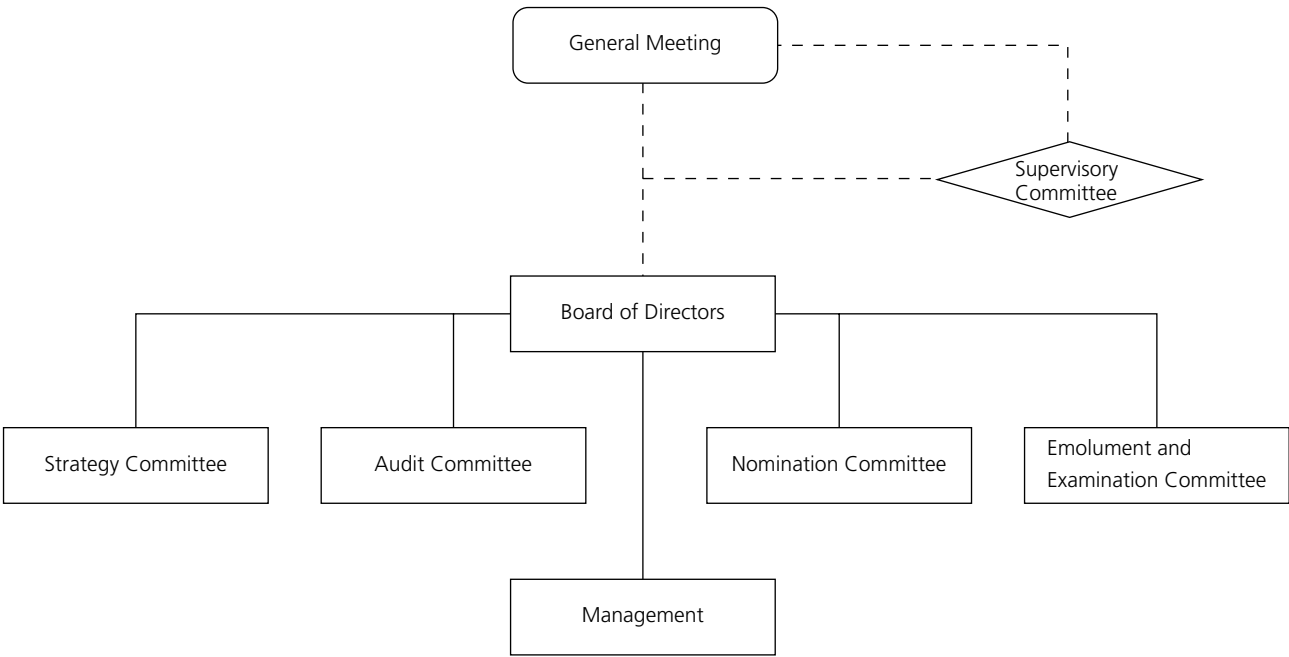


# CORPORATE GOVERNANCE

## I. CORPORATE GOVERNANCE INFORMATION

The corporate governance structure of the Company:



The Company always strictly conforms to the *Company Law* and the *Securities Law* of the PRC, relevant regulations issued by the China Securities Regulatory Commission and the listing rules of the Shanghai Stock Exchange and The Stock Exchange of Hong Kong Limited, actively consummates its corporate governance structure, standardizes its operations. During the period under review, the Company has strictly complied with all code provisions of the Code on Corporate Governance Practices set out in Appendix 14 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited.

During the period under review, the Company amended its Articles of Association in accordance with "Guide for Articles of Association of Listed Companies (2006 Revision)" issued by the China Securities Regulatory Commission on March 16, 2006, to further standardize its operations, establish its modern enterprise system, and protect interest of minority shareholders.

## II. BOARD OF DIRECTORS

### (I). Duties and Positions

The principal duties of the Board of Directors ("Board") are to exercise management and decision-making power as conferred by the general meeting in respect of corporate development strategies, management structures, investment and financing, planning, financial control and so forth. The authority of the Board on development strategy and management and its responsibility of supervising and inspecting the operation and development of the Company are set out in the *Articles of Association* of the Company in details. The directors acknowledge their responsibility for preparing the accounts in this annual report.

