MTR

Building on Strength

Annual Report 2008

Building on Strength

The successful implementation of the Rail Merger and the achievement of merger synergies have enabled the Company to build a strong platform for the future as we continue to capture growth opportunities in Hong Kong, the Mainland of China and overseas. The planning and design of five new rail lines in Hong Kong and the construction of Kowloon Southern Link represent the most significant network expansion in the Company's history. Despite challenging economic conditions, we are maintaining our pursuit of prudent growth based on a strong balance sheet, satisfactory liquidity and steady recurrent income generated by our core businesses.

Contents

Vision

We aim to be a globally recognised leader that connects and grows communities with caring service.

Mission

- Enhance customers' quality of life and anticipate their needs.
- Actively engage in communities we serve.
- Foster a company culture that staff can learn, grow and take pride in.
- Provide sustainable returns to investors.
- Set ourselves new standards through innovation and continuous improvement.
- Grow in Hong Kong, Mainland of China and capture opportunities in Europe by extending our core competencies.

Values

Excellent Service

- We are committed to proactively provide safe, efficient and caring service valued by customers.

Mutual Respect

- We work in an open team environment based on trust, joint commitment and respect.
- We listen and respect the views of the community and other stakeholders.

Value Creation

- We create profits through efficient execution, continuous improvement and innovation in delivering products and services valued by customers.

Enterprising Spirit

- We have the courage to question the status quo to seek improvement, proactively taking initiatives and having the resourcefulness to overcome obstacles and reach new horizons.

A new vision and mission that reaffirms our commitment to different stakeholders while guiding our corporation to reach greater heights as a globally recognised leader.

The four values will remain the foundation upon which we build our continued success.

Operating Network with Future Extensions

Legend

- Station
- Interchange Station
- Proposed Station
- Proposed Interchange Station
- Cable Car Ngong Ping 360
- Shenzhen Metro Network
- * Racing days only

Existing Network

- Airport Express
- Disneyland Resort Line
- East Rail Line
- Island Line
- Kwun Tong Line
- Light Rail
- Ma On Shan Line
- Tseung Kwan O Line
- Tsuen Wan Line
- Tung Chung Line
- West Rail Line

Projects in Progress

- Kowloon Southern Link
- Tseung Kwan O South

Extensions under Study

- Guangzhou-Shenzhen-Hong Kong Express Rail Link
- Kwun Tong Line Extension
- Shatin to Central Link
- South Island Line (East)
- West Island Line

Future Extensions

- North Island Line
- Northern Link
- South Island Line (West)

Properties Owned / Developed / Managed by the Corporation

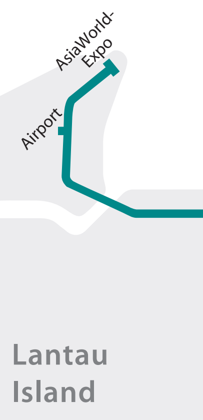
01 Telford Gardens / Telford Plaza I and II
02 World-wide House
03 Admiralty Centre
04 Argyle Centre
05 Luk Yeung Sun Chuen / Luk Yeung Galleria
06 New Kwai Fong Gardens
07 Sun Kwai Hing Gardens
08 Fairmont House
09 Kornhill / Kornhill Gardens
10 Fortress Metro Towers
11 Hongway Garden / Vicwood Plaza
12 Perfect Mount Gardens
13 New Jade Garden
14 Southorn Garden
15 Heng Fa Chuen / Heng Fa Villa / Paradise Mall
16 Park Towers
17 Felicity Garden
18 Tierra Verde / Maritime Square
19 Tung Chung Crescent / Citygate / Novotel Citygate / Seaview Crescent / Coastal Skyline / Caribbean Coast
20 Central Park / Island Harbourview / Park Avenue / Harbour Green / Bank of China Centre / HSBC Centre / Olympian City One / Olympian City Two
21 The Waterfront / Sorrento / The Harbourside / The Arch / Elements / The Cullinan / The Harbourview Place / W Hong Kong / International Commerce Centre
22 One International Finance Centre / Two International Finance Centre / IFC Mall / Four Seasons Hotel / Four Seasons Place
23 Central Heights / The Grandiose / The Edge
24 Residence Oasis / The Lane
25 No.8 Clear Water Bay Road / Choi Hung Park & Ride
26 Metro Town
27 Royal Ascot / Plaza Ascot
28 Pierhead Garden / Ocean Walk
29 Sun Tuen Mun Centre / Sun Tuen Mun Shopping Centre
30 Hanford Garden / Hanford Plaza
31 Citylink Plaza
32 MTR Hung Hom Building / Hung Hom Station Carpark
33 Trackside Villas
34 The Capitol
35 The Palazzo

Property Developments under Construction / Planning

21 Kowloon Station Package 5, 6 & 7
23 Tseung Kwan O Station Area 56
34 LOHAS Park Package 2-10
36 Wu Kai Sha Station
37 Tai Wai Maintenance Centre
38 Che Kung Temple Station
39 Tai Wai Station
40 Tin Shui Wai Light Rail Terminus
41 Kowloon Southern Link Site C
42 Kowloon Southern Link Site D

West Rail Line Property Development (As Government Agent)

43 Nam Cheong Station
44 Yuen Long Station
45 Tuen Mun Station
46 Tsuen Wan West Station
47 Long Ping Station
48 Tin Shui Wai Station
49 Kam Sheung Road Station
50 Pat Heung Maintenance Centre
51 Kwai Fong Site



Shenzhen
Lo Wu
Lok Ma Chau
Chau Tau
Sheung Shui
Fanling
Tai Wo
Tai Po Market
33
University
Fo Tan
27
35
Racecourse*
Sha Tin
31
Tai Wai
39
37
Through Train
Route Map
Beijing Line
Shanghai Line
Guangdong Line
Beijing
Shanghai
Zhaoqing
Guangzhou
Foshan
Dongguan
HONG KONG SAR
Yuen Long
44
Kam Sheung Road
49
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New Territories
Ma On Shan
36
Wu Kai Sha
Heng On
Tai Shui Hang
Shek Mun
City One
Sha Tin Wai
38
Che Kung Temple
Tsuen Wan West
46
Tsuen Wan
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Tai Wo Hau
Kwai Hing
07
Kwai Fong
06
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Mei Foo
Lai King
Tsing Yi
18
Sunny Bay
Disneyland Resort
Tung Chung
19
Cable Car
Ngong Ping 360
Lai Chi Kok
Cheung Sha Wan
Sham Shui Po
Kowloon Tong
Lok Fu
Wong Tai Sin
Diamond Hill
Choi Hung
25
Kowloon
Shek Kip Mei
Prince Edward
Mong Kok
04
Mong Kok East
Kai Tak
To Kwa Wan
Ma Tau Wai
Ho Man Tin
Whampoa
Kowloon Bay
01
Ngau Tau Kok
Kwun Tong
Lam Tin
Yau Tong
Po Lam
24
Hang Hau
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Tseung Kwan O
Tiu Keng Leng
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LOHAS Park
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Nam Cheong
20
Olympic
21
Kowloon
Yau Ma Tei
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42
Austin
Jordan
Tsim Sha Tsui
West Kowloon Terminus
Hung Hom
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East Tsim Sha Tsui
Exhibition
Tamar
Hong Kong
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Fortress Hill
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North Point
Quarry Bay
09
Tai Koo
Sai Wan Ho
17
Shau Kei Wan
12
Heng Fa Chuen
15
Chai Wan
13
Sai Ying Pun
11
Sheung Wan
02
Central
Central South
Admiralty
03
08
Wan Chai
14
Causeway Bay
Tin Hau
16
Kennedy Town
University
Hong Kong Island
Cyberport
Wah Fu
Aberdeen
South Horizons
Lei Tung
Wong Chuk Hang
Ocean Park

MTR Corporation at a Glance

The Rail Merger, now successfully completed in all aspects, significantly expanded the size, scale and geographic coverage of the business activities of the Company. At the same time, the growth momentum of the Company has continued with significant network expansion in Hong Kong and the capture of growth opportunities in the Mainland of China and overseas.

Hong Kong Railway Operations

Business Description

We operate a pre-dominantly rail based transportation system in Hong Kong, comprising Domestic and Cross-boundary services, a dedicated high-speed Airport Express and a light rail system, which in total stretches 211.6 kilometres with 82 stations and 68 stops. The Integrated MTR System is one of the most intensively used systems in the world, known for its reliability, safety and efficiency. We also provide intercity services to the Mainland of China as well as a bus operation in Hong Kong providing convenient feeder services.

2008 Highlights

- The merger integration process was implemented smoothly, with the physical integration of the two networks achieved ahead of schedule
- For the period from 2 December 2007 to 31 December 2008, we exceeded all the performance levels required by Government and our own Customer Service Pledges targets
- Customer satisfaction levels recorded during the year by our regular surveys remained high
- The excellence of our service performance levels was again recognised in a large number of awards

Station Commercial and Rail Related Businesses

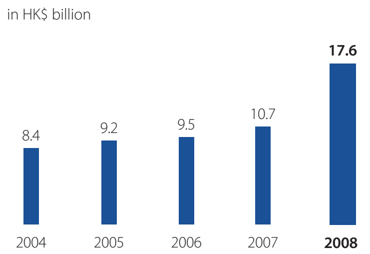
Business Description

We leverage our railway assets and expertise into additional businesses, including rental of station retail units (such as Duty Free shops), advertising in trains and stations, telecommunications, rail consulting and freight services.

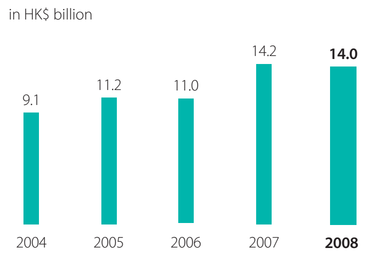
2008 Highlights

- The Rail Merger brought about increased scale and new business opportunities in the form of Duty Free shops
- Advertising innovations included the first digital escalator displays in Asia's metros and the renovated "The Galleria" in Causeway Bay Station
- 3G mobile phone coverage along the East Rail and Ma On Shan lines was fully launched
- Our consultancy business won an engineering and project management contract for the construction of the Delhi Airport Metro Express Line

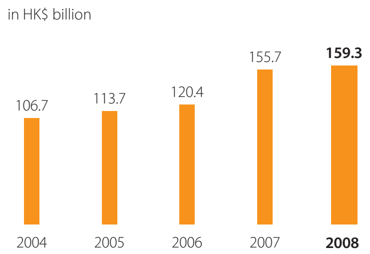
Turnover



Operating Profit before Depreciation and Amortisation (after Property Development Profit)



Total Assets



Property and Other Businesses

Business Description

We develop mainly residential properties in conjunction with property developers. We own investment properties, principally shopping centres and offices, and manage our properties and others. Our investment portfolio includes 12 shopping centres and 18 floors of the Two International Finance Centre office tower.

2008 Highlights

- All units of The Capitol at LOHAS Park were pre-sold as well as about 80% of the units available at The Palazzo in Shatin
- The development package for Che Kung Temple on the Ma On Shan Line was awarded to a subsidiary of New World Development Company Limited
- Close to 100% occupancy was maintained at our shopping centres. The Company's 18 floors at Two International Finance Centre were fully rented out
- Ginza Mall continued to set new benchmarks for service and quality within the shopping centre industry in Beijing

Mainland and Overseas Growth

Business Description

We continue our strategy to grow outside of Hong Kong by investing in urban rail networks in the Mainland of China, and pursuing "asset-light" operating concessions in European markets that are privatised or opening to new entrants.

2008 Highlights

- Our joint venture London Overground Rail Operations Limited brought steady improvements to the London Overground
- Awarded the concession rights to operate the Stockholm Metro Concession
- Good progress was made on the Beijing Metro Line 4 project, while approval was gained for the Shenzhen Metro Line 4 project
- Entered into Agreements in Principle for the operation and maintenance of Shenyang Metro Lines 1 and 2 and a Memorandum of Understanding for the operation and maintenance of the Daxing Line in Beijing
- Entered into a Principle Agreement for the investment, construction and operation of Hangzhou Metro Line 1

Chairman's Letter

"As a result, the Rail Merger delivered on its promise by strengthening our business and financial performance in the first full financial year of reporting."

Dear Stakeholders,

I am pleased to present to you the annual results of MTR Corporation for 2008.

They reflect three major successes. The Merger integration process progressed well both in terms of physical integration and alignment of resources. As a result, the Rail Merger delivered on its promise by strengthening our business and financial performance in the first full financial year of reporting. Secondly we made further advances in the approval, planning and design of five new rail lines in Hong Kong and in the construction of Kowloon Southern Link, representing the most significant network expansion in Hong Kong in the Company's history. Thirdly our projects in the Mainland of China and overseas made good progress. Despite the onset of volatile and uncertain economic conditions in the second half of the year, we maintained our pursuit of prudent growth based on a strong balance sheet, good liquidity and steady recurrent income generated by our core businesses.

The impact of the Rail Merger and buoyant economic conditions in the first half of the year enabled us to increase total revenue for 2008 by 64.9% to HK$17,628 million. Operating profit from railway and related businesses before depreciation and amortisation also increased by 57.7% to HK$9,325 million. However, property development profits in 2008 of HK$4,670 million were lower than in 2007 by HK$3,634 million due to the very significant development profits booked relating to Le Point in Tseung Kwan O in 2007. Hence, excluding the change in fair value of investment properties and the related deferred tax, net profit from underlying businesses attributable to equity shareholders decreased by 4.5% to HK$8,185 million. Including investment property revaluation deficit of HK$146 million (HK$99 million surplus net of deferred tax after accounting for the reduction in Hong Kong Profits Tax rate), our net profit attributable to equity shareholders for 2008 was HK$8,284 million and earnings per share were HK$1.47. Your Board has declared a final dividend of HK$0.34, giving a full year dividend of HK$0.48 per share, which is an increase of 6.7% compared to 2007.

Rail Merger

The merger integration process made strong progress throughout 2008. With the removal of the interchange ticket gates at Kowloon Tong, Mei Foo and Nam Cheong stations completed in November, passengers were able to enjoy truly seamless travel on the enlarged MTR network using only one ticket.

The year was also successful for the alignment of systems, divisional integration and training necessary for the full realisation of the Rail Merger. Increased patronage of the network saw the Company take the lead position in the public transport market in Hong Kong, while also becoming one of the largest employers with over 12,000 Hong Kong staff.

A new grading and salary structure for staff with aligned terms and conditions was implemented in March. We continued to work on creating harmonious staff relations, and we developed a new set of the Vision, Mission and Values for the Company. A large-scale review of energy efficiency was launched through benchmarking of best practices from both pre-merger rail operations, and we undertook a broad spectrum of training and development courses in the areas of railway safety and operations, multi-skilling and redeployment. Overall, we continued to achieve merger synergies, which when fully realised at the end of a three-year period are estimated at HK$450 million per year.

Growth Strategy

Our post-merger growth strategy is focused on significant new rail development in Hong Kong and our continued expansion into the Mainland of China and overseas.

In Hong Kong, the Government's approval, in March and April, for the planning and design of the Shatin to Central Link, the Kwun Tong Line Extension to Whampoa and the Hong Kong section of the Guangzhou-Shenzhen-Hong Kong Express Rail Link gave fresh impetus to our rail development plans. Together with the South Island Line (East) and West Island Line, for which approval to proceed with planning and design had previously been given by Government, these new lines together with the substantially completed Kowloon Southern Link (incorporating the new Austin Station) will add approximately 60 kilometres to our network. When completed, they will represent the largest home based network expansion in the history of our company. In Hong Kong, with the development of these five new rail lines, the Company will be better positioned to reach new catchment areas, capturing new customers and extending our service to even more communities.

In the Mainland of China, we made steady progress on the Beijing Metro Line 4 (BJL4) project, with train testing and production, and operations training proceeding on schedule

"In Shenzhen, approval for the Shenzhen Metro Line 4 project has been obtained from the National Development and Reform Commission."

for the opening of the line in the fourth quarter of 2009. In November 2008, a Memorandum of Understanding was signed for the operation and maintenance of the Daxing Line, which is the extension of BJL4. In Shenzhen, approval for the Shenzhen Metro Line 4 (SZL4) project has been obtained from the National Development and Reform Commission. We are now completing final regulatory procedures to sign the Concession Agreement in the near future. Projects works will be expanded to cover the whole line. Meanwhile, preparation works for taking over SZL4 Phase 1 are also underway. During the year, we continued to pursue further investment opportunities in other key cities in the Mainland of China. In November 2008, we entered into three non-binding Agreements in Principle with Shenyang Municipal Government and Shenyang Metro Group Company Limited for the operations and maintenance of Shenyang Metro Lines 1 and 2 for a term of 30 years, exploring investment in future lines and for investigatory property development opportunities along Lines 1 and 2. In Hangzhou, we entered into a non-binding Principle Agreement with Hangzhou Municipal Government and Hangzhou Metro Group Company Limited for the investment, construction and operation of Hangzhou Metro Line 1, as well as an agreement to explore property development opportunities along metro corridors, in January 2009.

In Europe, our UK joint venture London Overground Rail Operations Limited (LOROL) steadily improved the operations of the London Overground following takeover of the concession in November 2007. London Overground serves West, East and North London and will provide a significant link for the 2012 Olympic Games. In Sweden, we were awarded the concession rights to operate for eight years the Stockholm Metro concession in January 2009.

To meet the significant demand on our human resources in supporting this phase of growth both in and outside of Hong Kong, we have embarked on a number of programmes to hire, train and retain personnel. These programmes include the recruitment of Hong Kong and Mainland graduates under the Graduate Trainee Programme and the Executive Associate Scheme.

Sustainability

Concerns over the environment and the effects of unrestrained development on both social cohesion and the climate have become key business considerations for companies around the world. The Company continues to expand our commitment to fostering sustainable development and the well-being of the communities wherever we operate. As our new rail lines reach out to more communities in Hong Kong and our operations expand into the Mainland of China and overseas, we remain committed to becoming one of the most resource-efficient and ecologically sustainable railways and property service providers in the world.

In 2006, the Company adopted the MTR Corporation Climate Change Policy, which is modelled on the policy developed by the International Association of Public Transport (UITP). As Chair of the Sustainable Development Commission within the UITP, the Company played a significant role in developing these initiatives.

Several of the key actions under the Policy have been adopted and measured for impact under our internal Enterprise Risk Management Framework, particularly in regard to electricity consumption. The Rail Merger prompted a large-scale review of energy efficiency and synergy opportunities within the ex-Kowloon-Canton Railway Corporation's (KCRC) network as benchmarked against MTR Corporation's best practices, and a programme of enhancing asset efficiency began during the year. We also introduced energy efficiency as a major factor in the design of our capital works projects, beginning with our South Island Line (East) project. In addition, we have integrated life-cycle environmental concerns into the planning, design and construction of our new railway projects and property developments.

Our efforts to incorporate sustainability, environmental respect and best practice into all our business decisions continued to attract international recognition. In February, we were recognised as a Sustainability Leader within the global travel and tourism industry sector, and we won a Silver Class Award from SAM (Sustainable Asset Management). We also continued to be listed on the internationally recognised Dow Jones Sustainability Indexes and FTSE4Good Index series.

In May 2008 we published our seventh annual Sustainability Report 2007, *Building Capability*, which reflects our culture of continuous improvement. The Report offers our vision of the future challenges to our business from the changing physical environment and the benefits derived for the communities we serve. Our Sustainability Report 2007 was accredited the "Commendation for Excellent Communication Using the Internet" by the Association of Chartered Certified Accountants (ACCA) Hong Kong. This is the sixth consecutive year that our reporting has won an ACCA award.

In addition, we won the Hang Seng Pearl River Delta Environmental Award organised by the Federation of Hong Kong Industries and Hang Seng Bank. The award recognised our efforts in protecting the environment and embracing sustainability through our launching of a series of initiatives, including energy saving programmes in stations, recycling of industrial rechargeable batteries, construction of noise barriers and sustainability reporting.

Care for the Community

The Company's vision has always been to grow with the communities that we serve. In this spirit, we launched many volunteering activities during the year and further expanded our established "art in mtr" programme, which stages cultural shows and exhibitions by local artists at stations to enhance the travelling experience. A community art and viaduct beautification programme for the Kwun Tong Line was completed in May, and temporary exhibitions were set up throughout 2008 at different MTR stations to promote the appreciation of art to our passengers. As the East Rail Line approaches its 100th birthday, a new architectural theme – "In touch with Nature" – was developed to guide major station improvement works in the future.

We continue to encourage MTR colleagues to take part in community service. During the year, there were 87 volunteering projects in our "More Time Reaching Community" scheme involving a total of 2,000 volunteers. In April, the fourth MTR HONG KONG Race Walking event was held in Central to encourage Hong Kong people to integrate regular exercise into their daily lives. The event raised HK$1.3 million for health education. Further community initiatives included a variety show presented by schoolchildren, the elderly and executives of the Corporation for 350 members of the Shek Kip Mei community, and our MTR Volunteers' participation in a rice dumpling delivery day to the lonely elderly. Once more, six social organisations nominated us for the Caring Company Logo 2008/09 in recognition of the Company's contributions to society through community involvement, staff volunteering and providing a safe and family friendly environment for our employees.

Natural disasters in the Mainland in 2008 were a severe blow to everyone. In February, we donated HK$1 million to the Hong Kong Red Cross to provide clothing and emergency supplies for the victims of the record snow falls in Central China, and HK$1 million to the All-China Federation of Railway Trade Unions to show our care and concern. In response to the tragic Sichuan earthquake in May, following an initial early donation of HK$1 million by the Company, MTR colleagues raised another HK$5.6 million, which was "dollar matched" in donation by the Company, bringing the total to HK$11.27 million. Moreover, our colleagues working in various offices in the Mainland raised a further RMB300,000, while in our shopping centres in Hong Kong, customers contributed an additional HK$2 million. Overall, donations from MTR Corporation, our employees and our customers reached more than HK$14.6 million for those struggling in the aftermath of the Sichuan earthquake.

The excellence of our Board governance, management and staff, the loyalty of our customers and the trust of our shareholders underpin the continuing successful performance of the Company.

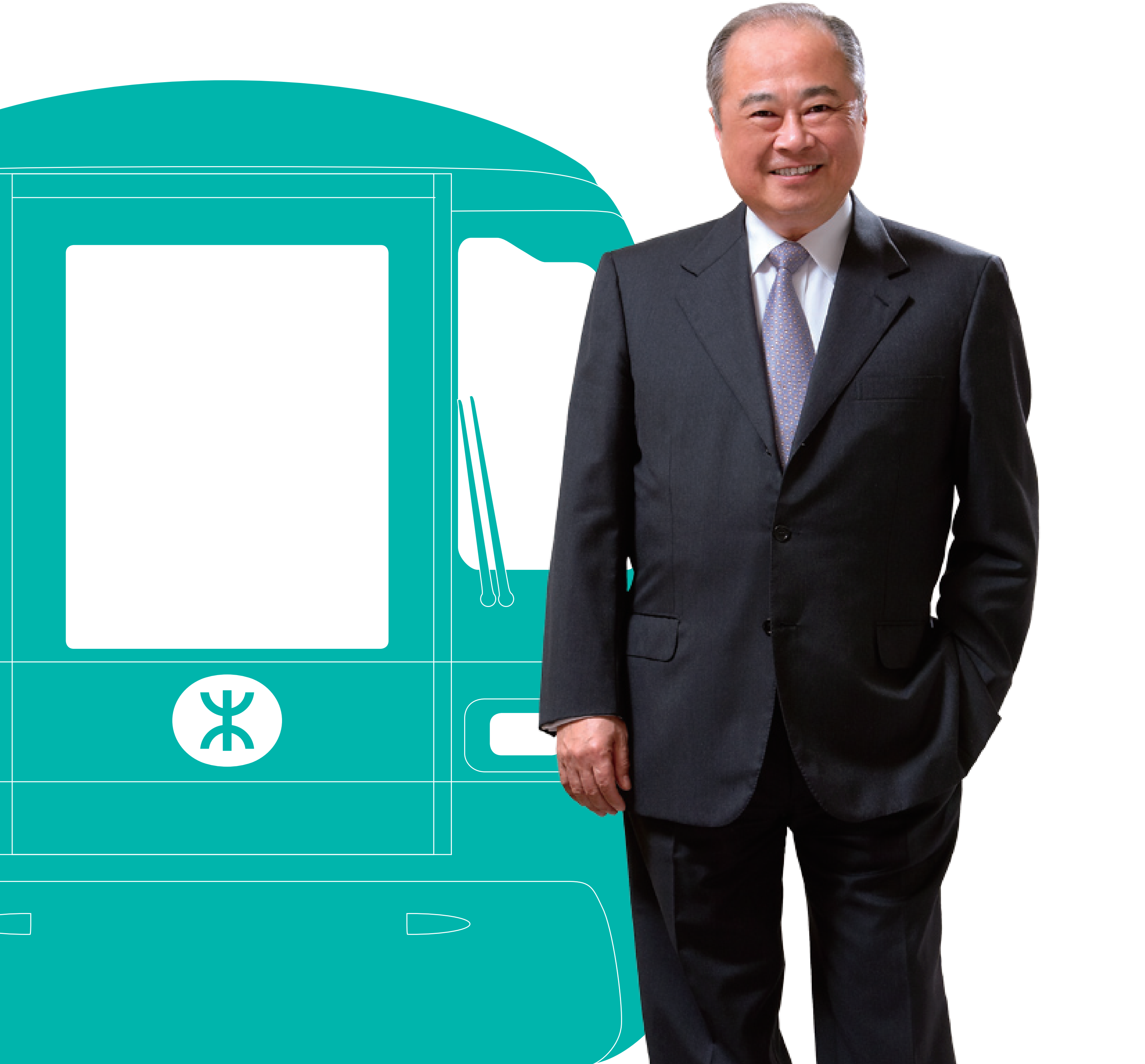
As we build on our legacy in the post-Rail Merger era, I would like to extend my warmest thanks to my fellow directors, our staff and all our stakeholders for their continued support in furthering our vision of sustainable growth. I would also like to express my gratitude to Professor Cheung Yau-kai, who will retire as an independent non-executive Director of the Company at our Annual General Meeting on 4 June 2009, for his significant contributions and long service to the Company.

Raymond K. F. Ch'ien

Dr. Raymond Ch'ien Kuo-fung, *Chairman,*
Hong Kong, 10 March 2009

CEO's Review of Operations and Outlook

"The Rail Merger was successfully implemented, and we have delivered on all of the promises we made to our stakeholders."



"With the strong financial results from our recurrent businesses, your Board has recommended a final dividend... brings the full year dividend to HK$0.48, an increase of 6.7% over 2007."

Dear Stakeholders,

I am pleased to report that 2008 was a successful year for the Company. The Rail Merger was successfully implemented, and we have delivered on all of the promises we made to our stakeholders. For our passengers, we pledged fare reduction, which was implemented immediately upon the Rail Merger, benefiting 2.8 million passengers. We promised job security for all of our front-line staff and this objective was achieved under the spirit of "One Company, One Team". We laid out a plan to integrate the two rail networks within one year of the Rail Merger. We have completed this plan through the physical integration of the three interchange stations in Kowloon Tong, Mei Foo and Nam Cheong in September 2008, more than two months ahead of schedule. For our shareholders, the Company's financial results in 2008 clearly demonstrate the benefits of the Merger. In addition, we have achieved synergies of over HK$350 million in 2008, ahead of schedule. The Rail Merger has made MTR Corporation a stronger company with the confidence to face the future.

After the Rail Merger, we turn our attention to growth. We forged ahead both in Hong Kong and overseas. In Hong Kong, the Government gave approval in March and April for the planning and design of the Shatin to Central Link, the Kwun Tong Line Extension to Whampoa and the Hong Kong section of the Guangzhou-Shenzhen-Hong Kong Express Rail Link (Express Rail Link). These new lines together with the West Island Line and South Island Line (East), for which approval to proceed with planning and design had already been given, mean that in total the Company has five new lines in various stages of development. Our efforts in the Mainland of China and Europe continued to expand, with progress being made on our projects in Beijing and Shenzhen as well as in London. Elsewhere, we also made progress with potential projects in Hangzhou and Shenyang and we were awarded the Stockholm Metro operating concession.

The Company's financial results for 2008 reflect the significant impact of the Rail Merger as we made a step change in our recurrent businesses of rail, station commercial, investment property and property management. Despite the less than favourable economic climate caused by the global financial turmoil, our revenue increased by 64.9% to HK$17,628 million. Operating profit from railway and related businesses before depreciation and amortisation rose by 57.7% to HK$9,325 million. On the other hand, property development profits in 2008 of HK$4,670 million were lower than in 2007 by HK$3,634 million due to the very significant development profits realised relating to Le Point in Tseung Kwan O in 2007. Hence excluding the change in fair value of investment properties and related deferred tax, net profit from underlying businesses attributable to equity shareholders was HK$8,185 million, a slight decline of 4.5% from 2007. Reflecting the overall downturn in the Hong Kong property market, investment property revaluation deficit for the year was HK$146 million (HK$99 million surplus net of deferred tax after accounting for the reduction in Hong Kong Profits Tax rate) compared to a revaluation surplus of HK$8,011 million in 2007 (HK$6,609 million net of deferred tax). Therefore, net profit attributable to equity shareholders was HK$8,284 million. The reported earnings per share were HK$1.45 before investment property revaluation and HK$1.47 after such revaluation. With the strong financial results from our recurrent businesses, your Board has recommended a final dividend of HK$0.34, which when combined with the interim dividend of HK$0.14 per share, brings the full year dividend to HK$0.48, an increase of 6.7% over 2007.

"In 2008, total patronage for all of our rail and bus passenger services (Integrated MTR System) increased by 56.6% to 1,485.1 million as compared to last year mainly due to the Rail Merger."

Operational Review

Hong Kong Railway Operations

Patronage

In 2008, total patronage for all of our rail and bus passenger services (Integrated MTR System) increased by 56.6% to 1,485.1 million as compared to last year mainly due to the Rail Merger. On a "like for like" basis, such passenger numbers would have increased by 3.6% when compared with the combined rail and bus patronage numbers of MTR Corporation and pre-merger Kowloon Canton Railway Corporation (KCRC) (as adjusted for interchange passengers) in 2007 (Comparable Combined Patronage).

Our Domestic Service, which includes the MTR Lines (comprising the Kwun Tong, Tsuen Wan, Island, Tung Chung, Tseung Kwan O and Disneyland Resort lines) and the KCR Lines (comprising the East Rail excluding Cross-boundary Service, West Rail and Ma On Shan lines), recorded total patronage of 1,205.4 million. This represents an increase of 31.6% when compared with 2007 and 4.0% when compared with the equivalent Comparable Combined Patronage.

For the Cross-boundary Service at Lo Wu and Lok Ma Chau, patronage was 93.4 million for 2008, representing an increase of 1.4% when compared with 2007 as a result of the growth in cross-boundary traffic.

Passengers using the Airport Express in 2008 rose 4.2% to 10.6 million when compared with the same period last year due to an increase in the market share of Airport Express despite a drop in number of travelers using Hong Kong International Airport, coupled with an increase in passengers going to and from AsiaWorld-Expo.

Passenger volume on Light Rail, Bus and Intercity was 175.6 million in 2008, an increase of 2.5% when compared with full year patronage of such services in 2007.

Market Share

Our overall share of the franchised public transport market rose to 42.7% in December 2008 as compared to 41.6% in the same month last year. Our share of cross-harbour traffic rose to 63.6% from 62.5% in 2007, and our share of traffic to and from the airport rose to 24% from 23% in 2007. However our market share in the Cross-boundary business declined to 56.2% from 57.0% in 2007 due to continued strong competition.

Fare Revenue

Total fare revenue was HK$11,467 million in 2008, which represents an increase of 61.2% over last year. Such fare revenue represents a slight decrease of 0.3% over the combined fare revenue of the rail and bus services of MTR Corporation and pre-merger KCRC in 2007 due to fare reductions given at the time of the Rail Merger.

Fare revenue of the Domestic Service was HK$7,930 million in 2008, which represents an increase of 27.6% over last year. However, compared with the combined fare revenue of MTR Lines and KCR Lines in 2007 (Combined Fare Revenue), there was a slight decline of 1.0% mainly as a result of the fare reduction implemented on the Rail Merger Day and the extension of student concession fares to the KCR Lines, which was partly offset by the increased patronage mentioned above.

