the dates the fair value was determined.

The results of foreign operations are translated into Hong Kong dollars at the average exchange rates approximating the foreign exchange rates ruling at the dates of the transactions. Balance sheet items, including goodwill arising on consolidation of foreign operations acquired on or after 1st January 2005, are translated into Hong Kong dollars at the foreign exchange rates ruling at the balance sheet date. The resulting exchange differences are recognised directly in a separate component of equity. Goodwill arising on consolidation of a foreign operation acquired before 1st January 2005 is translated at the foreign exchange rate that applied at the date of acquisition of the foreign operation.

On disposal of a foreign operation, the cumulative amount of the exchange differences recognised in equity which relate to that foreign operation is included in the calculation of the profit or loss on disposal.

Notes to the Financial Statements

(Expressed in Hong Kong Dollars)

2. Significant Accounting Policies (continued)

(w) Borrowing Costs

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

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

(x) Related Parties

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

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

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

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

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

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

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

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

(y) Segment Reporting

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

In accordance with the Group's internal financial reporting, the Group has chosen business segment information as the primary reporting format and geographical segment information as the secondary reporting format for the purposes of these financial statements.

3. Changes in Accounting Policies

The HKICPA has issued a number of new and revised HKFRSs that are first effective for or available for early adoption in the current accounting period of the Group and the Company.

The adoption of these new and revised HKFRSs has no material impact on the financial statements for the years presented.

The Group has not applied any new standard or interpretation that is not yet effective for the current accounting period (see note 39).

4. Turnover

The principal activities of the Group are the generation and supply of electricity.

Group turnover represents the sales of electricity, other electricity-related income and engineering and consulting services fees. The amount of each significant category of revenue recognised during the year is analysed as follows:

	2008 $ million	2007 $ million
Sales of electricity	**12,704**	12,452
Concessionary discount on sales of electricity	**(6)**	(5)
Electricity-related income	**33**	31
Technical service fees	**42**	46
	12,773	12,524

5. Other Revenue and Other Net Income

	2008 $ million	2007 $ million
Interest income from financial assets not at fair value through profit or loss	**959**	1,039
Dividend income from unlisted available-for-sale equity securities	**7**	–
Curtailment (loss)/gain on defined benefit retirement scheme (see note 27)	**(24)**	422
Foreign exchange differences – loans and receivables	**35**	10
Net profit on sale of fixed assets	**1**	3
Sundry income	**42**	73
	1,020	1,547

6. Segment Information

(a) Business Segments

The Group's principal business segments are sales of electricity and infrastructure investments. Financial information about the Group's business segments is set out in Appendix 1(a) on page 109.

(b) Geographical Segments

The Group operates, through its subsidiaries, associates and jointly controlled entities, in two major geographical regions – Hong Kong and Australia. Financial information about the Group's operations by geographical region is set out in Appendix 1(b) on page 110.

Notes to the Financial Statements

(Expressed in Hong Kong Dollars)

7. Finance Costs

	2008 $ million	2007 $ million
Interest on overdrafts, bank loans and other borrowings repayable within five years	482	620
Interest on other borrowings repayable over five years	82	138
Less: Interest capitalised to fixed assets	(89)	(111)
Interest transferred to fuel cost	(12)	(13)
Total interest expense relating to financial liabilities not at fair value through profit or loss	463	634

Interest expenses have been capitalised at an average rate of approximately 3.1% p.a. (2007: 4.5% p.a.) for assets under construction.

8. Profit before Taxation

	2008 $ million	2007 $ million
Profit before taxation is shown after charging/(crediting):		
Depreciation	1,456	1,963
Amortisation of leasehold land	58	57
Costs of inventories	3,609	2,176
Write down of inventories	5	4
Staff costs	509	493
Operating lease charges – equipment	62	62
Fixed assets written off and profit or loss on disposal of fixed assets	24	19
Net loss/(gain) on cash flow hedging instruments transferred from equity		
– interest rate swaps	(2)	–
– forward foreign exchange contracts	5	–
Auditors' remuneration:		
Audit and audit related work		
– KPMG	4	4
– Other auditors	1	1
Non-audit work		
– KPMG	2	2
– Other auditors	5	3

The consolidated profit attributable to equity shareholders of the Company includes a profit of $6,987 million (2007: $7,552 million) which has been dealt with in the financial statements of the Company.

9. Income Tax

(a) Taxation in the consolidated profit and loss account represents:

	2008 $ million	2007 $ million
Current Tax – Hong Kong Profits Tax		
Provision for the year	963	1,300
Current Tax – Overseas		
Net (credit)/provision for the year	(17)	1
	946	1,301
Deferred Tax (see note 26(a))		
Origination and reversal of temporary differences	364	(5)
Effect of change in tax rate	(310)	–
	54	(5)
	1,000	1,296

In June 2008, the Government promulgated a decrease in the Profits Tax rate from 17.5% to 16.5% applicable to the Group as from the year ended 31st December 2008. This decrease is taken into account in the preparation of these financial statements. Accordingly, the provision for Hong Kong Profits Tax for 2008 has been provided at the rate of 16.5% (2007: 17.5%) based on the estimated assessable profits for the year and the opening balance of deferred tax has been re-estimated accordingly.

Overseas taxation has been provided for at the applicable rates on the estimated assessable profits for the year.

(b) Reconciliation between Tax Expense and Accounting Profit at Applicable Tax Rates:

	2008 $ million	2007 $ million
Profit before taxation	9,339	8,759
Notional tax on profit before taxation, calculated at the rates applicable to profits in the countries concerned	1,423	1,443
Tax effect of non-deductible expenses	34	4
Tax effect of non-taxable revenue	(147)	(151)
Effect on opening deferred tax balance resulting from a decrease in tax rate (see note 9 (a))	(310)	–
Actual tax expense	1,000	1,296

Notes to the Financial Statements

(Expressed in Hong Kong Dollars)

10. Directors' Emoluments and Senior Management Compensation

(a) Directors' Emoluments

Directors' emoluments comprise payments to Directors by the Company and its subsidiaries in connection with the management of the affairs of the Company and its subsidiaries. The emoluments of each of the Directors of the Company are as follows:

Name of Directors	Fees $ million	Basic Salaries, Allowances & Other Benefits $ million	Retirement Scheme Contributions $ million	Bonuses $ million	2008 Total Emoluments $ million	2007 Total Emoluments $ million
Executive Directors						
Canning Fok Kin-ning [4]	0.12	0.61	–	–	0.73	0.39
Chairman						
Tso Kai-sum	0.07	6.23	–	9.02	15.32	16.92
Group Managing Director						
Susan Chow Woo Mo-fong	0.07	0.09	–	–	0.16	0.10
Andrew John Hunter	0.07	0.09	–	–	0.16	0.15
Kam Hing-lam	0.07	0.06	–	–	0.13	0.12
Victor Li Tzar-kuoi	0.07	0.61	–	–	0.68	0.44
Neil Douglas McGee [1]	0.07	3.97	0.29	2.39	6.72	6.59
Group Finance Director						
Frank John Sixt	0.07	0.04	–	–	0.11	0.11
Wan Chi-tin	0.07	4.14	0.34	3.49	8.04	7.52
Director of Engineering (Planning and Development)						
Yuen Sui-see [7]	0.06	3.21	0.51	1.08	4.86	–
Director of Operations						
Non-executive Directors						
Ronald Joseph Arculli [3]	0.14	0.06	–	–	0.20	0.19
Francis Lee Lan-yee [6]	0.07	2.70	–	2.38	5.15	8.73
George Colin Magnus	0.07	0.03	–	–	0.10	0.09
Holger Kluge [2] [3]	0.14	–	–	–	0.14	0.14
Ralph Raymond Shea [2] [3] [4]	0.16	0.04	–	–	0.20	0.19
Wong Chung-hin [2] [3] [4]	0.16	0.09	–	–	0.25	0.25
Ewan Yee Lup-yuen [5]	–	–	–	–	–	0.10
Total for the year 2008	**1.48**	**21.97**	**1.14**	**18.36**	**42.95**	42.03
Total for the year 2007	1.49	20.58	0.69	19.27		42.03

Notes:

(1) During the year, Mr. Neil Douglas McGee received director's fees of THB255,000 from Ratchaburi Power Company, Limited, an associate of the Group. The director's fees were then paid back to the Company.

(2) Independent non-executive director.

(3) Member of the Audit Committee.

(4) Member of the Remuneration Committee.

(5) Resigned as a director with effect from 2nd January 2008.

(6) Re-designated from an Executive Director to a Non-executive Director in August 2008.

(7) Appointed as a director with effect from 1st March 2008.

(b) Senior Management Compensation

The five highest paid individuals of the Group included five directors (2007: four) whose total emoluments are shown above.

The emoluments of the other one individual who comprised the five highest paid individuals of the Group in 2007 included salaries and other benefits of $3.80 million and retirement scheme contributions of $0.39 million.

