

Corporate Governance Report

Corporate Governance Practices

China Yurun Food Group Limited (“Yurun Food” or the “Company”) is committed to achieving high standards of corporate governance to safeguard the interests of all shareholders and to enhance corporate value and accountability. The Company has complied throughout the period from 1 January 2006 to 31 December 2006 (“Review Year”) with the applicable code provisions of the Code on Corporate Governance Practices (the “CG Code”) set out in Appendix 14 to the Rules (the “Listing Rules”) Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (“Stock Exchange”) except for a short period of deviation from code provision A.5.4, details of which have disclosed out in the Company’s 2005 annual report and the interim report for the six months ended 30 June 2006. The following summarises the Company’s corporate governance practices during the Review Year.

Directors’ Securities Transactions

The Company has adopted the Model Code for Securities Transactions by Directors of Listed Issuers (“Model Code”) set out in Appendix 10 to the Listing Rules as its own code of conduct regarding securities transactions of the directors of the Company (“Directors”). The Directors confirmed to the Company that they had complied with the required standard set out in the Model Code during the Review Year.

Board of Directors

The Board of Directors (the “Board”) currently comprises five executive Directors, two non-executive Directors and three independent non-executive Directors, serving the important function of guiding the management. The executive Directors have extensive experience in the food industry and the non-executive directors are well established in their respective professions. The Board has a diversified background and professional expertise, which as a group provides the Group with such core competencies such as industry knowledge, technical expertise, customer-based experience and knowledge in finance, accounting, business and management experience. Biographical details of the Board members are set out on pages 17 to 18 of this annual report.

The Chairman of the Board is Mr. Zhu Yicai, while the Chief Executive Officer is Mr. Zhu Yiliang. The positions of the Chairman of the Board and the Chief Executive Officer are held by separate individuals with a view to maintaining an effective segregation of duties respecting management of the Board and day-to-day management of the Group’s business.

The Board, led by the Chairman, is responsible for the approval and monitoring of the Group’s overall strategies and policies, approval of annual budgets and business plans, evaluating the performance of the Group, and overseeing the management. One of the important roles of the Chairman is to provide leadership to the Board to ensure that the Board acts in the best interests of the Group. To facilitate effective management, certain functions have been delegated by the Board to various board committees, namely, audit committee, remuneration committee and nomination committee. Each board committee operates under clearly defined written terms of reference.

Management is responsible for the day-to-day operations of the Group under the leadership of the Chief Executive Officer. The Chief Executive Officer, working with the executive management team, is responsible for managing the businesses of the Group, including implementation of approved strategies adopted by the Board for the operations of the Group.

None of the members of the Board has any connections (including financial, business, family relationship and other material/related relationships) with each other as required to be disclosed pursuant to Appendix 16 to the Listing Rules.

Corporate Governance Report

The Board held eight meetings in 2006. The attendance of individual Director during the Review Year is as follows:

	Board Committees			
	Board (Total no. of meetings: 8)	Audit Committee (Total no. of meetings: 4)	Remuneration Committee (Total no. of meetings: 1)	Nomination Committee (Total no. of meetings: 2)
Number of attendance				
Executive Directors				
Mr. Zhu Yicai (Chairman)	8/8	N/A	1/1	2/2
Mr. Zhu Yiliang (Chief Executive Officer)	8/8	N/A	N/A	N/A
Mr. Zhang Yuanfei (Chief Operating Officer)	8/8	N/A	N/A	N/A
Mr. Feng Kuande	8/8	N/A	N/A	N/A
Mr. Ge Yuqi	8/8	N/A	N/A	N/A
Non-executive Directors				
Mr. Jiao Shuge	8/8	2/2 ⁽²⁾	N/A	N/A
Miss Liu Yi Lan, Katherine	8/8	N/A	N/A	N/A
Independent Non-executive Directors				
Prof. Zheng Xueyi	8/8	N/A	N/A	N/A
Mr. Kang Woon	8/8	4/4	1/1	2/2
Mr. Gao Hui	8/8	4/4	1/1	2/2
Resigned Directors				
Mr. Bi Guoxiang ⁽¹⁾	7/8	N/A	N/A	N/A
Mr. Hsu Shang Wi, William	3/3 ⁽²⁾	2/2 ⁽²⁾	N/A	N/A
Miss Hsu I-Yin, Joyce	N/A ⁽³⁾	N/A	N/A	N/A

Note:

- (1) Mr. Bi Guoxiang resigned as Director and Chief Executive Officer of the Company on 12 April 2007. Mr. Zhu Yiliang and Mr. Zhang Yuanfei were appointed as Chief Executive Officer and Chief Operating Officer of the Company respectively on the same day.
- (2) Attendance taken during term of service for the Review Year.
- (3) Miss Hsu I-Yin, Joyce resigned as non-executive Director on 15 February 2006. Since no board meeting was held prior to her resignation during the Review Year, no attendance has been taken.