The roles of the chairman and the president are distinctively separated and the positions are undertaken by different persons. The chairman is responsible for overseeing the operation of the Board and monitoring the implementation of the Board's resolutions, whilst the president is responsible for managing and overseeing the Company's business operations implementing the resolutions laid down by the Board.

### (II). Composition

The Board is in its fifth term since the establishment of the Company, and is composed of eleven directors. The terms of office of the current directors are from May 27, 2005 or the respective dates of their appointments to the date of election of the next term of the Board.

Members of the Board have different industry backgrounds with expertise in corporate management, finance and accounting, investment and strategy, shipbuilding management and human resources management. The biography of the directors of the Company are set out in "Information of Directors, Supervisors, Senior Management and Staff" in this Annual Report.

Three directors, over 1/4 of the total number of directors, undertook specific management duties for the Company in 2006, enabling the Board to exercise close assessment and monitoring of the Company's management process. The Board has four independent non-executive directors, over 1/3 of the total number of directors.

# CORPORATE GOVERNANCE

## (III). Board Meetings

The Company held eleven Board meetings in 2006 to discuss the Group's development strategies, investment projects and the operational and financial performance of the Company. The Board meetings proceeded efficiently and arrived at prompt and prudent decisions. During the period under review, the four independent non-executive directors had no objection to decisions of the Company.

Attendance at meetings of the Board and its special committees (attendance in person/number of meetings):

Name	Board Meeting		Audit Committee	Emolument and Examination Committee	Strategy Committee	Nomination Committee
	Before 2005	After 2005				
	Annual	Annual				
	General Meeting	General Meeting				
<b>Directors</b>						
Li Zhushi	5/5	6/6	–	–	1/1	–
Yu Baoshan	4/5	6/6	–	1/1	–	–
Han Guangde	5/5	6/6	–	–	1/1	–
Chen Jingqi	5/5	6/6	–	–	1/1	–
Zhong Jian	5/5	6/6	–	–	1/1	2/2
Li Junfeng	4/5	6/6	–	–	1/1	–
Miao Jian	4/5	5/6	3/4	–	–	–
<b>Independent Directors</b>						
Wu Fabo	5/5	5/6	4/4	1/1	–	–
Bu Miaojin	5/5	6/6	–	1/1	–	2/2
Wang Xiaojun	4/5	4/6	–	–	–	2/2
Mak, Kin Kwong, Peter	2/5	–	2/2	–	–	–
Lee Sun-leung, Sunny	–	6/6	2/2	–	–	–

Except that the independent director Mr. Wu Fabo was unable to participate in the eighteenth meeting of the 5th term of Board in person or by proxy as he was abroad at that time and not contactable, other directors who had been unable to attend the meetings in person had appointed other directors as their proxies to attend and vote at the meetings on their behalf.

### (IV). Directors

Directors are elected or replaced at general meetings, where the election is conducted by way of cumulative voting. The directors may offer themselves for re-election after the serve terms expires. The office of independent non-executive director shall be undertaken by appointees not related to the Company's management and substantial shareholders in any aspect. Independent non-executive directors are eligible for re-election subject to a maximum of six consecutive years.

Through the company secretary, all directors obtain timely information and updates relating to statutory, regulatory and other ongoing obligations that directors of a listed company must comply with, ensuring understanding of their duties and assuring thorough implementation of procedures of the Board and due compliance with applicable laws and regulations. The directors, as well as the special committees of the Board, may seek the advice of independent professional institutions in the course of exercising their powers, performing their duties or fulfilling any business requirements. Reasonable expenses incurred in this connection will be borne by the Company.

The independent non-executive directors of the Company are familiar with the rights and obligations as directors and independent directors of a listed company. During the period under review, they all participated in the meetings of the Board in a highly conscientious and responsible manner, took the advantages of their experiences and special knowledge in the work of consummating the corporate governance and significant decision making, issued pertinent and external opinion on relevant matters such as significant events and connected transactions and so forth, improved the scientizing of the decision-making of the Board and its decision process, ensured the benefit of the shareholders and the Company as a whole. The four independent non-executive directors occupy positions in the special committees established under the Board.

The four independent non-executive directors has confirmed to the Company that they continued to satisfy the independence criteria as set out in rule 3.13 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited during the year.