11. Scheme of Control Transfers

The financial operations of HEC, a wholly-owned subsidiary of the Company, are governed by the SOC agreed with the Government which provides for HEC to earn a Permitted Return (see note 2(u)(i)). Any difference between this Permitted Return and the SOC net revenue as calculated in accordance with the SOC must be transferred to/(from) a Development Fund from/(to) the profit and loss account of HEC. Where the SOC net revenue is less than the Permitted Return, the amount transferred from the Development Fund to the profit and loss account shall not exceed the balance of the Development Fund. In addition, 8% of the average balance of the Development Fund is transferred from the profit and loss account of HEC to a Rate Reduction Reserve, which is subsequently to be rebated to customers. Movements in the Development Fund and Rate Reduction Reserve are as follows:–

(a) Development Fund

	2008 $ million	2007 $ million
At 1st January	**14**	–
Transfer from the profit and loss account	**297**	14
At 31st December	**311**	14

(b) Rate Reduction Reserve

	2008 $ million	2007 $ million
At 1st January	**1**	–
Transfer from the profit and loss account	**13**	1
At 31st December	**14**	1

Notes to the Financial Statements

(Expressed in Hong Kong Dollars)

12. Dividends

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

	2008 $ million	2007 $ million
Interim dividend declared and paid of 62 cents per ordinary share (2007: 58 cents per ordinary share)	1,323	1,238
Final dividend proposed after the balance sheet date of $1.49 per ordinary share (2007: $1.43 per ordinary share)	3,180	3,052
	4,503	4,290

The final dividend proposed after the balance sheet date is based on 2,134,261,654 ordinary shares (2007: 2,134,261,654 ordinary shares), being the total number of issued shares at the year end. The final dividend proposed after the balance sheet date has not been recognised as a liability at the balance sheet date.

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

	2008 $ million	2007 $ million
Final dividend in respect of the previous financial year, approved and paid during the year: $1.43 per ordinary share (2007: $1.27 per ordinary share)	3,052	2,710

13. Earnings per Share

The calculation of earnings per share is based on the profit attributable to ordinary equity shareholders of the Company of $8,029 million (2007: $7,448 million) and 2,134,261,654 ordinary shares (2007: 2,134,261,654 ordinary shares) in issue throughout the year.

There were no dilutive potential ordinary shares in existence during the years ended 31st December 2008 and 2007.

14. Fixed Assets

$ million	Site Formation and Buildings	Plant, Machinery and Equipment	Assets under Construction	Sub-total	Interests in Leasehold Land Held for Own Use under Operating Leases	Total Fixed Assets
Cost:						
At 1st January 2007	13,373	51,431	2,355	67,159	2,811	69,970
Additions	5	285	1,454	1,744	3	1,747
Transfers between categories	54	1,132	(1,186)	–	–	–
Disposals	(3)	(120)	–	(123)	(1)	(124)
At 31st December 2007	13,429	52,728	2,623	68,780	2,813	71,593
At 1st January 2008	13,429	52,728	2,623	68,780	2,813	71,593
Additions	8	321	1,753	2,082	2	2,084
Transfers between categories	215	1,651	(1,866)	–	–	–
Disposals	–	(167)	–	(167)	–	(167)
At 31st December 2008	13,652	54,533	2,510	70,695	2,815	73,510
Accumulated Depreciation and Amortisation:						
At 1st January 2007	3,830	19,211	–	23,041	433	23,474
Written back on disposals	(1)	(82)	–	(83)	–	(83)
Charge for the year	364	1,723	–	2,087	57	2,144
At 31st December 2007	4,193	20,852	–	25,045	490	25,535
At 1st January 2008	4,193	20,852	–	25,045	490	25,535
Written back on disposals	–	(130)	–	(130)	–	(130)
Charge for the year	234	1,325	–	1,559	58	1,617
At 31st December 2008	4,427	22,047	–	26,474	548	27,022
Net Book Value:						
At 31st December 2008	9,225	32,486	2,510	44,221	2,267	46,488
At 31st December 2007	9,236	31,876	2,623	43,735	2,323	46,058

The above are mainly electricity-related fixed assets in respect of which financing costs capitalised during the year amounted to $89 million (2007: $111 million).

The Group's leasehold land at 31st December 2008 is held in Hong Kong and comprises long term and medium term leasehold land with carrying values of $45 million (2007: $50 million) and $2,222 million (2007: $2,273 million) respectively.

Depreciation charges for the year included $103 million (2007: $124 million), relating to assets utilised in development activities which has been capitalised.

Notes to the Financial Statements

(Expressed in Hong Kong Dollars)

15. Interest in Subsidiaries

	Company	
	2008	2007
	$ million	$ million
Unlisted shares, at cost	**2,776**	2,425
Loan capital (see note below)	**21,845**	21,845
Amounts due from subsidiaries	**10,088**	4,531
	34,709	28,801

Loan capital is paid to HEC. These interest free loans, defined as "Loan Capital" in the Scheme of Control Agreement effective 1st January 1994, are not repayable without the prior agreement of the Government.

The amounts due from subsidiaries are unsecured, interest free and have no fixed repayment terms.

Particulars of the principal subsidiaries are set out in Appendix 2 on page 111.

16. Interest in Associates

	Group	
	2008	2007
	$ million	$ million
Share of net assets	**4,600**	4,113
Loans to unlisted associates (see note below)	**5,165**	4,748
Amounts due from unlisted associates (see note below)	**156**	192
	9,921	9,053

The loans to unlisted associates are unsecured, interest bearing at rates ranging from 6.28% p.a. to 13.79% p.a. (2007: 6.28% p.a. to 13.79% p.a.) and not due within five years.

Included in the loans to unlisted associates are subordinated loans totalling $4,542 million (2007: $4,652 million). The rights in respect of these loans are subordinated to the rights of any other lenders to the associates and they are treated as part of the investment in the associates.

The amounts due from unlisted associates are unsecured, interest free and have no fixed repayment terms.

Neither the loans to unlisted associates nor the amounts due from unlisted associates are past due or impaired.

The shares of an associate owned by the Group were pledged as part of the security arrangement for project financing facilities made available to that associate. The carrying value of the associate as at 31st December 2008 was $552 million (2007: $281 million).

The financial guarantees issued by the Company in respect of banking facilities available to associates have been disclosed in note 34.

Particulars of the principal associates are set out in Appendix 3 on page 112.

Summarised Financial Information based on the unaudited Management Accounts of the associates is as follows:

	2008 $ million	2007 $ million
Assets	**87,333**	101,826
Liabilities	**(74,513)**	(84,739)
Equity	**12,820**	17,087
Revenues	**18,107**	17,618
Profit	**1,503**	1,579

17. Interest in Jointly Controlled Entities

	Group	
	2008 $ million	2007 $ million
Share of net assets	**159**	18

The financial guarantees issued by the Group in respect of banking facilities available to jointly controlled entities have been disclosed in note 34.

Particulars of the jointly controlled entities are set out in Appendix 4 on page 113.

Summarised Financial Information based on the unaudited Management Accounts of the jointly controlled entities is as follows:

	2008 $ million	2007 $ million
Assets	**1,053**	140
Liabilities	**(706)**	(100)
Equity	**347**	40
Revenues	**–**	–
Profit	**–**	–

18. Other Non-current Financial Assets

	Group	
	2008 $ million	2007 $ million
Unlisted available-for-sale equity securities, at cost	**66**	66

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(Expressed in Hong Kong Dollars)

19. Inventories

	Group	
	2008	2007
	$ million	$ million
Work in progress	**1**	3
Coal, fuel oil and liquefied natural gas	**375**	255
Stores and materials (see note below)	**283**	281
	659	539

Included in stores and materials is capital stock of $190 million (2007: $177 million) which was purchased for future capital projects.

20. Trade and Other Receivables

	Group		Company	
	2008	2007	**2008**	2007
	$ million	$ million	**$ million**	$ million
Trade debtors (see note below)	**670**	643	**–**	–
Other receivables	**444**	519	**30**	94
	1,114	1,162	**30**	94
Derivative financial instruments				
– held as cash flow/fair value hedging instruments	**2**	10	**–**	5
Deposits and prepayments	**31**	25	**3**	3
	1,147	1,197	**33**	102

All of the trade and other receivables are expected to be recovered within one year.

Other receivables include unbilled electricity charges of $390 million (2007: $354 million) to be received from electricity customers.

The ageing analysis of trade debtors that are neither individually nor collectively considered to be impaired are as follows:

	Group		Company	
	2008	2007	**2008**	2007
	$ million	$ million	**$ million**	$ million
Current	**625**	600	**–**	–
1 to 3 months overdue	**31**	32	**–**	–
More than 3 months overdue but less than 12 months overdue	**14**	11	**–**	–
Total trade debtors	**670**	643	**–**	–

Electricity bills issued to domestic, small industrial, commercial and miscellaneous customers for electricity supplies are due upon presentation whereas maximum demand customers are allowed a credit period of 16 working days. If settlements by maximum demand customers are received after the credit period, a surcharge of 5% can be added to the electricity bills.

Trade debtors for electricity charges that were neither past due nor impaired relate to a wide range of customers for whom there was no recent history of default.

Trade debtors for electricity charges that were past due but not impaired relate to a number of independent customers. HEC, a wholly-owned subsidiary, obtains sufficient collateral in the form of security deposits from customers (see note 31(a)) and the balances are considered to be fully recoverable.

The Group's trade debtors are individually assessed for impairment. Any impairment losses are written off against the trade debtors directly. No separate account is maintained for impairment losses.

21. Fuel Clause Account

The surcharge per unit for electricity sales was 10.5 cents from 1st January 2008 (2007: 5.9 cents). Movements on the Fuel Clause Account were as follows:

	Group	
	2008	2007
	$ million	$ million
At 1st January	**336**	566
Transfer to profit or loss	**1,802**	413
Surcharge during the year	**(1,140)**	(643)
At 31st December	**998**	336

This account, inclusive of interest, has been and will continue to be used to stabilise electricity tariffs (see note 2(u)(ii)).

The outstanding amount of Fuel Clause Account was neither past due nor impaired (see note 2(u)(ii)).