Fare revenue of the Cross-boundary Service was HK$2,283 million in 2008, which represents an increase of 1.2% when compared with the equivalent 12-month revenue for such service in 2007. Fare revenue of the Airport Express was HK$673 million in 2008, which represents an increase of 2.7% over 2007.

Average fare per passenger for the Domestic Service in 2008 was HK$6.58, a decrease of 3.0% compared with that of 2007 due to the one-off fare reduction implemented on the Rail Merger Day. For Cross-boundary Service, average fare per passenger in 2008 was HK$24.45, a slight decrease of 0.2% when compared with 2007. For the Airport Express, average fare per passenger in 2008 decreased marginally by 1.4% to HK$63.47.

Attracting Patronage

In order to underpin patronage growth and to meet the high service levels expected by our customers, we continued to offer targeted promotions, as well as investing in service and efficiency improvements. Fare promotions included reduced fares for interchanging passengers from outlying island ferries as well as the extension of the student Concessionary Fare to cover the domestic services of East Rail, West Rail, Ma On Shan lines, Light Rail and MTR Bus. Special promotions were also offered to increase ridership for Cross-boundary Service and the Airport Express. To further enhance service, we brought into operation five 7-car new trains on the West Rail Line in the fourth quarter of 2008 as well as ordering an additional 10 new trains, to be delivered between 2011 to 2012, to increase train frequency on the existing Island, Kwun Tong, Tsuen Wan and Tseung Kwan O lines. Our intercity passengers also benefitted from the replacement of diesel-powered locomotives by electric-powered rolling stock on the Beijing/Shanghai-Kowloon Through Trains. We have renovated East Rail stations with the introduction of inspiring colours and graphics containing local heritage with better signage. This provides a refreshing ambience for our East Rail passengers.

Connectivity to our network was enhanced with additional pedestrian links and footbridges at Kowloon Bay and Sheung Wan stations. We also added seven more popular fare saver machines, bringing the total to 26 by the end of 2008.

Service Performance

With the Rail Merger, a new Operating Agreement was established to include the East Rail Line, West Rail Line, Ma On Shan Line and Light Rail. For the period from the Merger Date of 2 December 2007 to 31 December 2008, we exceeded all the performance levels required by Government and our own more stringent Customer Service Pledges targets. Train service delivery, passenger journeys on time and train punctuality were 99.7% or above. The high standard of our service performance levels delivered by our dedicated staff was again recognised in a large number of awards, including the Best Metro Asia Pacific Award at The Metro Rail 2008, Sing Tao Daily's Excellent Services Brand Award 2007 – Public Transportation Category, Next Magazine's "Top Service Award – Transportation Category" for the 10th consecutive year and the Bronze Award in the Customer Service Excellence Awards 2007 organised by the Hong Kong Association for Customer Service Excellence Limited. Ktt, which provides intercity passenger service between Hong Kong and Guangzhou, won the 2008 Prime Award for Brand Excellence in Cross Boundary Transportation Services organised by Prime Magazine.

Olympic Equestrian Event

A noteworthy event in the year was MTR Corporation's participation in the transportation of athletes, supporting personnel and spectators to the Equestrian Olympic venues in Hong Kong at Beas River and Shatin in August. Drawing on resources from across the Company, we ensured that passengers arrived at their venues safely, on time and in comfort.

Station Commercial and Rail Related Businesses

Revenue for our station commercial and rail related businesses in 2008 was HK$3,449 million, representing an increase of 98.1% over 2007. The increase would have been 33.4% over the comparable combined revenue of MTR Corporation and pre-merger KCRC for such businesses in 2007 (Combined Non-fare Revenue).

Revenue for our station retail business in 2008, comprising duty free shops and kiosk rental, was HK$1,546 million, representing an increase of 209.8% over 2007 (42.3% increase over the equivalent Combined Non-fare Revenue). This increase was mainly due to the inclusion of retail shops along the KCR Lines, particularly the 10 duty free shops serving Cross-boundary customers. Further growth was provided by increased new retail area and new rental contracts being awarded at higher rents. Although there were repossession of shops to facilitate renovation works, 45 renovated shops were completed at 9 stations and 18 new trades were added. The total number of shops as at 31 December 2008 was 1,186. Total area of station retail space at 31 December 2008 was 51,539 square metres.

Advertising revenue in 2008 was HK$741 million, representing an increase of 25.0% when compared with 2007 (11.3% increase over the equivalent Combined Non-fare Revenue). In addition to the merger benefits, there were higher advertising rates and more innovative advertising formats. New advertising formats included "The Galleria" launched in the lower adit of Causeway Bay Station in May and the Digital Escalator Crown Bank at Causeway Bay, Tsim Sha Tsui and Central stations, which is the first of its kind in Asia's metro.

Revenue from telecommunications services in 2008 was HK$356 million representing an increase of 49.0% when compared with 2007 (an increase of 27.6% over the equivalent Combined Non-fare Revenue). This increase was mainly due to a one-off payment received on termination of a telecommunication license. Excluding this one-off income, revenue would have increased by 13.0% to HK$270 million as compared to 2007 (3.2% decline compared with the equivalent Combined Non-fare Revenue).

Revenue from consultancy was HK$158 million during 2008, a decrease of 18.1% when compared with 2007, due to the more focused strategy on consulting services and the completion of the majority of works on Shanghai Metro Line 9 Phase 1, which opened in December 2007.

Property and Other Businesses

The Hong Kong property market performed strongly in the first half of 2008. Both office and retail markets enjoyed steady growth. However, with global credit market uncertainties developing into a global economic downturn, market activities slowed noticeably in the second half. Sale prices for residential units declined, and commercial rents started to consolidate.

Property Development

Profit on property development for 2008 was HK$4,670 million, a decrease of 43.8% when compared with that of HK$8,304 million in 2007. This is mainly due to the very significant development profits booking in 2007, particularly for Le Point in Tseung Kwan O. The major contributors to property development profit were from profit recognition relating to The Capitol at LOHAS Park and The Palazzo in Shatin as well as the sale of units from inventory at Harbour Green and The Arch. In addition, there was deferred income recognition, mainly from properties along the Airport Railway, such as Coastal Skyline and Caribbean Coast in Tung Chung Station, and Elements in Kowloon Station.

Property sales in the year included the pre-sale of all 2,096 units of The Capitol at LOHAS Park, about 80% or 1,100 units of the 1,375 units available at The Palazzo in Shatin and over 470 units at Le Bleu Deux in Tung Chung.

In our property tendering activities, the development package for Che Kung Temple on the Ma On Shan Line was awarded to a subsidiary of New World Development Company Limited (Deluxe Sign Limited) in April. Similar to LOHAS Park Package 1, The Capitol, we paid half of the land premium for this development in return for a larger share of profits. As agent for the West Rail Line property development, we awarded Tsuen Wan West Station TW7 Property Development to a subsidiary of Cheung Kong (Holdings) Limited (Queensway Investments Limited) in September.

"Total revenue from property rental, property management and other businesses in 2008 was HK$2,712 million, an increase of 47.9% over 2007."

Property Rental, Property Management and Other Businesses

Total revenue from property rental, property management and other businesses in 2008 was HK$2,712 million, an increase of 47.9% over 2007 (29.8% increase over the equivalent Combined Non-fare Revenue).

Demand for both office and retail space was strong in the first half of the year, but the rate of growth began to slow in the second half. Property rental income was HK$2,346 million, an increase of 48.4% over 2007 (28.8% increase over the equivalent Combined Non-fare Revenue). Visitors to the Company's retail centres remained strong throughout this year. The average increase in rental income of retail properties on renewal of leases or re-letting was 20% as compared to rental income achieved in the previous lettings.

We maintained close to 100% occupancy of our shopping centres. The Company's 18 floors at Two International Finance Centre were fully rented out.

At the end of December 2008, the Company's attributable share of investment properties was 221,661 square metres of lettable floor area of retail properties, and 41,059 square metres of lettable floor area of offices.

During the year, we continued to renovate our shopping centres to enhance their market appeal and competitiveness. Renovation works included the redevelopment of the cinema complex at Telford Plaza I. Our shopping centres were honoured with a variety of local and international awards. Elements, above Kowloon Station, won an international MIPIM award at the world's premier real estate summit in Cannes, France and the Urban Land Institute's 2008 Award for Excellence: Asia Pacific. The development was also named Project of the Year (Retail) in the Asia Pacific Real Estate Awards. Telford Plaza won the Prime Award for Eco-Business 2008 sponsored by Prime Magazine and the Hong Kong Service Award sponsored by East Weekly.

Ginza Mall, which opened in January 2007, continued to set new benchmarks for service and quality amongst shopping centres in Beijing. Average rental income increment for lease renewal and re-letting was 15% compared to 2007 and occupancy was 100%. The shopping centre received many awards and honours in its first full year of operation. These included being ranked No. 2 amongst the 156 major shopping centres and department stores in Beijing in a Customer Satisfaction Survey conducted by the Beijing Municipal Commerce Bureau.

Property management revenue in 2008 was HK$210 million, an increase of 25.0% over 2007 (a 15.4% increase over the equivalent Combined Non-fare Revenue). The number of residential units under our management totalled 73,947 as at the end of December, whilst commercial space under management was 770,556 square metres. Our managed property portfolio in the Mainland of China amounted to 1,158,254 square metres.

"Planning and design are underway for five new rail projects in Hong Kong, which together with the substantially completed Kowloon Southern Link, will extend our network by approximately 60 kilometres when they are all completed."

Octopus and Ngong Ping 360

Octopus performed strongly in 2008 with our share of Octopus' net profits increasing 40.2% to HK$136 million. The growth in profit was mainly due to continued increases in non-transport retail payments.

The Ngong Ping cable car and associated theme village on Lantau Island contributed HK$156 million of revenue in 2008, with visitor numbers reaching more than 1.6 million.

Future Growth

Hong Kong

Planning and design are underway for five new rail projects in Hong Kong, which together with the substantially completed Kowloon Southern Link, will extend our network by approximately 60 kilometres when they are all completed. These five new lines represent the most significant network expansion in the Company's history and will make a considerable contribution to our growth.

In March, the Government gave approval for the planning and design of the Shatin to Central Link and the Kwun Tong Line Extension. The Shatin to Central Link comprises two sections. The 11-km East West Corridor, expected to complete in 2015, will extend the Ma On Shan Line from Tai Wai to Hung Hom, via Diamond Hill, and will connect with the West Rail Line. The 6-km North South Corridor, expected to be completed in 2019, will form Hong Kong's fourth rail harbour crossing, extending the East Rail Line from Hung Hom to Hong Kong Island. The preliminary design started in September 2008 with a view to developing a scheme to be gazetted under the Railways Ordinance in late 2009.

The 3-km Kwun Tong Line Extension will run from the existing Yau Ma Tei Station of Kwun Tong Line to Whampoa via Ho Man Tin, which will be an interchange station with the East West Corridor of the Shatin to Central Link. The preliminary design started in June, and will be finished in early 2009. The project is expected to be completed in 2015.

In April, the Government asked the Company to proceed with the planning and design of the Express Rail Link, which will further enhance the strategic position of Hong Kong as the southern gateway to the Mainland of China. The 26-km Express Rail Link will provide cross-boundary high speed rail services connecting Hong Kong to Shenzhen, Guangzhou and the Mainland of China's new high speed intercity rail network. Trips to Futian in Shenzhen will take 14 minutes and to Guangzhou 48 minutes. The project was gazetted on 28 November 2008 and it is anticipated that construction will commence in late 2009 for completion by 2015.

Following the announcement of the Government's support for the planning and design of the South Island Line (East) in December 2007, preliminary design commenced in February 2008 and will be completed in early 2009. The final plan will be issued to Government for review and gazetting later in 2009.

The West Island Line was gazetted under the Railways Ordinance in October 2007. Frequent dialogue with, and input from local communities have led to a design that is sensitive to both local heritage and urban renewal opportunities for creating a "Community Railway". Detailed design commenced in early 2008, and construction is planned to commence in 2009 for completion in 2014.

In addition to the foregoing five new lines, satisfactory progress was made during 2008 on the Kowloon Southern Link, which incorporates the new Austin Station that will connect the existing East Rail Line's East Tsim Sha Tsui Station with West Rail Line's Nam Cheong Station. The main civil works, including the tunnel boring works, were substantially completed and the fitting out of the new Austin Station is rapidly approaching completion. The line is expected to open in the second half of 2009.

Phase 2 of the Tseung Kwan O Line is also on schedule for completion in the second quarter of 2009 to coincide with occupancy of The Capitol at LOHAS Park.

Hong Kong Project Funding

As noted previously, the funding model for all these new rail projects will take different forms, each appropriately designed for the project. For the West Island Line, which will use the capital grant model, we received the initial part of this grant of HK$400 million in February 2008 while the amount of the remaining portion, which forms the bulk of the total capital grant, is being discussed with Government.

The South Island Line (East) and the Kwun Tong Line Extension will likely follow the Company's traditional "Rail and Property" approach whereby property development rights will be granted to us. Suitable sites have been identified and negotiations with the Government on the development rights are continuing.

The Service Concession model used in the Rail Merger will be adopted for Kowloon Southern Link, Shatin to Central Link and the Express Rail Link. On this basis, the Finance Committee of the Legislative Council of Hong Kong (LegCo) approved an amount of HK$2.4 billion in May to be used for design and site investigation works for the Shatin to Central Link, and an amount of HK$2.8 billion in July for similar works for the Express Rail Link. On 24 November 2008, we entered into Entrustment Agreements with Government entrusting the Company to design the Shatin to Central Link and Express Rail Link with costs to be borne by Government. Further funding arrangements for construction of these two lines will be made by Government at the appropriate time. The construction of the Kowloon Southern Link is being funded by KCRC as part of the Rail Merger agreement.

Mainland of China and Overseas

Our projects in the Mainland of China and overseas continued to make good progress.

Mainland of China

In Beijing, the Public-Private-Partnership (PPP) company comprising MTR Corporation (49%), Beijing Infrastructure Investment Co. Ltd. (2%) and Beijing Capital Group (49%) is making steady progress with construction work on the Beijing Metro Line 4 (BJL4) project. BJL4 is expected to commence operation in the fourth quarter of 2009. The Company, together with our PPP company partners, also signed a Memorandum of Understanding (MOU) on 27 November 2008 with Beijing Metro Daxing Line Investment Company Limited, a wholly owned subsidiary of Beijing Municipal Government, for the operation and maintenance of the 22-km Daxing Line of the Beijing Metro Network. Discussions are ongoing on the Concession Agreement for Daxing Line.

In Shenzhen, approval for the Shenzhen Metro Line 4 (SZL4) project has been obtained from the National Development and Reform Commission. We are now completing final regulatory procedures for signing the Concession Agreement in the near future. Project works will be expanded to cover the whole line. Meanwhile, preparation works for taking over SZL4 Phase 1 are also underway.

We continue to seek investment opportunities in other cities in the Mainland of China.

After being selected as the "preferred bidder" in July 2008, the Company entered into a non-binding Principle Agreement in January 2009 for a PPP project with Hangzhou Municipal Government and Hangzhou Metro Group Company Limited for the investment, construction and operation of Hangzhou Metro Line 1 for 25 years. At the same time we also entered into a strategic agreement with the same parties to explore property development opportunities along the Hangzhou Metro lines. We moved forward in our discussions with the Shenyang Government on cooperation in the operation of the 50-km Shenyang Metro Lines 1 and 2 and possible investment in future lines by entering into non-binding Agreements in Principle with Shenyang Municipal Government and Shenyang Metro Group Company Limited in November 2008. In addition, a further non-binding agreement was entered into to plan and explore property development opportunities along the Lines 1 and 2 alignment. Discussions in Hangzhou and Shenyang on Concession Agreements are now progressing.

Europe

In the UK, our 50:50 joint venture London Overground Rail Operations Limited (LOROL) brought steady improvements to London Overground following the takeover of the concession in November 2007. Operational performance has been enhanced and 31 stations have undergone station upgrading works.

In Sweden, we submitted our bid for the Stockholm Metro concession in August 2008 and in January 2009, we were awarded the eight-year concession rights to operate the 108–km long, 100-station system.

Financial Review

With the full-year effect of the Rail Merger, the Group achieved strong growth in revenue and operating profits from recurrent businesses in 2008. Total fare revenue increased by 61.2% to HK$11,467 million, comprising HK$7,930 million from Domestic Service, HK$2,283 million from Cross-boundary Service, HK$673 million from the Airport Express and HK$581 million from Light Rail, Intercity and Bus. Non-fare revenue increased by 72.3% to HK$6,161 million with HK$3,449 million from station commercial and rail related businesses and HK$2,712 million from property rental, management and other businesses. Total revenue for 2008 therefore increased by 64.9% to HK$17,628 million, and total operating costs for 2008 rose by 73.8% to HK$8,303 million. Operating profit from railway and related businesses before depreciation and amortisation increased by 57.7% to HK$9,325 million whilst operating margin decreased from 55.3% in 2007 to 52.9% in 2008 due to fare reduction at the time of the Rail Merger as well as the lower margin of the pre-merger KCRC businesses.

Owing to the significant property profit recognition from Le Point in Tseung Kwan O in 2007 and the decline in property prices in the latter part of 2008, property development profits decreased by 43.8% to HK$4,670 million in 2008, mainly comprising profits from The Capitol and The Palazzo. Operating profit before depreciation and amortisation therefore decreased slightly by 1.6% to HK$13,995 million. Depreciation and amortisation increased by 7% to HK$2,930 million mainly due to the Rail Merger while merger related expenses decreased by 72.5% to HK$53 million. Interest and finance charges increased by 51.8% to HK$1,998 million, mainly due to interest on debt taken on for the Rail Merger and the notional interest expense on the capitalised fixed annual payments for the Rail Merger. MTR's share of profits from Octopus Holdings Limited and London Overground Rail Operations Ltd totalled HK$159 million. A non-cash revaluation deficit of HK$146 million was recorded for investment property versus a large gain of HK$8,011 million in 2007. Including the above, the reported profit before tax decreased by 50.6% from 2007 to HK$9,027 million.

With the decrease in profits and the deferred tax impact from the reduction in profits tax rate from 17.5% to 16.5%, income tax decreased by 75.8% to HK$747 million. Reported profit attributable to shareholders of the Company in 2008 therefore decreased by 45.4% to HK$8,284 million, or HK$1.47 per share as compared with HK$2.72 in 2007.

"Cash flow of the Group in 2008 was strengthened by the Rail Merger with net cash inflow from railway and related businesses increasing by 49.3% to HK$8,921 million."

Excluding investment property revaluation, the more representative net profit from underlying business attributable to shareholders of the Company decreased by 4.5% to HK$8,185 million, or HK$1.45 per share as compared with HK$1.54 in 2007. As stated earlier, this is the result of strong growth of profit from our recurrent businesses but lower property development profit when compared with the previous year.

The Group's balance sheet showed a 7.5% increase in net assets from HK$91,037 million as at 31 December 2007 to HK$97,822 million as at 31 December 2008. Total assets increased from HK$155,668 million to HK$159,338 million mainly attributable to increases in accounts receivable and properties held for sale relating to property development as well as investments in new railway projects both in Hong Kong and the Mainland of China. Total liabilities decreased from HK$64,631 million in 2007 to HK$61,516 million mainly due to reduced loans outstanding and deferred income. Including obligations under the service concession as a component of debt, the Group's net debt-to-equity ratio improved from 48.5% at 2007 year end to 42.1% at 2008 year end.

Cash flow of the Group in 2008 was strengthened by the Rail Merger with net cash inflow from railway and related businesses increasing by 49.3% to HK$8,921 million. Receipts from our property development business were HK$4,448 million. The Group also received HK$400 million of government grant for the West Island Line project as well as HK$132 million of loan repayments and dividend distribution from its non-controlled subsidiaries and associates. Total cash outflows, excluding the non-recurrent merger-related payments, increased by 88% to HK$9,887 million primarily due to new railway projects, increases in capital expenditures on the expanded railway network after the Rail Merger, payment for the half land premium for the Che Kung Temple property development as well as the fixed annual payment for the service concession. Therefore net cash inflow of HK$3,698 million was generated in 2008, which was used mainly to reduce debt.

The Board has recommended a final dividend of HK$0.34 per share, which, when added to the interim dividend of HK$0.14, will give a total dividend of HK$0.48 per share for the year, representing an increase of HK$0.03 or 6.7% as compared to last year. As in previous years, the Financial Secretary Incorporated has agreed to receive its entitlement to dividends in the form of shares to the extent necessary to ensure that a maximum of 50% of the Company's total dividend will be paid in cash.

Human Resources

The success of the Company is based on the commitment, professionalism and caring services of our staff. In the post-Rail Merger era, our goal is to create a culture of "One Company, One Team", so the new grading and salary structure together with aligned terms and conditions of our 12,000 Hong Kong staff were implemented across the entire organisation on 1 March 2008. The entire selection and appointment process was completed in April.

To meet post-Rail Merger challenges, a broad range of training and development programmes was undertaken throughout the year, particularly in the areas of railway safety, railway operations and maintenance, multi-skilling, redeployment and new recruits. In addition, Mainland local recruits for BJL4 and SZL4 were given comprehensive training with job attachment in Hong Kong to ensure operational readiness of these two key new projects. We continued to develop management and leadership quality for the future of the Company with major ongoing programmes such as our Executive Associate Scheme and a Graduate Trainee Programme with graduates from both Hong Kong SAR and the Mainland of China.

With the expansion of the railway network in Hong Kong, substantial manpower resources are required for the planning, construction and operations of these new lines. An intensive Human Resources planning and recruitment programme has commenced in 2008 to address these needs and is making good progress.

Outlook

Economic conditions globally and in Hong Kong remain uncertain with forecasts of negative economic growth in Hong Kong for 2009. Given these conditions, we are taking a cautious approach to 2009.

Our rail business is by nature defensive. It is, however, sensitive to the level of unemployment. We will benefit from incremental increase in passengers with the opening of Kowloon Southern Link and the Tseung Kwan O Line extension to LOHAS Park. Review of fares will be subject to the provisions of the Fare Adjustment Mechanism in July 2009. It should be noted that according to the agreed mechanism, if the calculated adjustment percentage is within ± 1.5%, no adjustment will take place in that year but the adjustment percentage will be carried forward to the next year. Our advertising business is more sensitive to economic conditions and together with the non-recurrence in 2009 of the one-off telecommunication termination revenue in 2008, will make 2009 a more challenging year for these two businesses.

Our station commercial and property rental businesses will be affected by rental renewals and reversions, which will be market dependent.

In our property development business, the second half of 2009 should see the issuance of the Occupation Permit for Phase 1 of LOHAS Park Package 2 comprising 1,688 units. As profit sharing for this property is based on "sharing in kind" , irrespective of sales, it will be accounted for based on the market value of those Phase 1 units due to MTR Corporation on the date of issuance of the Occupation Permit less the deemed interest subsidy on the interest free loan to the developer.

The launch of sales at Lake Silver at Wu Kai Sha and Tai Wai Maintenance Centre will be subject to a commercially driven decision dependent on the market and other considerations.

Our growth business will see a number of milestones in 2009. In Hong Kong, the Tseung Kwan O Line extension opens in mid-2009 and Kowloon Southern Link opens in the second half. In the Mainland of China, BJL4 will commence operations in the fourth quarter of 2009 while in Stockholm, we expect to take over the franchise in November 2009.

Given all the economic uncertainties we continue our focus on cost containment, and maintaining a strong cash flow.

Finally, I would like to take this opportunity to thank my fellow directors and all my 14,000 colleagues for their energy and dedication over the past year. They are the heroes of MTR.

C K Chow, *Chief Executive Officer*
Hong Kong, 10 March 2009

Key Figures

	2008	2007#	% Increase/ (Decrease)
Financial Highlights *in HK$ million*			
Revenue			
– Fare	**11,467**	7,115	61.2
– Non-fare	**6,161**	3,575	72.3
Operating profit from railway and related businesses before depreciation and amortisation	**9,325**	5,912	57.7
Profit on property developments	**4,670**	8,304	(43.8)
Operating profit before depreciation and amortisation	**13,995**	14,216	(1.6)
Profit attributable to equity shareholders	**8,284**	15,180	(45.4)
Profit attributable to equity shareholders (excluding change in fair value of investment properties and related deferred tax)	**8,185**	8,571	(4.5)
Total assets	**159,338**	155,668	2.4
Loans, other obligations and bank overdrafts	**31,289**	34,050	(8.1)
Obligations under service concession	**10,656**	10,685	(0.3)
Total equity attributable to equity shareholders	**97,801**	91,014	7.5
Financial Ratios *in %*			
Operating margin	**52.9**	55.3	-2.4% pts.
Net debt-to-equity ratio	**42.1**	48.5	-6.4% pts.
Return on average equity attributable to equity shareholders	**8.8**	18.1	-9.3% pts.
Return on average equity attributable to equity shareholders (excluding change in fair value of investment properties and related deferred tax)	**8.7**	10.2	-1.5% pts.
Interest cover *in times*	**6.0**	9.0	-3.0 times
Share Information			
Basic earnings per share *in HK$*	**1.47**	2.72	(46.0)
Basic earnings per share (excluding change in fair value of investment properties and related deferred tax) *in HK$*	**1.45**	1.54	(5.8)
Dividend per share *in HK$*	**0.48**	0.45	6.7
Share price at 31 December *in HK$*	**17.96**	28.70	(37.4)
Market capitalisation at 31 December *in HK$ million*	**101,674**	161,037	(36.9)
Operations Highlights			
Total passenger boardings			
– Domestic Service *in millions*	**1,205.4**	915.8	31.6
– Cross-boundary Service *in thousands*	**93,401**	8,243	1,033.1
– Airport Express *in thousands*	**10,601**	10,175	4.2
– Light Rail *in thousands*	**137,730**	11,100	1,140.8
Average number of passengers *in thousands*			
– Domestic Service *weekday*	**3,514**	3,364*	4.4
– Cross-boundary Service *daily*	**255.2**	252.3**	1.1
– Airport Express *daily*	**29.0**	27.9	3.9
– Light Rail *weekday*	**385.1**	378.6**	1.7
Fare revenue per passenger *in HK$*			
– Domestic Service	**6.58**	6.78	(2.9)
– Cross-boundary Service	**24.45**	24.45	–
– Airport Express	**63.47**	64.34	(1.4)
– Light Rail	**2.81**	2.68	4.8
Proportion of franchised public transport boardings (December)^ *in %*	**42.7**	41.6	1.1% pts.

Before the Rail Merger on 2 December 2007, the Company's rail operations comprised MTR Lines and Airport Express. After the Rail Merger, our Domestic Service comprised MTR Lines and KCR Lines (East Rail Line excluding Cross-boundary, West Rail Line and Ma On Shan Line). Also after the Rail Merger we gained new passenger services for Cross-boundary Service, Light Rail, Bus and Intercity.

* Comparable combined passenger number of the Company and KCR Lines (as adjusted for interchange passengers).

** Passenger number for the full year of 2007 including pre-merger KCR operations

^ Proportions of franchised public transport boardings for the full year of 2008 and 2007 are 42.0% and 26.7% respectively.

Key Events in 2008

January

The Company won the Bronze Award in The Hong Kong Association for Customer Service Excellence Limited's "Customer Service Excellence Award 2007".

February

The Company donated HK$1 million to provide warm clothing and other emergency supplies via the Hong Kong Red Cross for the victims of the snowstorm in the Mainland of China.

The Company was recognized as a Sustainability Leader within the global travel and tourism industry sector, and won a Silver Class Award from SAM (Sustainable Asset Management).

Pre-sales of all the 2,096 units at The Capitol, Package 1 of the LOHAS Park development.

March

The Government requested the Company to proceed with the further planning and design for the Shatin to Central Link and Kwun Tong Line Extension to Whampoa, marking an important milestone for railway development in Hong Kong.

The Company was awarded the Hong Kong Service Awards 2008 – Transportation Category and Corporate Social Responsibility Award by East Week Magazine in recognition of its excellence service and contribution to sustainable development of Hong Kong. The Company was for the second year awarded the Sing Tao Daily Excellent Services Brand Award – Public Transportation Category.

April

The Company announced the award of the Che Kung Temple Station Development project to Deluxe Sign Limited, a subsidiary of New World Development Company Limited.

The Company was selected as the best metro in Asia Pacific at "The MetroRail 2008 Awards" held in Copenhagen, Demark.

Co-organised by the Company and the Hong Kong Amateur Athletic Association, the 4th annual "MTR HONG KONG Race Walking" event took place on 20 April 2008 with record number of participants and donations for health education.

The Government requested the Company to proceed with further planning and design for the Hong Kong section of the Guangzhou-Shenzhen-Hong Kong Express Rail Link, which will enhance the strategic position of Hong Kong as the southern gateway of China.

Austin Station on the new Kowloon Southern Link was topped out in April.

May

Pre-sales of about 80% of the 1,375 units at The Palazzo, a property development in Shatin.

The Company donated HK$1 million to help Sichuan earthquake victims through the Liaison Office of the Central People's Government in the Hong Kong SAR.

June

Following an initial donation of HK$1 million by the Company to help the Sichuan earthquake victims to buy essential supplies, our staff raised another HK$5.6 million, which was "dollar matched" in donation by the Company, bringing total donations to HK$11.27 million.

The Company once again won the Next Magazine's "Top Service Award – Transportation Category" for the 10th consecutive year.

July

Elements, our flagship shopping centre in Hong Kong, won the Urban Land Institute's 2008 Award for Excellence: Asia Pacific.

To celebrate the 10th Anniversary of the Airport Express on 6 July, the Company launched souvenir tickets and the THOMAS & FRIENDS Live! On Stage Theme Train activity.

August

As a Beijing 2008 Olympic Games Equestrian Events Railway Passenger Services Associate, the Company provided safe, reliable and convenient train services to local and overseas guests visiting the HK Olympic venues in Shatin and Sheung Shui.

Wi-Fi service become first available on Airport Express in-train to provide value-added services and conveniences to frequent travelers.

The Company launched the Digital Escalator Crown Bank at Causeway Bay Station, which is the first of its kind in Asia's metro.

September

As agent of Tsuen Wan West TW7 Property Development Limited, the Company announced that Queensway Investments Limited, a subsidiary of Cheung Kong (Holdings) Limited, won the tender for the West Rail Tsuen Wan West Station TW7 Property Development.

The Company launched the trial of the integrated single journey fare system for the entire network, thus enabling single journey ticket holders to enjoy fare discounts of 9% to 30%.

The Company won the Prime Magazine's "Prime Awards for Brand Excellence 2008 – Transportation Category" for the third consecutive year. The award reconfirmed our outstanding performance in corporate culture, image and brand development.

October

The MTR Annual Report 2007 received the "Best of Hong Kong" Award in the 22nd International ARC Awards, the largest annual report design competition in the world.

The Company won three awards at the legal "Oscars" – the "ALB Hong Kong Law Awards 2008" – in recognition of outstanding professional achievement and major deals in the Hong Kong legal industry.

November

The Company's commitment to continuous learning and improvement was recognised by the "Best Practice Award-Training & People Development" from the Hong Kong Best Practice Management Group.

The Company's 2007 Sustainability Report, *Building Capability* won the "Commendation for Excellent Communication Using the Internet" by the Association of Chartered Certified Accountants (ACCA) Hong Kong. It was the sixth consecutive year that the Company received an ACCA award.

The removal of 100 interchange ticket gates at Kowloon Tong, Mei Foo and Nam Cheong stations was completed on 10 November, marking the final milestone in the Rail Merger integration process.

The Company signed an Agreement in Principle with Shenyang Municipal Government and Shenyang Metro Group Company Limited for the operation and maintenance of Shenyang Metro Lines 1 & 2 for a term of 30 years.

The Company together with our joint venture partners in Beijing, Beijing Infrastructure Investment Company Limited and Beijing Capital Group Company Limited signed a Memorandum of Understanding with Beijing Municipal Government for the operation and maintenance of the Daxing Line of the Beijing Metro Network.