The Chairman shall ensure that the Board works effectively and discharges its responsibilities, and that all key and appropriate issues are discussed by the Board in a timely and effective manner. The Chairman has delegated the responsibility for preparing agenda for each Board meeting to the Company Secretary and to ensure that all Directors are properly briefed on issues to be discussed at Board meetings and receive adequate and accurate information in a timely manner. Where possible and when opportunity arises, the non-executive Directors will be invited to locations where the Group operates to enable them to obtain a better perspective of the business and enhance their understanding of the Group's operations.

Corporate Governance Report

The non-executive Directors are appointed for a fixed term not exceeding three years and are subject to retirement by rotation and re-election by shareholders at annual general meeting in accordance with the Company's Bye-laws.

The Board has received from each independent non-executive Director a written confirmation confirming his independence during the Review Year pursuant to Rule. 3.13 of the Listing Rules.

Remuneration of Directors and Senior Management

The Company has established a remuneration committee ("Remuneration Committee") which currently comprises two independent non-executive Directors, namely, Mr. Kang Woon (chairman of the Remuneration Committee) and Mr. Gao Hui, as well as Mr. Zhu Yicai, the Chairman of the Company. During the Review Year, the Remuneration Committee held one meeting to review the remuneration packages of the Directors and senior management of the Company. All members of the Remuneration Committee were present and the attendance rate was 100%.

The main duties of the Remuneration Committee are to make recommendations to the Board on the Company's policy and structure for the remunerations of Directors and senior management, and to determine the specific remuneration packages of all executive Directors and senior management by reference to the Group's corporate goals and objectives.

The Remuneration Committee has to consult the Chairman of the Company about their proposals relating to the remuneration of Directors and senior management. The compensation structure for the Directors and senior management of the Group consists of two key components, that is, fixed cash and variable incentive. The fixed component includes salary, retirement benefit scheme contributions and other allowances which are determined by reference to the remuneration benchmark in the industry and the prevailing market conditions. The variable component comprises bonus and share options granted under the Company's share option scheme, which are performance-based and are payable and granted upon achievement of individual and corporate performance targets as determined by the Board from time to time.

Nomination of Directors

The Company has established a nomination committee ("Nomination Committee") which currently comprises two independent non-executive Directors, namely, Mr. Kang Woon (chairman of the Nomination Committee) and Mr. Gao Hui, as well as Mr. Zhu Yicai, the Chairman of the Company. During the Review Year, the Nomination Committee held two meetings to review the structure, size and composition of the Board, consider the resignation and appointment of non-executive Directors, assess the independence of independent non-executive Directors, and make recommendation on the re-election of the Directors who were subject to retirement and re-election at annual general meeting. All members were present at the meetings and the attendance rates were 100%.

The main duties of the Nomination Committee are to regularly review the structure, size and composition (including skills, knowledge and experience) of the Board and to make recommendations to the Board with regards to any proposed changes, identify and nominate for the approval of the Board, candidates to fill board vacancies as and when they arise, assess the independence of independent non-executive Directors, make recommendations on the succession planning for Directors and senior management of the Group.

The Nomination Committee adopted certain criteria and procedures in the nomination of new directors. The major criteria include the candidates' professional background, especially their experience in the Group's industry, the recommendations from the management team and other knowledgeable individuals. The Nomination Committee will shortlist the candidates and then submit to the Board for final approval.

Corporate Governance Report

Audit Committee

The Company established an audit committee ("Audit Committee") which currently comprises two independent non-executive Directors, namely, Mr. Gao Hui (chairman of the Audit Committee) and Mr. Kang Woon, as well as Mr. Jiao Shuge, a non-executive Director. Mr. Hsu Shang Wi, William, who resigned as a Director on 16 August 2006, ceased to be a committee member and his vacancy was filled by Mr. Jiao Shuge effective on the same day. The Audit Committee is mainly responsible for overseeing the Group's financial reporting, risk management and evaluating internal controls and auditing processes.