22. Bank Deposits and Cash

	Group		Company	
	2008	2007	**2008**	2007
	$ million	$ million	**$ million**	$ million
Deposits with banks and other financial institutions with three months or less to maturity when placed	**7,104**	8,070	**7,086**	8,052
Cash at bank and in hand	**31**	8	**6**	–
Cash and cash equivalents for the purpose of the cash flow statement	**7,135**	8,078		
Deposits with banks and other financial institutions with more than three months to maturity when placed	**1,827**	4,102	**1,827**	4,102
	8,962	12,180	**8,919**	12,154

Notes to the Financial Statements

(Expressed in Hong Kong Dollars)

23. Trade and Other Payables

	Group		Company	
	2008	2007	**2008**	2007
	$ million	$ million	**$ million**	$ million
Creditors measured at amortised cost (see note below)	**1,161**	1,068	**41**	43
Derivative financial instruments				
– held as cash flow/fair value hedging instruments	**12**	3	**2**	–
	1,173	1,071	**43**	43

All of the trade and other payables are expected to be settled within one year.

Creditors' ageing is analysed as follows:

	Group		Company	
	2008	2007	**2008**	2007
	$ million	$ million	**$ million**	$ million
Due within 1 month or on demand	**558**	474	**3**	11
Due after 1 month but within 3 months	**197**	240	**–**	–
Due after 3 months but within 12 months	**306**	321	**9**	6
	1,061	1,035	**12**	17
Other payables	**100**	33	**29**	26
	1,161	1,068	**41**	43

24. Non-current Interest-bearing Borrowings

	Group	
	2008	2007
	$ million	$ million
Bank loans	**8,241**	10,092
Current portion	**(1,687)**	(1,191)
	6,554	8,901
Hong Kong dollar notes (see note below)	**2,426**	3,403
Current portion	**–**	(1,000)
	2,426	2,403
Total	**8,980**	11,304

Hong Kong dollar fixed rate notes bear interest at rates between 4.13% p.a. to 4.55% p.a. (2007: 4.13% p.a. to 4.55% p.a.), while interest on floating rate notes is determined with reference to the Hong Kong Interbank Offered Rate. Details of the issuer of Hong Kong dollar notes are set out in Appendix 2 on page 111. None of the non-current interest-bearing borrowings is expected to be settled within one year. All the above borrowings are unsecured.

Some banking facilities of the Group are subject to the fulfilment of covenants relating to certain of the Group's balance sheet ratios, as are commonly found in lending arrangements with financial institutions. If the Group were to breach the covenants the drawn down facilities would become payable on demand. The Group regularly monitors its compliance with these covenants. Further details of the Group's management of liquidity risk are set out in note 31(b). As at 31st December 2008 none of the covenants relating to drawn down facilities had been breached.

These borrowings have final maturities extending up to 2016 and are repayable as follows:

	Bank Loans		Hong Kong Dollar Notes		Total	
$ million	**2008**	2007	**2008**	2007	**2008**	2007
Within 1 year	**1,687**	1,191	**–**	1,000	**1,687**	2,191
After 1 year but within 2 years	**–**	1,300	**–**	–	**–**	1,300
After 2 years but within 5 years	**6,554**	7,601	**529**	507	**7,083**	8,108
After 5 years	**–**	–	**1,897**	1,896	**1,897**	1,896
	8,241	10,092	**2,426**	3,403	**10,667**	13,495

25. Derivative Financial Instruments

	Group		Company	
	2008 $ million	2007 $ million	**2008 $ million**	2007 $ million
Derivative financial instruments used for hedging:				
Interest rate swaps	**(85)**	113	**–**	–
Foreign exchange forward contracts	**(6)**	9	**(2)**	5
Total	**(91)**	122	**(2)**	5
Current portion of derivative financial instruments (see notes 20 and 23)	**10**	(7)	**2**	(5)
	(81)	115	**–**	–
Represented by:				
Derivative financial instruments assets	**29**	122	**–**	–
Derivative financial instruments liabilities	**(110)**	(7)	**–**	–
	(81)	115	**–**	–

Notes to the Financial Statements

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26. Deferred Taxation

(a) Movements in deferred taxation during the year are as follows:

	Group		Company	
	2008 $ million	2007 $ million	2008 $ million	2007 $ million
At 1st January	(5,444)	(5,431)	–	1
(Charged)/credited to profit or loss (see note 9(a))	(54)	5	–	(1)
Credited/(charged) to reserves	30	(18)	–	–
At 31st December	(5,468)	(5,444)	–	–
Net deferred tax assets recognised in the Balance Sheet	11	–	–	–
Net deferred tax liabilities recognised in the Balance Sheet	(5,479)	(5,444)	–	–
At 31st December	(5,468)	(5,444)	–	–

(b) Major components of deferred tax assets/(liabilities) are set out below:

	Group		Company	
	2008 $ million	2007 $ million	2008 $ million	2007 $ million
Tax effects of:				
Depreciation allowances in excess of the related depreciation	(5,320)	(5,373)	–	–
Fuel Clause rebates	(164)	(59)	–	–
Others	16	(12)	–	–
	(5,468)	(5,444)	–	–

27. Employee Retirement Benefits

The Company and its principal subsidiaries offer three retirement schemes, two of which are defined benefit retirement schemes with the other being a defined contribution retirement scheme, which cover all permanent staff in the Group.

(a) Defined benefit retirement schemes ("the Schemes")

The Schemes are established under trust and are registered under the Hong Kong Occupational Retirement Schemes Ordinance. The assets of the Schemes are held independently of the Group's assets in separate trustee administered funds.

One of the Schemes provides retirement benefits based on the employee's final basic salary and length of service. The funding policy in respect of the scheme is based on valuations prepared periodically by independent professionally qualified actuaries at Watson Wyatt Hong Kong Limited. The policy for employer's contributions is to fund the scheme in accordance with the actuary's recommendations on an on-going basis. The most recent actuarial valuation of this scheme was carried out by the appointed actuary, represented by Mr. A. Wong, FSA, FCIA as at 1st January 2008. The principal actuarial assumptions used include a long term yield gap, which is the long term expected rate of investment return net of salary increase of 2.2% p.a., pension increase of 2.5% p.a., together with appropriate provisions for mortality rates, turnover and adjustments to reflect the short-term market expectation of salary increases. The valuation revealed that the assets of the scheme were sufficient to cover the aggregate vested liabilities as at the valuation date.

Retirement benefits under the other scheme are based on the returns of a portfolio of scheme assets with a minimum return guaranteed by the Group. As at 31st December 2008 scheme assets exceeded vested benefits and the scheme was fully funded.

Retirement scheme costs charged to profit or loss for the year ended 31st December 2008 were determined in accordance with HKAS 19 "Employee Benefits", under which the Schemes are required to be valued using the "Projected Unit Credit Method".

(i) The amounts recognised in the balance sheets are as follows:

	Group		Company	
	2008 $ million	2007 $ million	**2008 $ million**	2007 $ million
Present value of funded obligations	**(5,995)**	(4,510)	**(613)**	(464)
Fair value of assets of the Schemes	**4,458**	5,086	**349**	421
	(1,537)	576	**(264)**	(43)
Represented by:				
Employee retirement benefit assets	**–**	1,106	**–**	62
Employee retirement benefit liabilities	**(1,537)**	(530)	**(264)**	(105)
	(1,537)	576	**(264)**	(43)

The assets of the Schemes did not include ordinary shares issued by the Company for the years ended 31st December 2008 and 2007.

A portion of the above liability is expected to be settled after more than one year. However, it is not practicable to segregate this amount from the amounts payable in the next twelve months, as future contributions will also relate to future services rendered and future changes in actuarial assumptions and market conditions.

Notes to the Financial Statements

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27. Employee Retirement Benefits (continued)

(a) Defined benefit retirement schemes ("the Schemes") (continued)

(ii) Changes in present value of funded obligations are as follows:

	Group		Company	
	2008 **$ million**	2007 $ million	**2008** **$ million**	2007 $ million
At 1st January	**4,510**	4,410	**464**	438
Current service cost	**129**	162	**9**	10
Interest cost	**155**	173	**16**	17
Employee contributions paid to the Schemes	**28**	26	**2**	2
Actuarial losses	**1,401**	420	**145**	41
Benefits paid	**(252)**	(259)	**(24)**	(23)
Curtailment loss/(gain)	**24**	(422)	**1**	(21)
At 31st December	**5,995**	4,510	**613**	464

(iii) Changes in fair value of assets of the Schemes are as follows:

	Group		Company	
	2008 **$ million**	2007 $ million	**2008** **$ million**	2007 $ million
At 1st January	**5,086**	4,599	**421**	391
Expected return on assets of the Schemes	**225**	300	**22**	25
Actuarial (losses)/gains	**(686)**	387	**(76)**	23
Employer contributions paid to the Schemes	**57**	33	**4**	3
Employee contributions paid to the Schemes	**28**	26	**2**	2
Benefits paid	**(252)**	(259)	**(24)**	(23)
At 31st December	**4,458**	5,086	**349**	421

The Group expects to contribute $94 million to its defined benefit retirement schemes in 2009.

(iv) The expense/(income) recognised in profit or loss, prior to any capitalisation of employment costs attributable to fixed assets additions, is as follows:

	2008 $ million	2007 $ million
Current service cost	**129**	162
Interest cost	**155**	173
Expected return on assets of the Schemes	**(225)**	(300)
Curtailment loss/(gain) (see note below)	**24**	(422)
	83	(387)

A decision was made in December 2007 to restructure a defined benefit retirement scheme in 2008 which would lead to a decrease in the Group's defined benefit obligations. This event triggered a curtailment gain of $422 million for the year ended 31st December 2007. The curtailment gain was calculated based on the difference between the defined benefit obligations of the scheme before curtailment and the estimated amount of funds to be transferred to the new scheme attributable to the members' services. A curtailment loss of $24 million was recognised for the year ended 31st December 2008 upon completion of the restructuring as the final transfer value differed from the preliminary transfer value calculated in 2007.