The Company won the "Hong Kong Corporate Branding Awards 2008 – Consumers' Choice Grand Prize (Transportation & Logistics)" organized by Ming Pao Daily News and MSC Marketing Programme of The Chinese University of Hong Kong for the second year.

On 24 November, the Company entered into Entrustment Agreements with the Government entrusting the Company to design the Shatin to Central Link and the Express Rail Link with costs to be borne by Government.

December

After having a six-month evaluation on the share of market, brand loyalty and global leadership of more than 1,000 well-known Hong Kong brands by the World Brand Laboratory ("WBL"), the Company has been awarded as one of the "Hong Kong's 100 Most Influential Brands" in December.

More than 100 senior citizens took a special train on the West Rail Line on 3 December on the first anniversary of the Rail Merger. It formed part of the annual Elderly Programme jointly organised by the Company and RTHK Radio 5 to promote railway safety awareness to elderly passengers.

Building on **Service Quality**

A Broader, More Efficient Network

MTR Corporation is the leading public transport operator in Hong Kong.

Hong Kong Railway Operations

Total fare revenue for the Company in 2008 increased by 61.2% to HK$11,467 million, largely due to increased patronage as a result of the Rail Merger. Such fare revenue also represents a slight decrease of 0.3% over the combined fare revenue of the rail and bus services of MTR Corporation and pre-merger KCRC in 2007 due to the fare reduction as a result of the Rail Merger.

The Rail Merger

The integration of the rail operations of ex-MTR and ex-KCRC has progressed well since the Rail Merger date on 2 December 2007. In 2008, the two key focuses were achievement of synergies and completion of the "Day 2" changeover.

We are continuing to achieve merger synergies through continuous efforts on energy optimisation, development of combined procurement to create scale, revenue maximisation resulting from the expanded network and staff cost rationalisation. We are confident of reaching the target synergy of HK$450 million per annum that we have indicated would take three years to realise following the Rail Merger.

The "Day 2" changeover began with the trial for the Integrated Single Journey Ticket Automatic Fare Collection (AFC) System, which was launched on 28 September. Single journey ticket passengers were able to enjoy reduced fares and travel within the whole MTR network using only one ticket, with the interchange ticket gates remaining in place when such passengers interchanged between the pre-merger MTR and pre-merger KCR systems at Kowloon Tong, Mei Foo and Nam Cheong stations. Also on 28 September, the Student Concessionary Fare promotion, which enables eligible students to enjoy fare concessions of up to 50% off normal fares, was extended to cover the domestic service of East Rail, West Rail and Ma On Shan lines, Light Rail and MTR Bus (except Airport Express, journeys to or from Lo Wu and Lok Ma Chau stations and travel on first class of East Rail Line). Seven wall openings were created on the platform level of Nam Cheong Station to facilitate a convenient new cross-platform interchange for passengers from Hong Kong bound Tung Chung Line trains to the Tuen Mun bound West Rail Line. To ensure smooth integration of the two different Single Journey AFC systems, more than 150,000 regularly used fare combinations were used to test software applications to confirm that proper fares were deducted.

With the successful completion of the trial, the progressive removal of 100 interchange ticket gates at the three interchange stations was completed by 10 November 2008. More than 150 Customer Service Ambassadors wearing yellow T-shirts were readily available to assist passengers to adapt to changes in the station layout at Kowloon Tong, Mei Foo and Nam Cheong stations. The successful completion of the "Day 2" changeover marked a key milestone in the final chapter of the Rail Merger.

42.7% Share of Franchised Public Transport Market
in December 2008

3.5 Million Average Weekday Patronage
For Domestic Services in 2008

HK$7.72 Average Fare
Per Passenger for All Services in 2008

HK$4.02 Operating Costs
Per Passenger for All Services in 2008

99.9% Passenger Journeys On Time

Patronage

For the year as a whole, total patronage on the Integrated MTR System increased by 56.6% to 1,485.1 million as compared to last year, due mainly to the Rail Merger. On a "like for like" basis such passenger numbers would have increased by 3.6% when compared with combined rail and bus patronage numbers of MTR Corporation and pre-merger KCRC in 2007 (Comparable Combined Patronage).

Our Domestic Service, which includes the MTR Lines (comprising the Kwun Tong, Tsuen Wan, Island, Tung Chung, Tseung Kwan O and Disneyland Resort lines) and the KCR Lines (comprising the East Rail excluding Cross-boundary Service, West Rail and Ma On Shan lines), recorded total patronage of 1,205.4 million for 2008, an increase of 31.6% when compared with 2007. Comparable Combined Patronage increased 4%, mainly due to the fare reduction implemented on the Rail Merger Day as well as the added convenience in the integrated rail system.

For the Cross-boundary Service at Lo Wu and Lok Ma Chau, patronage was 93.4 million for 2008, representing an increase of 1.4% increase when compared with full year Cross-boundary Service patronage in 2007 as a result of the growth in cross-boundary traffic.

Passengers using the Airport Express rose 4.2% to 10.6 million in 2008 due to an increase in air travellers using Airport Express to the Airport despite a slight drop in air passengers coupled with more passengers going to and from the AsiaWorld-Expo.

Passenger volume on Light Rail, Bus and Intercity was 175.6 million in 2008, an increase of 2.5% when compared with full year patronage of such services in 2007.

Overall, average weekday patronage for all rail and bus passenger services on the Integrated MTR System was 4.3 million in 2008, an increase of 4.1% over the equivalent Comparable Combined Patronage . Average weekday patronage for the Domestic Service in 2008 was 3.5 million, representing a rise of 4.4% over the equivalent Comparable Combined Patronage.

Our overall share of the franchised public transport market rose from 41.6% for December 2007 after the Rail Merger to 42.7% for December 2008. Our share of cross-harbour traffic rose to 63.6% from 62.5% in 2007 and our share of traffic to and from the airport rose to 24% from 23% in 2007. However our market share in the Cross-boundary business declined to 56.2% from 57.0% in 2007 due to continued strong competition.

Fare Revenue

Total fare revenue in 2008 was HK$11,467 million, an increase of 61.2% over 2007 due to the Rail Merger. However, such fare revenue also represents a slight decrease of 0.3% over the combined fare revenue of the rail and bus services of MTR Corporation and pre-merger KCRC in 2007 due to fare reductions given on the Rail Merger Day.

Fare revenue in 2008 of the Domestic Service was HK$7,930 million, an increase of 27.6% over last year because of the Rail

Airport Express continues to attract new passengers.

Merger. However, compared with the combined fare revenue of MTR Lines and KCR Lines in 2007 (Combined Fare Revenue), there was a slight decline of 1.0% mainly as a result of the fare reduction implemented on the Rail Merger Day, which was partly offset by the increased patronage mentioned above. Fare revenue contribution from the Cross-boundary Service in 2008 was HK$2,283 million, an increase of 1.2% when compared with the equivalent 12 month revenue for such service in 2007. Fare revenue of the Airport Express in 2008 was HK$673 million, an increase of 2.7% over 2007.

Average fare per passenger in 2008 for the Domestic Service was HK$6.58, a decrease of 3.0% compared with that of 2007 (a decrease of 4.8% when compared with the weighted average fares of MTR Lines and KCR Lines of HK$6.91, as adjusted for interchange passengers for the same period last year). The decrease was again due to the one-off fare reduction implemented on the Rail Merger Day. Average fare per passenger in 2008 for Cross-boundary Service was HK$24.45, a slight decrease of 0.2% when compared with the equivalent comparable average fare in 2007. For the Airport Express, average fare per passenger in 2008 decreased slightly by 1.4% to HK$63.47.

Service Promotions

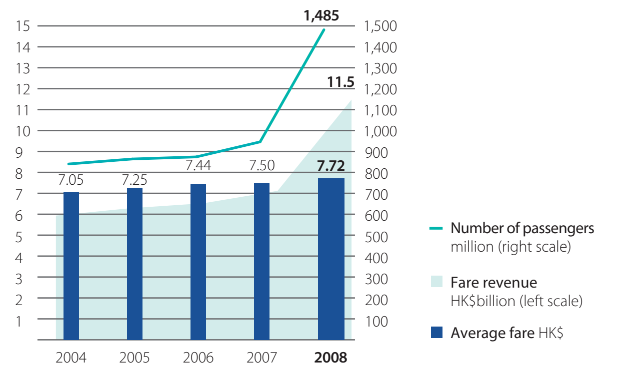
The Company's highly effective service promotions have been a key driver for incremental patronage growth while also increasing brand awareness and demonstrating our commitment to meeting customers' high service expectations.

In line with this commitment, a campaign "Serving you with joy and care" was launched from June to August, which was supported by TV commercials, print adverts and advertorials in newspapers and magazines, as well as station decorations. A "Smiling Photo Booth" was set up in Hong Kong Station for three consecutive weekends, where cheerful ambassadors took photos of passengers and played interactive games with them. To offer our customers a comfortable, cheerful and relaxing journey on the MTR, a specially designed "Happy Train" ran on the Tsuen Wan Line from June to August.

A variety of programmes were introduced to show the dedication of the Company to building a better community. We introduced an "Ecology and Heritage Study Project" to encourage primary students to preserve and love the environment, and a "Be my Courteous Hong Kong Video Shooting Competition" aimed to promote good behaviour and

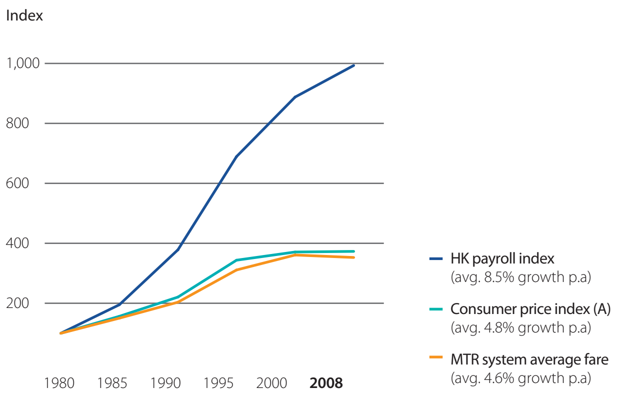
Passengers and Fares

Total fare revenue and patronage rose due to the Rail Merger.



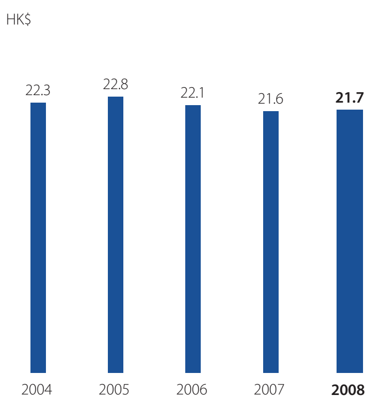
Fare Trend

In recent years, MTR fares have consistently lagged wage growth but were in line with the long-term changes in consumer prices in Hong Kong.



Railway Operating Costs Per Car-km Operated

Operating costs per car-km were maintained at a low level.



The extended network connects to new catchment areas.

good manners through a video competition for secondary and post-secondary students. A joint promotion with Hong Kong Wetland Park offered discount admission and free rides on Light Rail and MTR Bus in the Northwest New Territories, encouraging the general public to visit the park to learn about wetlands and the various habitats.

A new passenger behaviour campaign was launched in May to promote good manners and behavior in our network. As a symbol of "doing better for others", passengers were encouraged to make rabbits out of origami papers that carried good behavior messages. They then gave the origami rabbits to their friends to pass on the message. The origami papers were also distributed in kindergartens and primary schools by the Hong Kong Education Bureau.

Further promotions included a new bonus point scheme for the MTR Club, a "Love Our Site" blog campaign on the MTR Club website, and a "Most Cheerful Station Staff Election", which attracted 20,000 votes in two weeks. At the award presentation ceremony held in July, 81 winning staff received the "Most Cheerful Station Staff Award".

During the summer, to encourage visitors to explore the diversity of Hong Kong by using the MTR network, we joined hands with the Hong Kong Tourism Board to promote a Hong Kong Summer Temptations campaign. Two tourist guidebooks with the theme of "Explore Hong Kong by MTR" and "Hong Kong Train Tour" were developed and distributed in Hong Kong and over 30 cities in the Mainland of China.

The Airport Express's 10th Anniversary was celebrated with various initiatives, including a "Children Travel Free" promotion in July and August to boost patronage from family travel. We continued to offer a 34% discount on the Airport Express Single Journey to our shareholders as well as a number of privileges to Ride-to-Rewards members.

Fare promotions continued to be a major tool to attract walk-in passengers. In July and for a period of six months, we introduced fare savers for interchange passengers from outlying island ferries. Our Student Concessionary Fare was extended to East Rail, West Rail and Ma On Shan lines domestic services from late September, allowing eligible students to enjoy a 50% reduction in adult fares throughout our network. Other fare promotion offers included a Monthly Pass for frequent travellers on the East Rail and West Rail lines.

Service Connectivity

Enhanced connectivity with other forms of transport helps drive MTR patronage growth. In our East Rail feeder bus service, to replace aging Leyland Olympian buses, the first batch of nine new Alexander Dennis Dart Enviro 200 buses fitted with low-emission Euro IV engines and a super-low floor design was put into service in April. Another four were delivered in February

2009, with the final batch of 15 double-deckers scheduled for delivery in the second quarter of 2009. The first two of 11 similar buses to replace the aging Mitsubishi single-deckers were put into revenue service on the North West New Territories feeder bus route in September. By the end of the year, 70% of the total bus fleet comprised super-low floor design buses.

New pedestrian links and entrances at various stations were opened, including a footbridge connection at Kowloon Bay Station connecting to Choi Ying Estate and a new integrated entrance at Sheung Wan Station linking to Vicwood Plaza.

Market Recognition

Our efforts in marketing, branding and enhancing passenger awareness continued to be widely recognised. Our TV commercial "Morning Congestion" launched in 2007 to encourage the passengers to travel before the morning peak hours won the UITP "Golden Cinérail for Advertising Film" in the 2008 Cinérail Film Festival. For the second consecutive year, we won the "Category Award of Public Transportation" in the Sing Tao Excellent Services Brand Award 2007 and we also won the "Prime Award for Eco-Business 2008" for our outstanding performance in environmental protection. The print advertisement for the Rail Merger was selected as one of the three "Best Integrated" adverts of the year in the Metro Creative Awards 2008 held by Metropolis Daily, while our Rail Merger TV commercial jingle won the "Most Popular Jingle" in the TVB Most Popular TV Commercial Awards 2008.

Service Performance

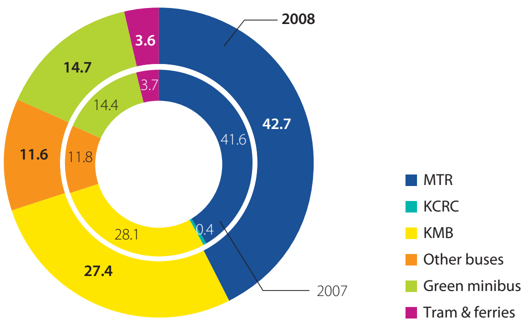
In an era of rapid changes and intense competition, a culture of continuous improvement is essential for the growth of our business. In 2008, we continued to enhance our customer services to provide the highest standards of passenger comfort, reliability and safety.

With the Rail Merger, a new Operating Agreement came into effect from 2 December 2007 to include the East Rail Line, West Rail Line, Ma On Shan Line and Light Rail. For the period from 2 December 2007 to 31 December 2008, we exceeded all the performance levels required by Government and our own more stringent Customer Service Pledges targets. Train service delivery, passenger journeys on time and train punctuality were 99.7% or above.

Market Shares of Major Transport Operators in Hong Kong (December only)

MTR's overall market share increased to 42.7% for December 2008 from 41.6% for December 2007 after Rail Merger.

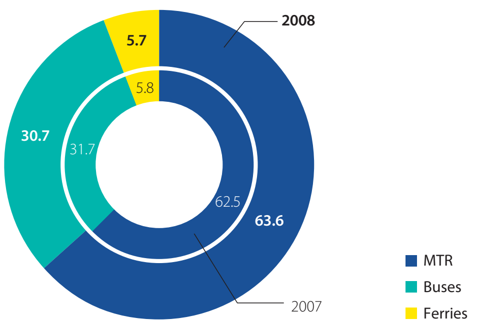
Percentage



Market Shares of Major Transport Operators Crossing the Harbour (December only)

The Company's market share of cross-harbour traffic rose to 63.6%.

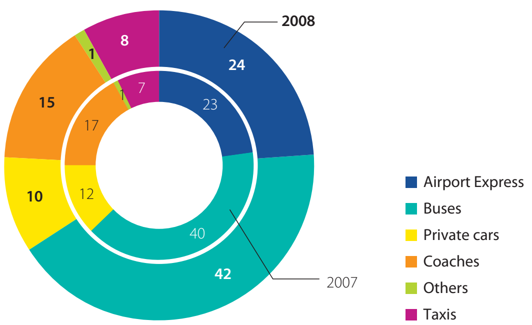
Percentage



Market Shares of Major Transport Operators to/from the Airport

The proportion of people travelling to and from the Hong Kong International Airport on MTR increased.

Percentage



Safety and maintenance are paramount.

Training in 2008 focused on rules and safety qualifications in preparation for the launch of the new Railway Safety Rules for the merged Railway, with a total of 7,000 operations staff and 2,500 contractors trained. Other training initiatives supporting post-merger operations included staff redeployment, multi-skilling and roster alignment. In terms of safety, a train door safety campaign was launched along with an escalator safety campaign in May and August respectively, while November was nominated Safety Month. Other measures included the tightening of controls on the conveyance of potable spirits and chemical cargoes on East Rail Line. During the Beijing Olympic Games period, we enhanced the security of intercity through train services by introducing an x-ray security check and metal detector inspection at Hung Hom Station.

Customer satisfaction levels recorded during the year by our regular surveys remained high. In 2008, the Service Quality Index for the Domestic / Cross-boundary services and Airport Express stood at 71 and 82 respectively (2007: 70 and 81 respectively), while the Fare Index, which measures the level of satisfaction of customers with our fares, stood at 61 and 64 respectively (2007: 58 and 62 respectively). In the benchmarking performed by the 12-member international Community of Metros (CoMET) for 2007, we maintained our leading position in the areas of customer service, service reliability, business performance and safety.

The excellent standard of our service performance levels was again recognised in the winning of a large number of awards, including the "Best Metro Asia Pacific Award" at The MetroRail 2008 Awards, the "2008 Hang Seng Pearl River Delta Environmental Award" organised by Federation of Hong Kong Industries and Hang Seng Bank, and the Bronze award in the Customer Service Excellence Award 2007 organised by the Hong Kong Association for Customer Service Excellence Limited.

Ktt, our intercity train to Guangzhou, won the "2008 Prime Award for Brand Excellence" in Cross Boundary Transportation Service organised by Prime Magazine.

Service Improvements

We continued to enhance train services and network infrastructure to support the MTR network as the backbone of public transport in Hong Kong.

As part of our commitment to improving passenger comfort, five 7-car new trains were brought into passenger service on the West Rail Line in the fourth quarter of 2008. For the opening of the Kowloon Southern Link, 22 new Light Rail Vehicles are being procured with the first batch of vehicles scheduled for delivery in the fourth quarter of 2009. Ten new trains will also be delivered to Hong Kong between 2011 and 2012 to enhance train frequency on the existing lines to cater for ongoing patronage growth on the Island Line, Kwun Tong Line, Tsuen Wan Line and Tseung Kwan O Line. In addition, electric-powered rolling stock replaced the diesel-powered Beijing/Shanghai-Kowloon Through Trains in January, providing better services to passengers as well as offering benefits to the environment. Long-haul travelers welcomed this move. Average daily patronage of the Beijing-Kowloon Through Train and Shanghai-Kowloon Through Train in 2008 increased by about 21% and 14% respectively compared to 2007.

After the Rail Merger, a "fast track" renovation programme was carried out in East Rail stations with the introduction of inspiring colours and graphics containing local heritage and station name characters to provide both a refreshing ambience and easy recognition of stations when trains arrive at the platform. Station facilities were improved, including the standardisation of platform seats to provide better comfort, and of all signage to offer a consistent means of route-finding throughout the network. Renovation works also commenced at Mongkok East Station, with 25 new commercial shops scheduled for opening in March 2009.

The fresh design and convenience of our station platforms.

The retrofitting of automatic platform gates, as used on the Disneyland Resort Line, for eight aboveground stations on the Island, Tsuen Wan and Kwun Tong lines began at the end of the year, with the whole project expected to complete in 2012. A wide gate was installed at the Kwun Tong Line concourse of Kowloon Tong Station, while another wide gate was installed at Mei Foo Station Entrance D. In the first quarter of 2008, we completed the application of photo-catalytic coating to all trains, buses and Airport Express shuttle buses to improve the hygiene level of our stations, trains and bus compartments.

As a value-added service to frequent travelers, Wi-Fi service became first available on Airport Express In-train in Aug 2008. This service became fully available on all Airport Express trains in early 2009. This service was additional to Wi-Fi availability at our 30 stations, including all Airport Express Stations.

To capture the increasing trend of tourist rides and extended reach of the railway network, MTR Travel was revamped and re-positioned as an icon of service commitment to the tourists. The MTR Travel at Lo Wu Station introduced a wide range of travel related services and products to the inbound tourists while the product variety at the Admiralty Station shop was enhanced to strengthen the services.

Access to the Network for the Disabled

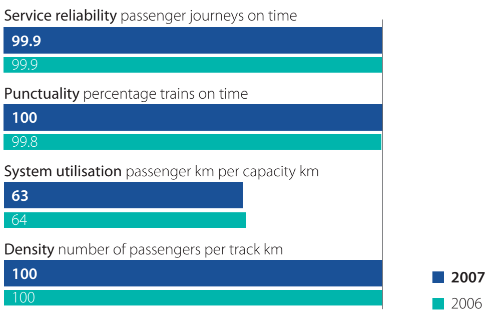
Following the Rail Merger, the Company actively reviewed the integration and standardisation of facilities for passengers with disabilities across the network. In particular, we undertook the extension of the tactile guide path covering all platforms of Light Rail, which is targeted for completion in early 2009.

"Efficiency and productivity remained a key priority for the Company in 2008."

Benchmarking Comparisons

MTR Corporation maintained its strong position, particularly in service reliability, against international benchmarks.

MTR performance vs. best performance

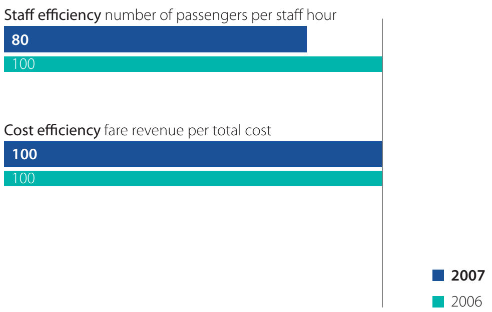


Best Performance = 100

Staff Efficiency and Cost Efficiency

New initiatives will further be introduced to enhance operating efficiency.

MTR performance vs. best performance



Best Performance = 100

Construction began at Tai Wo Hau on an external lift connecting the footbridge and street level to the station concourse, while planning for lifts at Sham Shui Po, Wong Tai Sin, Jordan, and Yau Ma Tei stations commenced with completion scheduled by 2012. Braille maps were introduced at all stations on the Tseung Kwan O Line as well as at Airport, Choi Hung, Kwai Fong, Jordan, and Ngau Tau Kok stations, and mechanical escalator audible devices were installed at all MTR Lines stations.

Productivity

Efficiency and productivity remained a key priority for the Company in 2008. The multi-disciplinary Rapid Response Unit was extended to the West Rail, East Rail, Light Rail and Ma On Shan lines in 2008, improving response to incidents whilst achieving cost savings of approximately HK$1 million per annum. Ticket sorting operations were outsourced and sorting centres at Kam Sheung Road Station and Tai Wai Station were shut down. Due to a change of operations strategy, 68 staff in the Ticket Inspection Unit were replaced by contractor staff, thereby achieving cost savings of some HK$8.8 million.

MTR staff help the disabled passengers with portable ramp.

System and Market Information

Railway operation data	2008		2007	
Total route length *in km*	**211.6**		211.6	
Number of rail cars	**1,919**		1,871	
Number of stations (Island Line, Tsuen Wan Line, Kwun Tong Line, Tseung Kwan O Line, Tung Chung Line, Disneyland Resort Line, West Rail Line, Airport Express Line, East Rail Line and Ma On Shan Line)	**82**		82	
Number of stops (Light Rail only)	**68**		68	
Number of "e-Instant Bonus" machines in stations	**31**		24	
Number of station kiosks and mini-banks in stations	**1,186**		1,230	
Number of advertising points in stations	**20,539**		20,564	
Number of advertising points in trains	**26,619**		27,011	
Daily hours of operation				
Island Line, Tsuen Wan Line, Kwun Tong Line,Tseung Kwan O Line, Tung Chung Line, Disneyland Resort Line, West Rail Line, Airport Express Line and Light Rail	**19.0**		19.0	
East Rail Line and Ma On Shan Line	**19.5**		19.5	
Minimum train headway in seconds	**Morning Peak**	**Evening Peak**	Morning Peak	Evening Peak
– Tsuen Wan Line	**128**	**130**	128	140
– Kwun Tong Line	**128**	**144**	128	144
– Island Line	**120**	**150**	124	156
– East Rail Line				
East Tsim Sha Tsui to Sheung Shui	**212**	**212**	212	212
East Tsim Sha Tsui to Lo Wu	**327**	**327**	327	327
East Tsim Sha Tsui to Lok Ma Chau	**600**	**600**	600	600
– Ma On Shan Line	**180**	**240**	180	240
– Tseung Kwan O Line	**160**	**180**	160	180
– Tung Chung Line				
Hong Kong – Tung Chung	**360**	**480**	360	480
Hong Kong – Tsing Yi	**240**	**240**	240	240
– Airport Express	**720**	**720**	720	720
– West Rail Line	**210**	**270**	210	270
– Disneyland Resort Line	**270**	**270**	270	270
– Light Rail	**270**	**300**	270	300

International Performance Comparisons: The 12-member Community of Metros (CoMET)

Metro system network data (2007)	MTR*	Metro A	Metro B	Metro C	Metro D	Metro E	Metro F	Metro G	Metro H	Metro I	Metro J	Metro K
Passenger journeys *in million*	**888**	473	1,080	1,352	692	2,529	1,568	1,431	458	612	781	612
Car kilometres *in million*	**118**	122	505	363	184	686	571	239	102	97	85	101
Route length *in km*	**84**	144	439	201	275	281	480	212	115	86	117	61
Number of stations	**51**	170	269	147	239	159	424	297	66	85	77	55

* For the data year 2007, the lines included in the CoMET metro benchmarking programme are Kwun Tong Line, Tsuen Wan Line, Island Line, Tung Chung Line, Tseung Kwan O Line and Disneyland Resort Line. The Airport Express is excluded from the benchmarking.

Note: The other metros in the comparison are Berliner Verkehrsbetriebe, London Underground Limited, New York City Transit, Sistema de Transporte Colectivo, Régie Autonome des Transports Parisiens Metro, Régie Autonome des Transports Parisiens Réseau Express Régional, Metropolitano de São Paulo, Moscow Metro, Metro de Madrid, Metro de Santiago and Shanghai Metro Operation Corporation. The benchmarking agreement prohibits specifically identifying the data by metro system.

Operations Performance in 2008

Service performance item	Performance Requirement	Customer Service Pledge target	**Actual Performance##**
Train service delivery			
– Kwun Tong Line, Tsuen Wan Line, Island Line, Tseung Kwan O Line, Tung Chung Line, Disneyland Resort Line and Airport Express	98.5%	99.5%	**99.9%**
– East Rail Line (including Ma On Shan Line)	98.5%	99.5%	**99.9%**
– West Rail Line	98.5%	99.5%	**99.9%**
– Light Rail	98.5%	99.5%	**99.9%**
Passenger journeys on time			
– Kwun Tong Line, Tsuen Wan Line, Island Line, Tseung Kwan O Line, Tung Chung Line and Disneyland Resort Line	98.5%	99.5%	**99.9%**
– Airport Express	98.5%	99.0%	**99.9%**
– East Rail Line (including Ma On Shan Line)	98.5%	99.0%	**99.9%**
– West Rail Line	98.5%	99.0%	**99.9%**
Train punctuality			
– Kwun Tong Line, Tsuen Wan Line, Island Line, Tseung Kwan O Line, Tung Chung Line and Disneyland Resort Line	98.0%	99.0%	**99.7%**
– Airport Express	98.0%	99.0%	**99.9%**
– East Rail Line (including Ma On Shan Line)	98.0%	99.0%	**99.8%**
– West Rail Line	98.0%	99.0%	**99.9%**
– Light Rail	98.0%	99.0%	**99.9%**
Train reliability: train car-km per train failure causing delays ≥5 minutes			
– Kwun Tong Line, Tsuen Wan Line, Island Line, Tseung Kwan O Line, Tung Chung Line, Disneyland Resort Line and Airport Express	N/A	500,000	**2,294,126**
– East Rail Line (including Ma On Shan Line) and West Rail Line	N/A	500,000	**2,167,927**
Ticket reliability: magnetic ticket transactions per ticket failure			
– Kwun Tong Line, Tsuen Wan Line, Island Line, Tseung Kwan O Line, Tung Chung Line, Disneyland Resort Line, Airport Express, East Rail Line (including Ma On Shan Line) and West Rail Line *	N/A	8,000	**11,224**
Add value machine reliability			
– Kwun Tong Line, Tsuen Wan Line, Island Line, Tseung Kwan O Line, Tung Chung Line, Disneyland Resort Line and Airport Express	98.0%	99.0%	**99.6%**
– East Rail Line (including Ma On Shan Line)	98.0%	99.0%	**99.8%**
– West Rail Line	98.0%	99.0%	**99.8%**
– Light Rail	N/A	99.0%	**99.7%**
Ticket machine reliability			
– Kwun Tong Line, Tsuen Wan Line, Island Line, Tseung Kwan O Line, Tung Chung Line, Disneyland Resort Line and Airport Express	97.0%	99.0%	**99.5%**
– East Rail Line (including Ma On Shan Line)	97.0%	99.0%	**99.7%**
– West Rail Line	97.0%	99.0%	**99.8%**
– Light Rail	N/A	99.0%	**99.8%**

Operations Performance in 2008 *(continued)*

Service performance item	Performance Requirement	Customer Service Pledge target	**Actual Performance##**
Ticket gate reliability			
– Kwun Tong Line, Tsuen Wan Line, Island Line, Tseung Kwan O Line, Tung Chung Line, Disneyland Resort Line and Airport Express	97.0%	99.0%	**99.7%**
– East Rail Line (including Ma On Shan Line)	97.0%	99.0%	**99.9%**
– West Rail Line	97.0%	99.0%	**99.6%**
Light Rail platform Octopus processor reliability	N/A	99.0%	**99.9%**
Escalator reliability			
– Kwun Tong Line, Tsuen Wan Line, Island Line, Tseung Kwan O Line, Tung Chung Line, Disneyland Resort Line and Airport Express	98.0%	99.0%	**99.9%**
– East Rail Line (including Ma On Shan Line)	98.0%	99.0%	**99.9%**
– West Rail Line	98.0%	99.0%	**99.9%**
Passenger lift reliability			
– Kwun Tong Line, Tsuen Wan Line, Island Line, Tseung Kwan O Line, Tung Chung Line, Disneyland Resort Line and Airport Express	98.5%	99.5%	**99.7%**
– East Rail Line (including Ma On Shan Line)	98.5%	99.5%	**99.7%**
– West Rail Line	98.5%	99.5%	**99.7%**
Temperature and ventilation			
Trains, except Light Rail: to maintain a cool, pleasant and comfortable train environment generally at or below 26°C	N/A	97.0%	**99.8%**
Light Rail: on-train air-conditioning failures per month	N/A	<3	**0**
Stations: to maintain a cool, pleasant and comfortable environment generally at or below 27°C for platforms and 29°C for station concourses, except on very hot days	N/A	90.0%	**99.6%**
Cleanliness			
Train compartment: cleaned daily	N/A	98.5%	**99.9%**
Train exterior: washed every 2 days (on average)	N/A	99.0%	**100.0%**
Northwest Transit Service Area Bus Service			
– Service Delivery	N/A	99.0%	**100.0%**
– Cleanliness: washed daily	N/A	99.0%	**99.3%**
Passenger enquiry response time within 6 working days	N/A	99.0%	**100.0%**

The actual performance figures are for the operating period from 2 December 2007 to 31 December 2008 as per the post-merger Operating Agreement.

