

Audit Committee Report

As at the date of this Report, the Audit Committee of the Company (referred to as the “Committee” in this report) consists of five non-executive Directors, four of whom are Independent Non-executive Directors of the Company (“INEDs”).

Members of the Committee during the year

INEDs

Dr Eddy Fong Ching¹ (member since 13 January 2015 and chairman since 20 May 2015)
Mrs Lucia Li Li Ka-lai
Mr Alasdair George Morrison
Dr Allan Wong Chi-yun (since 11 August 2015)
Mr T. Brian Stevenson² (member and chairman up to 20 May 2015)
Professor Frederick Ma Si-hang³

Non-executive Director

Commissioner for Transport (Mrs Ingrid Yeung Ho Poi-yan)

Notes:

- ¹ Dr Eddy Fong Ching, an INED, was appointed as a member of the Committee with effect from 13 January 2015, and became chairman of the Committee with effect from the conclusion of the Company's 2015 Annual General Meeting held on 20 May 2015 (the “2015 AGM”).
- ² Mr T. Brian Stevenson retired as an INED, and ceased to be the chairman and a member of the Committee and a member of the Remuneration Committee of the Company with effect from the conclusion of the 2015 AGM.
- ³ Professor Frederick Ma Si-hang ceased to be a member of the Committee with effect from 1 January 2016.

None of the Committee Members is a partner or former partner of KPMG, the Company's external auditor. The Finance Director (the “FD”), the Head of Internal Audit (the “Head of IA”) and representatives of the external auditor are expected to attend meetings of the Committee. At the discretion of the Committee, others may also be invited to attend meetings. The Committee meets regularly, and the external auditor or the FD may request a meeting if they consider it necessary.

Duties of the Committee

Under the Committee's Terms of Reference (available on the respective websites of the Company (www.mtr.com.hk) and The Stock Exchange of Hong Kong Limited), the duties of the Committee include the financial and efficiency aspects of the Company's business, as described below. Amongst other things, the Committee is required to oversee the relationship with the external auditor, to review the financial information of the Company, and to oversee the Company's financial reporting system and internal control procedures.

The Committee discusses with the external auditor the nature and scope of audit and reporting obligations before the audit commences. Apart from giving pre-approval of all audit services, the Committee also pre-approves any non-audit services and ensures that the external auditor's provision of non-audit services does not impair its independence or objectivity. The Committee is primarily responsible for making recommendations to the Board on the appointment, re-appointment and removal of the Company's external auditor, and approving the remuneration and terms of such engagement.

With respect to the financial information of the Company, the Committee monitors the integrity of financial statements, interim and annual reports and accounts, together with the preliminary announcement of results and other announcements regarding the Company's financial information to be made public. In dealing with the financial information, the Committee liaises with the Board and the Executive Directorate, and the chairman of the Committee further meets on an ad hoc basis with the Head of IA, representatives of the external auditor, and Management, as and when required. Apart from considering issues arising from audits, the Committee discusses any matters that the Head of IA or external auditor may wish to raise, either privately or together with Members of the Executive Directorate and any other person.

The Committee assists the Board in overseeing the Company's financial controls and internal control systems on an ongoing basis. The Committee reviews, at least annually, the effectiveness of the Company's financial controls and internal control systems and reports to the Board that such a review has been carried out. These controls and systems allow the Board to monitor the Company's overall financial position and to protect its assets. As mentioned in last year's report, the duty to review the effectiveness of the Company's risk management system has been fully vested with the Company's Risk Committee. Further details of the mechanism of the above are set out in the “Risk Management and Internal Control Systems” section of the Corporate Governance Report on pages 117 to 120 of this Annual Report. The Committee's review also covers its role in overseeing the Management's review of the adequacy of resources, qualifications and experience of staff of the Company's accounting and financial reporting function, and their training programmes and budget.

The Committee reviews and approves the annual Internal Audit Plan which includes audits on the efficiency of chosen activities or operations of the Company. In addition, the Committee reviews periodic reports from the Head of IA and the follow-up of major action plans recommended, and puts forward recommendations to the Board, where appropriate. The Committee reviews the annual assessment conducted by the Head of IA on the adequacy of resources, qualifications and experience of staff of the Company's internal audit function, and its training programmes and budget.

During 2015 and in addition to the abovementioned duties, the Committee also reviewed the financial impact on the Company's 2014 Annual Accounts and 2015 Interim Accounts in light of the development of the Express Rail Link project and the Company's other new railway projects.