The Company has strictly complied with the relevant restrictive provisions imposed by Hong Kong and PRC regulatory organs in relation to securities transactions by directors and has consistently upheld the principle of complying with the most stringent provisions. The Company has adopted Model Code for Securities Transactions by Directors of Listed Companies in Appendix 10 of Listing Rules. The Company has made specific inquiries of all directors of the Company for preparing this report and all directors have confirmed that they have complied with such code of conduct during the period under review.

# CORPORATE GOVERNANCE

## III. COMMITTEES OF THE BOARD

The Board has set up four special committees. Each with defined terms of reference to monitor specific areas of the Company's business, and has established work team to assist the committees' work.

### 1. Audit Committee

Established under proposals set forth in "A Guide for Effective Audit Committees" issued by the Hong Kong Institute of Certified Public Accountants, the Audit Committee is principally responsible for reviewing and monitoring the quality and procedures for the Group's financial reporting; evaluating the soundness and effectiveness of the Company's internal control systems; reviewing the appointment of independent auditors and coordination and reviewing the efficiency and quality of their work.

The Audit Committee comprises Mr. Wu Fabo (director member), Mr. Lee Sun-leung, Sunny and Mr. Miao Jian, of which Mr. Wu and Mr. Lee are independent non-executive directors.

The Audit Committee held four meetings during 2006. All members of the committee and work team attended the meetings. All matters passed at the committee meetings have been properly recorded and filed in accordance with relevant rules. The director member reported to the Board on significant matters discussed.

Major tasks accomplished by the Audit Committee during the period under review are as follows:

- Reviewing the annual, interim and quarterly reports and financial statements of the Group;
- Reviewing the accounting policies and practices adopted by the Group and related matters;
- Checking and ensuring the connected transactions of the Company are fair, impartial and open, offering sufficient protection to the interests of minority shareholders;
- Assisting the Board to conduct independent evaluation of the effectiveness of the Group's financial reporting procedures and internal control systems;
- Providing opinions or reminding the management of related risks in respect of significant matters of the Company.

## 2. Strategy Committee

The Strategy Committee is principally responsible for examining and reviewing the directions of the Company's strategic development, formulating the Company's strategic plans, monitoring the implementation of strategic planning, and facilitating timely adjustments to the Company's strategies and governance structure.

The Strategy Committee comprises Mr. Li Zhushi (director member), Mr. Han Guangde, Mr. Chen Jingqi, Mr. Zhong Jian and Mr. Li Junfeng.

During the year 2006, the Strategy Committee held one meeting which researched the Company's development strategic analyses report, and worked out the medium-term and long-term development strategy and target.

## 3. Nomination Committee

The Nomination Committee is principally responsible for selecting the candidates for directors and president and for choosing the selection standard and process of directors and president.

The Nomination Committee comprises independent non-executive director Mr. Bu Miaojin (director member), independent non-executive director Mr. Wang Xiaojun and Mr. Zhong Jian. The Nomination Committee held two meetings in the year 2006 to discuss the nomination of the persons for the fifth term of the Board and the senior management.

## 4. Emolument and Examination Committee

The Emolument and Examination Committee is principally responsible for researching examination standard of the directors, supervisors and senior management of the Company, examining them and putting forward proposals, researching and examining remuneration policies and scheme of the directors, supervisors and senior management of the Company.

The Emolument and Examination Committee comprises independent non-executive director Mr. Bu Miaojin (director member), independent non-executive director Mr. Wu Fabo and Mr. Yu Baoshan. In 2006, the Emolument and Examination Committee held one meeting to discuss and work out the annual reward scheme for executive directors, internal supervisors and senior management for the year 2005.

# CORPORATE GOVERNANCE

## IV. CONTROL MECHANISMS

### 1. Supervisory Committee

The Supervisory Committee is in its fifth term since the establishment of the Company, and was elected by the 2005 annual general meeting. The Supervisory Committee composed of five supervisors, including two external supervisors. The supervisors number and composition are accordant with relevant laws and regulations.