The expense/(income) is recognised in the following line items in the consolidated profit and loss account:

	2008 $ million	2007 $ million
Direct costs	**36**	19
Other operating costs	**23**	16
Other revenue and other net income	**24**	(422)
	83	(387)

The actual return on assets of the Schemes (taking into account all changes in the fair value of the assets of the Schemes excluding contributions paid and received) was a net loss of $461 million (2007: net income of $687 million).

(v) The cumulative amount of actuarial gains and losses recognised in the statement of recognised income and expense is as follows:

	2008 $ million	2007 $ million
At 1st January	**151**	118
Actuarial losses recognised in the statement of recognised income and expense during the year	**2,087**	33
At 31st December	**2,238**	151

Notes to the Financial Statements

(Expressed in Hong Kong Dollars)

27. Employee Retirement Benefits (continued)

(a) Defined benefit retirement schemes ("the Schemes") (continued)

(vi) The major categories of assets of the Schemes as a percentage of total assets of the Schemes are as follows:

	2008	2007
Hong Kong equities	**3.7%**	17.4%
Europe equities	**6.6%**	13.0%
North America equities	**5.2%**	13.3%
Other Asia Pacific equities	**3.9%**	11.4%
Global bonds	**78.1%**	38.6%
Deposits, cash and others	**2.5%**	6.3%

(vii) The principal actuarial assumptions used at 31st December (expressed as a weighted average) are as follows:

	Group and Company	
	2008	2007
Discount rate	**1.2%**	3.4%
Expected rate of return on assets of the Schemes	**5.3% – 7.2%**	6.5% – 7.0%
Long term salary increase rate	**5.0%**	5.0%
Future pension increase rate	**2.5%**	2.5%

The expected long-term rate of return on assets of the Schemes is based on the portfolio as a whole and not on the sum of the returns on individual asset categories.

(viii) The amounts recognised in respect of defined benefit retirement schemes for the current and previous years are as follows:

	Group					**Company**				
$ million	**2008**	2007	2006	2005	2004	**2008**	2007	2006	2005	2004
Present value of funded obligations	**(5,995)**	(4,510)	(4,410)	(4,151)	(3,701)	**(613)**	(464)	(438)	(393)	(354)
Fair value of assets of the Schemes	**4,458**	5,086	4,599	3,986	3,639	**349**	421	391	337	312
(Deficit)/surplus	**(1,537)**	576	189	(165)	(62)	**(264)**	(43)	(47)	(56)	(42)
Experience adjustments on:										
Scheme liabilities	**21**	(26)	(45)	(8)	(26)	**(4)**	(8)	(26)	(10)	(18)
Scheme assets	**(686)**	387	447	67	148	**(76)**	23	49	13	14

(b) Defined Contribution Retirement Scheme

Since the introduction of the Hong Kong Mandatory Provident Fund Scheme ("the MPF Scheme") in December 2000, the Group has also participated in a master trust MPF Scheme operated by an independent service provider. All new recruits not previously covered by the defined benefit retirement schemes are enrolled in the MPF Scheme.

The MPF Scheme is a defined contribution retirement scheme with the employer and its employees each contributing to the plan in accordance with the relevant scheme rules. The MPF Scheme rules provide for voluntary contributions to be made by the employer calculated as a percentage of the employees' basic salaries. Forfeited contributions of $0.2 million have been received during the year (2007: $0.9 million).

	2008 $ million	2007 $ million
Expenses recognised in profit or loss	4	3

28. Share Capital

		Company	
	Number of Shares	2008 $ million	2007 $ million
Authorised:			
Ordinary shares of $1 each	3,300,000,000	3,300	3,300
Issued and fully paid:			
Ordinary shares of $1 each	2,134,261,654	2,134	2,134

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at meetings of the Company. All ordinary shares rank equally with regard to the Company's residual assets.

Notes to the Financial Statements

(Expressed in Hong Kong Dollars)

29. Total Equity

(a) Group

$ million	Share Capital (note 28)	Share Premium (note 29(c))	Exchange Reserve (note 29(d))	Hedging Reserve (note 29(e))	Revenue Reserve (note 29(f))	Proposed/ Declared Dividend	Total Equity
	Attributable to Equity Shareholders of the Company						
Total equity at 1st January 2007	2,134	4,476	202	107	34,456	2,710	44,085
Exchange differences on translation of:							
– financial statements of overseas subsidiaries	–	–	282	–	–	–	282
– overseas associates	–	–	171	–	–	–	171
Redesignation of available-for-sale investment as an associate	–	–	–	–	(79)	–	(79)
Cash flow hedge:							
– effective portion of changes in fair value, net of deferred tax	–	–	–	122	–	–	122
– transferred to initial carrying amount of non-financial hedged items	–	–	–	3	–	–	3
Actuarial gains and losses of defined benefit retirement schemes, net of deferred tax	–	–	–	–	20	–	20
Net income/(expense) recognised directly in equity	–	–	453	125	(59)	–	519
Profit for the year	–	–	–	–	7,448	–	7,448
Total recognised income and expense for the year	–	–	453	125	7,389	–	7,967
Final dividend in respect of the previous year approved and paid (see note 12(b))	–	–	–	–	–	(2,710)	(2,710)
Interim dividend paid (see note 12(a))	–	–	–	–	(1,238)	–	(1,238)
Proposed final dividend (see note 12(a))	–	–	–	–	(3,052)	3,052	–
Total equity at 31st December 2007	2,134	4,476	655	232	37,555	3,052	48,104

$ million	Share Capital (note 28)	Share Premium (note 29(c))	Exchange Reserve (note 29(d))	Hedging Reserve (note 29(e))	Revenue Reserve (note 29(f))	Proposed/ Declared Dividend	Total Equity
	Attributable to Equity Shareholders of the Company						
Total equity at 1st January 2008	2,134	4,476	655	232	37,555	3,052	48,104
Exchange differences on translation of:							
– financial statements of overseas subsidiaries	–	–	(870)	–	–	–	(870)
– overseas associates	–	–	(394)	–	–	–	(394)
Cash flow hedge:							
– effective portion of changes in fair value, net of deferred tax	–	–	–	(707)	–	–	(707)
– transferred to profit or loss	–	–	–	(3)	–	–	(3)
– transferred to initial carrying amount of non-financial hedged items	–	–	–	(3)	–	–	(3)
Actuarial gains and losses of defined benefit retirement schemes, net of deferred tax	–	–	–	–	(2,454)	–	(2,454)
Net expense recognised directly in equity	–	–	(1,264)	(713)	(2,454)	–	(4,431)
Profit for the year	–	–	–	–	8,029	–	8,029
Total recognised income and expense for the year	–	–	(1,264)	(713)	5,575	–	3,598
Final dividend in respect of the previous year approved and paid (see note 12(b))	–	–	–	–	–	(3,052)	(3,052)
Interim dividend paid (see note 12(a))	–	–	–	–	(1,323)	–	(1,323)
Proposed final dividend (see note 12(a))	–	–	–	–	(3,180)	3,180	–
Total equity at 31st December 2008	2,134	4,476	(609)	(481)	38,627	3,180	47,327

Group revenue reserves as at 31st December 2008 include the Group's share of the retained profits of its associates amounting to $1,222 million (2007: $1,445 million).

Notes to the Financial Statements

(Expressed in Hong Kong Dollars)

29. Total Equity (continued)

(b) Company

$ million	Share Capital (note 28)	Share Premium (note 29(c))	Hedging Reserve (note 29(e))	Revenue Reserve (note 29(f))	Proposed/ Declared Dividend	Total Equity
Total equity at 1st January 2007	2,134	4,476	–	28,048	2,710	37,368
Cash flow hedge:						
– effective portion of changes in fair value, net of deferred tax	–	–	5	–	–	5
Actuarial gains and losses of defined benefit retirement schemes, net of deferred tax	–	–	–	(18)	–	(18)
Net income/(expense) recognised directly in equity	–	–	5	(18)	–	(13)
Profit for the year	–	–	–	7,552	–	7,552
Total recognised income and expense for the year	–	–	5	7,534	–	7,539
Final dividend in respect of the previous year approved and paid (see note 12(b))	–	–	–	–	(2,710)	(2,710)
Interim dividend paid (see note 12(a))	–	–	–	(1,238)	–	(1,238)
Proposed final dividend (see note 12(a))	–	–	–	(3,052)	3,052	–
Total equity at 31st December 2007	2,134	4,476	5	31,292	3,052	40,959
Total equity at 1st January 2008	2,134	4,476	5	31,292	3,052	40,959
Cash flow hedge:						
– transferred to profit or loss	–	–	(5)	–	–	(5)
Actuarial gains and losses of defined benefit retirement schemes, net of deferred tax	–	–	–	(221)	–	(221)
Net expense recognised directly in equity	–	–	(5)	(221)	–	(226)
Profit for the year	–	–	–	6,987	–	6,987
Total recognised income and expense for the year	–	–	(5)	6,766	–	6,761
Final dividend in respect of the previous year approved and paid (see note 12(b))	–	–	–	–	(3,052)	(3,052)
Interim dividend paid (see note 12(a))	–	–	–	(1,323)	–	(1,323)
Proposed final dividend (see note 12(a))	–	–	–	(3,180)	3,180	–
Total equity at 31st December 2008	2,134	4,476	–	33,555	3,180	43,345

All of the Company's revenue reserve is available for distribution to equity shareholders. After the balance sheet date, the directors proposed a final dividend of $1.49 (2007: $1.43) per ordinary share, amounting to $3,180 million (2007: $3,052 million). This dividend has not been recognised as a liability at the balance sheet date.

(c) Share Premium

The application of the share premium account is governed by Section 48B of the Hong Kong Companies Ordinance.