* East Rail Line (including Ma On Shan Line) and West Rail Line are included since 28 September 2008.

Supporting the Olympic Games

The Company took its role as Olympic Games Equestrian Events Railway Passenger Services Associate to heart, surpassing our pledge to serve with joy and care.

Drawing on strengths from many departments, the Company ensured spectators, athletes and their entourage travelled swiftly, safely and on time to the Equestrian events venues at Sha Tin and Beas River over the 10 days of dressage, jumping and eventing. An Equestrian Events Special Task Force was set up to ensure that the Company rose to the challenge of this special assignment.

Using additional portable ramps, station staff also helped disabled passengers enjoy smooth train journeys to Shatin to attend the Paralympic Equestrian Event from 7 to 11 September. Station lifts and stair lifts were checked to ensure that wheelchair passengers would not encounter any difficulties on the way to their events.

Moreover, the Company also showed its support to the Beijing Olympic Games by sponsoring the 2008 Beijing Olympic Games Volunteers (HK Group) to travel by the Beijing-Kowloon Through Train in August.

Building on
Service from the Heart

Enhanced Scale, Service Quality and Innovation


Wi Fi
Wi Fi
Wi Fi
Wi Fi

More retail zone, shop renovation and new trade mix helped to increase customer satisfaction and revenue.

Station Commercial and Rail Related Businesses

Our station commercial and rail related businesses continued to benefit from rising patronage in 2008 and a robust economy, particularly in the first half of the year. The Rail Merger brought about increased scale and strengthened revenue growth as well as new business opportunities in the form of freight transportation and Duty Free shops.

Revenue Performance

Revenue for our station commercial and rail related businesses increased by 98.1% in 2008 to HK$3,449 million. The increase would have been 33.4% over the comparable combined revenue of MTR Corporation and pre-merger KCRC for such businesses in 2007 (Combined Non-fare Revenue).

Station Retail

Station retail revenue, comprising duty free shops and kiosk rental, increased by 209.8% in 2008 to HK$1,546 million, a 42.3% increase over the equivalent Combined Non-fare Revenue. This increase was mainly due to the inclusion of retail shops along the KCR Lines, particularly the 10 duty free shops serving Cross-boundary customers. Further growth was provided by increased new retail area and new rental contracts being awarded at higher rents. To enhance customer satisfaction and increase revenue, 45 shops were renovated at 9 stations and 18 new trades were added. With repossession of shops to facilitate renovation works, the total number of shops as at 31 December 2008 was 1,186, a slight reduction from 1,230 as at the end of 2007 with such retail area totaling 51,539 square metres of which 9,510 square metres relates to Duty Free businesses. We completed renovation works for shops at Ngau Tau Kok, Wong Tai Sin, Tai Po Market, Kowloon, Tiu Keng Leng, Kowloon Tong, Kwun Tong, Mong Kok East stations and Lo Wu Arrival Concourse Hall by the end of the year.

Advertising points increased to 20,539 in the MTR stations after the Rail Merger.

Over 47,000
Advertising Points
in Stations and Trains

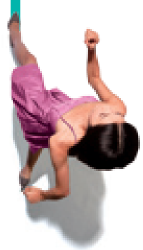
HK$9.04 million
Advertising Revenue
Per Station

1,186 Kiosks
in Stations

18 New Trades Added
in Station Kiosks

30 Stations with Brands Wi-Fi Access, first Wi-Fi train introduced
in August

Station Commercial and Rail Related Revenue Comprised 19.6% of Total Revenue
for the Year 2008



A series of 1-minute TV segments was launched in September and October to reinforce the public's awareness of MTR Shops. To further stimulate customer spending, a MTR Shops Lucky Draw Promotion "Tokyo Group Shopping Extravaganza" was the finale of our 2008 consumer programmes.

Advertising

Advertising revenue grew by 25.0% in 2008 to HK$741 million when compared with 2007, a 11.3% increase over the equivalent Combined Non-fare Revenue. In addition to the merger benefits, there were higher advertising rates and advertising innovations, which included the renovated "The Galleria" launched at the lower adit of Causeway Bay Station in May and the Digital Escalator Crown Bank at Causeway Bay, Tsim Sha Tsui and Central stations, the first of its kind in Asia's metro systems. At the end of 2008, there were 20,539 advertising points in stations, 26,619 in trains (including 4,341 Liquid Crystal Displays) and 228 on buses.

Telecommunications

Revenue from telecommunications services increased by 49.0% in 2008 to HK$356 million as compared to 2007 (a 27.6% increase over the equivalent Combined Non-fare Revenue). The key reason for the increase of revenue was a one-off payment received on termination of a telecommunications license. Excluding this one-off income, revenue still grew by 13.0% to HK$270 million as compared to 2007 but would have shown a decline of 3.2% compared with the equivalent Combined Non-fare Revenue, since 3G usage continues to increase at the expense of 2G usage. The full launch of 3G mobile phone coverage along the East Rail Line and Ma On Shan Line took place in June and October respectively while preparation works for 3G coverage on the West Rail Line are in progress with expected completion in phases during 2009. There was also an increase in one-off revenue generated from operators' mobile equipment migration projects along the stations.

During the year, TraxComm Limited achieved higher revenue with expanded growth in the market. Key achievements included the extension of Wi-Fi coverage to 9 MTR Lines stations, as well as all 5 Airport Express stations and Airport Express train sets, bringing the total of MTR stations with Wi-Fi coverage to 30.

External Consultancy

During the year, we made good progress in existing consultancy projects and signed various new contracts in line with our focused strategy of using consultancies to enhance skill-sets

MTR's spacious interchanges are ideal for creative advertising.

and to seek new investment opportunities. As a result, revenue from external consultancy activities was HK$158 million during 2008, a decrease of 18.1% when compared with 2007, mainly due to the completion of the majority of works on Shanghai Metro Line 9 Phase 1, which was opened in December 2007.

In India, our consultancy business won an HK$128 million engineering and project management contract for the construction of the Delhi Airport Metro Express Line. Leveraging our competency in non-fare business, we secured a consultancy contract with Dubai Roads and Transport Authority (RTA) on the retail outlets leasing for the Red and Green lines of Dubai Metro Stations. We secured a consultancy project to provide technical advice to Metro Rio in Brazil for rolling stock procurement from China.

In 2008, we also extended the Automated People Mover operations and maintenance agreement with the Airport Authority of Hong Kong for five more years, whilst our existing consultancy works for Kaohsiung Rapid Transit Corporation in Taiwan proceeded well.

Freight Services

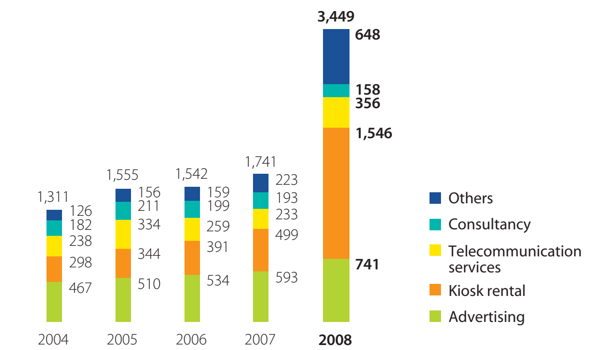
Revenue from freight services was HK$37 million during 2008, a decrease of 10% over the equivalent Combined Non-fare Revenue.

"At the end of 2008, there were 20,539 advertising points in stations, 26,619 in trains (including 4,341 Liquid Crystal Displays) and 228 on buses."

Revenue from Station Commercial and Rail Related Businesses

Growth in revenue from station commercial and other activities was led by advertising income and kiosk rental.

in HK$ million



Innovations include Asia metro's first digital escalator bank.

3G coverage was launched on East Rail and Ma On Shan lines.

Building on
Solid Foundations

World-class Design, Planning and Management

All units at The Capitol at LOHAS Park were pre-sold.

Property and Other Businesses

The Hong Kong property market performed strongly in the first half of 2008. Both office and retail markets enjoyed steady growth. However, with global credit market uncertainties developing into a global economic downturn, market activities slowed noticeably in the second half. Sale prices for residential units declined, and commercial rents started to consolidate.

Profit from property development was HK$4,670 million in 2008, while revenue from property rental, management and other businesses grew by 47.9% to HK$2,712 million.

Property Development

Profit on property development for 2008 was HK$4,670 million, a decrease from the HK$8,304 million recognised in 2007. This decrease was mainly due to very significant development profits booking in 2007, particularly for Le Point in Tseung Kwan O. The major contributors to property development profits were from profit recognition relating to The Capitol at LOHAS Park and The Palazzo in Shatin, as well as the sale of units from inventory at Harbour Green and The Arch. In addition, there was deferred income recognition, mainly from properties along the Airport Railway, such as Coastal Skyline and Caribbean Coast in Tung Chung Station, and Elements in Kowloon Station.

Property sales continued to perform well, with the pre-sale of all 2,096 units of The Capitol at LOHAS Park as well as about 80% or 1,100 units of the 1,375 units available at The Palazzo in Shatin. These property sales took place in the first half of 2008 with final settlements for units sold under the "stage payment" method not due until issuance of Consent to Assign or Certificate of Compliance, expected for both developments by June 2009. There was also a successful pre-sale of over 470 units at Le Bleu Deux in Tung Chung where the Company has a nominal financial interest.

In our property tendering activities, the development package for Che Kung Temple on the Ma On Shan Line was awarded to a subsidiary of New World Development Company Limited (Deluxe Sign Limited) in April. Similar to LOHAS Park Package 1, The Capitol, we paid half of the land premium for this development in return for a larger share of profits. As an agent for West Rail Line property development, Tsuen Wan West Station TW7 property development package was awarded to a subsidiary of Cheung Kong (Holdings) Limited (Queensway Investments Limited) in September.

Following the Government's decision to proceed with the planning and design of South Island Line (East) and the Kwun Tong Line Extension, consultancies commenced on the preliminary property scheme design for potential sites along these new lines.

Property Development

HK$4.67 Billion
Property Development Profit

2 Property Tenders
Awarded
with a Total GFA of 203,719 sq.m.

Property Rental

48.4% Increase
in Rental Income

Phase 2 of Elements
opened on 1 November 2008

Cinema complex
at Telford Plaza I reopened
on 19 August 2008

273,122 sq.m.
of Investment Properties in Hong Kong

Property Management

73,947
HK Residential Units

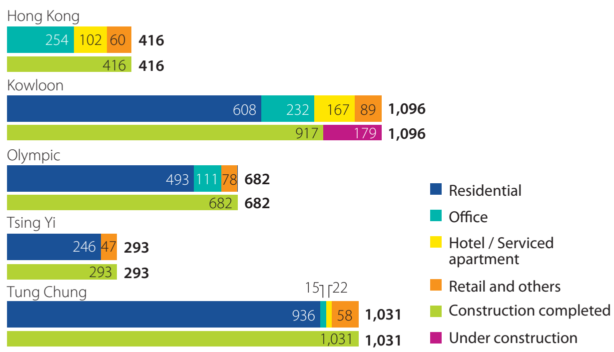
770,556 sq.m.
of HK Commercial Properties

1,158,254 sq.m.
of managed GFA
in Mainland China

Airport Railway Property Development Plan and Progress

There was deferred income recognition from properties along the Airport Railway in 2008.

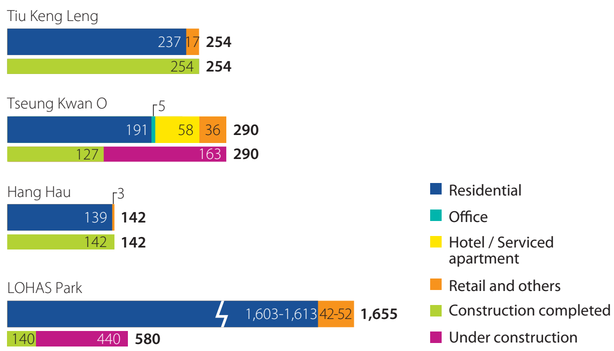
Gross floor area Thousand sq.m.



Tseung Kwan O Line Property Development Plan and Progress

The completion of The Capitol at LOHAS Park contributed to the property development profit in 2008.

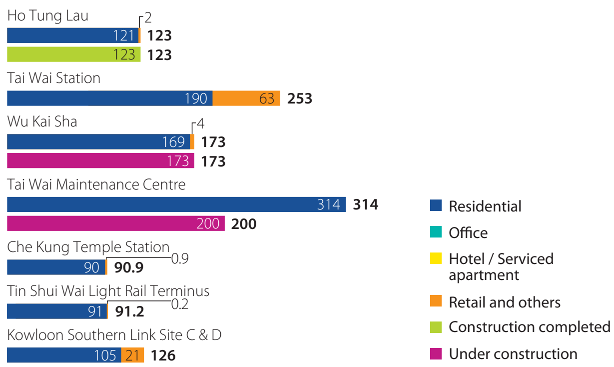
Gross floor area Thousand sq.m.



East Rail Line, Ma On Shan Line, Kowloon Southern Link and Light Rail Property Development Plan and Progress

The completion of The Palazzo also contributed to the property development profit in 2008.

Gross floor area Thousand sq.m.



Property Rental, Property Management and Other Businesses

Total revenue from property rental, property management and other businesses increased by 47.9% in 2008 to HK$2,712 million (29.8% increase over the equivalent Combined Non-fare Revenue).

Property Rental

Demand for both office and retail space was strong in the first half of the year, but the rate of growth began to slow in the second half. Property rental income was HK$2,346 million, an increase of 48.4 % over 2007 (28.8% increase over the equivalent Combined Non-fare Revenue). Number of visitors to the Company's retail centres remained strong throughout the year. Our commitment to the continuous enhancement of our shopping centres and other investment properties, as well as our emphasis on providing "Premier" management services, enabled us to capitalise on Hong Kong's strong consumer sentiment and robust tourism growth. The average increase in rental income of retail properties on renewal of leases or re-letting was 20% as compared to rental income achieved in the previous lettings.

We maintained close to 100% occupancy of our shopping centres. The Company's 18 floors at Two International Finance Centre were fully rented out.

At the end of December 2008, the Company's attributable share of investment properties was 221,661 square metres of lettable floor area of retail properties, 41,059 square metres of lettable floor area of offices, and 10,402 square metres for other usage.

We continued to renovate our shopping centres in 2008 to enhance their market appeal and competitiveness. These works included the redevelopment of the cinema complex at Telford Plaza I to create an iconic building for the area.

Our shopping centres were once again honoured with a broad spectrum of local and international awards. Our flagship luxury shopping mall Elements, situated above Kowloon Station, won the Marché International des Professionels d'Immobilier (MIPIM) Asia 2008 award for the best shopping centre at the world's premier real estate summit in Cannes, France, as well as the Urban Land Institute's 2008 Award for Excellence: Asia Pacific. The development was also named Project of the Year (Retail) in the Asia Pacific Real Estate Awards and won an EFFIE Bronze Award Hong Kong 2008 in the Real Estate Agents / Real Estate Development category. Telford Plaza won the Prime Award for

Elements shopping mall won several international awards.

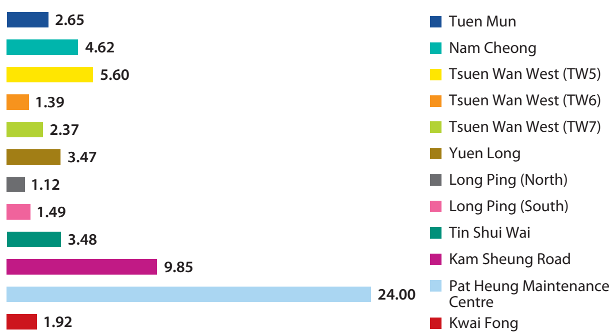
Eco-Business 2008 sponsored by Prime Magazine and the Hong Kong Service Award sponsored by East Weekly, while Maritime Square won the Progressive Award (Shopping Mall) – Caring Environment issued by the Caring Environment Recognition Scheme 2007.

A number of innovative promotions were launched in our shopping centres to attract more shoppers. Elements organised a summer campaign, "Flirting with Sound", between July and September, which started with a redemption programme and finished with a Party on Ice and a jazz concert. This event won the 2008 Grand Kam Fan Award. Elements also joined hands with HSBC Platinum and Premier cards to offer attractive spending incentives including cash rebates and Asia Miles, recording excellent results. Maritime Square lined up with Disney to launch "Mickey's Magic Chinese Palace" during Chinese New Year, exhibiting the largest gold Mickey Mouse

West Rail Property Development Plan

The Company acts as development agent for the West Rail property projects.

Site Area (in Hectare)



NP 360 cable car brings increasing crowds to the associated theme village.

in town. A "Saturday Shopping Fever" event was held every Saturday from September to November in Telford Plaza and Maritime Square, featuring rewards with hampers and gift sets for spending more than HK$1,000.

New tenants in our shopping centres included PLUSIT, Church's and Lenscrafters at Elements; Marks & Spencer, MOS Burger, CD Warehouse, Uniqlo, Shu Uemura, GEOX, Ajisen Ramen, AV Life, Chung Yuen Electrical and Levi's at Maritime Square; and Shu Uemura, IPSA, Lowrys Farm, Mango, Viva Violet, Xia Mian Guan, Initial, Cithara, Lei Garden, Tasty Noodles & Wantun, Bubble, Chevignon, Samsonite, Red Door, and MCL Telford Cinema at Telford Plaza.

In the Mainland of China, Ginza Mall, which opened in January 2007, continued to set new benchmarks for service and quality within the shopping centre industry in Beijing. Average rental income increment for lease renewals and re-lettings was 15% compared to 2007 and occupancy was 100%. The shopping centre received many awards and honours in its first full year of operation. These included being ranked No. 2 amongst the 156 major shopping centres and department stores in Beijing in a Customer Satisfaction Survey conducted by the Beijing Municipal Commerce Bureau. Promotional highlights of the year included a series of activities focusing on the linkage between ancient Chinese sports and their modern counterparts, which were held during the summer in support of the 2008 Beijing Olympics. Our ongoing refinement of the trade mix in Ginza Mall reinforced the centre's market positioning as a place for the stylish and young, bringing a new shopping experience to Beijing customers. Newcomers to the Beijing retail market in 2008 that chose Ginza Mall as their initial expansion point included Euromoda by Mecoxlane and Costa Coffee.

Property Management

Our property management business achieved revenue growth of 25.0% in 2008 to HK$210 million (15.4% increase over the equivalent Combined Non-fare Revenue). During the year, 2,096 residential units were added to our property management portfolio at Le Point (Phase 2 of Metro Town), bringing the total number of residential units under our management to 73,947 as at the end of December, whilst total commercial space under management was 770,556 square metres.

Our managed property portfolio in Mainland of China amounted to 1,158,254 square metres. 338,000 square metres were added to our property management portfolio, including Mei Li Shan Shui Phase 2 in Chongqing and Rich Gate Shopping Mall Phase 1 in Shenyang.

Other Businesses

Octopus

Octopus performed strongly with the Company's share of net profits in 2008 increasing by 40.2% to HK$136 million. The rise was mainly due to continued increases in non-transport retail payments. To improve transaction volume in this area, Octopus continued its retail merchant expansion helped by the "Portable Octopus Processor" (POP), which enables Octopus to extend its reach into the small to medium-sized retail market sector. By the end of December, the total number of service providers (including those serviced by Octopus-appointed acquirers) had risen to 2,495 from 1,440 at the end of December 2007. "Auto-add value" customers who generally use Octopus for non-transport payments much more than customers without this feature, reached a record high of over 1 million customers. Total cards in circulation rose to 18.7 million and average daily transaction volume and value rose to 10.7 million and HK$89.8 million respectively.

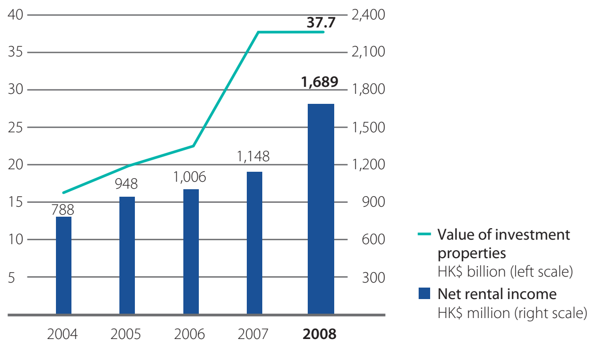
Ngong Ping 360

The Ngong Ping cable car and associated theme village on Lantau Island contributed HK$156 million of revenue in 2008, with visitor numbers reaching more than 1.6 million. After its re-opening on 31 December 2007, the cable car system achieved a reliability rate of over 99% for the year. Awards received included the "Gold Award – Website Category" from the Pacific Asia Travel Association (PATA), and the "Globe Award 2008" from the British Guild of Travel Writers. Ngong Ping 360 also holds the Guinness record for "Most people playing wood Chinese block", which took place at the Ngong Ping Buddha's Birthday Celebration event in May 2008.

MTR's shopping centre management services are five-star standard.

Investment Properties

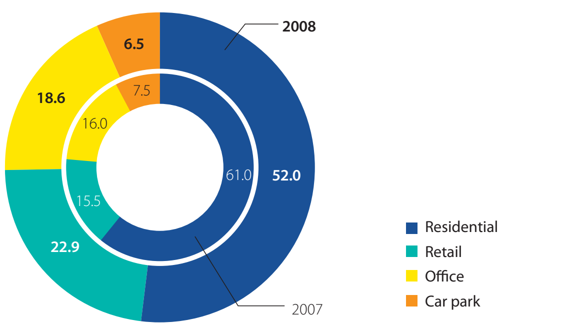
Revenue from investment properties increased as rentals rose, together with contributions from the opening of Elements as well as additional investment properties acquired in the Rail Merger.



Distribution of Property Management Income

At the end of the year, the Company had 73,947 residential units and 770,556 sq.m. commercial properties under management in Hong Kong, and 1,158,254 sq.m. of managed GFA in Mainland China.

Percentage



Airport Railway Property Developments (Packages Awarded)

Location	Developers	Type	Gross floor area (sq. m.)	No. of parking spaces	Actual or expected completion date
Hong Kong Station					
(International Finance Centre, IFC Mall, Four Seasons Hotel / Four Seasons Place)	Sun Hung Kai Properties Ltd. Henderson Land Development Co. Ltd. The Hong Kong & China Gas Co. Ltd.	Office Retail Hotel Car park	254,186 59,458 102,250	 1,344	Completed by phases from 1998-2005
Sub-total			415,894		
Kowloon Station					
Package One (The Waterfront)	Wing Tai Holdings Ltd. Temasek Holdings (Pte) Ltd. Singapore Land Ltd. Keppel Land Ltd. Lai Sun Development Co. Ltd. Worldwide Investment Co. (Bermuda) Ltd.	Residential Car park	147,547	 1,332	Completed in 2000
Package Two (Sorrento)	The Wharf (Holdings) Ltd. Wheelock and Company Ltd. Wheelock Properties Ltd. Realty Development Corporation Ltd. Harbour Centre Development Ltd.	Residential Car park	210,319	 1,270	Completed by phases from 2002-2003
Package Three (The Arch)	Sun Hung Kai Properties Ltd.	Residential Cross border bus terminus Car park	100,000 5,113	 412	Completed in 2005
Package Four (The Harbourside)	Hang Lung Properties Ltd.	Residential Car park	128,845	 864	Completed in 2003
Packages Five, Six and Seven (Elements, International Commerce Centre, The Cullinan, W Hong Kong, The Harbourview Place)	Sun Hung Kai Properties Ltd.	Retail Office Service apartment Hotel Residential Kindergarten Car park	82,750 231,778 72,472 95,000 21,300 1,045	 1,683*	By phases from 2006-2010
Sub-total			1,096 ,169		

* The number of car parking spaces is subject to review

Airport Railway Property Developments (Packages Awarded) *(Continued)*

Location	Developers	Type	Gross floor area (sq. m.)	No. of parking spaces	Actual or expected completion date
Olympic Station					
Package One (Island Harbourview, HSBC Centre, Bank of China Centre and Olympian City One)	Sino Land Co. Ltd.	Office Retail Residential Indoor sports hall Car park	111,000 14,900 169,950 13,219	1,380	Completed in 2000
Package Two (Park Avenue, Central Park and Olympian City Two)	Sino Land Co. Ltd.	Retail Residential Market Car park	47,500 220,050 1,100	932	Completed in 2001
Package Three (Harbour Green)	Sun Hung Kai Properties Ltd.	Residential Kindergarten Car park	103,152 1,300	264	Completed in 2006
Sub-total			682,171		
Tsing Yi Station					
(Tierra Verde and Maritime Square)	Cheung Kong (Holdings) Ltd. Hutchison Whampoa Ltd. CITIC Pacific Ltd.	Retail Residential Kindergarten Car park	46,170 245,700 925	920	Completed in 1999
Sub-total			292,795		
Tung Chung Station					
Package One (Tung Chung Crescent, Citygate, Novotel Citygate and Seaview Crescent)	Hang Lung Group Ltd. Henderson Land Development Co. Ltd. New World Development Co. Ltd. Sun Hung Kai Properties Ltd. Swire Properties Ltd.	Office Retail Hotel Residential Kindergarten Car park	14,913 48,298 21,986 275,479 855	2,037	Completed by phases from 1999-2005
Package Two (Coastal Skyline)	HKR International Ltd. Hong Leong Holdings Ltd. Recosia Pte Ltd.	Retail Residential Kindergarten Car park	2,499 253,100 350	625	Completed by phases from 2002-2008
Package Three (Caribbean Coast)	Cheung Kong (Holdings) Ltd. Hutchison Whampoa Ltd.	Retail Residential Wet market Kindergarten Car park	4,996 407,300 508 350	1,185	Completed by phases from 2002-2008
Sub-total			1,030,634		
Grand Total:			3,517,663	14,248	

Tseung Kwan O Line Property Developments (Packages Awarded)

Location	Developers	Type	Gross floor area (sq. m.)	No. of parking spaces	Status	Actual or expected completion date
Tseung Kwan O Station						
Area 57a (Central Heights)	Sun Hung Kai Properties Ltd. Nan Fung Development Ltd. Henderson Land Development Co. Ltd. Chime Corporation Ltd.	Residential Retail Car park	26,005 3,637	74	Awarded in July 2000	Completed in 2005
Area 55b (The Grandiose and The Edge)	New World Development Co. Ltd. Chow Tai Fook Enterprises Ltd. Wee Investments Pte. Ltd.	Residential Retail Car park	84,920 11,877	249	Awarded in January 2002	Completed in 2006
Area 56	Sun Hung Kai Properties Ltd.	Residential Hotel Retail Office Car park	80,000 58,130 20,000 5,000	363	Awarded in February 2007	2011
Hang Hau Station						
(Residence Oasis and The Lane)	Sino Land Co. Ltd. Kerry Properties Ltd.	Residential Retail Car park	138,652 3,500	369	Awarded in June 2002	Completed in 2004
Tiu Keng Leng Station						
(Metro Town)	Cheung Kong (Holdings) Ltd.	Residential Retail Car park	236,965 16,800	609	Awarded in October 2002	Completed by phases in 2006-2007
Area 86 (LOHAS Park)						
Package One (The Capitol)	Cheung Kong (Holdings) Ltd.	Residential Retail Car park Residential Care Home for the Elderly	136,240 500 3,100	325	Awarded in January 2005	Completed in 2008
Package Two	Cheung Kong (Holdings) Ltd.	Residential Kindergarten Car park	309,696 800	905	Awarded in January 2006	By phases from 2009-2010
Package Three	Cheung Kong (Holdings) Ltd.	Residential Kindergarten Car park	128,544 1,000	350	Awarded in November 2007	2012

East Rail Line, Ma On Shan Line and West Rail Line Property Developments (Packages Awarded)

Location	Developers	Type	Gross floor area (sq. m.)	No. of parking spaces	Status	Actual or expected completion date
Fo Tan Station						
Ho Tung Lau (The Palazzo)	Sino Land Co. Ltd.	Residential Retail Car park	120,900 2,000	239	Awarded in November 2002	Completed in 2008
Wu Kai Sha Station	Sino Land Co. Ltd.	Residential Retail Kindergarten Car park	168,650 3,000 1,000	309	Awarded in July 2005	2009
Tai Wai Maintenance Centre	Cheung Kong (Holdings) Ltd.	Residential Car park	313,955	711	Awarded in April 2006	By phases from 2009-2011
Tuen Mun Station*	Sun Hung Kai Properties Ltd.	Residential Retail Car park	119,512 25,000	384	Awarded in August 2006	By phases from 2012-2013
Che Kung Temple Station	New World Development Co. Ltd.	Residential Retail Kindergarten Car park	89,792 193 670	236	Awarded in April 2008	2012
Tsuen Wan West Station TW7*	Cheung Kong (Holdings) Ltd.	Residential Car park	113,064	444	Awarded in September 2008	2013

* as development agent for the Government of HKSAR

The Palazzo in Shatin performed well.

Tseung Kwan O Line Property Developments (Packages to be Awarded)**

Location	No. of packages envisaged	Type	Gross floor area (sq. m.)	Expected No. of parking spaces	Period of package tenders	Expected completion date
LOHAS Park	6 – 10	Residential	1,025,220– 1,035,220		2009-2015	2019
		Retail	39,500 – 49,500			
		Car park		3,303 (max.)		