The Supervisory Committee exercises independently the power of supervision upon the Company in accordance with the law to protect the lawful rights of the shareholders, the Company and its staff against any infringement. The size and composition of the Company's Supervisory Committee are in compliance with the requirements of the relevant laws and regulations. The Supervisory Committee held 5 meetings during 2006, each attended by all supervisors in person, to carry out supervision on behalf of the shareholders in respect of the Company's financial matters and the lawfulness and compliance on the discharge of duties by the directors and senior management. The Supervisory attended all Board meetings and general meetings, and diligently performed its supervisory duties. The work information refers to "Report of the Supervisory Committee" in this Annual Report.

### 2. Internal Control and Audit

The Board is responsible for developing and maintaining an internal control system of the Company to protect shareholders' interest and to safeguard the Group's assets by reviewing the control procedures for financial, operational and supervisory matters. Such internal control system is implemented by management upon the authorization of the Board and the effectiveness of the internal control system is reviewed by the Audit Committee.

The Company has established an internal audit department. Depending on the materiality of potential risks existing in the internal control systems of various businesses and processes of the Company, the internal audit department carries out inspection, supervision and evaluation of the Company's financial information disclosure, operations and internal control activities on a regular or as-needed basis, with the purpose of ensuring transparency in information disclosure, operational efficiencies and effectiveness of the corporate control regimes. It furnishes independent and objective evaluations and recommendations in the form of audit reports.

The Company always puts great efforts in internal control and to that end the Company has developed corresponding internal management systems and procedures in areas including corporate governance, operation, construction, finance, administration and personnel management and so forth. The Company formulated the internal control implementation framework in December 2005, and this framework was approved by sixth meeting of the fifth term of the Board of the Company on December 1, 2005. In order to formalize the corporate governance, the Board will review the Company's internal control system once half a year.

## CORPORATE GOVERNANCE

The Company finished the 2006 interim and annual internal control review and analysis in August 2006 and March 2007 respectively. The analysis reports have been submitted to the Audit Committee and directors for review. All the directors affirmed that the Company has consummated its internal control system to ensure the effective implementation of management systems of the Company and avoid operating risk of the Company.

The establishment of the internal control system is for managing foreseeable risk, but could not avoid risk entirely. In view of the limits of internal control system, the Company's internal control system could only provide reasonable but not absolute insurance to the realization of operation goal of the Company. It also is impossible for the system to avoid significant error and loss.

### 3. Auditors

The financial statements for the year ended December 31, 2006 prepared under PRC Accounting Rules and Regulations and the HKFRS have been audited by the domestic auditors Ascenda Certified Public Accountants, Limited (Beijing) and international auditors PricewaterhouseCoopers, Certified Public Accountants, respectively.

Under the latest requirements by the State-owned Assets Supervision and Administration Commission of the State Council in respect of appointment of auditors, and with approval of the first extraordinary general meeting of 2006, the Company changed its domestic auditors from Guangdong Yangcheng Certified Accountants Co., Ltd. to Ascenda Certified Public Accountants, Limited (Beijing), whose payment for audit services for the year 2006 amounted to RMB0.5 million.

The international auditors PricewaterhouseCoopers, Certified Public Accountants has provided audit services to the Company for 14 years, its payment for audit services for the year 2006 amounted to HKD1.67 million.

Moreover, the domestic auditor (including any entity that is under common control, ownership or management with the audit firm or any entity that a reasonable and informed third party having knowledge of all relevant information would reasonably conclude as part of the audit firm nationally or internationally) provided special audit services concerning connected transactions and external guarantee to the Company during 2006. The international auditor also provided professional services to perform the procedures agreed with the Company with respect to the continuing connected party transactions and the preliminary announcement of results of the Company for the year ended 2006.

The Company strictly complied with the requirements in the "Regulations on Regular Rotation of Signing Certified Accountant in Securities and Futures Audit Business", and changed the signing certified accountant of domestic audit report periodically. The certified accountants who signed on the domestic audit report in 2006 Annual Report are Mr. Xiong Jianyi and Mr. Tu Zhenlian.



# CORPORATE GOVERNANCE

## 4. Chief Accountant

The chief accountant oversees all financial matters of the Company and is accountable to the president. The chief accountant is responsible for preparing financial statements in accordance with the PRC and HKFRS and in compliance with relevant provisions of The Stock Exchange of Hong Kong Limited, China Securities Regulatory Commission and Shanghai Stock Exchange. The chief accountant is also responsible for organizing the preparation of the Company's annual budget plans and annual accounts and monitoring the implementation of annual financial and operational plans. The chief accountant is also required to collaborate with the Board in the formulation of relevant internal control systems and to make recommendations thereof to the Board.