During the Review Year, four meetings were held by the Audit Committee with all the members present, which attendance rates were 100%. The external auditors, the executive Director overseeing the finance functions of the Group, the Chief Financial Officer, and the management staff of the Finance Department and the Internal Audit Department attended those meetings to answer questions raised by the Audit Committee. The major works of the Audit Committee during the Review Year include:

- reviewing the Group's annual and interim financial statements before submission to the Board for approval;
- reviewing the development in accounting standards and its impacts on the Group;
- reviewing the external auditors' letter to management and ensuring the Board provides a timely response to the issues raised therein;
- reviewing the independence of external auditors for providing non-audit services to the Group and approving the remuneration and terms of engagement of external auditors;
- making recommendation on the re-appointment of external auditors;
- reviewing the effectiveness of the Group's financial management, internal control and risk management systems;
- reviewing the continuing connected transactions of the Group; and
- working with the Group's Internal Audit Department to carry out internal audit works.

Auditors' Remuneration

Details of fees paid or payable to the Group's external auditors for the year ended 31 December 2006 are as follows:

Services	Fees RMB'000
2006 annual audit	3,269
2006 interim review	511
Non-audit service	463
Total:	4,243

Corporate Governance Report

Internal Control and Risk Management

The Board acknowledges that it is responsible for maintaining a sound system of internal controls to safeguard shareholders' interest. The Group's internal control systems have been designed to provide reasonable assurance that assets are safeguarded, operational controls are in place, business risks are suitably reduced, proper accounting records and financial information are maintained, and, where appropriate, relevant legislation, regulation and best practices are complied with.

The Board has delegated to the Audit Committee responsibility for reviewing the effectiveness of the Group's internal control system. The Audit Committee works with the Group's Internal Audit Department to carry out internal audit works based on an internal audit plan which is reviewed and approved by the Audit Committee. The Group's Internal Audit Department, which is staffed by qualified and experienced personnel, reports its findings and recommendations for any corrective action required to the Audit Committee directly. The Audit Committee reviews the reports submitted by the Internal Audit Department and the issues on the internal control system of the Group are then discussed and evaluated by the Board every year.

The Internal Audit Department conducted an examination on various material control aspects during the Review Year including financial, operational and compliance controls with the aim of mitigating the overall business and operational risk of the Group. It identified key risk areas and developed appropriate control measures and management actions for correction. Crisis management procedures have also been developed in order to respond swiftly and positively to any event that results in abrupt loss of consumer confidence. Internal control reports were submitted to the Audit Committee for review and the findings and recommendations were discussed at Audit Committee meetings and Board meetings.

The Audit Committee, with the assistance of the Internal Audit Department, has reviewed the Group's material internal controls, including financial, operational and compliance controls, and risk management functions during the Review Year.

Directors' Responsibility for the Financial Statements

The Directors acknowledge their responsibility for preparing the financial statements of the Group.

With the assistance of the Finance Department of the Company which is under the supervision of the Qualified Accountant of the Company, the Directors have ensured that the preparation of the financial statements of the Group is in accordance with statutory requirements and applicable accounting standards. The Directors have also ensured the publication of the financial statements of the Group is in a timely manner in accordance with the applicable rules and regulations.

The statement of the auditors of the Company about their reporting responsibilities on the financial statements of the Group is set out in the Independent Auditor's Report on page 43 of this annual report.

Investor Relations and Communication with Shareholders

Yurun Food aims at providing its shareholders and potential investors with high standards of disclosure and financial transparency. The Company has set up an Investor Relations Department specialising in handling investor relations matters. During the Review Year, the Company held press conferences for results announcement, one-on-one and group meetings with analysts and senior representatives from renowned fund management companies, participated in large investment conferences in China and Hong Kong, and organised site visits for shareholders and institutional investors to our manufacturing facilities in China, giving them a better understanding of the Group's manufacturing capability. We also kept dialogue with international investors through frequent teleconferences.

Corporate Governance Report

Yurun Food makes use of various formal communication channels to account to shareholders for the performance of the Company. These include annual and interim reports, announcements made through the Company's as well as the Stock Exchange's websites, and annual general meetings. We launched webcasts on our website www.yurun.com.hk allowing investors to view our presentations online and obtain detailed slide presentations. We also revamp and enrich the contents of our investor relations webpage regularly to include all key information such as corporate calendar, Stock Exchange announcements, stock price information, operation statistics, slide presentations, financial reports and so forth. We believe that through proactive communications with the investor community, corporate transparency can be enhanced and the Company's potential and actual value can be more fully reflected in the market.