** Subject to review in accordance with planning approval, land grant conditions and completion of statutory processes

Ma On Shan Line/Light Rail/Kowloon Southern Link Property Developments (Packages to be Awarded)**

Location	No. of packages envisaged	Type	Gross floor area (sq. m.)	Expected No. of parking spaces	Period of package tenders	Expected completion date
Tai Wai Station	1-2	Residential	190,480		Under review	Under review
		Retail	62,000			
		Kindergarten	1,110			
		Car park		713		
Tin Shui Wai Light Rail Terminus	1	Residential	91,051		Under review	Under review
		Retail	205			
		Car park		267		
Site C & Site D Austin Station, Tsim Sha Tsui	2	Residential	104,795		2009 - 2010	2013 - 2014
		Retail	20,959			
		Car park		321		

** Subject to review in accordance with planning approval, land grant conditions and completion of statutory processes

Investment Property Portfolio (as at 31 December 2008)

Location	Type	Lettable floor area (sq. m.)	No. of parking spaces	Company's ownership interest
Telford Plaza I, Kowloon Bay, Kowloon	Shopping Centre	39,483	–	100%
	Car park	–	993	100%
Telford Plaza II, Kowloon Bay, Kowloon	Shopping Centre	19,411	–	50%
	Car park	–	136	50%
Luk Yeung Galleria, Tsuen Wan, New Territories	Shopping Centre	11,234	–	100%
	Car park	–	651	100%
Paradise Mall, Heng Fa Chuen, Hong Kong	Shopping Centre	18,772	–	100%
	Wet Market	1,216	–	100%
	Car park	–	415	100%
Maritime Square, Tsing Yi	Shopping Centre	28,860	–	100%
	Kindergarten	920	–	100%
	Car park	–	220	100%
	Motorcycle park	–	50	100%
The Lane, Hang Hau	Shopping Centre	2,645	–	100%
	Car park	–	16	100%
	Motorcycle park	–	1	100%
The Edge, Tseung Kwan O	Shopping Centre	7,683	–	70%
	Car park	–	50	70%
G/F, No. 308 Nathan Road, Kowloon	Shop unit	70	–	100%
G/F, No. 783 Nathan Road, Kowloon	Shop unit	36	–	100%
New Kwai Fong Gardens, Kwai Chung, New Territories	Kindergarten	540	–	100%
	Car park	–	126	100%
International Finance Centre (IFC), Central, Hong Kong				
– Two IFC	Office	39,373	–	100%
– One and Two IFC	Car park	–	1,308	51%
Phase I, Carpark Building, Kornhill, Quarry Bay, Hong Kong	Car park	–	292	100%
Roof Advertising Signboard, Admiralty Centre, No.18 Harcourt Road, Hong Kong	Advertising signboard	–	–	100%
Ten Shop Units, First Floor Podium, Admiralty Centre, No. 18 Harcourt Road, Hong Kong	Shops	286	–	50%
Olympian City One, Tai Kok Tsui, Kowloon	Indoor sports hall	13,219	–	100%
Olympian City Two, Tai Kok Tsui, Kowloon	Shop unit	1,252	–	100%
Caribbean Coast, Tung Chung, New Territories	Wet market	508	–	100%
Choi Hung Park & Ride Public Car Park, No. 8 Clear Water Bay Road, Choi Hung, Kowloon	Car park	–	54	51%
	Motorcycle park	–	10	51%
	Park & Ride	–	450	51%
Elements, No. 1 Austin Road West, Kowloon	Shopping Centre (Phase 1&2)	40,499	–	81%
	Car park	–	898	81%
Cross Border Coach Terminus, No. 1 Austin Road West, Kowloon	Coach terminus	5,113	–	100%
Kindergarten, No. 1 Austin Road West, Kowloon	Kindergarten	1,045	–	81%
Plaza Ascot, Sha Tin	Shopping Centre	7,381	–	100%
Royal Ascot, Sha Tin	Residential	2,784	–	100%
	Car park	–	20	100%
Ocean Walk, Tuen Mun	Shopping Centre	6,086	–	100%
	Car park	–	32	100%
Sun Tuen Mun Shopping Centre, Tuen Mun	Shopping Centre	9,039	–	100%
	Car park	–	421	100%
Hanford Plaza, Tuen Mun	Shopping Centre	1,950	–	100%
	Car park	–	22	100%
Retail Floor and 1-6/F, Citylink Plaza, Sha Tin	Shopping Centre	12,031	–	100%
Portion of G/F and portion of 1/F, MTR Hung Hom Building, Hung Hom	Office	1,686	–	100%

All properties are held by the Company and its subsidiaries under Government Leases for over 50 years except for:

- Telford Plaza I and II, Luk Yeung Galleria, Maritime Square, New Kwai Fong Gardens, IFC, Olympian City, Caribbean Coast, Elements, Cross Border Coach Terminus and Kindergarten at No. 1 Austin Road West, Plaza Ascot, Royal Ascot, Ocean Walk, Sun Tuen Mun Shopping Centre and Hanford Plaza where the Government Leases expire on 30 June 2047

Investment Property Portfolio (as at 31 December 2008) *(Continued)*

- Choi Hung Park & Ride where the Government Lease expires on 11 November 2051
- The Lane where the Government Lease expires on 21 October 2052
- The Edge where the Government Lease expires on 27 March 2052
- Citylink Plaza and MTR Hung Hom Building where the grant of Government Leases to Kowloon-Canton Railway Corporation (KCRC) and the subsequent assignment of the properties by KCRC to the Company are underway

Properties Held for Sale (as at 31 December 2008)

Location	Type	Gross floor area (sq. m.)	No. of parking spaces	Company's ownership interest
Island Harbourview, 11 Hoi Fai Road, Kowloon	Car park	–	579	40%
Olympian City One, 11 Hoi Fai Road, Kowloon	Shopping centre	6,042*	–	40%
	Car park	–	330	40%
Bank of China Centre, 11 Hoi Fai Road, Kowloon	Car park	–	117	40%
The Arch, 1 Austin Road West, Kowloon	Residential	1,880	–	38.5%
	Car park	–	27	38.5%
Residence Oasis, 15 Pui Shing Road, Hang Hau, Tseung Kwan O	Car park	–	182	71%
	Motorcycle park	–	18	71%
The Grandiose, 9 Tong Chun Street, Tseung Kwan O	Car park	–	144	70%
	Motorcycle park	–	25	70%
Metro Town, 8 King Ling Road, Tseung Kwan O	Car park	–	8	72%
	Motorcycle park	–	22	72%
Central Heights, 9 Tong Tak Street, Tseung Kwan O	Car park	–	54	35%
	Motorcycle park	–	4	35%
Harbour Green, 8 Sham Mong Road, Kowloon	Residential	661	–	35%
	Car park	–	71	35%
	Kindergarten	1,299	–	50%
Caribbean Coast, 1 Kin Tung Road, Tung Chung	Car park	–	163	20%
Coastal Skyline, 12 Tung Chung Waterfront Road, Tung Chung	Residential	289	–	20%
	Car park	–	146	20%
The Capitol, LOHAS Park, Tseung Kwan O	Residential	1,520	–	84.05%
	Car park	–	300	84.05%
The Palazzo, 28 Lok King Street, Shatin	Residential	37,606	–	55%
	Retail	2,000	–	55%
	Car park	–	239	55%

* Lettable floor area

Managed Properties (as at 31 December 2008)

Number of managed residential flats	73,947 units
Area of managed commercial and office space	770,556 sq.m.

西九龍
總站
West Kowloon
Terminus

Building on
Hong Kong's Rail Network

The Network For Hong Kong's Future Growth

堅尼地城
Kennedy Town

柯士甸
Austin

大學
University

馬頭圍
Ma Tau Wai

海怡半島
South Horizons

黃埔
Whampoa

利東
Lei Tung

西營盤
Sai Ying Pun

何文田
Ho Man Tin

黃竹坑
Wong Chuk Hang

啟德
Kai Tak

海洋公園
Ocean Park

土瓜灣
To Kwa Wan

Design of new stations is ultra-modern and sophisticated.

Hong Kong Network Expansion

As a result of the Rail Merger and the Government's commitment to a number of priority rail infrastructure projects, 2008 was again a milestone year for the design and planning of the Company's future Hong Kong rail projects.

New Hong Kong Projects

Planning and design are underway for five new rail projects in Hong Kong, which together with the substantially completed Kowloon Southern Link (incorporating the new Austin Station) will extend our network by approximately 60 kilometres when they are all completed. These five new lines represent the most significant network expansion in the Company's history, adding to our growth opportunities as well as enhancing rail services as the backbone of public transportation in Hong Kong.

Shatin to Central Link

In March, the Government gave approval for the planning and design of the Shatin to Central Link. The Shatin to Central Link comprises two sections that will add 17 kilometres to the railway network, creating a number of new interchanges and connections and forming both a north-south and an east-west rail corridor. The 11-km Tai Wai to Hung Hom Section, the East West Corridor, expected to be completed in 2015, will extend the Ma On Shan Line to Hung Hom via Diamond Hill with four new stations in East Kowloon, and will link up with the West Rail Line at Hung Hom. The 6-km Cross Harbour Section, the North South Corridor, expected to be completed in 2019, will form Hong Kong's fourth rail harbour crossing, extending the East Rail Line from Hung Hom to Hong Kong Island with new stations initially at Exhibition and Admiralty, and eventually in Central. The preliminary design of the new link was started in September with a view to developing a scheme to be gazetted under the Railways Ordinance in late 2009.

West Island Line will be a "Community Railway".

Kowloon Southern Link

Tunnel Boring Works Substantially Completed – Mar 2008

Austin Station Topped Out – Apr 2008

Architectural and Building Services Fit-out Works Substantially Completed – Jan 2009

Tseung Kwan O South

Architectural and Building Services Fit-out Works Completed – Nov 2008

West Island Line

Detailed Design Commenced – Feb 2008

Environmental Permit Received – Dec 2008

South Island Line (East)

Preliminary Planning and Design Commenced – Feb 2008

Shatin to Central Link

LegCo Finance Committee Approved Funding – May 2008

The Company and Government Signed an **Entrustment Agreement** for the Design and Site Investigation – Nov 2008

Kwun Tong Line Extension

Preliminary Planning and Design Commenced – Jun 2008

Express Rail Link

Government Decision to Proceed with **Further Planning and Design** – Apr 2008

Gazette of Express Rail Link Scheme under the Railways Ordinance – Nov 2008

Kwun Tong Line Extension

The 3-km Kwun Tong Line Extension, the planning and design for which was also approved in March, will run from the existing Yau Ma Tei Station of Kwun Tong Line to Whampoa via Ho Man Tin, which will be an interchange station with the East West Corridor of the Shatin to Central Link. This extension will provide a much needed railway service to the 146,000 people living in these areas and will relieve road traffic congestion in the existing east-west corridors in Kowloon. With this extension, passengers from Whampoa will be able to reach Mong Kok via Ho Man Tin in five minutes.

Preliminary design started in June, and will be completed in early 2009. The current plan is to gazette the scheme under the Railways Ordinance and to proceed with the detailed design in the second half of 2009. The project agreement with Government is anticipated to be signed in 2010, which allows for construction works to commence by the end of that year. The project is expected to be completed in 2015.

Hong Kong Section of the Guangzhou-Shenzhen-Hong Kong Express Rail Link (Express Rail Link)

In April, the Government asked the Company to proceed with planning and design of the Express Rail Link, which will further enhance the strategic position of Hong Kong as the southern gateway to the Mainland of China. The 26-km Express Rail Link will provide cross-boundary high speed rail services connecting Hong Kong to Shenzhen, Guangzhou and Mainland of China's new high speed intercity rail network.

When the Hong Kong section commences service, it will take only 14 minutes to travel from the new West Kowloon Terminus to Futian in Shenzhen and 48 minutes to Guangzhou. This Hong Kong terminus may possibly be the largest underground high speed rail terminus in the world, serving both shuttle trains for journeys within the Pearl River Delta and long haul trains for other destinations. Long haul journeys will take about five hours to Wuhan, eight hours to Shanghai and ten hours to Beijing.

During 2008, preliminary design and planning for the Express Rail Link made significant progress, together with the Environmental Impact Assessment study and other preparatory works. The project was gazetted under the Railways Ordinance on 28 November 2008.

Express Rail Link will connect Hong Kong to the Mainland's intercity rail network.

South Island Line (East)

The South Island Line (East) is envisaged to be a medium capacity railway service connecting Admiralty Station to South Horizons on Ap Lei Chau via Ocean Park, Wong Chuk Hang and Lei Tung. Following the announcement of Government's support for the planning and design of the line in December 2007, preliminary design commenced in February 2008 and will be completed in early 2009. The design will provide a comprehensive foundation for the project to progress to detailed design in 2009. Extensive consultation with the local community, District Councils and other stakeholders has been undertaken and will continue as the project progresses. The feedback received so far has resulted in an optimisation of the design to cater for the needs of the community. The final plan will be issued to Government for review and gazetting in early 2009.

Hong Kong Network Expansion at a Glance

Network Extensions	Estimated Route Length	Estimated Completion Date	Project Funding
Kowloon Southern Link	3.8 km	2nd half of 2009	Service Concession
West Island Line	3 km	2014	Capital Grant
Shatin to Central Link			Service Concession
– Tai Wai to Hung Hom	11 km	2015	
– Hung Hom to Hong Kong Island	6 km	2019	
Kwun Tong Line Extension	3 km	2015	Rail and Property
Express Rail Link	26 km	2015	Service Concession
South Island Line (East)	7 km	2015	Rail and Property

On-going Projects

West Island Line

The West Island Line will extend the Island Line with three new underground stations at Sai Ying Pun, University (at The University of Hong Kong) and Kennedy Town. Through early proactive engagement with stakeholders and identification of their interests, the Company proposed a community-oriented rail line, sensitive to local heritage and urban renewal opportunities, thereby creating a "Community Railway". Frequent dialogue with, and input from the local communities on design and access points for the rail line has facilitated the planning, design and gazettal processes.

The West Island Line was gazetted under the Railways Ordinance in October 2007. Detailed design was commenced in early 2008 and the Environmental Impact Assessment report for the project has been approved. Tendering for advance works contracts has begun. The line is planned to commence in 2009 for completion in 2014.

Kowloon Southern Link

Satisfactory progress was made during 2008 on the Kowloon Southern Link, which will connect the existing East Rail Line's East Tsim Sha Tsui Station with West Rail Line's Nam Cheong Station and provide a new intermediate station, Austin Station, in the West Kowloon area. The main civil works, including the tunnel boring works, were substantially completed and the fitting out of Austin Station is rapidly approaching completion.

Kowloon Southern Link will connect East Rail Line to West Rail Line in West Kowloon.

Both ends of the project are now fully connected to the existing West Rail and East Rail lines and trial operations will commence in the second quarter of 2009. The line is expected to open in the second half of 2009. The extension of the pedestrian subway system in the Peking Road area, constructed under the umbrella of the Kowloon Southern Link project, has also made significant progress with the civil works now 40% complete.

Project Funding

The funding model for these new Hong Kong rail projects will take different forms, appropriately designed for each project. For the West Island Line, Government has indicated that it will consider a capital grant model whereby Government grants to the Company a sum of money to establish the financial viability of the project. The Company will be responsible for the balance of the capital costs and all of the operation, maintenance and asset replacement costs. The first part of this grant, HK$400 million, was received in February 2008 while the amount of the remaining portion, which will form the bulk of the total capital grant, is being discussed with Government.

The South Island Line (East) and the Kwun Tong Line Extension will likely follow the Company's traditional "Rail and Property" approach whereby property development rights will be granted to the Company. Suitable sites have been identified and negotiations with Government on the development rights are continuing.

A third model for future rail lines is the Service Concession model established in the Rail Merger, whereby Government or KCRC pays for the initial capital costs of the rail line, with the Company being entrusted to design and construct such lines. The Company will pay an annual concession payment to operate the line following its completion as well as being responsible for maintenance and replacement costs of the related rail assets. The Kowloon Southern Link has adopted this approach, and Shatin to Central Link and the Express Rail Link will also adopt this approach. On this basis, the Finance Committee of the Legislative Council of Hong Kong (LegCo) approved an amount of HK$2.4 billion in May to be used for design and site investigation works for the Shatin to Central Link and an amount of HK$2.8 billion in July for similar works for the Express Rail Link. On 24 November 2008, The Company entered into Entrustment Agreements with Government entrusting the Company to design the Shatin to Central Link and Express Rail

Link with costs to be borne by Government. Further funding arrangements for construction of these two lines will be made by Government at the appropriate time. The construction of the Kowloon Southern Link is being funded by KCRC as part of the Rail Merger agreement.

Completion of Projects

Phase 2 of the Tseung Kwan O Line, which provides a new station at LOHAS Park, is on schedule for completion in the second quarter of 2009 to coincide with occupancy of The Capitol at LOHAS Park.

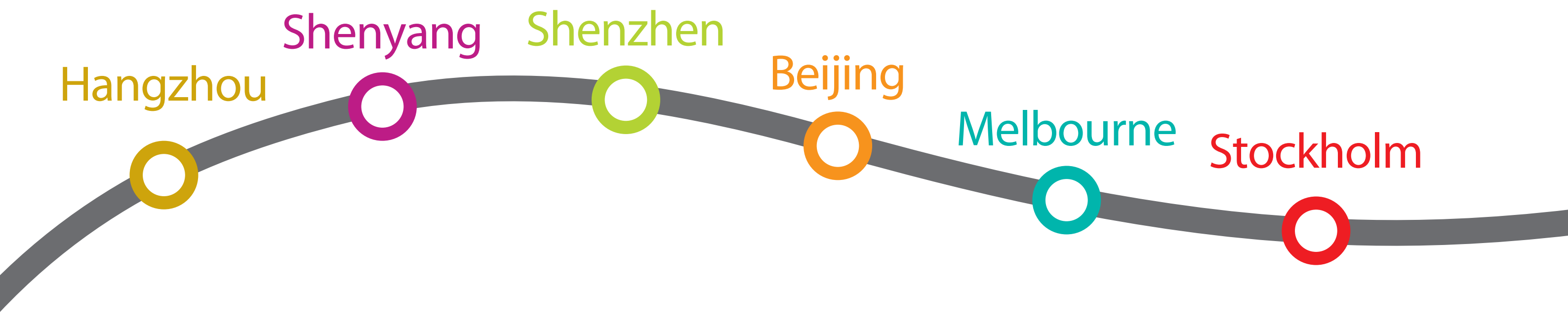
Subways and Pedestrian Links

Subways and pedestrian links extend the Company's catchment areas, enabling more members of the community to access rail benefits and customer services.

Development of the integrated entrance within the new development at No. 63 Nathan Road at Tsim Sha Tsui station (Entrance C) made good progress during the year. Structural breakthrough and electrical and mechanical modifications will be carried out in 2009.

The new subway connection to Liberte, the residential property in Lai Chi Kok, and new entrances at Cheung Lai Street at Lai Chi Kok Station began civil construction with the opening date scheduled for the second quarter of 2010. The new subway extension and satellite concourse at the north end of Tsim Sha Tsui Station is planned to be gazetted and put out to tender in the first quarter of 2009. Included in this project is the upgrading of the existing entrance A1 at Kowloon Park to provide a lift for the disabled as well as three new integrated entrances connecting to The Mira Hong Kong and Tung Ying Building redevelopment upon completion of the subway extension.

South Island Line (East) will connect Admiralty Station to Ap Lei Chau.



Building on
Our Vision and Experience

Greater Expertise and Enlarged Resources


London

The Company's operating concessions now extend to London and Stockholm.

Mainland and Overseas Growth

We made good progress in our mainland and overseas business. Overseas, our joint venture London Overground Rail Operations Limited (LOROL) brought steady improvements to the London Overground while in Sweden, we were awarded in January 2009 the franchise rights to operate the Stockholm Metro concession.

In Mainland of China, good progress was made on the Beijing Metro Line 4 (BJL4) project, while approval has been obtained from the National Development and Reform Commission (NDRC) in January 2009 for the Shenzhen Metro Line 4 (SZL4) project. In November 2008, we entered into Agreements in Principle for the operation and maintenance of Shenyang Metro Lines 1 and 2 and a Memorandum of Understanding ("MOU") for the operation and maintenance of the Daxing Line in Beijing. In January 2009, we entered into a Principle Agreement for the investment, construction and operation of Hangzhou Metro Line 1.

Mainland of China

In Beijing, the Public-Private-Partnership (PPP) company comprising MTR Corporation (49%), Beijing Infrastructure Investment Co. Ltd. (2%) and Beijing Capital Group (49%), is making steady progress with construction work on the BJL4 project. BJL4 is expected to commence operation in the fourth quarter of 2009.

Train testing and production proceeded on schedule. 20 trains were completed and tested by January 2009 and the first 10 trains were delivered to Beijing. Electrical & mechanical installation began in 24 stations, with equipment design and manufacturing well on track. Under the operation training programme at Beijing Communication School, 271 train operator trainees and station controller trainees had completed the training by January 2009.

By year end civil works construction, which is the responsibility of Beijing Municipal Government, was nearing completion with track laying well advanced.

Signing ceremony for the Principle Agreement of Hangzhou Metro Line 1.

Beijing Metro Line 4

Equipment Design and Manufacturing
Well on Track

Electrical & Mechanical Installation
in 24 Stations Began

271 Operations Trainees Completed Training
in January 2009

London Overground

Enhanced Operational Performance

Station Upgrade Works
Undertaken in 31 Stations

Stockholm Metro

Awarded Stockholm Metro concession
in January 2009

108 Kilometres of Total Route Length and 100 Stations

Delivery of new trains for BJL4.

Together with our PPP company partners, we also signed a MOU on 27 November 2008 with Beijing Metro Daxing Line Investment Company Limited, a wholly owned subsidiary of Beijing Municipal Government, for the operation and maintenance of the Daxing Line of the Beijing Metro Network. Under the MOU, the PPP company will proceed with further discussions for the operation and maintenance of the Daxing Line, a 22-km extension of BJL4, at a fee to be agreed. The proposed operation and maintenance period shall commence from the date of trial operations of the Daxing Line and conclude upon the expiry of the 30 years concession period for BJL4.

In Shenzhen, approval has been obtained from the NDRC for the SZL4 project comprising investment and construction of Phase 2 of Line 4, and the operation of Phase 1 and Phase 2 for a term of 30 years. We are now completing final regulatory processes for signing the Concession Agreement in the near future. As indicated previously, the public sector funding support for this project will be in the form of cash grants from the Shenzhen Municipal Government. Project works will be expanded to cover the whole line. Meanwhile, preparation works for taking over SZL4 Phase 1 are also underway.

Elsewhere in the Mainland, after being selected as the "preferred bidder" in July 2008, the Company entered into a Principle Agreement in January 2009 for a PPP project with Hangzhou Municipal Government and Hangzhou Metro Group Company Limited for the investment, construction and operation of Hangzhou Metro Line 1.

The Principle Agreement sets out the framework for the Company to further discuss with Hangzhou Municipal Government the Concession Agreement for investment in Hangzhou Metro Line 1 and for the operational rights for Hangzhou Metro Line 1 for a period of 25 years.

The project will be divided into Part A and Part B representing approximately 63% and 37% of the RMB 22billion investment respectively. Part A, being the civil construction of the metro system, is being undertaken and funded by the Hangzhou Metro Group Company Limited. The investment in and construction of Part B, which mainly covers the electrical and mechanical system and operation of the entire metro line, will be undertaken by the Cooperative Joint Venture, which will be owned by the Company (49%) and the Hangzhou Metro Group Company Limited (51%).

The 48-km Hangzhou Metro Line 1 consists of 41 kilometres of underground section and 7 kilometres of at-grade and elevated sections. The line is expected to commence service in 2012.

At the time of entering into the Principle Agreement with the Hangzhou partners, we also entered into a strategic agreement with the same partners to explore property development opportunities along the Hangzhou metro lines.

In November 2008, we entered into three Agreements in Principle with Shenyang Municipal Government and Shenyang Metro Group Company Limited: for the operation and maintenance of the 50-km Shenyang Metro Lines 1 and 2 for a term of 30 years; for a study of town planning and exploring property development opportunities along the corridors of Lines 1 and 2; and for conducting planning studies for future Shenyang Metro Lines 4, 9 and 10 as well as the extension of Shenyang Metro Lines 1 and 2. A Joint Venture Company comprising MTR Corporation (49%) and Shenyang Metro Group Company Limited (51%) shall be set up to work towards an Operation and Maintenance Franchise Agreement with the Shenyang Municipal Government. Lines 1 and 2 are expected to begin service by 2010 and 2012 respectively.

Overseas

Our strategy overseas continues to be "asset light", focusing on operating concessions in the railway and metro markets. In the UK, our 50:50 joint venture, LOROL brought steady improvements to the London Overground following our takeover of the concession in November 2007. London Overground is a semi-orbital route serving West, North and East London and will be a vital link for the 2012 Olympic Games. The total route network measures 107.2 kilometres and under the concession, LOROL will eventually manage 55 of the 78 stations in the network. Since taking over the concession, operational performance has been enhanced and 31 stations have undergone station upgrading works. LOROL has reduced ticketless travel, improved punctuality, which is running ahead of the contractual target, and introduced full staffing of stations throughout the hours of operation to provide better service and security.

In Sweden, we submitted our bid for the Stockholm Metro concession in August 2008, and were pleased to be awarded the franchise in January 2009. The franchise has the rights to operate the system for eight years beginning 2 November 2009 with an option for the Stockholm authorities to extend the agreement for an additional six years. The 108-km Stockholm Metro consists of three lines and 100 stations. 1.2 million passenger trips are made each day. The concession includes train and station operations as well as rolling stock maintenance. For servicing, maintenance and cleaning of trains, we will team up with Norway's Mantena, a leading maintainer of rolling stock. One of the losing bidders is taking action against the Stockholm tendering authorities regarding the award of this franchise to MTR Corporation. We await the outcome of such action.

In Australia, a joint venture comprising MTR Corporation (60%), John Holland Pty Ltd (20%) and United Group Rail Services Ltd (20%) was short-listed in September 2008 to submit a bid in April 2009 for the Melbourne Train franchise. The Melbourne train network consists of 15 routes, 213 train stations and a total of 386 kilometres. In 2006/07, the network serviced the metropolitan area of Melbourne with an annual patronage of 178.6 million passengers. In Ireland, we submitted a bid in February 2009 for the operations of the Dublin Metro North.

Punctuality has improved on London Overground.

London Overground serves West, North and East London.

Building on
Harmony and Commitment

Harmonious and United Workforce

The spokesperson for MTR Corporation's new Vision, Mission and Values is the smiling sunflower

Our 2,000 strong MTR Volunteers dedicate to caring for our community.

Human Resources

The success of the Company is based on the commitment, professionalism and caring service of our staff. Our people are our most important asset, enhancing the Company's ability to respond to change and driving forward our business expansion. In order to support business growth in the post-Rail Merger era, our goal is to create a culture of "One Company, One Team".

Our key priorities are to harmonise staff relations to ensure a stable and united workforce, to retain and develop staff resources, and to attract high-quality recruits while also showing our care and responsiveness to the community in which we operate.

One Company, One Team

With the interests of our staff being one of our key considerations, we strive to maintain harmonious staff relations within the Company as well as to support our competitiveness in the marketplace. In reflection of the unity of our culture after the Rail Merger, the new grading and salary structure together with aligned terms and conditions of our 12,000 Hong Kong staff were implemented across the entire organisation on 1 March 2008. The entire selection and appointment process was completed in April, which was ahead of the original plan by one month.

To achieve the spirit of "One Company, One Team", a new set of Vision, Mission and Values (VMV) was developed and adopted across the Company. With strong support from Senior Management, a series of VMV cascade workshops were held in all divisions. In line with the new VMV, the Company introduced a "Living the MTR Values" motivational scheme to recognise good demonstration of Values. To further build a high performance management culture and to reinforce commitment to the Values, a comprehensive review of the performance management system was conducted. It was successfully revamped to incorporate the new VMV and was launched with an extensive communications and training programme.

One of the key priorities in the larger post-Rail Merger organisation is to sustain harmonious staff relations through the establishment of a new staff consultative structure. This structure was successfully implemented in August with an enthusiastic voting response, reflecting the strongly representative nature of the new Joint Consultative Committees and Staff Consultative Council.

As one of the means to help the Company seek continuous improvement, Staff Attitude Surveys are held periodically. The first of such after the Rail Merger was successfully conducted for all staff in November 2008 with a high response rate of 96 %. This initiative provided a direct means for staff to express their views and opinions about different aspects of the Company, helping us to identify key areas for improvement. The findings reflected that during a time of intense change, the Company had done well to maintain high staff engagement and commitment.

Selection and **Appointment Process**
Completed for **Over 12,000 HK Staff in April 2008,** One Month Ahead of the Schedule

1st Staff Attitude Survey
after Rail Merger was Successfully Conducted, Reflecting **High Staff Engagement & Commitment**
84% of Staff Feel Proud to be a Member of the Company;
81% of Staff are Willing to Do Extra in Order to Help the Company to Succeed

73,225 / 10,821 Man Days for **Operations / Management Training** Respectively

Successful Launch of Improved **Performance Management System** Incorporating **New Set of Vision, Mission and Values**

87 More Time Reaching Community Projects Completed with **2,000 Volunteers** Involved

In addition, to show appreciation for the dedication and hard work of staff in maintaining high quality service during the merger process, a large-scale merger celebration event was held early in the year and Special Grand Awards were also given to certain teams in recognition of their significant contribution to the success of the Rail Merger.

Caring for the Community

The Company has long prided itself on commitment to the community and believes strongly in its central role as a caring organisation that contributes wholeheartedly to the quality of life, health and progress of Hong Kong's society.

In 2008, our colleagues continued to take part in various forms of community service. During the year, there were 87 volunteering projects in our "More Time Reaching Community" scheme in which a total of 2,000 volunteers participated in activities involving the elderly, the physically and mentally challenged, as well as underprivileged children and families. In April, the fourth MTR HONG KONG Race Walking event was held in Central to encourage Hong Kong people to integrate regular exercise into their daily lives. The event raised HK$1.3 million for health education. Further community initiatives included a variety show presented by schoolchildren, the elderly and executives of the Corporation for 350 members of the Shek Kip Mei community, and our MTR Volunteers' participation in a rice dumpling delivery day to the lonely elderly. In 2008, in recognition of the Company's contributions to society through community involvement, staff volunteering and providing a safe and family friendly environment for our employees, we were once again awarded by the Hong Kong Council of Social Service the Caring Company Logo for the year 2008/09.

Training and Development

A broad range of proactive training and development programmes was undertaken throughout the year to meet post-Rail merger challenges, particularly in the areas of railway safety, railway operations and maintenance, multi-skilling, redeployment and new recruits. We also focused on rules and safety qualification training in preparation for the launch of the new Railway Safety Rules for the merged Railway.

In order to enhance service operations and provide caring customer services, a customised programme, "Being a Service Coach", was launched to more than a thousand supervisors. The programme highlights changes in mindset and enhancement of service coaching skills and knowledge.

Training is essential and ongoing to equip staff with skills.

Our strong commitment to training and development has gained recognition from global and local professional associations, including the "American Society for Training and Development (ASTD)", "Hong Kong Best Practice Management Group" and the "China STAFF magazine". The award- winning initiative of "'You Have a Say' Work Improvement Team (WIT) Training Scheme" won the "ASTD Excellence in Practice Awards" and "Best Practice Award – Training and People Development" in 2008, which was highly appreciated. The motto "You have a Say in what you do everyday!" summaries the spirit of WIT, since all our staff are engaged in improving daily work processes and creating value for the Company.

Leadership Development

We continue to devote efforts to leadership development through ongoing programmes such as our Executive Associate Scheme and a Graduate Trainee programme with graduates from both Hong Kong SAR and the Mainland of China.

During 2008, all 11 young managers in the Executive Associate Scheme underwent cross-functional placements including offshore assignments to widen their exposure and pave the way for a broader career horizon. The 12-month mentoring scheme for Executive Associates was completed in May.

Five Hong Kong and six Mainland of China Graduate Trainees were recruited in 2008 to provide a continuous source of high potential staff for the leadership pipeline. In addition, several Graduate Engineers and functional associates were recruited with the aim of grooming them for their chosen professional path.

Support for Growth Business

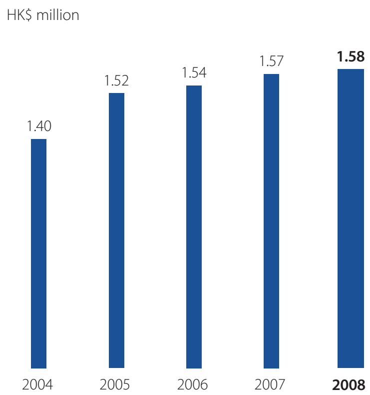
As our activities expand outside Hong Kong, we continue to provide proactive training support to offshore projects. During the year, Mainland local recruits for BJL4 and SZL4 were given comprehensive training with job attachment in Hong Kong to ensure operational readiness of these two key new projects.

In Hong Kong, with the expansion of the railway network, substantial manpower resources are required for their planning, construction and operations. To cater for the upsurge in manpower requirements, early planning for the recruitment and retention of expertise commenced in 2008 and is making good progress.

Staff embracing the new Vision, Mission and Values in workshops.

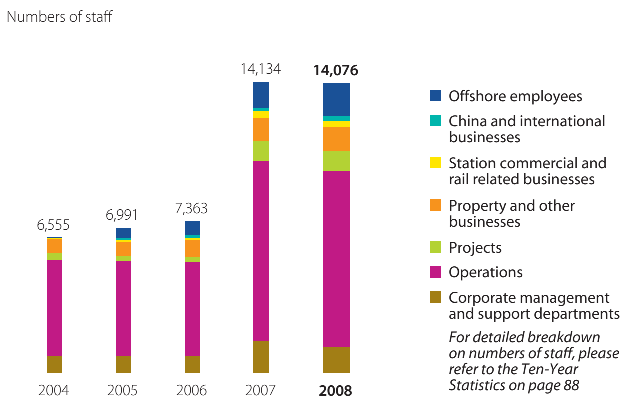
Staff Productivity – Turnover Per Operating Railway Employee

Productivity has shown continuous improvement.



Total Staff Strength

The Company maintained a pool of skilled employees in support of our business expansion in Hong Kong and overseas.



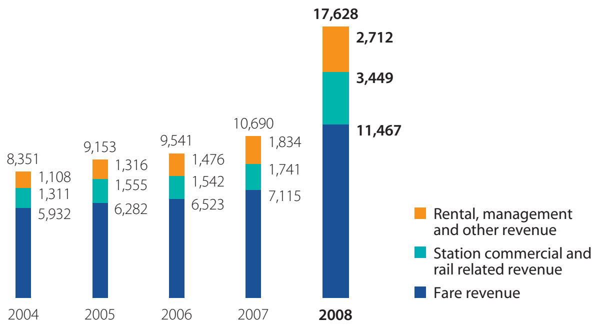
For detailed breakdown on numbers of staff, please refer to the Ten-Year Statistics on page 88

Financial Review

Turnover

Revenue increased across the board due to full-year impact of the Rail Merger.