The chairman of the Committee summarises the activities of the Committee and highlights issues arising therefrom by a report to the Board after each Committee meeting.

The minutes of the Committee meetings are prepared by the secretary of the meetings with details of the matters considered by the Committee Members and decisions reached, including any concerns raised by the Committee

Members and dissenting views expressed. The draft minutes are circulated to Committee Members for comments within a reasonable time after the meeting. The Committee formally adopts the draft minutes at the next subsequent meeting, after taking into account any comments that the Committee Members may have on the draft minutes. Minutes of the Committee meetings are open for inspection by Committee Members at the Company's registered office.

In January each year, the secretary of the meetings pre-agrees key agenda items for the year with the chairman of the Committee who makes a final determination on the agenda for the regular Committee meetings. A total of four meetings have been scheduled to be held on a quarterly basis in February, May, August and November 2016.

Work Performed by the Committee in 2015

In 2015, the Committee held four meetings. Of the four meetings, two were allocated to the review of the Company's annual results for the year ended 31 December 2014. In addition, the first meeting concentrated on business operations in Hong Kong, internal control and internal audit related items, while the second meeting focused on accounting and financial reporting matters, business operations outside of Hong Kong as well as outstanding litigation and compliance issues.

The major work performed by the Committee in 2015 included:

Financial

- Review of the draft 2014 Annual Report and Accounts and 2015 Interim Report and Accounts, in particular, the financial impact in light of the development of the Express Rail Link project and the Company's other new railway projects, and recommendation of the same for the Board's approval;
- Review and recommendation for presentation to the Remuneration Committee of the paper headed "2014 payout under "2008 Variable Incentive Scheme" - confirmation of the financial figures"; and
- Preview of 2015 annual accounting and financial reporting issues.

Internal Audit

- Approval of the 2016 Internal Audit Plan;
- Review of two Half-yearly Reports prepared by Internal Audit Department for July to December 2014 and for January to June 2015 respectively;
- Review of the Report on the Company's Internal Control system for the year ended 31 December 2014;
- Review of two Half-yearly Reports on Whistle-blowing prepared by Internal Audit Department for July to December 2014 and for January to June 2015 respectively;
- Review of the Report on Evaluation of Effectiveness of Internal Audit Department for 2014; and
- Holding of private sessions with Head of IA without the presence of Management.

External Auditors - KPMG

- Review of KPMG's Audit Plan;
- Pre-approval of audit and non-audit services provided by KPMG;
- Review of tax issues, compliance and salient features of 2014 Annual Accounts and 2015 Interim Accounts prepared by KPMG;
- Review of KPMG's fees proposal for the 2015 audit;
- Review of KPMG internal controls and clearance processes on independence; and
- Holding of private sessions with representatives of KPMG without the presence of Management.

Others

- Review of outstanding litigation, and compliance with statutes and regulations, Operating Agreement and Rail Merger Related Agreements;
- Review of an Update on the Management Governance Framework which is set out on page 120 of this Annual Report under the Corporate Governance Report;
- Review of the Audit/Governance Committees Minutes of MTR's subsidiaries; and
- Presentation on the early adoption of the revised Corporate Governance Code.

The attendance record of each Committee Member is shown on pages 110 to 111 of this Annual Report under the "Board and Board Committee Meetings" section of the Corporate Governance Report.

Representatives of the external auditor, the FD and the Head of IA attended all four meetings for reporting and answering questions about their work.

Further to that and by invitation, the Chief Executive Officer (formerly the Acting Chief Executive Officer), the Operations Director, the Commercial Director, the Projects Director, the Property Director and the Legal Director and Secretary (or their representatives) had respectively provided an overview of the Company's business development and expansion outside of Hong Kong, railway operations, non-fare businesses, latest cost position and progress of new railway projects, property business as well as outstanding litigation and compliance matters to the Members at the meetings.

Re-appointment of External Auditor

The Committee was satisfied with KPMG's work, its independence and objectivity, and therefore recommended the re-appointment of KPMG (which has indicated its willingness to continue in office) as the Group's external auditor for 2016 for approval by the Company's Shareholders at the 2016 Annual General Meeting.

Dr Eddy Fong Ching
Audit Committee Chairman
Hong Kong, 11 March 2016

The Audit Committee Report has been reviewed and endorsed by the Committee.