(d) Exchange Reserve

The exchange reserve comprises all foreign exchange differences arising from the translation of the financial statements of foreign operations. The reserve is dealt with in accordance with the accounting policies set out in note 2(v).

(e) Hedging Reserve

The hedging reserve comprises the effective portion of the cumulative net change in the fair value of hedging instruments used in cash flow hedges (net of any deferred tax effect) pending subsequent recognition of the hedged cash flow in accordance with the accounting policy adopted for cash flow hedges in note 2(i)(ii).

(f) Revenue Reserve

The revenue reserve comprises the accumulated profits retained by the Company and its subsidiaries and includes the Group's share of the retained profits of its associates.

(g) Capital Management

The Group's primary objectives when managing capital are:

– to safeguard the Group's ability to continue as a going concern, so that it can continue to provide returns for shareholders and benefits for other stakeholders;

– to provide returns to shareholders by pricing products and services commensurately with the level of risk and by securing access to finance at a reasonable cost;

– to support the Group's stability and future growth; and

– to provide capital for the purpose of strengthening the Group's risk management capability.

The Group actively and regularly reviews and manages its capital structure, taking into consideration the future capital requirements of the Group and capital efficiency, forecast profitability, forecast operating cash flows, forecast capital expenditure and projected investment opportunities.

Consistent with industry practice, the Group monitors its capital structure on the basis of a net debt-to-equity ratio. For this purpose the Group defines net debt as interest-bearing borrowings (as shown in the consolidated balance sheet) less bank deposits and cash. Equity comprises all components of equity (as shown in the consolidated balance sheet).

During 2008, the Group's strategy, which was unchanged from 2007, was to control its net debt-to-equity ratio in order to secure access to finance at a reasonable cost. In order to maintain or adjust the ratio, the Group may adjust the amount of dividends paid to shareholders, issue new shares, return capital to shareholders, raise new debt financing or sell assets to reduce debt.

Notes to the Financial Statements

(Expressed in Hong Kong Dollars)

29. Total Equity (continued)

(g) Capital Management (continued)

The net debt-to-equity ratio at 31st December 2008 and 2007 was as follows:

	Group 2008 $ million	Group 2007 $ million
Interest-bearing borrowings	**10,667**	13,495
Less: Bank deposits and cash	**(8,962)**	(12,180)
Net debt	**1,705**	1,315
Total equity	**47,327**	48,104
Net debt-to-equity ratio	**4%**	3%

During the current year, the Company acted as the guarantor in respect of certain loan facilities granted to its subsidiaries and associates and fully complied with the capital requirements under the loan facility agreements.

30. Notes to the Consolidated Cash Flow Statement

Reconciliation of profit before taxation to cash generated from operations

	2008 $ million	2007 $ million
Profit before taxation	**9,339**	8,759
Adjustments for:		
Share of profits less losses of associates	**(732)**	(524)
Interest income	**(959)**	(1,039)
Dividend income from unlisted available-for-sale equity securities	**(7)**	–
Finance costs	**475**	647
Depreciation	**1,456**	1,963
Amortisation of leasehold land	**58**	57
Fixed assets written off	**25**	22
Net profit on sale of fixed assets	**(1)**	(3)
Exchange gains	**(35)**	(13)
Financial instrument revaluation loss	**3**	–
Operating profit before changes in working capital	**9,622**	9,869
Increase in inventories	**(107)**	(52)
Increase in trade and other receivables	**(29)**	(43)
(Increase)/decrease in Fuel Clause Account	**(662)**	230
Increase in trade and other payables	**37**	55
Increase/(decrease) in net employee retirement benefit liabilities	**26**	(420)
Cash generated from operations	**8,887**	9,639

31. Financial Instruments

The Group is exposed to credit, liquidity, interest rate and currency risks in the normal course of its businesses. The Group is also exposed to equity price risk arising from its equity investments in other entities. In accordance with the Group's treasury policy, derivative financial instruments are only used to hedge its exposure to foreign exchange and interest rate risks arising from operational, financing and investment activities. The Group does not hold or issue derivative financial instruments for trading or speculative purposes.

(a) Credit Risk

The Group's credit risk is primarily attributable to trade and other receivables relating to electricity customers, bank deposits and over-the-counter derivative financial instruments entered into for hedging purposes. The Group has a credit policy in place and the exposures to these credit risks are monitored on an ongoing basis.

In respect of trade and other receivables relating to electricity customers, HEC, a wholly-owned subsidiary, obtains collateral in the form of security deposits from customers in accordance with the Supply Rules. The outstanding amount of deposits received from customers at 31st December 2008 was $1,634 million (2007: $1,585 million). The credit policy is set out in note 20.

The Group has a defined minimum credit rating requirement and transaction limit for counterparties when dealing in financial derivatives or placing deposits to minimise credit exposure. The Group does not expect any counterparty to fail to meet its obligations.

The Group has no significant concentrations of credit risk in respect of trade and other receivables relating to electricity customers, as the five largest customers combined did not exceed 30% of the Group's total turnover.

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

Disclosures in respect of the Group's exposure to credit risk arising from trade and other receivables is set out in note 20.

Notes to the Financial Statements

(Expressed in Hong Kong Dollars)

31. Financial Instruments (continued)

(b) Liquidity Risk

The Group operates a central cash management system for all its subsidiaries in order to achieve a better control of risk and minimise the costs of funds. The Group's policy is to regularly monitor current and expected liquidity requirements and its compliance with loan covenants, to ensure that it maintains sufficient reserves of cash and adequate committed lines of funding to meet its liquidity requirements in the short and longer term. The Group had undrawn committed bank facilities of $7,450 million at 31st December 2008 (2007: $7,145 million).

The following table details the remaining contractual maturities at the balance sheet date of the Group's and the Company's non-derivative financial liabilities and derivative financial liabilities, which are based on contractual undiscounted cash flows (including interest payments computed using contractual rates or, if floating, based on rates current at the balance sheet date) and the earliest date the Group and the Company can be required to pay.

Group

			2008			
$ million	Carrying Amount	Total Contractual Undiscounted Cash Flows	Within 1 Year or on Demand	More than 1 Year but less than 2 Years	More than 2 Years but less than 5 Years	More than 5 Years
Bank loans and other borrowings and interest accruals	10,708	11,780	1,999	304	7,405	2,072
Trade and other payables (excluding interest accruals)	1,116	1,116	1,116	–	–	–
Interest rate swaps (net settled)	87	39	27	19	(7)	–
	11,911	12,935	3,142	323	7,398	2,072
Derivatives settled gross:						
Foreign exchange forward contracts held as cash flow hedging instruments (note 31(d)(i)):	4					
Outflow		2,464	2,464	–	–	–
Inflow		(2,460)	(2,460)	–	–	–
Other foreign exchange forward contracts (note 31(d)(ii)):	2					
Outflow		1,044	1,044	–	–	–
Inflow		(1,046)	(1,046)	–	–	–

$ million	Carrying Amount	2007 Total Contractual Undiscounted Cash Flows	Within 1 Year or on Demand	More than 1 Year but less than 2 Years	More than 2 Years but less than 5 Years	More than 5 Years
Bank loans and other borrowings and interest accruals	13,579	15,986	2,820	1,893	9,120	2,153
Trade and other payables (excluding interest accruals)	988	988	988	–	–	–
Interest rate swaps (net settled)	(119)	(133)	(37)	(42)	(54)	–
	14,448	16,841	3,771	1,851	9,066	2,153
Derivatives settled gross:						
Foreign exchange forward contracts held as cash flow hedging instruments (note 31(d)(i)):	(8)					
Outflow		1,759	1,759	–	–	–
Inflow		(1,762)	(1,762)	–	–	–
Other foreign exchange forward contracts (note 31(d)(ii)):	(1)					
Outflow		189	187	2	–	–
Inflow		(190)	(188)	(2)	–	–

Company

$ million	Carrying Amount	2008 Total Contractual Undiscounted Cash Flows	Within 1 Year or on Demand	More than 1 Year but less than 2 Years	More than 2 Years but less than 5 Years	More than 5 Years
Trade and other payables	41	41	41	–	–	–

$ million	Carrying Amount	2007 Total Contractual Undiscounted Cash Flows	Within 1 Year or on Demand	More than 1 Year but less than 2 Years	More than 2 Years but less than 5 Years	More than 5 Years
Trade and other payables	43	43	43	–	–	–

Notes to the Financial Statements

(Expressed in Hong Kong Dollars)

31. Financial Instruments (continued)

(c) Interest Rate Risk

The Group is exposed to cash flow interest rate risk on its interest-bearing assets and liabilities. Cash flow interest rate risk is the risk that the future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

(i) Hedging

The Group's policy is to maintain a balanced combination of fixed and variable rate debt to reduce its interest rate exposure. The Group also uses interest rate derivatives to manage the exposure in accordance with its treasury policy. At 31st December 2008, the Group had interest rate swaps with a total notional amount of $4,255 million (2007: $7,554 million).

The Group classifies interest rate swaps as cash flow or fair value hedges and states them at fair value in accordance with the policy set out in note 2(i).

The fair values of swaps entered into by the Group at 31st December 2008 were recognised as derivative financial instrument assets and liabilities amounting to $29 million (2007: $122 million) and $114 million (2007: $9 million) respectively.

(ii) Interest Rate Profile

The following table details the interest rate profile of the Group's and the Company's net interest-bearing assets and liabilities at the balance sheet date, after taking into account of the effect of interest rate swaps designated as cash flow or fair value hedging instruments (see (i) above).