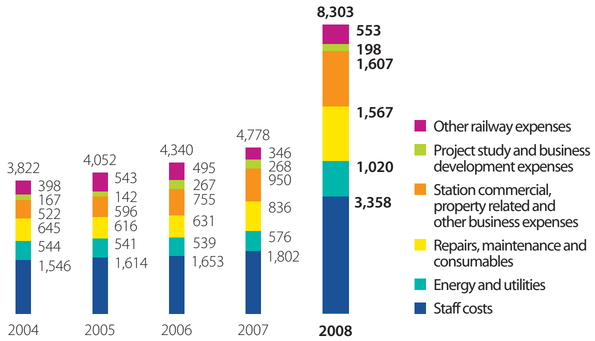
in HK$ million



Operating Expenses

The cost increases were in line with network expansion after the Rail Merger.

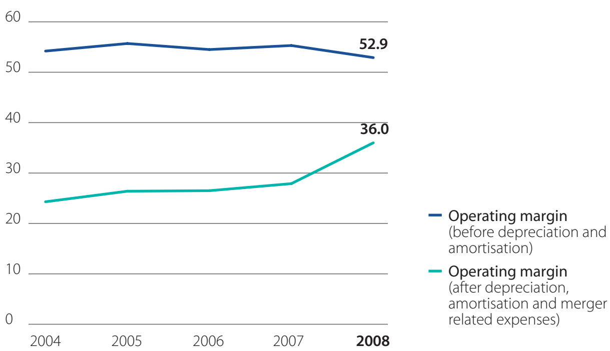
in HK$ million



Operating Margin

Operating margin before depreciation and amortisatin dropped due to fare reduction and lower margin of the pre-merger KCRC businesses.

Percentage



Review of 2008 Financial Results

Profit and Loss

The Group's revenue and operating profit from recurring businesses achieved strong growth in 2008 with the full-year impact of the Rail Merger. Total revenue rose by 64.9% to HK$17,628 million while operating profit from railway and related businesses increased by 57.7% to HK$9,325 million.

Total fare revenue for 2008 increased by 61.2% to HK$11,467 million with fare revenue from Domestic Service increasing by 27.6% to HK$7,930 million as a result of a 31.6% increase in patronage to 1,205 million and a 3% decrease in average fare to HK$6.58. Compared with the combined fare revenue of the Company and pre-merger KCRC in 2007, fare revenue from Domestic Service in 2008 decreased by 1% due to a 4.8% decrease in average fare resulting from the one-off fare reduction implemented on the Rail Merger Day partly offset by a 4% increase in patronage. Fare revenue from Cross-boundary Service, when compared with the equivalent 12 month revenue for such service in 2007, rose by 1.2% to HK$2,283 million with patronage increasing by 1.4% to 93 million and average fare decreasing slightly by 0.2% to HK$24.45. Fare revenue from Airport Express increased by 2.7% to HK$673 million with a patronage growth of 4.2% to 10.6 million and an average fare decrease of 1.4% to HK$63.47 due to the change in trip distribution and free ride promotions. Light Rail, Bus and Intercity services contributed a total of HK$581 million in fare revenue, a growth of 0.8% from the equivalent 12 month revenue for such services in 2007.

Revenue from station commercial and rail related businesses also recorded strong growth in 2008. Advertising revenue increased by 25% to HK$741 million, an increase of 11.3% over the equivalent comparable combined revenue of the Company and pre-merger KCRC in 2007 (Combined Non-fare Revenue). Revenue from station retail business rose 209.8% to HK$1,546 million, or 42.3% from the equivalent Combined Non-fare Revenue, mainly attributable to the increased retail area from the Rail Merger, which included the addition of Duty Free shops, favourable rental renewal rates and the full-year effect of new shops at Lok Ma Chau station. Telecommunication income increased by 49% from last year and 27.6% from the equivalent Combined Non-fare Revenue in 2007 to HK$356 million, mainly due to a termination payment received from a telecommunication service operator. Excluding this one-off item, telecommunication income would have increased by 13% as compared to 2007, or decreased by 3.2% from the equivalent Combined Non-fare Revenue in 2007 due to the shift of mobile usage from 2G to 3G. Consultancy business recorded a revenue decrease of 18.1% to HK$158 million mainly due to the completion of the majority of the works on Shanghai Metro Line 9 and a more focused strategy on consulting. Including other miscellaneous incomes, total revenue from station commercial and rail related businesses increased by 98.1% to HK$3,449 million, or a growth of 33.4% from the equivalent Combined Non-fare Revenue in 2007.

Rental, management and other revenue in 2008 increased by 47.9% from last year to HK$2,712 million with revenue from property rental and management in 2008 increasing by 46.1% to HK$2,556 million, or 27.6% over the equivalent Combined Non-fare Revenue in 2007, reflecting the strong demand for office and retail space early on in the year, as well as the full-year effect of the opening of Elements. Ngong Ping 360 generated HK$156 million of revenue in 2008.

Total operating costs rose by 73.8% to HK$8,303 million in 2008, mainly due to the Rail Merger with increases in staff costs, energy and utilities, operational rent and rates, repairs and maintenance as well as general and administration expenses. The larger increase in stores and spares consumed was attributable to the overhaul of West Rail and East Rail trains. In line with revenue growth, expenses relating to station commercial and rail related businesses increased by 100.5% while expenses relating to property ownership, management and other businesses increased by 45.4%. Compared with the comparable combined operating costs of the Company and pre-merger KCRC in 2007, total operating costs would have increased by 9.9%.

Operating profit from railway and related businesses before depreciation and amortisation therefore increased by 57.7% to HK$9,325 million. Operating margin decreased from 55.3% in 2007 to 52.9% in 2008 due to the fare reduction at the time of the Rail Merger and the lower operating margin of the pre-merger KCRC businesses.

Profit from Underlying Businesses of
HK$8,185 million

Net Profit attributable to Equity Shareholders of
HK$8,284 million

Turnover Increased 64.9% to
HK$17,628 million

Profit Contribution from Property Development of
HK$4,670 million

Net Assets Increased 7.5% to
HK$97,822 million

Net Cash Inflow of
HK$3,698 million
Generated to Reduce Borrowings

HK$1,750 million
New Financings Raised on Attractive Terms

Credit Ratings Upgraded
to **AA+** and Affirmed
at **Aa2** on par with Hong Kong SAR

Profits on property developments in 2008 amounted to HK$4,670 million mainly from profit booking relating to The Capitol at LOHAS Park and The Palazzo in Shatin, and to a lesser extent, the sale of units in inventory at Harbour Green and The Arch, as well as deferred income recognition for properties at Coastal Skyline and Caribbean Coast at Tung Chung Station and Elements at Kowloon Station. Compared with 2007, property development profits decreased by 43.8% due to the significant profit recognised from Le Point in Tseung Kwan O in 2007 and the decline in property prices in the second half of 2008. As a result, operating profit before depreciation and amortisation decreased slightly by 1.6% to HK$13,995 million.

Depreciation and amortisation charges increased by 7% to HK$2,930 million due to the additional amortisation charge on service concession assets relating to the Rail Merger. Merger related expenses, comprising post-merger integration expenses not eligible for capitalisation, decreased by 72.5% to HK$53 million as a result of the one-off provision for Voluntary Separation Scheme payments in 2007.

Interest and finance charges increased by 51.8% to HK$1,998 million mainly due to the full year interest on debt and the capitalised fixed annual payment, both relating to the Rail Merger. Average borrowing cost decreased to 4.8% from 5.6% in 2007. With the decline in property prices during the second half of the year, a net pre-tax loss in investment property valuation of HK$146 million was recorded as compared with a net pre-tax gain of HK$8,011 million last year. The Company's share of net profit from non-controlled subsidiaries and associates increased by 60.6% to HK$159 million, comprising HK$136 million from Octopus Holdings Limited and HK$23 million from London Overground Rail Operations Ltd.

Profit before taxation decreased by 50.6% to HK$9,027 million and accordingly, taxation decreased by 75.8% to HK$747 million due to the profit reduction as well as the impact on deferred tax from the lowering of the Hong Kong profits tax rate from 17.5% to 16.5% effective from 2008. Current tax for 2008 amounted to HK$1,024 million, which was partly offset by deferred tax credit of HK$277 million resulting mainly from the reduction in profits tax rate. Net profit for the Group in 2008 decreased by 45.5% to HK$8,280 million whilst net profit attributable to equity shareholders was HK$8,284 million. Correspondingly, earnings per share decreased from HK$2.72 in 2007 to HK$1.47 in 2008.

Excluding investment property revaluation and the related deferred tax provision, net profit from underlying businesses attributable to equity shareholders decreased by 4.5% from HK$8,571 million to HK$8,185 million, reflecting lower property development profits being offset by substantial growth in earnings from our recurring businesses. Earnings per share based on underlying profit decreased by 5.8% from HK$1.54 to HK$1.45.

With the strong financial results, particularly from our recurring businesses, the Board has recommended a final dividend of HK$0.34 per share, which when added to the interim dividend of HK$0.14 per share, will bring full year dividend to HK$0.48 per share, an increase of HK$0.03 per share or 6.7% compared with 2007. The final dividend, amounting to HK$1,925 million in total, offers a scrip dividend option to all shareholders except those with registered addresses in the United States of America or any of its territories or possessions. As in previous years, The Financial Secretary Incorporated ("FSI") has agreed to receive its entitlement to dividends in the form of shares to the extent necessary to ensure that a maximum of 50% of the Company's total dividend will be paid in cash.

Balance Sheet

The Group's balance sheet strengthened further in 2008 with a 7.5% increase in net assets from HK$91,037 million as at 31 December 2007 to HK$97,822 million as at 31 December 2008.

Total fixed assets decreased from HK$132,417 million in 2007 to HK$131,004 million as at 31 December 2008 due to depreciation charges for the year. Railway construction in progress, mainly related to the LOHAS Park Station project, increased from HK$424 million in 2007 to HK$658 million. Deferred expenditure, comprising advance works on Shenzhen Metro Line 4 and design costs on potential railway extensions such as the West Island Line and South Island Line East, increased from HK$825 million in 2007 to HK$1,988 million.

Property development in progress includes development costs incurred on property developments, costs for acquiring property development rights in the Rail Merger, land premium payments and the deemed interest element of the interest free loan to a developer. During the year, property development in progress decreased from HK$9,066 million in 2007 to HK$7,895 million due to the transfer-out of the half land premium for The Capitol and acquisition cost of The Palazzo upon completion of these developments, partly offset by the half land premium paid for the Che Kung Temple development site. Properties held for sale increased from HK$756 million in 2007 to HK$2,228 million, mainly comprising residential units at The Palazzo and The Arch as well as retail space at Island Harbourview. Property management rights decreased from HK$40 million in 2007 to HK$35 million due to amortisation.

Investment in securities increased from HK$333 million to HK$471 million. Derivative financial assets and liabilities increased from HK$273 million and HK$192 million respectively in 2007 to HK$528 million and HK$305 million as at 31 December 2008, mainly due to decline in interest rates during the period.

Interests in non-controlled subsidiaries and associates increased from HK$268 million and HK$205 million respectively in 2007 to HK$381 million and HK$743 million in 2008 as a result of continued net asset growth at Octopus Holdings Limited and London Overground Rail Operations Ltd as well as, for interest in associates, the injection of the last tranche of equity into the Beijing Metro Line 4 project.

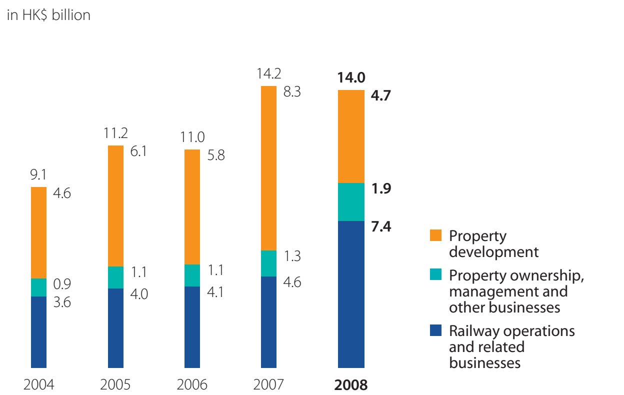
Debtors, deposits and payments in advance increased from HK$5,167 million in 2007 to HK$7,190 million as at 31 December 2008 due to the increase in accounts receivable relating to property development, which increased from HK$3,774 million to HK$5,818 million. This increase in property development receivable was mainly due to receivables from pre-sales of units at The Capitol and The Palazzo. Amounts due from the Government and other related parties decreased from HK$544 million in 2007 to HK$426 million, comprising mainly payments due from KCRC in respect of project management for the Kowloon Southern Link and various capital works relating to the Rail Merger as well as payments from the Government in respect of West Rail property developments and detailed design works on the Express Rail Link and Shatin to Central Link.

Total loans outstanding decreased from HK$34,050 million in 2007 to HK$31,289 million due to loan reduction from net cash generated during the year.

Amounts due to related parties included the Group's obligation to reimburse KCRC after tender award on the costs of property enabling works for certain KCRC property development sites and the accrued fixed annual payment for the service concession. The amount decreased from HK$975 million in 2007 to HK$882 million as at 31 December 2008, reflecting the reimbursement made to KCRC on enabling works for the Che Kung Temple development upon tender award during the year.

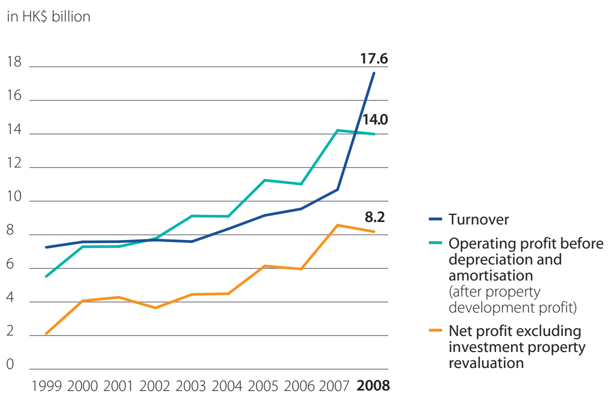
Operating Profit Contributions

Significant growths in profits were achieved in recurring businesses after the Rail Merger.



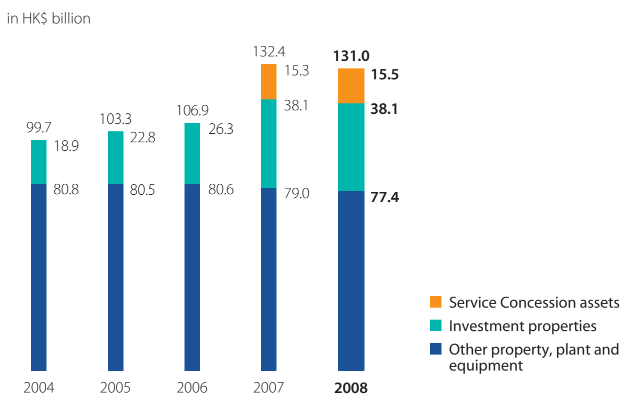
Net Results from Underlying Businesses

Net profits remained strong due to increased profits from recurring businesses despite lower property development profits.



Fixed Assets Growth

Fixed assets as at 31 December 2008 slightly decreased due to depreciation charges for the year.



Deferred income decreased from HK$515 million in 2007 to HK$156 million as at 31 December 2008 following profit recognition for Coastal Skyline and Caribbean Coast at Tung Chung Station and Elements at Kowloon Station.

With the Company's cumulative tax losses being full-utilised in 2008, provisional tax for the assessable year of 2008/09 of HK$575 million was paid in 2008. Current tax liabilities as at 31 December 2008 amounted to HK$450 million. Deferred tax liabilities decreased from HK$12,574 million in 2007 to HK$12,220 million, mainly due to the reduction in profits tax rate.

Share capital, share premium and capital reserve increased by HK$1,291 million to HK$41,119 million at the end of 2008 as a result of shares issued for scrip dividend and share options exercised. Together with the increase in retained earnings, net of dividends, of HK$5,796 million partly offset by the decrease in fixed asset revaluation reserve and other reserves of HK$300 million, total equity attributable to equity shareholders of the Company increased by HK$6,787 million to HK$97,801 million as at 31 December 2008. Including obligations under service concession as a component of debt, the Group's net debt-to-equity ratio decreased from 48.5% at 2007 year end to 42.1% at 2008 year end.

Cash Flow

Net cash inflow generated from railway and related activities increased from HK$5,974 million in 2007 to HK$8,921 million in 2008, while cash receipts from developers and purchasers in respect of property development projects decreased from HK$5,824 million in 2007 to HK$4,448 million in 2008 due to timing difference on property receipts. Including the HK$400 million of government grant for the West Island Line project as well as the loan repayments and dividend distribution from non-controlled subsidiaries and associates of HK$132 million, total cash inflow for 2008 increased by HK$2,165 million to HK$13,901 million over 2007. Outflows for capital projects and property developments increased by HK$3,407 million to HK$5,896 million in 2008 primarily due to new railway projects, an increase in capital expenditures on the expanded railway network after the Rail Merger, and the half land premium for the Che Kung Temple property development. After settlement of the fixed annual payment of HK$750 million on the service concession, the equity injection of HK$515 million into the Beijing Line 4 associate company and payments on interest, dividends and other working capital, net cash inflow before non-recurring merger related payments decreased from HK$6,477 million in 2007 to HK$4,014 million in 2008. Net cash inflow of the Group in 2008, after non-recurring merger related expenses of HK$316 million, amounted to HK$3,698 million, of which HK$3,538 million was used to reduce borrowings.

Financing Activities

New Financings

In September 2008, what began in the USA in 2007 as a subprime mortgage crisis developed into a full-blown global financial crisis. With major banks and financial institutions suffering unprecedented losses and much depleted capital bases, global debt markets almost ground to a halt with lenders unwilling to lend and credit spreads increasing to unprecedented levels. As major governments worldwide moved to recapitalise banks, improve credit market liquidity and formulate massive fiscal stimulus plans, the US Federal Reserve aggressively cut the Fed Funds rate to an unprecedented level of 0 – 0.25%. In response, short- and long-term rates declined precipitously in the USA and yield curves flattened, reflecting the significant risk of price deflation.

In Hong Kong, both interbank and corporate lending activities also contracted significantly as banks continued to deleverage. Credit margins increased, further straining the financing capability of even the most creditworthy borrowers. Mirroring the drop in US interest rates, 3-month HIBOR rates declined significantly from a high of 4.5% in October to 0.95% by year end, whilst the yield of 10-year Hong Kong Exchange Fund Note dropped to 1.2%.

As the current crisis unfolded, the Group continued to be in a strong liquidity position, enjoying significant operating cash surplus and maintaining substantial undrawn committed banking facilities, all of them arranged prior to the crisis. Because of its well funded position, the Group did not embark on any major financing activities during the year. Instead, to further strengthen liquidity, it had chosen to tap, on an opportunistic basis, pockets of supply of Hong Kong dollars in the debt market via private placements. In this manner the Group raised a total of HK$1.75 billion during the year at highly attractive rate levels through note issuance from the debt issuance programme, reflecting investors' continued strong confidence in the Group. As at the end of 2008, the Group had total undrawn committed facilities of HK$10.4 billion, which together with continuing strong operating cash flows are expected to meet all our cash requirements well into the second half of 2010.

Cost of Borrowing

Benefitting from declining interest rates, the Group's average borrowing cost for 2008 fell to 4.8% from 5.6% in 2007. However, net interest expense charged to the Profit and Loss Account, after interest capitalised of HK$149 million, rose to HK$1,998 million in 2008 from HK$1,316 million in 2007, mainly due to the full year impact of interest on additional borrowings to finance the Rail Merger as well as the interest element of HK$721 million on the capitalised fixed annual merger payments.

Treasury Risk Management

The Board of Directors approves policies for overall treasury risk management including specific areas, such as liquidity risk, interest rate risk, foreign exchange risk, credit risk, concentration risk, use of derivative and non-derivative financial instruments, as well as investment of excess liquidity.

The Group's well established Preferred Financing Model (the "Model") is an integral part of these risk management policies. The Model specifies the preferred mix of fixed and floating rate debts, sources of funds from capital and loan markets, and debt maturity profile as well as a permitted level of foreign currency debts and an adequate length of financing horizon for coverage of forward funding requirements, against which the Group's financing related liquidity, interest rate and currency risk exposures are measured, monitored and controlled. During 2008, in accordance with the Model, the Group has maintained a well diversified debt portfolio with adequate forward coverage of funding requirements.

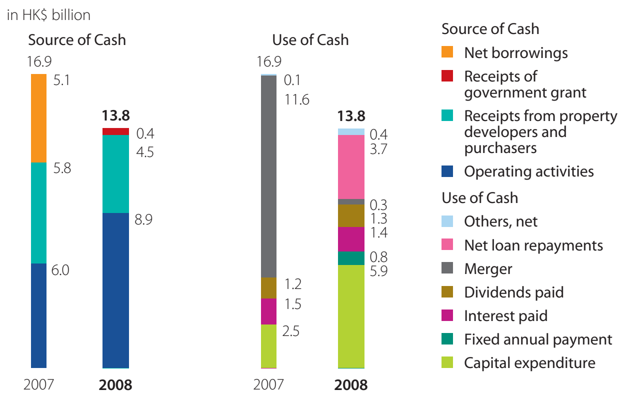
The use of derivative financial instruments to control and hedge against interest rate and foreign exchange risk exposures forms an integral part of the Group's risk management strategy. In accordance with Board policy, these instruments shall only be used for controlling or hedging risk exposures, and cannot be used for speculative purposes. All of the derivative instruments used by the Group are over-the-counter derivatives comprising principally interest rate swaps, cross currency swaps and foreign exchange forward contracts.

To control and diversify counterparty risks, the Group limits its exposure to credit risk by placing deposits and transacting derivative financial instruments only with financial institutions with acceptable investment grade credit ratings.

All derivative financial instruments are subject to a maximum counterparty limit based on the respective counterparty's credit ratings in accordance with policy approved by the Board. Credit exposure in terms of estimated fair market value of and

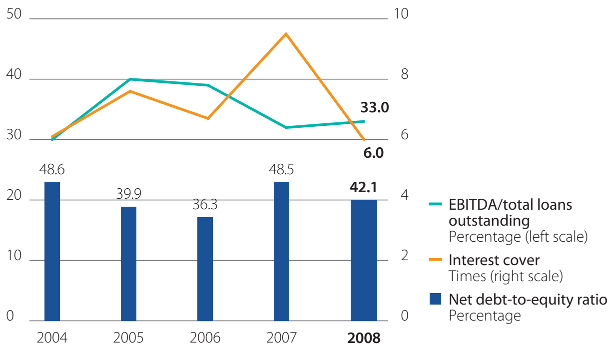
Cash Utilisation

Net cash inflow generated in 2008 was used to reduce borrowings.



Debt Servicing Capability

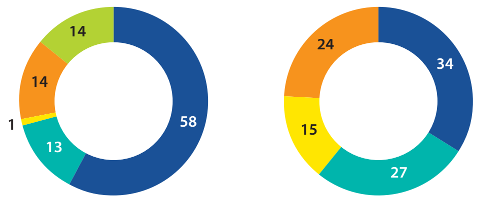
Total debt outstanding including obligations under service concession decreased in 2008, with a corresponding decrease in debt-to-equity ratio.



Sources of Borrowing

One of our strategies is to diversify our funding sources both in terms of markets and instruments.

Percentage (As at 31 December 2008)



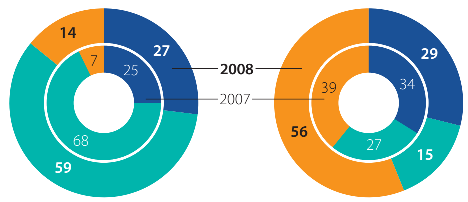
By market
- Hong Kong
- US
- Japan
- Europe
- Asia (excluding Japan)

By instrument
- US$ Global bonds
- Medium term notes
- US$ Eurobonds
- Bank loans & export credits

Use of Interest Rate and Currency Risk Hedging Products

Derivative financial instruments are used for hedging purposes only, and no speculation is allowed.

Percentage* (As at 31 December 2008)



By instrument
- Interest rate swaps
- Cross currency & interest rate swaps
- Foreign exchange forwards

By maturity
- Beyond 5 years
- 2 to 5 years
- Within 2 years

* Calculated based on nominal value

largest potential loss arising from these instruments based on the "value-at-risk" concept is measured, monitored and controlled against respective counterparty limits. To further reduce risk exposure, the Group also applies set-off and netting arrangements across all derivative financial instruments and other financial transactions with the same counterparty.

All deposits are similarly subject to a separate counterparty limit based on the respective counterparty's credit ratings and/or status as Hong Kong's note issuing bank. There is also a limit on the length of time that the Group can maintain a deposit with a counterparty based upon its credit ratings. Deposit outstanding and maturity profile are monitored on a frequent basis to ensure they are within the approved limits.

The Group actively monitors credit ratings and changes of all its counterparties and other information such as the counterparties' credit default swap levels, and would on the basis of this information adjust the maximum counterparty limits of and/or credit exposure to its counterparties.

The Group adopts a prudent approach to managing liquidity risk, and will maintain sufficient undrawn committed banking facilities to provide forward coverage of at least 6 to 15 months of all projected cash requirements, including debt repayments and capital expenditures, as specified by the Model. The Group also conducts stress testing of its projected cash flow to analyse liquidity risk, and would arrange additional banking facilities or debt issuance or otherwise take appropriate actions if necessary should such stress tests reveal significant risk of material cash flow shortfall.

Credit Ratings

The Company was the first Hong Kong corporate entity to obtain internationally recognised credit ratings and has since maintained strong investment grade ratings on a par with the Hong Kong SAR Government, reflecting its strong financial position and support from the Government.

In June, Moody's re-affirmed the Company's foreign currency issuer and senior unsecured debt ratings at Aa2 with a stable outlook, the same as the Hong Kong SAR Government. Subsequently in July, Standard & Poor's upgraded the Company's foreign currency issuer and senior unsecured debt ratings from AA to AA+ with a stable outlook, in line with the same corresponding upgrade of the sovereign rating for the Hong Kong SAR Government.

In August, Rating & Investment Inc. of Japan raised the Company's foreign currency issuer and Hong Kong dollar issuer ratings to AA+ from AA, and re-affirmed its Hong Kong dollar short-term credit rating at a • 1+, with a stable outlook.

Credit ratings	Short-term ratings*	Long-term ratings*
Standard & Poor's	A-1+/A-1+	AA+/AA+
Moody's	-/P-1	Aa2/Aa2
Rating & Investment Information Inc.	a • 1+/-	AA+/AA+

* Ratings for Hong Kong dollar/foreign currency denominated debts respectively

Financing Capacity

The Group's capital expenditure programme consists mainly of three parts – railway projects in Hong Kong, property investment and development in Hong Kong, and overseas investments.

Capital expenditure for railway projects in Hong Kong comprises mainly investment in and expenditures relating to new railway projects, such as the West Island Line, South Island Line East and Kwun Tong Line Extension, as well as outlays for maintaining and upgrading the existing rail lines. For property investment and development, it comprises mainly the remaining fit-out works for Elements, fit-out works for the retail areas of The Capitol and Tseung Kwan O Area 56, common infrastructure works for the Area 86 development sites, as well as renovation of various existing shopping centres in Hong Kong. For overseas investments, it consists mainly of equity contribution to Shenzhen Metro Line 4.

Based on current programmes, total capital expenditures for the next three years of 2009, 2010 and 2011 are estimated at HK$23.3 billion for railway projects in Hong Kong, HK$1.0 billion for property investment and development in Hong Kong, and HK$1.9 billion for overseas investments, mainly our equity contribution to Shenzhen Metro Line 4. Out of this total budget of HK$26.2 billion, an estimated amount of HK$6.0 billion is expected to be incurred in 2009, HK$5.9 billion in 2010, and HK$14.3 billion in 2011. These numbers exclude Government grants receivable for West Island Line.

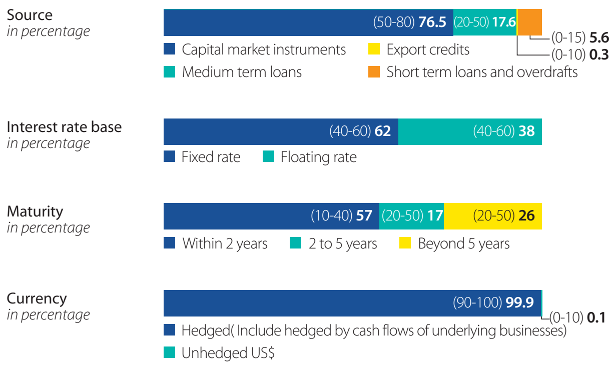
Our current financing coverage horizon based on the above capital expenditure programme taking into account loan repayments, strong cash flows from our businesses and committed undrawn banking facilities of HK$10.4 billion as at 31 December 2008, extends into the second half of 2010.

With the current global financial crisis continuing to develop, fund raising in the capital and loan markets will remain difficult in the foreseeable future. However, with our well funded situation, significant forward coverage, and continuing support from investors, we remain confident that we will attract the necessary funds for our capital expenditure programme.

Preferred Financing Model and Debt Profile

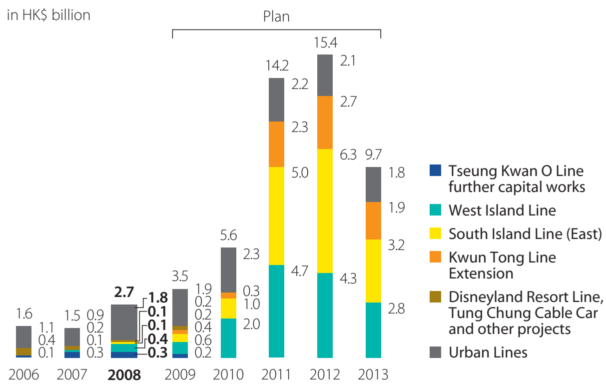
The Preferred Financing Model provides guidance on fund raising and risk management, helping to achieve a well balanced debt portfolio.

(Preferred Financing Model) vs. **Actual debt profile** As at 31 December 2008



Investment in New Railway Lines and Existing Network in Hong Kong

Projected capital expenditures between 2009-2011, based on existing network and committed projects, are estimated at HK$23.3 billion, excluding Government grants receivable for West Island Line.