## 5. Qualified Accountant

The financial advisor of the Company, qualified accountant Mr. Li Chi Sing died of illness in October 2006. The Company has engaged Mr. Donald K W Chau, a fellow of the association of Chartered Certified Accountants and a practicing member of HKICPA, as consultant to assist the chief accountant in the discharge of the duties in the oversight of the Company's financial reporting procedures and internal controls.

## V. SHAREHOLDERS AND OTHER STAKEHOLDERS

The Company strives to ensure that all shareholders, especially the minority shareholders, are able to fully exercise their rights on an equal basis.

### 1. General Meeting

The general meeting is vested with the supreme authority of the Company, where powers are exercised in accordance with the law to determine significant matters of the Company. The annual or extraordinary general meeting provides a channel for direct communication between the Board and the shareholders. The Company pays high regard to the general meetings. Notice convening general meeting is issued 45 days prior to the date of the meeting, and all directors, supervisors and members of the senior management are requested to make their best efforts to attend. All shareholders are encouraged to attend general meetings and make their voice heard. Details of general meetings held in 2006 refer to "Brief of General Meetings" in this Annual Report.

## 2. Substantial Shareholders

CSSC, as substantial shareholder of the Company, conducts its activities in a regulated manner. It has never been involved in any acts of by passing the general meeting or interfering, whether directly or indirectly, the Company's policy decisions or operations. The Company and the substantial shareholder are independent of each other in terms of staffing, assets, finance, institution and business.

The information about CSSC and other substantial shareholders as at the end of the period under review are set out in "Changes of Share Capital and Shareholders" of this Annual Report.

## 3. Information Disclosure and Investor Relations Management

The Company believes that the core of the investor relations is effective communication, satisfying information disclosure is the basis of good investor relations. The Company has formulated Information Disclosure Management System and Investor Relations Management System to ensure openness, fairness and impartiality in information disclosure and to enhance transparency. The company secretary and securities affairs representative are responsible for information disclosure of the Company and reception of visiting shareholders and investors.

During the year 2006, the Company enhanced work in investor relations, issued annual report, interim report and quarterly report, almost 30 announcements and 4 circulars in time in accordance with relevant regulations, objectively provided relevant information of legal and those possibly influence investors' interest, and improved the information disclosure standards continuously. Apart from that, the Company also expatiated its operation situation and developing foreground to investors through conference call, visiting investors, analyst interview, attending investors' forum and road-performance through internet.

The company secretary of the Company Mr. Li Zhidong won the "Best Capital Innovation Award" in the best company secretary choose through public appraisal undertook by Shanghai Securities News in 2006.

# CORPORATE GOVERNANCE

## 4. Other Stakeholders

The Company established “Remuneration Scheme for the Fifth Term Senior Management” and “Performance Examination Rules of Directors, Supervisors and Senior Management”, to prompting directors, supervisors and senior management to make concerted effort and devote for the continuous steady healthy development. At the same time of promoting profitability and development of enterprise, the Company concerns social cost and staff’s health, actively participate in social commonweal and environment protection. The Company has passed the attestation of “Safe, Healthy and Environment Management System” in 2005 and the examination of “cleanly production” in 2006. The Company is stepping to the direction of green shipbuilding production.

The labour union of the Company established “staff benefit association” in 2004, through voluntary contributing money from employees and donation from the Company, to help employees who fall sick or be injured.

## VI. CONCLUSION

The corporate governance regime adopted by the Company is an indication of the standard in managing and operating its business. Sound corporate governance contributes to the healthy development of a company and enhances investors’ confidence in the Company. To be effective in corporate governance, relevant measure must be reviewed on a regular basis to ensure that they are in tandem with market trends and requirements of regulatory authorities. It is a long-term goal of the Company to achieve unwavering corporate system leadership, through establishing and improving upon a modernized corporate system. As such, we will continue to enhance corporate governance as part of our efforts to ensure stable development and to increase shareholders’ value.