Group

	2008		2007	
	Weighted Average Interest Rate %	$ million	Weighted Average Interest Rate %	$ million
Net fixed rate assets/(liabilities)				
Loans to associates	11.4	5,165	11.2	4,748
Bank loans and other borrowings	5.2	(5,649)	5.4	(7,945)
		(484)		(3,197)
Net variable rate assets/(liabilities)				
Cash at bank and in hand	<0.1	31	<0.1	8
Deposits with banks and other financial institutions	2.4	8,931	4.6	12,172
Bank loans and other borrowings	0.9	(5,018)	4.4	(5,550)
Customers' deposits	<0.1	(1,634)	1.3	(1,585)
		2,310		5,045

Company

	2008		2007	
	Weighted Average Interest Rate %	**$ million**	Weighted Average Interest Rate %	$ million
Variable rate assets				
Cash at bank and in hand	**<0.1**	**6**	–	–
Deposits with banks and other financial institutions	**2.4**	**8,913**	4.6	12,154
		8,919		12,154

(iii) Sensitivity Analysis

At 31st December 2008, it is estimated that a general increase/decrease of 100 basis points in interest rates, with all other variables held constant, would have increased/decreased the Group's profit for the year and revenue reserve by approximately $48 million (2007: increased/decreased by approximately $67 million). Other components of consolidated equity would have increased/decreased by approximately $15 million (2007: increased/decreased by approximately $6 million) in response to the general increase/decrease in interest rates.

The sensitivity analysis above has been determined assuming that the change in interest rates had occurred at the balance sheet date and had been applied to the exposure to interest rate risk for both derivative and non-derivative financial instruments in existence at that date. The analysis has been performed on the same basis as for 2007.

(d) Currency Risk

(i) Committed and Forecast Transactions

The Group is exposed to foreign currency risk primarily through purchases that are denominated in a currency other than the functional currency of the operations to which they relate, as well as through income from its overseas investments. The currencies giving rise to this risk are primarily United States dollars, Sterling pounds, Japanese Yen, New Zealand dollars and Canadian dollars.

The Group uses forward exchange contracts to manage its foreign currency risk and classifies these as cash flow hedges. At 31st December 2008, the Group had forward exchange contracts hedging committed and forecast transactions with a net fair liability value of $4 million (2007: $8 million asset) recognised as derivative financial instruments.

(ii) Recognised Assets and Liabilities

The net fair value of forward exchange contracts used by the Group as economic hedges of monetary assets and liabilities in foreign currencies at 31st December 2008 was $2 million liability (2007: $1 million asset) recognised as derivative financial instruments.

Except for borrowings designated to hedge overseas investments (see note 31(d)(iii)), the Group's borrowings are denominated in Hong Kong dollars. Given this, the management does not expect that there would be any significant currency risk associated with the Group's borrowings.

Notes to the Financial Statements

(Expressed in Hong Kong Dollars)

31. Financial Instruments (continued)

(d) Currency Risk (continued)

(iii) Overseas Investments

Currency exposure arising from overseas investments is mitigated in part by funding a portion of the investment through external borrowings in the same currency as the underlying investment. The fair value of these borrowings at 31st December 2008 was $3,207 million (2007: $4,942 million).

(iv) Exposure to Currency Risk

The following table details the Group's and the Company's exposure at the balance sheet date to currency risk arising from highly probable forecast transactions or recognised assets or liabilities denominated in a currency other than the functional currency of the entity to which they relate.

Group

			2008		
'million	USD	JPY	GBP	CAD	NZD
Trade and other payables	46	285	1	1	1
Less: Trade and other receivables	(3)	(2)	–	–	–
Bank deposits and cash	(1,013)	(9)	–	(1)	–
Gross exposure arising from recognised assets and liabilities	(970)	274	1	–	1
Notional amounts of forward exchange contracts used as economic hedges	(132)	(122)	–	–	–
Net exposure arising from recognised assets and liabilities	(1,102)	152	1	–	1
Estimated forecast purchases (see note below)	611	1,011	–	–	–
Gross exposure arising from forecast transactions	611	1,011	–	–	–
Notional amounts of forward exchange contracts used as cash flow hedging instruments	(316)	(119)	–	–	–
Net exposure arising from forecast transactions	295	892	–	–	–
Overall net exposure	(807)	1,044	1	–	1

Note: Included in estimated forecast purchases are forecast purchases of fuel which are for one year's commitment only.

'million	USD	JPY	2007 GBP	CAD	NZD
Trade and other payables	34	454	1	8	–
Less: Trade and other receivables	(8)	(1)	–	–	–
Bank deposits and cash	(804)	(8)	(11)	–	–
Gross exposure arising from recognised assets and liabilities	(778)	445	(10)	8	–
Notional amounts of forward exchange contracts used as economic hedges	(28)	(301)	9	–	–
Net exposure arising from recognised assets and liabilities	(806)	144	(1)	8	–
Estimated forecast purchases (see note below)	285	162	1	–	–
Estimated forecast income	–	–	(4)	–	–
Gross exposure arising from forecast transactions	285	162	(3)	–	–
Notional amounts of forward exchange contracts used as cash flow hedging instruments	(224)	(91)	3	–	–
Net exposure arising from forecast transactions	61	71	–	–	–
Overall net exposure	(745)	215	(1)	8	–

Note: Included in estimated forecast purchases are forecast purchases of fuel which are for one year's commitment only.

Notes to the Financial Statements

(Expressed in Hong Kong Dollars)

31. Financial Instruments (continued)

(d) Currency Risk (continued)

(iv) Exposure to Currency Risk (continued)

Company

		2008		
'million	**USD**	**AUD**	**GBP**	**CAD**
Trade and other receivables	**(3)**	**–**	**–**	**–**
Bank deposits and cash	**(1,013)**	**–**	**–**	**(1)**
Gross exposure arising from recognised assets and liabilities	**(1,016)**	**–**	**–**	**(1)**
Notional amounts of forward exchange contracts used as economic hedges	**(131)**	**–**	**–**	**–**
Overall net exposure	**(1,147)**	**–**	**–**	**(1)**

		2007		
'million	USD	AUD	GBP	CAD
Trade and other receivables	(7)	–	–	–
Bank deposits and cash	(804)	–	(11)	–
Gross exposure arising from recognised assets and liabilities	(811)	–	(11)	–
Notional amounts of forward exchange contracts used as economic hedges	(18)	–	9	–
Net exposure arising from recognised assets and liabilities	(829)	–	(2)	–
Estimated forecast purchases	8	–	–	–
Estimated forecast income	–	(10)	(4)	–
Gross exposure arising from forecast transactions	8	(10)	(4)	–
Notional amounts of forward exchange contracts used as cash flow hedging instruments	(25)	10	4	–
Net exposure arising from forecast transactions	(17)	–	–	–
Overall net exposure	(846)	–	(2)	–

(v) Sensitivity Analysis

The following table indicates that a 10 percent strengthening in the following currencies against Hong Kong dollars at the balance sheet date would have increased/(decreased) the Group's profit for the year (and revenue reserve) and other components of consolidated equity.

Group

	2008		2007	
'million	Effect on Profit for the year and Revenue Reserve Increase/ (Decrease)	Effect on Other Components of Equity Increase/ (Decrease)	Effect on Profit for the year and Revenue Reserve Increase/ (Decrease)	Effect on Other Components of Equity Increase/ (Decrease)
Japanese yen	–	1	–	1
Pounds sterling	–	–	17	1
Canadian dollars	(1)	–	(5)	–
New Zealand dollars	–	–	–	–

A 10 percent weakening in the above currencies against Hong Kong dollars at the balance sheet date would have had an equal but opposite effect on the Group's profit for the year (and revenue reserve) and other components of consolidated equity.

This sensitivity analysis assumes that the change in foreign exchange rates had been applied to re-measure those financial instruments held by the Group which expose the Group to currency risk at the balance sheet date, and that all other variables, in particular interest rates, remain constant. In this respect, it is assumed that the pegged rate between the Hong Kong dollar and the United States dollar would be materially unaffected by any changes in movement in value of the United States dollar against other currencies. Results of the analysis as presented in the above table represent an aggregation of the effects on each of the Group entities' profit after tax and equity measured in their respective functional currencies, translated into Hong Kong dollars at the exchange rate ruling at the balance sheet date for presentation purposes. The analysis has been performed on the same basis as for 2007.

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(Expressed in Hong Kong Dollars)

31. Financial Instruments (continued)

(e) Equity Price Risk

The Group is exposed to equity price changes arising from unlisted available-for-sale equity securities which are held for strategic purposes (see note 18).

All of the Group's unlisted investments are held for long term strategic purposes. Their performance is reviewed regularly based on information available to the Group.

These unlisted investments do not have a quoted market price in an active market and are stated at cost. Any increase or decrease in impairment losses in respect of these investments would affect the Group's net profit. As at the balance sheet date, none of these unlisted investments was considered to be impaired. The review has been performed on the same basis as for 2007.

(f) Fair Value

The carrying amounts of financial instruments are estimated to approximate their fair value.

(g) Estimation of Fair Value

The following summarises the major methods and assumptions used in estimating the fair values of financial instruments.

(i) Securities

Fair value is based on quoted market prices at the balance sheet date without any deduction for transaction costs. Unquoted equity investments do not have a quoted market price in an active market and are measured at cost as their fair value cannot be measured reliably.

(ii) Derivatives

The fair value of forward foreign exchange contracts is determined using forward exchange market rates at the balance sheet date. The fair value of interest rate swaps is determined by discounting the future cash flows of the contracts at the current market interest.

(iii) Interest-bearing Bank Loans and Other Borrowings

The fair value is estimated as the present value of future cash flows, discounted at current market interest rates for similar financial instruments.