Ten-Year Statistics

	2008*	#2007*	2006*	2005*	2004*	2003*	2002*	2001*	2000*	1999
Financial										
Profit and Loss Account *in HK$ million*										
Turnover	**17,628**	10,690	9,541	9,153	8,351	7,594	7,686	7,592	7,577	7,252
Operating profit before depreciation and amortisation	**13,995**	14,216	11,018	11,246	9,097	9,116	7,769	7,301	7,290	5,523
Depreciation and amortisation	**2,930**	2,739	2,674	2,682	2,499	2,402	2,470	2,178	2,091	2,039
Interest and finance charges	**1,998**	1,316	1,398	1,361	1,450	1,539	1,125	874	1,143	1,104
Change in fair value (net of deferred tax) on investment properties†	**99**	6,609	1,797	2,310	2,051	–	–	–	–	–
Profit	**8,280**	15,182	7,758	8,463	6,543	4,450	3,579	4,278	4,069	2,116
Profit from underlying businesses attributable to equity shareholders††	**8,185**	8,571	5,962	6,140	4,492	4,450	3,579	4,278	4,069	2,116
Dividend proposed and declared	**2,715**	2,522	2,328	2,299	2,259	2,215	2,161	2,118	500	–
Earnings per share *in HK$*	**1.47**	2.72	1.41	1.55	1.23	0.85	0.70	0.85	0.81	0.42
Balance Sheet *in HK$ million*										
Total assets	**159,338**	155,668	120,421	113,666	106,674	102,366	101,119	98,126	92,565	87,250
Loans, other obligations and bank overdrafts	**31,289**	34,050	28,152	28,264	30,378	32,025	33,508	31,385	27,203	23,177
Obligations under service concession	**10,656**	10,685	–	–	–	–	–	–	–	–
Deferred income	**156**	515	1,682	3,584	4,638	5,061	6,226	8,411	10,403	13,776
Total equity attributable to equity shareholders	**97,801**	91,014	76,767	69,875	61,892	57,292	53,574	53,893	50,355	45,115
Financial Ratios *in percentage*										
Operating margin	**52.9**	55.3	54.5	55.7	54.2	49.3	52.2	53.4	51.7	48.2
Non-fare revenue as a percentage of turnover	**35.0**	33.4	31.6	31.4	29.0	27.7	25.6	24.6	24.6	22.2
Net debt-to-equity ratio	**42.1**	48.5	36.3	39.9	48.6	55.2	59.3	57.8	53.7	51.2
Net debt-to-equity ratio (excluding revaluation reserves)	**42.5**	49.2	36.7	40.3	48.9	62.6	67.4	66.0	61.8	58.3
Interest cover *in times*	**6.0**	9.0	6.7	7.6	6.1	5.6	4.5	3.8	3.8	3.7
Employees										
Corporate management and support departments	**1,235**	1,530	823	810	792	793	824	870	911	967
Station commercial and rail related businesses	**293**	305	82	82	67	61	62	60	55	64
Operations	**8,540**	8,770	4,521	4,600	4,669	4,730	4,836	4,756	4,943	5,132
Projects	**995**	942	260	242	362	398	546	973	898	912
Property and other businesses	**1,170**	1,141	832	688	660	642	618	567	519	456
China and international businesses	**197**	135	112	83	–	–	–	–	–	–
Offshore employees	**1,646**	1,311	733	486	5	5	5	5	6	6
Total	**14,076**	14,134	7,363	6,991	6,555	6,629	6,891	7,231	7,332	7,537

† New accounting standard requirement

†† Excluding change in fair value of investment properties net of related deferred tax

	2008*	#2007*	2006*	2005*	2004*	2003*	2002*	2001*	2000*	1999
Railway Operations										
Revenue car km operated *in thousands*										
Domestic and Cross-boundary	**245,856**	128,041	115,784	114,449	114,364	112,823	103,318	96,751	92,199	94,704
Airport Express	**19,891**	19,956	20,077	17,122	16,081	15,227	19,467	19,458	19,557	19,394
Light Rail	**8,984**	755	–	–	–	–	–	–	–	–
Total number of passengers *in thousands*										
Domestic Service	**1,205,448**	915,755	866,754	857,954	833,550	770,419	777,210	758,421	767,416	779,309
Cross-boundary Service	**93,401**	8,243	–	–	–	–	–	–	–	–
Airport Express	**10,601**	10,175	9,576	8,493	8,015	6,849	8,457	9,022	10,349	10,396
Light Rail	**137,730**	11,100	–	–	–	–	–	–	–	–
Bus	**34,736**	2,757	–	–	–	–	–	–	–	–
Intercity	**3,220**	285	–	–	–	–	–	–	–	–
Average number of passengers *in thousands*										
Domestic Service – weekday average	**3,514**	2,662§	2,523	2,497	2,403	2,240	2,261	2,231	2,240	2,284
Cross-boundary Service – daily average	**255**	–@	–	–	–	–	–	–	–	–
Airport Express – daily average	**29**	28	26	23	22	19	23	25	28	29
Light Rail – weekday average	**385**	–@	–	–	–	–	–	–	–	–
Bus – weekday average	**99**	–@	–	–	–	–	–	–	–	–
Intercity – daily average	**9**	–@	–	–	–	–	–	–	–	–
Average passenger km travelled										
Domestic and Cross-boundary	**10.4**	7.9	7.7	7.6	7.7	7.7	7.6	7.4	7.3	7.4
Airport Express	**29.4**	29.5	29.7	30.4	30.2	29.7	29.9	29.8	29.7	29.9
Light Rail	**3.0**	3.0	–	–	–	–	–	–	–	–
Bus	**4.6**	4.6	–	–	–	–	–	–	–	–
Average car occupancy *number of passengers*										
Domestic and Cross-boundary	**55**	58	58	57	56	53	57	58	61	61
Airport Express	**16**	15	14	15	15	13	13	14	16	16
Light Rail	**46**	45	–	–	–	–	–	–	–	–
Proportion of franchised public transport boardings *in percentage*	**42.0**	26.7	25.0	25.2	24.8	24.3	23.5	23.5	24.1	25.2
HK$ per car km operated (all services)										
Fare revenue	**41.7**	47.8	48.0	47.7	45.5	42.9	46.6	49.3	51.1	49.4
Railway operating costs	**21.7**	21.6	22.1	22.8	22.3	22.5	22.8	24.6	26.8	27.3
Railway operating profit	**20.0**	26.2	25.9	24.9	23.2	20.4	23.8	24.7	24.3	22.1
HK$ per passenger carried (all services)										
Fare revenue	**7.72**	7.50	7.44	7.25	7.05	7.06	7.28	7.46	7.35	7.14
Railway operating costs	**4.02**	3.39	3.43	3.47	3.45	3.70	3.57	3.72	3.85	3.94
Railway operating profit	**3.70**	4.11	4.01	3.78	3.60	3.36	3.71	3.74	3.50	3.20
Safety Performance										
Domestic, Cross-boundary and Airport Express										
Number of reportable events^	**1,514**	989	826	748	701	641	690	686	748	859
Reportable events per million passengers carried^	**1.16**	1.05	0.94	0.86	0.83	0.82	0.88	0.89	0.96	1.09
Number of staff and contractors' staff accidents	**42**	26	23	31	25	33	24	39	36	49
Light Rail										
Number of reportable events^	**136**	6	–	–	–	–	–	–	–	–
Reportable events per million passengers carried^	**0.99**	0.54	–	–	–	–	–	–	–	–
Number of staff and contractors' staff accidents	**5**	–	–	–	–	–	–	–	–	–

^ Reportable events are occurrences affecting railway premises, plant and equipment, or directly affecting persons (with or without injuries), that are reportable to the Secretary for Transport and Housing, Government of the Hong Kong SAR under the Mass Transit Railway Regulations, ranging from suicides / attempted suicides, trespassing onto tracks, to accidents on escalators, lift and moving paths.

Before the Rail Merger on 2 December 2007, the Company's rail operations comprised MTR Lines and Airport Express. After the Rail Merger, our Domestic Service comprised MTR Lines and KCR Lines (East Rail Line excluding Cross-boundary, West Rail Line and Ma On Shan Line). Also after the Rail Merger we gained new passenger services for Cross-boundary Service, Light Rail, Bus and Intercity.

§ The figure includes 1 month's post-merger passenger number of the KCR Lines. On a "like for like" basis, comparable combined passenger numbers of the Company and pre-merger KCRC (as adjusted for interchange passengers) would have been 3,364,000.

@ No figure is shown as there was only 1 month's post-merger passenger number. For the full year of 2007 including pre-merger KCR operations, passenger numbers of the services were 252,000 for Cross-boundary Service, 379,000 for Light Rail, 92,000 for Bus and 9,000 for Intercity.

* Consolidated results

Investor Relations

Investors and MTR Corporation

The Company is committed to maintaining good relations with its wide base of institutional and retail investors. We believe that shareholder value can be enhanced by clearly communicating the Company's corporate strategies, business development and future outlook through a continuous and active dialogue with existing and potential investors.

As a result of this commitment, for over two decades in the international capital markets, the Company has demonstrated a high standard of corporate governance and disclosure, becoming recognised as a leader in investor relations practices in Asia.

Communicating with Institutional Investors

Our pro-active approach to investor relations has made the Company one of the most widely covered companies in Hong Kong. A number of local and international research houses currently publish reports on the Company on a regular basis and we are also followed by a wide range of institutional investors.

Management remains dedicated to maintaining an open dialogue with the investment community to ensure a thorough understanding of the Company and its business strategies. The Company participates in a number of major investor conferences and pro-actively organises other non-deal investor roadshows to maintain good communications with our investors. During the year, the Company organised non-deal roadshows to US, UK, Singapore, Japan and China. In total, over 300 meetings were held with institutional investors and research analysts in 2008.

Retail Shareholder Programmes

The Company greatly values the long-standing shareholder support from our many individual shareholders. Following the success of shareholder programmes in previous years, shareholders were able to enjoy various exclusive benefits in 2008, such as special promotions for the Rail Merger 1-year Anniversary and Airport Express 10-year Anniversary, Lok Ma Chau free ride coupons, and ticket discounts on Airport Express and Ngong Ping 360 cable car.

Access to Information

To ensure all shareholders have equal and timely access to important company information, the Company makes extensive use of the company website to deliver up-to-date information. English and Chinese versions are available for both annual and interim reports. Full and summary versions are also available for our annual report. These reports, together with other company news and stock exchange filings, are also accessible on the corporate website.

The Company's dedicated hotline to answer individual shareholders' enquiries handled more than 45,000 such calls in 2008.

Index Recognition

The Company's position in the Hong Kong market as a blue chip stock with a sizeable market capitalisation and a high degree of liquidity is affirmed through the continued inclusion of our stock in some of the most important benchmark indices. The stock is currently a constituent member of the Hang Seng Index, MSCI Index and FTSE Index series. Since 2002, our achievements in the areas of corporate social responsibility and sustainability have been recognised by both the Dow Jones Sustainability Indexes and the FTSE4Good Index. The Company remains one of the few companies in Hong Kong that is able to meet and maintain the globally recognised standards required for inclusion in these sustainability indices.

Market Recognition

The Company's 2007 Annual Report received the "Best of Hong Kong" Award in the 2008 International ARC (Annual Report Competition) Awards. For the 20th consecutive year our Annual Report also achieved recognition in the Hong Kong Management Association (HKMA) Annual Report Awards, with the 2007 report winning the Silver Award under the "General Category" in the 2008 Best Annual Reports Awards competition. Our Sustainability Report 2007, *Building Capability*, won the "Commendation for Excellent Communication Using the Internet" by the Association of Chartered Certified Accountants (ACCA) Hong Kong. During the year, the Company was also awarded "Honorable Mentions - Grand prix for best overall investor relations by a Hong Kong company (Large cap)" from <<IR Magazine>> and "Best Investor Relations" from <<FinanceAsia>>.

Key Shareholder Information

Financial Calendar 2009

Announcement of 2008 results	10 March
Last day to register for 2008 final dividend	2 April
Book closure period	3 to 14 April (both dates inclusive)
Annual General Meeting	4 June
2008 final dividend payment date	On or about 17 June
Announcement of 2009 interim results	August
2009 interim dividend payment date	October
Financial year end	31 December

Principal Place of Business and Registered Office

MTR Corporation Limited, incorporated and domiciled in Hong Kong
MTR Headquarters Building, Telford Plaza, Kowloon Bay, Kowloon, Hong Kong

Telephone: (852) 2993 2111
Facsimile: (852) 2798 8822

Share Information

Listing

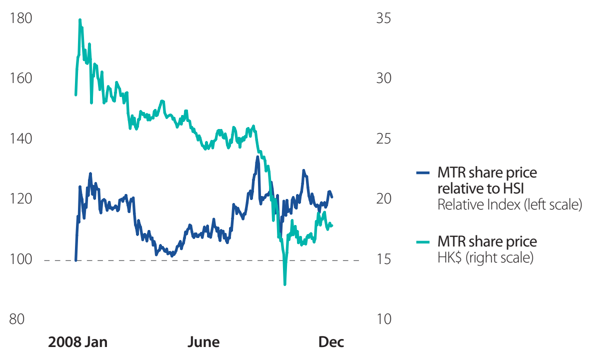
MTR Corporation Limited's shares are listed on the Stock Exchange of Hong Kong. In addition, shares are traded in United States through an American Depositary Receipt (ADR) Level 1 Programme sponsored by JP Morgan Depositary Receipts.

Ordinary Shares *(as at 31 December 2008)*

Shares outstanding	5,661,143,113 shares
Hong Kong SAR Government Shareholding	4,344,710,490 shares (76.7%)
Free float	1,316,432,623 shares (23.3%)

Nominal Value	HK$1 per share
Market Capitalisation *(as at 31 December 2008)*	HK$101,674 million

Share Price Performance



Dividend Policy

Subject to the financial performance of the Company, we expect to pay two dividends each financial year with interim and final dividends payable around October and June respectively.

Dividend per Share

	(in HK$)
2007 Total Dividend	0.45
2008 Interim Dividend	0.14
2008 Final Dividend	0.34

ADR Level 1 Programme

Ordinary share to ADR ratio	10.1
Depositary Bank	JPMorgan Depositary Receipts 4 New York Plaza, 13th Fl. New York, NY 10004

Stock Codes

Ordinary Shares

The Stock Exchange of Hong Kong	66
Reuters	0066.HK
Bloomberg	66 HK

ADR Level 1 Programme	MTRJY

Annual Report 2008

Shareholders can obtain copies of our annual report by writing to:

Computershare Hong Kng Investor Services Limited,
Rooms 1806-1807, 18th Floor, Hopewell Centre,
183 Queen's Road East, Wan Chai, Hong Kong

If you are not a shareholder, please write to:

Corporate Relations Department, MTR Corporation Limited
MTR Headquarters Building, Telford Plaza, Kowloon Bay,
Kowloon, Hong Kong

Our annual/interim reports and accounts are also available online at our corporate website at http://www.mtr.com.hk

Shareholder Services

Any matters relating to your shareholding, such as transfer of shares, change of name or address, and loss of share certificates should be addressed in writing to the Registrar:

Computershare Hong Kong Investor Services Limited
Shops 1712-1716, 17th Floor, Hopewell Centre
183 Queen's Road East, Wan Chai, Hong Kong

Telephone: (852) 2862 8628
Facsimile: (852) 2529 6087

Shareholder Enquiries

Our enquiry hotline is operational during normal office hours:
Telephone: (852) 2881 8888

Investor Relations

For enquiries from institutional investors and securities analysts, please contact:

Investor Relations Department, MTR Corporation Limited
MTR Headquarters Building, Telford Plaza, Kowloon Bay,
Kowloon, Hong Kong
Email: investor@mtr.com.hk

Sustainability

The Company's concept of corporate sustainability continues its necessary evolution, combining risk management with stakeholder engagement. During the year, we continued to create value for stakeholders through Sustainable Competitive Advantage to help drive forward the long-term sustainable development of MTR Corporation.

The Sustainability Journey

Our Sustainable Competitive Advantage model is a dynamic interaction between focused strategy, cost leadership and value-added services. It embraces by nature of its processes the four sustainability principles, namely stewardship, integrity, transparency and inclusiveness. By recognising these principles as inherent to our business development, we continue the sustainability journey while we focus on translating these principles into measurable actions within the risk management and stakeholder engagement cycles.

The sustainable development journey of the expanded MTR Corporation organisation is best reflected in our Diamond Vision of people, process, strategy and community. This vision forms the framework in which we as a company steward the community asset. Our strategy is to evolve with stakeholders' expectations and maintain dialogue to anticipate and deliver beyond expectations.

Corporate Responsibility Committee

In 2008, we established the Board-level Corporate Responsibility Committee. This initiative reflects our commitment to drive forward our corporate responsibility programmes. Under direct governance of the Board, the Committee is responsible for monitoring and overseeing the implementation of the Corporate Responsibility Policy, which will be introduced in 2009, and for identifying emerging corporate responsibility issues as they arise from our business.

Membership of the Corporate Responsibility Steering Committee has been reviewed to better draw upon existing in-house sustainability and corporate responsibility expertise. This review clearly identifies corporate responsibility as an integral part of sustainable development, and promotes the necessary senior-level ownership to ensure corporate responsibility integration into our business strategy.

Sustainability in Action

In 2008, our sustainability and corporate responsibility activities focused on delivering One Company One Team to strengthen cohesion and engagement. These initiatives addressed internal cohesion, the development and implementation of common directions, recognising and rewarding sustainable actions, and encouraging the process of continuous learning as well as value diversity.

The Company has undertaken a thorough assessment of the enterprise risks due to climate change and concluded these require ongoing monitoring at the business unit level. We are in the process of reviewing how climate change can be incorporated into our design, construction, and asset management to prepare more definitively an adaptation based scenario in future years.

Sustainability Reporting

Our sustainability communications continue to gain widespread recognition. The Company's 2007 Sustainability Report won the "Commendation for Excellent Communication Using the Internet" Award in the ACCA Hong Kong Sustainability Reporting Awards 2008. This was the sixth year in a row that the Company received honours for sustainability reporting from the Association of Chartered Certified Accountants (ACCA) Hong Kong. It was also the first year that an award for internet communication was given. The Award gives recognition to companies for using innovative on-line techniques like podcasts to communicate environmental, social and sustainability performance. The MTR Sustainability Report www.mtr.com.hk/sustainability was commended for being user-friendly and easy to navigate.

Global Benchmarks

We actively maintain membership in global benchmarks that promote and measure sustainability such as DJSI, FTSE4Good and Ethibel indices. We also participate each year in major best practice reporting exercises under the GRI (Global Reporting Initiative), CoMET (Community of Metros), and CDP (Carbon Disclosure Project).

The Way Ahead

We recognise that the Company must be prepared for challenges that may change the footprint of the organisation as it is today. Such a change will require a systematic yet flexible approach to best practice in relation to the further internationalisation of the Company's business, especially in developing countries. Our Sustainability Report will evolve as both an internal and external guideline and benchmark for formulating best practices to meet these challenges, risks and opportunities.

Corporate Governance Report

Corporate Governance Practices

The Company is committed to ensuring high standards of corporate governance in the interests of shareholders and devotes considerable effort to identifying and formalising best practices. This Report describes how the Company has applied the principles of the Code on Corporate Governance Practices (the "Code") contained in Appendix 14 of the Listing Rules.

The Company has complied throughout the year ended 31 December 2008 with the Code Provisions except that, with respect to Code Provision A.4.1, non-executive Directors of the Company are not appointed for a specific term but are subject (save for those appointed pursuant to Section 8 of the MTR Ordinance) to retirement by rotation and re-election at the Company's annual general meetings in accordance with Articles 87 and 88 of the Company's Articles of Association. As there are currently nine Directors subject to the requirement to retire by rotation, and one-third of them shall retire at each annual general meeting of the Company (subject to re-election by the shareholders), each of these Directors is effectively appointed for a term of approximately three years.

The Board of Directors

The overall management of the Company's business is vested in the Board. Pursuant to the Articles of Association and the Protocol adopted by the Board, the Board has delegated the day-to-day management of the Company's business to the Executive Directorate, and focuses its attention on matters affecting the Company's overall strategic policies, finances and shareholders. These include financial statements, dividend policy, significant changes in accounting policy, annual operating budget, certain material contracts, strategies for future growth, major financing arrangements and major investments, risk management strategies, treasury policies and fare structures.

The Board comprises 11 members, consisting of one executive Director (the Chief Executive Officer) and ten non-executive Directors, of whom six are independent non-executive Directors. In this regard, the Company well exceeds the requirement of the Listing Rules which requires every board of directors of a listed issuer to have at least three independent non-executive directors.

Dr. Raymond Ch'ien Kuo-fung, a Member of the Board since 1998, was appointed by the Government on 8 August 2007 as the non-executive Chairman of the Company for a term of 24 months with effect from the Rail Merger, which took effect from 2 December 2007. Dr. Ch'ien was first appointed as the non-executive Chairman of the Company with effect from 21 July 2003 for a term of three years, which was renewed in 2006 for a further term up to 31 July 2007. In July 2007, Dr. Ch'ien was re-appointed as the non-executive Chairman of the Company with effect from 1 August 2007 for a term up to 31 December 2007 or the day to be appointed by the Secretary for Transport and Housing ("S for T&H") by notice published in the Gazette under the Rail Merger Ordinance, whichever was the earlier. The Rail Merger Ordinance relates to the Rail Merger between the Company and KCRC.

Mr. Chow Chung-kong, a Member of the Board since 2003, was selected by the Government on 8 August 2007 as the Chief Executive Officer of the Company after the Rail Merger. Mr. Chow was first appointed as the Chief Executive Officer of the Company with effect from 1 December 2003 for a term of three years. He was also appointed as a Member of the Board on the same date. His contract as the Chief Executive Officer of the Company was renewed for a further term of three years with effect from 1 December 2006.

Two of the non-executive Directors (being the S for T&H and the Commissioner for Transport) are appointed by the Chief Executive of the HKSAR. Another non-executive Director, Professor Chan Ka-keung, Ceajer, is the Secretary for Financial Services and the Treasury of the Government. The Government through FSI, holds approximately 76.7% of the issued share capital of the Company.

With effect from the conclusion of the 2008 Annual General Meeting on 29 May 2008 (the "2008 AGM"), Mr. David Gordon Eldon resigned as an independent non-executive Director, while Mr. Lo Chung-hing retired as an independent non-executive Director by rotation pursuant to Articles 87 and 88 of the Articles of Association of the Company, and did not offer himself for re-election.

Coming from diverse business and professional backgrounds, the non-executive Directors actively bring their valuable experience to the Board for promoting the best interests of the Company and its shareholders. On the other hand, the independent non-executive Directors contribute to ensuring that the interests of all shareholders of the Company are taken into account by the Board and that relevant issues are subjected to objective and dispassionate consideration by the Board. The Company has received confirmation from each independent non-executive Director about his/her independence under the Listing Rules, and continues to consider each of them to be independent.

Each Director ensures that he/she can give sufficient time and attention to the affairs of the Company. During the year, Directors had been requested to disclose the number and nature of offices held in public companies or organisations and other significant commitments as well as their identity to the Company twice a year. At the January 2009 Board Meeting, Directors had been advised of the increased level of continuous disclosure of information about and by them, together with other matters relating to Directors, in the light of the amendments to the Listing Rules which came into effect on 1 January 2009.

Biographies of the Members of the Board are set out on pages 108 to 111. None of the Members of the Board and the Executive Directorate has any relationship (including financial, business, family or other material or relevant relationships) between each other, although the S for T&H (Ms. Eva Cheng) and Commissioner for Transport (Mr. Alan Wong Chi-kong) were appointed by the Chief Executive of the HKSAR, and Professor Chan Ka-keung, Ceajer is the Secretary for Financial Services and the Treasury of the Government, and Ms. Christine Fang Meng-sang sits on various government advisory committees.

As permitted under its Articles of Association, the Company has arranged Directors' and Officers' Liability Insurance for which Members of the Board and officers of the Company do not have to bear any excess.

Chairman and Chief Executive Officer

The posts of Chairman and Chief Executive Officer are distinct and separate (please refer to the respective appointment of Dr. Raymond Ch'ien Kuo-fung as the non-executive Chairman of the Company, and Mr. Chow Chung-kong as the Chief Executive Officer of the Company and a Member of the Board on page 93). The non-executive Chairman is responsible for chairing and managing the operations of the Board, as well as monitoring the performance of the Chief Executive Officer and Members of the Executive Directorate. Apart from ensuring that adequate information about the Company's business is provided to the Board on a timely basis, the Chairman also ensures that the non-executive Directors make an effective contribution at Board meetings. As head of the Executive Directorate and chairman of the Executive Committee (which comprises all other Members of the Executive Directorate, General Manager – Corporate Relations, and General Manager – Marketing & Station Commercial), the Chief Executive Officer is responsible to the Board for managing the business of the Company. Biographies of the Members of the Executive Committee are set out on page 113.

The Chairman held a meeting on 15 April 2008 with the non-executive Directors without the presence of Members of the Executive Directorate. Matters discussed were Board responsibilities and effectiveness; governance and compliance infrastructure; management reporting transparency; succession plan for Members of the Executive Directorate; and general human resource issues in respect of the Company's development objectives.

Another meeting has been scheduled to be held by the Chairman in May 2009.

Board Proceedings

The Board meets in person regularly, and all Members of the Board have full and timely access to relevant information and may take independent professional advice at the Company's expense, if necessary, in accordance with the approved procedures. The draft agenda for regular Board meetings is prepared by the Legal Director & Secretary and approved by the Chairman of the Company. Members of the Board are advised to inform the Chairman or the Legal Director & Secretary not less than one week before the relevant Board meeting if they wish to include a matter in the agenda of the meeting. The Board meeting dates for the following year are usually fixed by the Legal Director & Secretary and agreed by the Chairman some time in the third quarter of each year.

At each regular Board meeting, Members of the Executive Directorate together with senior managers report to the Board on their respective areas of business, including the operations, progress of projects, financial performance, corporate governance and outlook. The Chief Executive Officer also submits his Executive Summary, which focuses on the overall strategies and principal issues of the Company, to the Board. These reports, together with the discussions at Board meetings, provide information to enable all Members of the Board to make informed decisions for the benefit of the Company. The agenda together with board papers are sent in full at least three days before the intended date of the Board meeting.

All Members of the Board have access to the advice and services of the Legal Director & Secretary, who is responsible for ensuring that the correct Board procedures are followed and advises the Board on all corporate governance matters. The Members of the Board also have full access to all Members of the Executive Directorate as and when they consider necessary.

Unless specifically permitted by the Articles of Association, a Director cannot cast a vote on any contract, transaction, arrangement or any other kind of proposal in which he has an interest and which he knows is material. For this purpose, interests of a person who is connected with a Director (including any of his associates) are treated as the interests of the Director himself. Interests purely as a result of an interest in the Company's shares, debentures or other securities are disregarded. A Director may not be included in the quorum for such part of a meeting that relates to a resolution he is not allowed to vote on but he shall be included in the quorum for all other parts of that meeting. This reduces potential conflicts which might otherwise arise between the Company's business and an individual Director's other interests or appointments.

In 2008, the Board held nine meetings. When matters which might result in conflicts of interest between the Company and Government were discussed at Board meetings, the Government-nominated Members of the Board, who during the course of 2008 consisted of the S for T&H, Professor Chan Ka-keung, Ceajer (the Secretary for Financial Services and the Treasury), and the Commissioner for Transport (or their respective alternates) either did not attend the relevant Board meetings, or where they did attend, they declared their interests and did not vote in any relevant motion and were not included in the calculation of the relevant quorum.

The attendance record of each Member of the Board is set out below:

Directors	Attendance of Board meetings in 2008
Non-executive Directors	
Dr. Raymond Ch'ien Kuo-fung (Chairman)	9/9
Commissioner for Transport (Alan Wong Chi-kong)	8/9
Secretary for Transport and Housing (Eva Cheng) 4 meetings were attended by her alternate directors	9/9
Professor Chan Ka-keung, Ceajer 2 meetings were attended by his alternate director	8/9
Independent Non-executive Directors	
Professor Cheung Yau-kai	4/9
David Gordon Eldon (Note)	3/3
Christine Fang Meng-sang	9/9
Edward Ho Sing-tin	7/9
Lo Chung-hing (Note)	3/3
T. Brian Stevenson	8/9
Ng Leung-sing	8/9
Abraham Shek Lai-him	8/9
Executive Director	
Chow Chung-kong (Chief Executive Officer)	9/9

Note

Messrs Eldon and Lo ceased to be independent non-executive Directors with effect from the conclusion of the 2008 AGM on 29 May 2008.

The minutes of Board meetings are prepared by the Secretary of the meeting with details of the matters considered by the Board and decisions reached, including any concerns raised by the Members of the Board or dissenting views expressed. The draft minutes are circulated to all Members of the Board for their comment within a reasonable time after the meeting. The approved procedure is that the Board formally adopts the draft minutes at the subsequent meeting. If Members of the Board have any comment on the draft minutes, they will discuss it at that meeting, followed by a report on what has been agreed in the minutes of that meeting. Minutes of Board Meetings are kept by the Legal Director & Secretary and open for inspection by all Members of the Board at the Company's registered office.

Material Interests and Voting

All Directors are required to comply with their common law duty to act in the best interests of the Company and have particular regard to the interest of the shareholders as a whole. The Government is a substantial shareholder of the Company and the Chief Executive of the HKSAR, may, pursuant to Section 8 of the MTR Ordinance, appoint up to three persons as "additional directors". Each Director appointed by the Chief Executive of the HKSAR pursuant to Section 8 of the MTR Ordinance or by the Government through its shareholding must, like any other Director, act in the best interests of the Company.

Directors are required to declare their interests, if any, in any transaction, arrangement or other proposal to be considered by the Board at Board meetings and to abstain from voting on any related resolutions. As a result, if a conflict arises between the interests of the Company and those of the Government, a Director appointed by the Chief Executive of the HKSAR pursuant to Section 8 of the MTR Ordinance or by the Government, would not be included in the quorum of part of a meeting that relates to the transaction, arrangement or other proposal being considered by the Board and would not be allowed to vote on the related resolution.

There are a number of contractual arrangements that have been entered into between the Company and the Government (and its related entities), some of which are continuing in nature. As the Government is a substantial shareholder of the Company, such contractual arrangements are connected transactions (and in some cases continuing connected transactions) for the purposes of the Listing Rules. The section headed "Connected Transactions" explains how, in accordance with the Listing Rules, these transactions are treated.

Appointment, Re-election and Removal of Members of the Board

A person may be appointed as a Member of the Board at any time either by the shareholders in general meeting or by the Board upon recommendation by the Nominations Committee of the Company. Directors who are appointed by the Board must retire at the first annual general meeting after their appointment. A Director who retires in this way is eligible for election at that annual general meeting, but is not taken into account when deciding which and how many Directors should retire by rotation. In either case, the Directors so elected and appointed are eligible for re-election and re-appointment. At each annual general meeting of the Company, one third of the Directors (or, if the number of Directors is not divisible by three, such number as is nearest to and less than one third) must retire as Directors by rotation.

The Chief Executive of the HKSAR may, pursuant to Section 8 of the MTR Ordinance, appoint up to three persons as "additional directors". Directors appointed in this way may not be removed from office except by the Chief Executive of the HKSAR. These Directors are not subject to any requirement to retire by rotation nor will they be counted in the calculation of the number of Directors who must retire by rotation. In all other respects, the "additional directors" are treated for all purposes in the same way as other Directors and are, therefore, subject to the normal common law duties of directors, including to act in the best interests of the Company. The Chief Executive of the HKSAR has appointed the office of the S for T&H and the office of Commissioner for Transport as "additional directors". As there are currently nine Directors subject to the requirement to retire by rotation, and one-third of them shall retire at each annual general meeting of the Company (subject to re-election by the shareholders), each of these Directors is effectively appointed for a term of approximately three years.

Each of the Directors, on appointment to the Board, is given a comprehensive induction programme on key areas of business operations and practices of the Company, as well as a Directors' Manual. Amongst other things, the Manual not only sets out the general and specific duties of the Directors under general law (common law and legislation) and the Listing Rules, but also includes the Terms of Reference of the Board Committees. The Directors' Manual is updated from time to time to reflect developments in those areas.

To assist their continuous professional development, the Legal Director & Secretary recommends Directors to attend relevant seminars and courses. The costs for such training are borne by the Company.

Accountability

The Members of the Board are responsible for preparing the accounts of the Company and of the Group. The accounts are prepared on a going concern basis and give a true and fair view of the state of affairs of the Company and of the Group as at 31 December 2008, and of the Group's profit and cash flow for the year then ended. In preparing the accounts for the year ended 31 December 2008, the Members of the Board have selected appropriate accounting policies and, apart from those new and amended accounting policies as disclosed in the notes to the accounts for the year ended 31 December 2008, have applied them consistently with previous financial periods. Judgments and estimates have been made that are prudent and reasonable. The reporting responsibilities of the External Auditor are set out on page 138.

In support of the above, the accounts presented to the Board have been reviewed by the Members of the Executive Directorate. For both the annual and interim reports and accounts, the Finance Division is responsible for clearing them with the External Auditor and then the Audit Committee. In addition, all new and amended accounting standards and requirements, as well as changes in accounting policies adopted by the Company have been discussed and approved at the Audit Committee before adoption by the Company.

Board Committees

As an integral part of good corporate governance, the Board has established the Audit Committee, Remuneration Committee and Nominations Committee to oversee particular aspects of the Company's affairs. These Board Committees comprise only non-executive Directors who have been invited to serve as members. Further and in December 2008, the Board set up the Corporate Responsibility Committee. Each of these Committees is governed by its respective Terms of Reference which are available on the Company's website: www.mtr.com.hk.

All Committees are provided with sufficient resources to discharge their duties.