(iv) Financial Guarantees

The fair value of financial guarantees issued is determined by reference to fees charged in an arm's length transaction for similar services, when such information is obtainable, or is otherwise estimated by reference to interest rate differentials, by comparing the actual rates charged by lenders when the guarantee is made available with the estimated rates that lenders would have charged, had the guarantees not been available, where reliable estimates of such information can be made.

32. Operating Lease

At 31st December 2008, the total future minimum lease payments by the Group under a non-cancellable equipment operating lease are payable as follows:

	Group	
	2008	2007
	$ million	$ million
Within 1 year	**46**	62
After 1 year but within 5 years	**–**	46
	46	108

During the current year, under the terms of the non-cancellable equipment operating lease agreement, the lessee exercised the option to purchase all of the equipment at the fair market value at the end of the lease.

33. Commitments

The Group's commitments outstanding at 31st December and not provided for in the financial statements were as follows:

	Group	
	2008	2007
	$ million	$ million
Contracted for:		
Capital expenditure	**1,263**	1,106
Investment in associates and jointly controlled entities	**37**	212
Others	**1**	6
	1,301	1,324
Authorised but not contracted for:		
Capital expenditure	**11,821**	8,436

34. Contingent Liabilities

	Group		Company	
	2008	2007	**2008**	2007
	$ million	$ million	**$ million**	$ million
Financial guarantees have been issued in respect of banking facilities available to (see note below):				
Subsidiaries	**–**	–	**3,207**	4,156
Associates	**836**	2,482	**836**	2,482
Jointly controlled entities	**206**	–	**–**	–
Other guarantees given in respect of:				
Subsidiaries	**10**	10	**10**	1,130
Others	**210**	210	**–**	–
	1,262	2,702	**4,053**	7,768

As at the balance sheet date, the Group and the Company have issued guarantees to banks in respect of banking facilities granted to wholly-owned subsidiaries, associates and jointly controlled entities.
The Directors do not consider it probable that a claim will be made against the Group and the Company under any of the guarantees. The maximum liability of the Group and the Company at the balance sheet date under the issued guarantees is disclosed above.

Notes to the Financial Statements

(Expressed in Hong Kong Dollars)

35. Material Related Party Transactions

The Group had the following material transactions with related parties during the year:

(a) Associates

Interest income received/receivable from associates in respect of the loans to associates amounted to $603 million (2007: $519 million) for the year. At 31st December 2008, the total outstanding interest bearing loan balances due from associates were $5,165 million (2007: $4,748 million). The outstanding balances with associates are disclosed in note 16.

(b) Key Management Personnel Compensation

Remuneration for key management personnel, including amounts paid to the Company's Directors as disclosed in note 10(a) and the highest paid employees as disclosed in note 10(b), is as follows:

	Group		Company	
	2008 $ million	2007 $ million	**2008 $ million**	2007 $ million
Short-term employee benefits	**63**	63	**37**	38
Post-employment benefits	**3**	3	**1**	1
	66	66	**38**	39

Total remuneration is included in "staff costs" (see note 8). At 31st December 2008, the total outstanding amount due from the key management personnel was $Nil (2007: $0.3 million).

(c) Subsidiaries

Management fees and services fees recharged by the Company to subsidiaries amounted to $139 million (2007: $129 million) for the year. The outstanding balances with subsidiaries at 31st December 2008 are disclosed in note 15. The transactions and balances with subsidiaries are eliminated on consolidation.

(d) Other Related Parties

On 28th April 2008, Cheung Kong Infrastructure Holdings Limited ("CKI"), a substantial shareholder holding approximately 38.87% of the issued shares of the Company, announced the proposed acquisition of an electricity network in New Zealand at a purchase price of NZ$785 million (HK$4,674 million). On 16th May 2008, the Company entered into a conditional agreement for the Company to acquire from CKI 50% of its proposed investment for NZ$392.5 million (HK$2,337 million). The transaction was completed on 24th July 2008.

36. Substantial Shareholder of the Company

The Company is a Hong Kong listed company and its shares are widely held by the public. Cheung Kong Infrastructure Holdings Limited currently holds approximately 38.87% of the issued share capital of the Company and is a substantial shareholder of the Company.

37. Post Balance Sheet Event

On 5th February 2009, the Company entered into an agreement with CKI to purchase the entire issued share capital of Outram Limited, which holds a 45% equity interest in three joint ventures owning power plants in the People's Republic of China. The consideration for the transaction is HK$5,680 million. The transaction constitutes a connected transaction for the Company. Completion of the transaction is conditional upon approval by the Company's shareholders at an Extraordinary General Meeting and consent from the lenders to one of the power plants. The transaction has not yet been completed up to the date of issue of these financial statements.

38. Critical Accounting Estimates and Judgements

The methods, estimates and judgements the Directors used in applying the Group's accounting policies have a significant impact on the Group's financial position and operating results. Some of the accounting policies require the Group to apply estimates and judgements on matters that are inherently uncertain. In addition to notes 27 and 31 which contain information about the assumptions and their risk factors relating to valuation of defined benefit retirement obligations and financial instruments, certain critical accounting judgements in applying the Group's accounting policies are described below.

(a) Depreciation and amortisation

Fixed assets are depreciated on a straight-line basis over their estimated useful lives, after taking into account the estimated residual value. The Group reviews annually the useful life of an asset and its residual value, if any.

Interests in leasehold land held for own use under operating leases are amortised on a straight-line basis over the shorter of the estimated useful lives of the leased assets and the lease term. Both the period and methods of amortisation are reviewed annually.

The depreciation and amortisation expenses for future periods is adjusted if there are significant changes from previous estimates.

Pursuant to its annual review of the useful lives of fixed assets, based on historical experience and other relevant factors, the Group has revised the estimated useful lives of the fixed assets set out below with effect from 1st January 2008 (see note 2(j)(vi)). These changes in accounting estimates have been applied prospectively. As a result of these changes, the depreciation of fixed assets before capitalisation for the year was reduced by $546 million. The amount of the effect for future periods is not disclosed because estimation is impracticable.

(i) Buildings;

(ii) Ash lagoon and gas pipeline;

(iii) Transmission and distribution equipment, overhead lines and cables; and

(iv) Mechanical meters.

Notes to the Financial Statements

(Expressed in Hong Kong Dollars)

38. Critical Accounting Estimates and Judgements (continued)

(b) Impairment

In considering the impairment losses that may be required for the Group's assets which include available-for-sale securities and fixed assets, the recoverable amount of the asset needs to be determined. The recoverable amount is the greater of the net selling price and the value in use. It is difficult to precisely estimate the net selling price because quoted market prices for these assets may not be readily available. In determining the value in use, expected cash flows generated by the assets are discounted to their present value, which require significant judgement. The Group uses all readily available information in determining an amount that is a reasonable approximation of the recoverable amount.

Any increase or decrease in the above impairment loss would affect the net profit in future years.

39. Possible Impact of Amendments, New Standards and Interpretations Issued but not yet effective for the Year Ended 31st December 2008

Up to the date of issue of these financial statements, the HKICPA has issued a number of amendments, new standards and interpretations which are not yet effective for the year ended 31st December 2008 and which have not been adopted in these financial statements.

The Group is in the process of making an assessment of what the impact of these amendments, new standards and new interpretations is expected to be in the period of initial application. So far it has concluded that the adoption of them is unlikely to have a significant impact on the Group's results of operations and financial position.

In addition, the following developments may result in new or amended disclosures in the financial statements:

		Effective for accounting periods beginning on or after
HKAS 1 (Revised)	Presentation of Financial Statements	1st January 2009
HKAS 23 (Revised)	Borrowing Costs	1st January 2009
HKFRS 8	Operating Segments	1st January 2009

Appendix I
Segment Information

(a) Business Segments

For the year ended 31st December

$ million	Sales of Electricity 2008	Sales of Electricity 2007	Infrastructure Investments 2008	Infrastructure Investments 2007	Unallocated & Other Items 2008	Unallocated & Other Items 2007	Consolidated 2008	Consolidated 2007
Revenue								
Group turnover	12,731	12,478	–	–	42	46	12,773	12,524
Other revenue and other net income	3	426	43	46	15	36	61	508
Segment revenue	12,734	12,904	43	46	57	82	12,834	13,032
Result								
Segment result	8,140	7,858	42	46	(71)	(74)	8,111	7,830
Interest income	–	–	603	519	356	520	959	1,039
Finance costs	(166)	(369)	(297)	(265)	–	–	(463)	(634)
Operating profit	7,974	7,489	348	300	285	446	8,607	8,235
Share of profits less losses of associates	–	–	731	523	1	1	732	524
Profit before taxation	7,974	7,489	1,079	823	286	447	9,339	8,759
Income tax	(1,016)	(1,290)	17	(1)	(1)	(5)	(1,000)	(1,296)
Profit after taxation	6,958	6,199	1,096	822	285	442	8,339	7,463
Scheme of Control transfers	(310)	(15)	–	–	–	–	(310)	(15)
Profit attributable to equity shareholders	6,648	6,184	1,096	822	285	442	8,029	7,448
At 31st December								
Assets								
Segment assets	49,276	49,107	77	183	45	134	49,398	49,424
Interest in associates and jointly controlled entities	–	–	10,071	9,062	9	9	10,080	9,071
Bank deposits and cash	–	–	–	–	8,962	12,180	8,962	12,180
Consolidated total assets	49,276	49,107	10,148	9,245	9,016	12,323	68,440	70,675
Liabilities								
Segment liabilities	3,922	2,848	138	118	394	227	4,454	3,193
Current and deferred taxation	5,667	5,836	(9)	19	9	13	5,667	5,868
Interest-bearing borrowings	7,463	8,559	3,204	4,936	–	–	10,667	13,495
Rate Reduction Reserve	14	1	–	–	–	–	14	1
Development Fund	311	14	–	–	–	–	311	14
Consolidated total liabilities	17,377	17,258	3,333	5,073	403	240	21,113	22,571
Other information								
Capital expenditure	2,084	1,747	–	–	–	–	2,084	1,747
Depreciation and amortisation	1,617	2,144	–	–	–	–	1,617	2,144

Notes to the Financial Statements

(Expressed in Hong Kong Dollars)

Appendix I (continued)

Segment Information (continued)

(b) Geographical Segments

For the year ended 31st December

$ million	Hong Kong 2008	Hong Kong 2007	Australia 2008	Australia 2007	Unallocated & Other Items 2008	Unallocated & Other Items 2007	Consolidated 2008	Consolidated 2007
Revenue								
Group turnover	12,759	12,503	–	–	14	21	12,773	12,524
Other revenue and other net income	13	460	35	46	13	2	61	508
Segment revenue	12,772	12,963	35	46	27	23	12,834	13,032
Result								
Segment result	8,144	7,885	33	45	(66)	(100)	8,111	7,830
Interest income	356	520	521	519	82	–	959	1,039
Finance costs	(166)	(369)	(260)	(257)	(37)	(8)	(463)	(634)
Operating profit	8,334	8,036	294	307	(21)	(108)	8,607	8,235
Share of profits less losses of associates	1	1	301	327	430	196	732	524
Profit before taxation	8,335	8,037	595	634	409	88	9,339	8,759
Income tax	(1,017)	(1,295)	(2)	(2)	19	1	(1,000)	(1,296)
Profit after taxation	7,318	6,742	593	632	428	89	8,339	7,463
Scheme of Control transfers	(310)	(15)	–	–	–	–	(310)	(15)
Profit attributable to equity shareholders	7,008	6,727	593	632	428	89	8,029	7,448
At 31st December								
Assets								
Segment assets	49,318	49,220	11	115	69	89	49,398	49,424
Interest in associates and jointly controlled entities	9	9	4,715	7,030	5,356	2,032	10,080	9,071
Bank deposits and cash	–	–	–	–	8,962	12,180	8,962	12,180
Consolidated total assets	49,327	49,229	4,726	7,145	14,387	14,301	68,440	70,675
Other information								
Capital expenditure	2,084	1,747	–	–	–	–	2,084	1,747
Depreciation and amortisation	1,617	2,144	–	–	–	–	1,617	2,144

Appendix 2
Principal Subsidiaries

The following list contains only the particulars of subsidiaries as at 31st December 2008 which principally affected the results, assets or liabilities of the Group. The class of shares held is ordinary unless otherwise stated.

Name of Company	Issued Share Capital and Debt Securities	Percentage of Equity Held by the Company	Place of Incorporation/ Operation	Principal Activity
The Hongkong Electric Company, Limited	HK$2,411,600,000	100	Hong Kong	Electricity generation and supply
Associated Technical Services Limited	HK$1,000,000	100	Hong Kong	Consulting
Cavendish Construction Limited	HK$4,200,000	100	Hong Kong	Contracting
Fortress Advertising Company Limited	HK$2	100	Hong Kong	Advertising
Gusbury Enterprises Inc.	US$2	100	Panama/Hong Kong	Investment holding
Hongkong Electric (Natural Gas) Limited	US$1	100	British Virgin Islands/ Hong Kong	Investment holding
Hongkong Electric (Cayman) Limited	US$1	100	Cayman Islands/ Hong Kong	Financing
Hongkong Electric Finance (Cayman) Limited	US$1	100	Cayman Islands/ Hong Kong	Financing
Fenning Limited	HK$20	100	Hong Kong	Contracting
Dunway Investment Limited	US$1	100	British Virgin Islands	Investment
Coty Limited	US$1	100	British Virgin Islands	Investment holding
Bonlink Investment Limited	US$1	100	British Virgin Islands	Investment holding
Hongkong Electric International Limited	US$50,900	100	British Virgin Islands	Investment holding
Hongkong Electric Finance Limited	US$1 and HK$2,400 million Hong Kong dollar notes (see note 24)	100*	British Virgin Islands/ Hong Kong	Financing
HEI Investment Holdings Limited	HK$2	100*	Hong Kong	Investment holding
Sigerson Business Corp.	US$101	100*	British Virgin Islands	Investment holding
HEI Utilities (Malaysian) Limited	A$637,510	100*	British Virgin Islands	Investment holding
HEI Power (Malaysian) Limited	A$52,510	100*	British Virgin Islands	Investment holding
Hong Kong Electric International Finance (Australia) Pty Limited	A$1	100*	Australia	Financing
HEI Transmission Finance (Australia) Pty Limited	A$12	100*	Australia	Financing
HEI Distribution Finance (Australia) Pty Limited	A$100	100*	Australia	Financing
Riverland Investment Limited	US$1	100*	British Virgin Islands	Investment holding
Hongkong Electric International Power (Mauritius) Limited	US$2	100*	Mauritius	Investment holding
Kentson Limited	US$1	100*	British Virgin Islands	Investment holding
Beta Central Profits Limited	GBP63,772,525	100*	United Kingdom	Investment holding
HEI China Limited	US$1	100*	British Virgin Islands	Investment holding
Hongkong Electric Yunnan Dali Wind Power Company Limited	HK$1	100*	Hong Kong	Investment holding
Dako International Limited	US$1 + C$53,550,000	100*	British Virgin Islands	Investment holding
More Advance Development Limited	HK$200,010,000	100*	Hong Kong	Investment holding
HEI Tap Limited S.A.	C$53,550,000	100*	Belgium	Investment holding
Kongwell Development Limited	HK$1	100*	Hong Kong	Financing
Kindmax Enterprises Limited	HK$1	100*	Hong Kong	Financing
Goldteam Resources Limited	US$1 + NZ$58,500,000	100*	British Virgin Islands	Investment holding
HEI Leting Limited	HK$1	100*	Hong Kong	Investment holding

* Indirectly held

Notes to the Financial Statements

(Expressed in Hong Kong Dollars)

Appendix 3
Principal Associates

The following list contains only the particulars of associates as at 31st December 2008 which principally affected the results or assets of the Group:

Name of Associate	Issued Share Capital	Percentage of Group's Effective Interest	Place of Incorporation/ Operation	Principal Activity
Secan Limited	HK$10	20%	Hong Kong	Property development
CKI Spark Holdings No. One Limited (see note (a) below)	A$250,818,796	54.76%	Bahamas/ Australia	Electricity distribution
CKI Spark Holdings No. Two Limited (see note (b) below)	A$498,038,537	54.76%	Bahamas/ Australia	Electricity distribution
Ratchaburi Power Company, Limited (see note (c) below)	THB7,325,000,000	25%	Thailand	Electricity generation and supply
Northern Gas Networks Holdings Limited (see note (d) below)	GBP571,670,980	35.1%	United Kingdom	Gas distribution
Stanley Power Inc. (see note (e) below)	Ordinary share C$107,000,000 Preference share C$46,666,800	50%	Canada	Electricity generation
Wellington Electricity Distribution Network Holdings Limited (see note (f) below)	NZ$117,000,100	50%	New Zealand	Electricity distribution

Notes:

(a) CKI Spark Holdings No. One Limited holds a 51% attributable interest in CHEDHA Holdings Pty Limited ("CHEDHAH"). CHEDHAH is the holding company of Powercor Australia Limited ("Powercor") and CitiPower I Pty Limited ("CitiPower"). Powercor operates and manages an electricity distribution business in the State of Victoria, Australia. CitiPower, which is similar to Powercor, is one of five electricity distributors in the State of Victoria, Australia. The Group holds 54.76% of CKI Spark Holdings No. One Limited but the Group does not have effective control over it and, therefore, it has been accounted for as an associate.

(b) CKI Spark Holdings No. Two Limited holds a 51% attributable interest in ETSA Utilities Partnership ("ETSA"). ETSA is an unincorporated body and operates and manages the electricity distribution business in the State of South Australia. The Group holds 54.76% of CKI Spark Holdings No. Two Limited but the Group does not have effective control over it and, therefore, it has been accounted for as an associate.

(c) Ratchaburi Power Company, Limited is incorporated in Thailand and is principally engaged in the development, financing, operation and maintenance of a power generating station in Thailand.

(d) Northern Gas Networks Holdings Limited ("NGN") operates a gas distribution network in the North of England.

(e) Stanley Power Inc. indirectly holds a 49.99% partnership interest in TransAlta Cogeneration L.P.. TransAlta Cogeneration L.P. owns interests in five gas-fired cogeneration facilities in Alberta, Ontario and Saskatchewan and in a coal-fired, mine-mouth generation facility in Alberta, Canada.

(f) Wellington Electricity Distribution Network Holdings Limited owns interests of the Wellington electricity distribution network, which supplies electricity to the city of Wellington, the capital of New Zealand, and extends to the Porirua and Hutt Valley regions of New Zealand.

Appendix 4
Jointly Controlled Entities

The following list contains the particulars of jointly controlled entities as at 31st December 2008:

Name of Jointly Controlled Entities	Issued Share Capital	Percentage of Group's Effective Interest	Place of Incorporation/ Operation	Principal Activity
Huaneng Hongkong Electric Dali Wind Power Company Limited (see note (a) below)	RMB126,048,280	45%	People's Republic of China	Electricity generation
Huaneng Laoting Wind Power Company Limited (see note (b) below)	RMB180,427,511	45%	People's Republic of China	Electricity generation

Notes:

(a) Huaneng Hongkong Electric Dali Wind Power Company Limited is engaged in wind power development, operation, management and supply of electricity in the People's Republic of China.

(b) Huaneng Laoting Wind Power Company Limited is engaged in wind power development, operation, management and supply of electricity in the People's Republic of China.