Following the completion of the Rail Merger, the Independent Committee of the Board which was established for the purpose of the Rail Merger was formally disbanded in May 2008.

Audit Committee

The Audit Committee consists of four non-executive Directors, three of whom are independent non-executive Directors. The Members of the Committee are T. Brian Stevenson (chairman), Professor Cheung Yau-kai, the Commissioner for Transport (Alan

Wong Chi-kong), and Ng Leung-sing. None of the Committee Members is a partner or former partner of KPMG, the Company's External Auditor. The Finance & Business Development Director, the Head of Internal Audit and representatives of the External Auditor of the Company 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 Finance & Business Development Director may request a meeting if they consider it necessary.

The Terms of Reference of the Audit Committee were revised in April 2008 to improve clarity. Further and in January 2009, the Terms of Reference were updated in the light of the amendments to the Listing Rules, which became effective on 1 January 2009, to reflect the new oversight role of the Audit Committee in the 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, as well as the removal of the requirement for a qualified accountant. Accordingly, the revised Terms of Reference were approved by the Board in April 2008 and January 2009 respectively. Under its Terms of Reference, the duties of the Audit Committee include financial and efficiency aspects as described below. Amongst other things, the Committee is required to oversee the relationship with the Company's 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 for complying with relevant legal requirements. The Committee is primarily responsible for making recommendations to the Board on the appointment and removal of the External Auditor, and approving the remuneration and terms of such engagement. With respect to financial information of the Company, the Committee monitors the integrity of financial statements, annual and interim 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 (including the Finance & Business Development Director), and the chairman of the Committee further meets on an ad hoc basis with the Head of Internal Audit, representatives of the External Auditor, and Management. Apart from considering issues arising from the audit, the Committee discusses any matters that auditor(s) may wish to raise either privately or together with executive Director(s) and any other person. The Committee is required to review, at least annually, the effectiveness of the Company's financial controls, internal control and risk management systems and to report 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. Commencing from the financial year 2009 and as mentioned above, the Committee's review will also cover discussion with the Management on their 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. Regarding the Company's readiness in compliance with this new requirement, please refer to the section headed "Internal Controls" below. 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 Internal Audit and the follow-up of major action plans recommended, and puts forward recommendations to the Board where appropriate.

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

The minutes of the Audit Committee meetings are prepared by the secretary of the meeting 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 the Committee Members for comments and the final version of the minutes is sent to the Committee Members for their records within a reasonable time after the meeting and the minutes are open for inspection by the Committee Members at the Company's registered office. A framework of the agenda items for the meetings for the following year is set out for the Committee Members' reference and comment in the last quarter of each year. The chairman of the Committee makes the final determination on the agenda for the regular Committee meetings.

In 2008, the Audit Committee held three meetings where all the agenda items set out in the Agenda Framework pre-agreed with the chairman of the Committee in 2007 for 2008 had been discussed. In 2009, a total of four meetings have been scheduled. The major work performed by the Committee in 2008 included:

- Review of and recommendation for the Board's approval the draft 2007 Annual Report and Accounts and 2008 Interim Report and Accounts;

- Approval of the 2008 Audit Plan and review of the periodic report prepared by the Internal Audit Department;
- Approval of the 2009 Audit Plan;
- Pre-approval of the audit and non-audit services provided by KPMG, the External Auditor, for 2008;
- Approval of the remuneration and terms of engagement of KPMG for the 2008 audit;
- Preview of 2008 annual accounting and compliance issues;
- Review of the effectiveness of the Company's internal control systems;
- Review of the effectiveness of the Internal Audit Department;
- Review of a report on staff complaints; and
- Review of enterprise risk management.

The attendance record of each Audit Committee Member is set out below. Representatives of the External Auditor, the Finance & Business Development Director and the Head of Internal Audit attended all those meetings for reporting and answering questions about their work. Further to that and by invitation, the Operations Director, the Property Director and the Legal Director & Secretary (or their representatives) had respectively provided an overview of the Company's railway operations, property business as well as outstanding litigation, compliance and enterprise risk management matters to the Members at the meetings. The Finance & Business Development Director also provided an overview of the business development and expansion overseas.

Directors	Attendance of Audit Committee meetings in 2008
T. Brian Stevenson (chairman)	3/3
Professor Cheung Yau-kai	2/3
Commissioner for Transport (Alan Wong Chi-kong)	3/3
Ng Leung-sing	2/3

Remuneration Committee

The Remuneration Committee consists of three non-executive Directors, two of whom are independent non-executive Directors. The Members of the Remuneration Committee are Edward Ho Sing-tin (chairman), T. Brian Stevenson and Professor Chan Ka-keung, Ceajer. Mr. Ho and Mr. Stevenson are independent non-executive Directors.

The principal responsibilities of the Remuneration Committee include formulating a remuneration policy and practices that facilitate the employment of top quality personnel, recommending to the Board the remuneration of the Members of the Board who are non-executive Directors, determining the remuneration packages of the Members of the Board who are executive Directors and other Members of the Executive Directorate, and reviewing and approving performance-based remuneration by reference to the Company's goals and objectives.

In 2008, the Remuneration Committee held three meetings. In accordance with its Terms of Reference, the Committee performed the following work during the year:

- Approved the 2007 Remuneration Report as incorporated in the 2007 Annual Report;
- Reviewed and approved payouts under the Company's performance-based variable incentive scheme for the 2007 performance period;
- Reviewed and approved the remuneration package for the Finance & Business Development Director, following his assumption of additional responsibilities for business development in the Mainland of China and overseas in May 2008;
- Conducted an annual review of the remuneration packages for the Chief Executive Officer and other Members of the Executive Directorate, which took effect in July 2008;
- Reviewed and approved share options awards for Members of the Executive Directorate and other eligible employees; and
- Approved the framework, to be conducted by independent third parties, for auditing the payout calculation under the Variable Incentive Scheme.

The attendance record of each Committee Member is set out below:

Directors	Attendance of Remuneration Committee meetings in 2008
Edward Ho Sing-tin (chairman)	3/3
T. Brian Stevenson	2/3
Professor Chan Ka-keung, Ceajer 1 meeting was attended by his alternate director	3/3

The Remuneration Committee also met on 3 March 2009 to approve the 2008 Remuneration Report, which is set out on pages 104 to 107 and includes a description of the remuneration policy of the Company.

Nominations Committee

The Committee consists of seven non-executive Directors, four of whom are independent non-executive Directors. Both Mr. David Gordon Eldon (chairman) and Mr. Lo Chung-hing served the Committee up to the conclusion of the 2008 AGM. Mr. Edward Ho Sing-tin succeeded Mr. Eldon as chairman and a Member of the Committee, while Mr. Ng Leung-sing was appointed as a Member of the Committee in place of Mr. Lo, both with effect from the conclusion of the 2008 AGM. The other five Members of the Nominations Committee are Dr. Raymond Ch'ien Kuo-fung, Christine Fang Meng-sang, Abraham Shek Lai-him, Professor Chan Ka-keung, Ceajer and the S for T&H (Ms. Eva Cheng). Mr. Ho, Mr. Ng, Ms. Fang and Mr. Shek are also independent non-executive Directors.

The Nominations Committee nominates and recommends to the Board candidates for filling vacancies on the Board, and the positions of Chief Executive Officer ("CEO"), Finance Director ("FD") and Chief Operating Officer ("COO") (provided that the COO position exists). For the positions of FD and COO, the Committee may consider candidates recommended by the CEO, or any other candidates (provided that the CEO shall have the right to first agree to such other candidates).

Since there was no new Board appointments in 2008, the Nominations Committee did not convene any meeting during the year.

Corporate Responsibility Committee

In December 2008, the Board endorsed the setting up of the Corporate Responsibility Committee. Under its Terms of Reference, the Members shall consist of at least three non-executive Directors, two of whom shall be independent non-executive Directors, and two Members of the Executive Directorate. The Chairman of the Company is the chairman of the Committee. Current Members of the Committee are Dr. Raymond Ch'ien Kuo-fung (Chairman), S for T&H (Ms. Eva Cheng), Ms. Christine Fang Meng-sang, Mr. Abraham Shek Lai-him, Mr. Leonard Bryan Turk (Legal Director & Secretary) and Mr. Thomas Ho Hang-kwong (Property Director). The Committee normally meets two times a year. The Committee did not hold any meeting in 2008.

The duties of the Committee are to recommend a corporate responsibility policy to the Board for approval, monitor and oversee the implementation of the Company's corporate responsibility policy and initiatives, identify emerging corporate responsibility issues arising from external trends, review annual Sustainability Report and recommend endorsement by the Board, and provide update to the Board as required. Please also refer to the "Sustainability" section on page 92 of this Annual Report.

Internal Controls

The Board is responsible for the system of internal controls of the Company and its subsidiaries, setting appropriate policies and reviewing the effectiveness of such controls. Internal control is defined as a process effected by the Board, Management and other personnel, designed to manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable, and not absolute assurance of the following:

- effectiveness and efficiency of operations
- reliability of financial reporting
- compliance with applicable laws and regulations
- effectiveness of risk management functions

Pursuant to the Protocol adopted by the Board, the Board has delegated the day-to-day management of the Company's business to the Executive Committee, and focuses its attention on matters affecting the Company's overall strategic policies, finances and shareholders.

Supported by the Members of the Executive Committee, the Chief Executive Officer who chairs the Executive Committee is responsible to the Board for the conduct of the business of the Company.

A number of committees have been established to assist the Executive Committee in the day-to-day management and control of the various core businesses and functions of the Company and its subsidiaries. Key committees include:

- Operations Executive Management Committee
- Operations Business Meeting
- Property Executive Management Committee
- Project Control Group
- Railway Extensions Steering Group

- Consultancy Services Management Committee
- European Business Executive Committee
- China Business Executive Committee
- Information Technology Executive Management Committee
- Financial Planning Committee
- Investment Committee
- Corporate Safety Management Committee
- Enterprise Risk Committee
- Code of Conduct Steering Committee
- Tender Board
- Executive Tender Panel
- Corporate Responsibility Steering Committee

The Executive Committee is responsible for implementing the Board's policies on risk and control. In fulfilling its responsibilities, the Executive Committee identifies and evaluates the risks faced by the Company for consideration by the Board, and designs, operates and monitors a suitable system of internal controls which implements the policies adopted by the Board. The Executive Committee is accountable to the Board for monitoring the system of internal controls and providing assurance to the Board that it has done so. Additionally, all employees have responsibility for internal controls within their areas of accountability.

Various risk management strategies have been established by the Board as advised by the Executive Committee to identify, assess and reduce risks, including construction, business operations, finance, treasury, safety and enterprise risks as well as to ensure appropriate insurance coverage.

Risk Assessment and Management

The Company has established an Enterprise Risk Management ("ERM") framework for the strategic management of business risks. The framework covers all key business areas of the Company and provides a useful forum for communicating risk issues at different levels of the organisation and thereby improves awareness and understanding of risk. The framework has been in operation since early 2006 and its application has been enhanced through annual reviews of the framework, user feedback surveys and experience sharing with leading UK ERM-practising companies. Structured cross-discipline processes and organisations are in place at corporate and divisional levels for risk identification, assessment, mitigation and monitoring. A standard rating system is employed across the Company to prioritise risks for mitigation, effective monitoring and reporting to the Executive Committee and the Board. The ERM Manual that governs the working of the ERM framework has been enhanced, and regular briefing sessions are conducted, to promulgate the application and ensure consistent understanding of ERM.

The operation of the ERM framework, which is overseen by the Enterprise Risk Committee ("ERC"), is underpinned by line management taking direct risk management responsibilities as risk owners. Changes to existing and emerging risks are regularly reviewed by line management. The ERC reviews the operation of the ERM framework and key business risks every three months. The reviews cover the changes in business environments, the key internal and external risks facing the Company, and the risk perspectives of the Executive Committee, business managers and outside stakeholders. The ERC promotes a proactive risk culture by learning from risk events and failures.

Risks assessment is now part of the everyday management processes. Risks associated with major changes and new businesses such as Rail Merger integration, material local and overseas railway construction, investment businesses and consultancy projects are assessed at key stages and project milestones to support decision making. The Enterprise Risk Management Department plays a central role in facilitating risk assessments and reviewing existing and emerging business risks.

The Executive Committee reviews key enterprise risks half-yearly and the Board annually to ensure that such risks are under satisfactory control. The Audit Committee also reviews annually the implementation and the ERM organisation and processes that have been put in place.

Control Activities and Processes

To ensure the efficient and effective operation of business units and functions, and safety of operating railway and construction works in railway projects, Corporate General Instructions ("CGIs"), divisional/departmental procedures and manuals, committees, working groups and quality assurance units are established to achieve, monitor and enforce internal controls and evaluate their effectiveness.

CGIs and various departmental procedures and manuals are established for preventing or detecting unauthorised expenditures/payments, safeguarding the Company's assets, ensuring the accuracy and completeness of accounting records and timely preparation of reliable financial information.

All Department Heads, including Business and Project Managers for overseas projects, are responsible for ensuring the compliance with statutes and regulations applicable to their own functional units. They are required to identify any new or updated statutes, to assess their impact on the Company's operations, and to review at least once a year that relevant statutes/regulations are complied with. Potential and actual non-compliances are also reported and followed up by Department Heads and significant ones are reported to the respective Divisional Directors and the Executive Committee. Issues relating to compliance with statutes and regulations including potential and actual non-compliances, if any, and the status of rectification and actions taken to prevent recurrence are reported annually to the Executive Committee and Audit Committee.

The Internal Audit Department plays a major role, independent of the Company's management, in assessing and monitoring the internal controls of the Company. The Head of Internal Audit reports to the Chief Executive Officer and has direct access to the Audit Committee. The Department has unrestricted access to information that allows it to review all aspects of the Company's risk management, control and governance processes. On a regular basis, it conducts audits on financial, operational and compliance controls, and effectiveness of risk management functions of all business and functional units as well as subsidiaries. Management is responsible for ensuring that control deficiencies highlighted in internal audits are rectified within a reasonable period. The Department produces an annual internal audit plan derived from risk assessment for the Audit Committee's approval. On a half-yearly basis, the Head of Internal Audit reports to the Audit Committee his audit findings and his opinion on the system of internal controls.

On behalf of the Board, the Audit Committee evaluates the effectiveness of the Company's system of internal controls, including the reliability of financial reporting, effectiveness and efficiency of operations, compliance with applicable laws and regulations and effectiveness of risk management functions. This is achieved primarily through approving the annual internal audit plan and reviewing the findings of internal audit work, in addition to reviewing the annual and interim financial statements, and the nature, scope of work, and report of the external auditors, and consideration of the following:

- the changes in the nature and extent of significant risks since the previous review and the Company's ability to respond to changes in its business and external environment;
- the scope and quality of management's ongoing monitoring of risks and the system of internal controls, the work of the Internal Audit Department, and the assurance provided by the Executive Committee;
- the extent and frequency with which the results of monitoring are communicated, enabling the Audit Committee to build up a cumulative assessment of the state of control in the Company and the effectiveness with which risk is being managed;
- the incidence of any significant control failings or weaknesses that have been identified at any time during the period and the extent to which they have resulted in unforeseen outcomes or contingencies that have had, could have had, or may in the future have, a material impact on the Company's financial performance or condition; and
- the effectiveness of the Company's processes in relation to financial reporting and statutory and regulatory compliance.

The processes for assessing internal controls by the Audit Committee have included: regular interviews with Members of the Executive Committee in relation to key business operations, internal control and compliance issues, both financial and non-financial; review of significant issues arising from internal audit reports and external audit report, and private sessions with internal and external auditors. The Audit Committee has also reviewed the papers prepared by the Executive Committee and Internal Audit Department covering: 2007 Annual Report and Accounts, Preview of 2008 Annual Accounting and Compliance issues, 2008 Interim Accounts, 2008 and 2009 Internal Audit Plans, Internal Audit's Half-yearly Reports, Annual Report on Staff Complaints, Reporting of Internal Control Systems, Reporting of Outstanding Litigation and Compliance Issues, ERM Report 2007 and Evaluation of Effectiveness of Internal Audit Department. The chairman of the Committee meets on an ad hoc basis with the Head of Internal Audit, representatives of the External Auditor and Management of the Company as appropriate. He summarizes activities of the Committee and highlights issues arising therefrom by a report to the Board after each Audit Committee meeting.

The Board has, through the Audit Committee, conducted the review of the effectiveness of the Company's system of internal controls for the year ended 31 December 2008, covering all material financial, operational and compliance controls, and risk management function, and concluded that adequate and effective internal controls are maintained to safeguard the shareholders' investment and the Company's assets. There were no significant control failings, weaknesses or significant areas of concern identified during the year which might affect shareholders.

With regard to the new role of the Audit Committee required by the revised Listing Rules to oversee the Management's review of the adequacy of staffing of the financial and reporting function which came into effect on 1 January 2009, the Company has in place a comprehensive annual budgeting system, an effective recruitment process as well as a training and development programme for staff of the accounting and financial reporting function which will enable the Board, through the Audit Committee, to review the adequacy of resources, qualifications and experience of staff of the Company's accounting and financial reporting function, and their training programmes and budget.

Model Code for Securities Transactions by Directors of Listed Issuers (the "Model Code")

The Company has adopted the Model Code. After having made specific enquiry, the Company confirms that Members of the Board and the Executive Directorate complied throughout the year with the Model Code set out in Appendix 10 to the Listing Rules. Senior managers, other nominated managers and staff who, because of their office in the Company, are likely to be in possession of unpublished price sensitive information, have been requested to comply with the provisions of the Model Code. In addition, every employee is bound by the Code of Conduct issued by the Company, amongst other things, to keep unpublished price sensitive information in strict confidence.

An alternate director has reported in writing to the Company and the Stock Exchange that in January 2009, due to an oversight, he and his spouse disposed of an aggregate of 2,084 shares in the Company without having first notified in writing the Chairman of the Company and received a dated written acknowledgement from the Chairman in accordance with the Model Code. The report was made shortly after the dealings. He has also given the Company and the Stock Exchange a written confirmation that he did not possess any unpublished price sensitive information of the Company at the time of the dealings. With a view to ensuring compliance with the Model Code, the Company has reminded him in writing of his obligations under the Model Code.

Business Ethics

The Company is committed to a high standard of business ethics and integrity. The contents of the Company's Code of Conduct and the Corporate Guidebook for All Staff are reviewed every two years by Human Resources to ensure appropriateness and compliance with legislation. Commitment to our Code of Conduct and Guidebook is reinforced by a biennial certification programme, which requires all staff to acknowledge their understanding of and agreement to abide by the Code. The Code of Conduct and Guidebooks, which had been reviewed in the fourth quarter of 2008, were issued to all staff in January 2009. Certification will be completed in the first quarter of 2009. The Code of Conduct is available on the Company's website: www.mtr.com.hk.

To uphold the ethical culture of our subsidiaries in the Mainland of China, and internationally, similar biennial certification programme has been arranged. Briefing on the Company's Code of Conduct and Guidebook is also included in the local Induction Programme. For other joint venture companies, guidelines on business ethics have also been published for staff's observation and compliance.

External Auditor

The Company engages KPMG as its External Auditor. In order to maintain KPMG's independence and objectivity and the effectiveness of the audit process in accordance with applicable standards, the Audit Committee, under its Terms of Reference, pre-approves all audit services to be provided by KPMG and discusses with KPMG the nature and scope of their audit and reporting obligations before the audit commences.

The Audit Committee also reviews and pre-approves the engagement of KPMG to provide any non-audit services for complying with relevant legal requirements and seeks to balance the maintenance of objectivity with value for money.

The nature of audit and non-audit services provided by KPMG and fees paid to KPMG (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) are set out in note 6D to the accounts on page 159.

On the part of KPMG, for maintaining integrity and objectivity, it also requires its audit partner serving the Group to rotate off the audit engagement with the Company at least once every seven years.

Communication with Shareholders

Annual General Meeting ("AGM")

The Company's AGM is one of the principal channels of communication with its shareholders. It provides an opportunity for shareholders to communicate face to face with the Directors about the Company's performance and operations. The Chairman of the Company and the chairmen of the Board Committees were present at the 2008 AGM to answer shareholders' questions.

At the 2008 AGM, the Chairman gave a verbal account of the business operation and development of the Company to shareholders. He started the formal business by highlighting the positive impact of the Rail Merger on the Company in terms of the economies of scale of the rail and related businesses, and the property development land bank and rental property portfolio. Apart from an immediate fare reduction to 2.8 million rail users everyday, the Rail Merger had also provided a better integrated network in Hong Kong and linkages to the Mainland of China. The Chairman then summarised the Company's finance performance during 2007. On business operations, he highlighted the patronage, overall market share, customer service, station commercial and rail related businesses, property development, rental and management businesses. Looking ahead, the Chairman gave a succinct account of the Company's new rail developments in Hong Kong, as well as its continued expansion into the Mainland of China and Europe.

Separate resolutions were proposed for each substantially separate issue at that AGM. Before the resolutions were considered, the Chairman exercised his right as the Chairman of the Meeting under Article 67 of the Company's Articles of Association to call a poll on all resolutions. Being the first listed company in Hong Kong to conduct electronic poll voting, the Company conducted electronic poll voting for a second time at the 2008 AGM. The poll results were posted on the websites of the Company and HKSE on the same day after the AGM. The webcast of the AGM was also posted on the Company's website in the same evening after the AGM.

Extraordinary General Meeting ("EGM")

The Company may also communicate with its shareholders through EGMs if and when appropriate.

If shareholders want to convene an EGM of the Company, those shareholders may requisition the Directors of the Company to do so, provided that at the date of requisition they hold, in aggregate, not less than one-twentieth of the paid-up capital of the Company. The shareholders' requisition must state the objects of the meeting requested and must be deposited at the registered office of the Company. The requisition may consist of several documents in like form, each signed by one or more of the shareholders concerned.

If, within 21 days from the date of the deposit of the requisition, the Directors of the Company do not proceed duly to convene an EGM for a day not more than 28 days after the date on which the notice convening the EGM is given, the relevant shareholders, or any of them representing more than one-half of the total voting rights of all of them, may themselves convene an EGM, provided that any EGM so convened is held within three months from the date of the original requisition.

Enquiries from Shareholders

Details of other means of communication with shareholders are set out in the section of Investor Relations on pages 90 and 91.

Remuneration Report

This Remuneration Report has been reviewed and approved by the Remuneration Committee of the Company.

Remuneration policy

It is the Company's policy to ensure that remuneration is appropriate and aligns with the Company's goals, objectives and performance. To this end, the Company considers a number of relevant factors including salaries paid by comparable companies, job responsibilities, duties and scope, employment conditions elsewhere in the Company and its subsidiaries, market practices, financial and non-financial performance, and desirability of performance-based remuneration.

The Company is committed to effective corporate governance and employing and motivating top quality personnel, and recognises the importance of a formal and transparent remuneration policy covering its Board and Executive Directorate.

The Board has established a Remuneration Committee consisting of three non-executive Directors, two of whom are independent non-executive Directors. It considers and recommends to the Board the Company's remuneration policy and has a delegated authority to review and determine the remuneration packages of the Chief Executive Officer and other Members of the Executive Directorate.

As necessary and with the agreement of the Chairman, the Remuneration Committee is authorised to obtain outside independent professional advice to support the Committee on relevant issues.

A summary of the work performed by the Remuneration Committee during 2008 is set out in the "Corporate Governance Report" on pages 93 to 103.

The Remuneration Committee also ensures that no individual Director or any of his associates is involved in deciding his own remuneration.

Non-Executive Directors, Chief Executive Officer and the Executive Directorate

The Remuneration Committee makes recommendations to the Board from time to time on the remuneration of the Members of the Board who are non-executive Directors. To ensure that non-executive Directors are appropriately paid for their time and responsibilities devoted to the Company, the Committee considers factors such as fees paid by comparable companies, time commitment, responsibilities of the non-executive Directors, and employment conditions elsewhere in the Company.

The Remuneration Committee is responsible for establishing policies, and reviewing and determining the remuneration of the Members of the Board who are executive Directors (namely, the Chief Executive Officer) and the Executive Directorate in accordance with the Company's remuneration policy. In the case of the Chief Executive Officer, the Committee will consult with the Chairman and in the case of other Members of the Executive Directorate, the Committee will consult with both the Chairman and the Chief Executive Officer in respect of their recommendations.

Remuneration Structure for Employees

The Company's remuneration structure for its employees, including the Chief Executive Officer and other Members of the Executive Directorate, comprises fixed compensation, variable incentives, discretionary awards, long-term incentives, and retirement schemes. The specifics of these components are described below.

Fixed Compensation

Fixed compensation comprises base salary, allowances and benefits-in-kind (e.g. medical). Base salary and allowances are set and reviewed annually for each position taking into consideration the Company's remuneration policy, competitive market positioning, market practice, as well as the Company's and individuals' performance. Benefits-in-kind are reviewed regularly taking into consideration market practices.

Variable Incentives

The Chief Executive Officer, other Members of the Executive Directorate and selected management of the Company are eligible to receive an annual cash incentive under the Company's Variable Incentive Scheme, the rules of which are regularly reviewed by the Remuneration Committee.

Under the current scheme rules, the payouts are based on the performance of the Company and individual performance. The Company's performance is measured by the return on fixed assets and operating profit on an annual and rolling three-year basis, the fulfillment of the Customer Service Pledges, and the Performance Requirements in relation to "Train Service Delivery", "Passenger Journeys on Time" and "Train Punctuality" as defined in Schedule 2, Part 1 of the Operating Agreement.

A portion of the target incentive levels under the scheme was originally funded by participants by foregoing their 13th month pay and portions of their fixed allowances. Target incentive levels for the Chief Executive Officer and other Members of the Executive Directorate represent approximately 15-30% of total remuneration. If performance exceeds pre-defined threshold standards, then payouts under the scheme are made annually.

In addition, the Company operates other business-related incentive schemes to motivate the staff concerned to reach specific business targets of the Company.

Discretionary Awards

In 2008, special discretionary awards were provided to staff with competent or above performance as a recognition of their contribution to the Company's good performance and achievements in the past year and to motivate staff to strive for continuous business growth.

Long-Term Incentives

The Company operates three share option schemes, namely the Pre-Global Offering Share Option Scheme (the "Pre-IPO Scheme"), the New Joiners Share Option Scheme (the "New Option Scheme") and the 2007 Share Option Scheme (the "2007 Scheme").

The 2007 Scheme was approved and adopted by shareholders at the Company's Annual General Meeting on 7 June 2007. The 2007 Scheme is intended to provide employees of the Company and of its subsidiaries the opportunity to participate in the growth and success of the Company. Awards under this Scheme were granted to the Chief Executive Officer, other Members of the Executive Directorate and selected employees of the Company in 2008.

Options exercised and outstanding in respect of each Member of the Executive Directorate as at 31 December 2008 under the three Schemes are set out under the paragraph "Board Members' and Executive Directorate's Interests in Shares" of the Report of the Members of the Board.

Details of the three Schemes and options granted to Members of the Executive Directorate and selected employees of the Company under the Schemes are set out in notes 7 & 47 to the accounts.

The Chief Executive Officer does not participate in the Pre-IPO and New Option Schemes. He is entitled to receive an equivalent value in cash of 418,017 Shares on completion of his three-year contract on 30 November 2009.

Retirement Schemes

The Company operates five retirement schemes, the MTR Corporation Limited Retirement Scheme (the "MTR Retirement Scheme"), the MTR Corporation Limited Retention Bonus Scheme (the "MTR RBS"), the MTR Corporation Limited Provident Fund Scheme (the "MTR Provident Fund Scheme") and two Mandatory Provident Fund Schemes (the "MTR MPF Scheme" and the "KCRC MPF Scheme") with details as follows:

(a) MTR Retirement Scheme

The MTR Retirement Scheme is a registered scheme under the Occupational Retirement Schemes Ordinance (Cap. 426) and has been granted an MPF Exemption so that it can be offered to employees as an alternative to the MTR MPF Scheme.

The MTR Retirement Scheme originally contained both a hybrid benefit section and a defined contribution section. Following the Rail Merger with Kowloon-Canton Railway Corporation ("KCRC"), and with the approval of the scheme's trustees effective 1 March 2008, the defined contribution section of the MTR Retirement Scheme was transferred to the MTR Provident Fund Scheme. Following the transfer, the MTR Retirement Scheme only contains a hybrid benefit section.

The MTR Retirement Scheme currently provides benefits based on the greater of a multiple of final salary times service or the accumulated contributions with investment returns. Members' contributions to the scheme are based on fixed percentages of base salary. The Company's contributions are determined by reference to an annual actuarial valuation carried out by an independent actuarial consulting firm.

The scheme has been closed to new employees since 31 March 1999. All employees who joined the Company between 1 April 1999 and 29 February 2008 who would have been eligible to join the MTR Retirement Scheme could choose to join either the defined contribution section of the scheme which was subsequently transferred to the MTR Provident Fund Scheme on 1 March 2008 or, from 1 December 2000, the MTR MPF Scheme.

(b) MTR RBS

The MTR RBS is a registered scheme under the Occupational Retirement Schemes Ordinance. It is a top-up scheme to supplement the MTR Retirement Scheme for employees who are classified by the Company as staff working on designated projects and who are not on gratuity terms. It provides benefits only in the event of redundancy for service accrued up to 31 December 2002, offset by any benefits payable from the MTR Retirement Scheme. Members are not required to contribute while the Company's contributions are determined by reference to an annual actuarial valuation carried out by an independent actuarial consulting firm.

(c) MTR Provident Fund Scheme

The MTR Provident Fund Scheme, in order to reflect its integrated nature, was renamed from the KCRC Retirement Benefit Scheme following its incorporation of the defined contribution section of the MTR Retirement Scheme on 1 March 2008. It contains 3 sections, all of which are defined contribution schemes. One section consists of the members of the KCRC Retirement Benefit Scheme prior to 1 March 2008, one section consists of the members of the defined contribution section of the MTR Retirement Scheme prior to 1 March 2008 and the final section consists of those appointees eligible to join the MTR Provident Fund Scheme on or after 1 March 2008.

The MTR Provident Fund Scheme is a registered scheme under the Occupational Retirement Schemes Ordinance and has been granted an MPF Exemption so that it can be offered to employees as an alternative to the MPF Scheme. On or after 1 March 2008, employees who are eligible to join the MTR Provident Fund Scheme can choose between the MTR Provident Fund Scheme and the MTR MPF Scheme, except where they were previously members of the KCRC MPF Scheme, whereupon they can choose between the MTR Provident Fund Scheme and the KCRC MPF Scheme. All benefits payable under the MTR Provident Fund Scheme are calculated by reference to the Company's contributions and members' own contributions, together with investment returns on these contributions. Both members' and the Company's contributions are based on fixed percentages of members' base salary.

(d) MTR MPF Scheme

The MTR MPF Scheme, which has been registered with the Mandatory Provident Fund Schemes Authority, covers those employees who did not opt for or who are not eligible to join the MTR Retirement Scheme or the MTR Provident Fund Scheme. Both members and the Company each contribute to the MTR MPF Scheme at the mandatory levels as required by the Mandatory Provident Fund Schemes Ordinance ("the MPF Ordinance"). The Company makes additional contributions above the mandatory level for eligible employee members who joined the MTR MPF Scheme before 1 April 2008, subject to individual terms of employment.

(e) KCRC MPF Scheme

The KCRC MPF Scheme, which has been registered with the Mandatory Provident Fund Schemes Authority, covers those former KCRC employees who did not opt for or who were not eligible to join the former KCRC Retirement Benefit Scheme, now known as MTR Provident Fund Scheme, and those employees who, on or after 1 March 2008, were previously members of the KCRC MPF scheme and are eligible to join the MTR Provident Fund Scheme but opt to re-join the KCRC MPF Scheme. Both members and the Company each contribute to the KCRC MPF Scheme at the mandatory levels as required by the MPF Ordinance.

The executive Directors who were hired by the Company before 1 April 1999 were eligible to join the hybrid benefit section of the MTR Retirement Scheme.

The executive Directors who were hired on or after 1 April 1999 but prior to 1 March 2008 are eligible to join the defined contribution benefit section of the MTR Retirement Scheme (which since 1 March 2008 has been transferred to the MTR Provident Fund Scheme).

The Chief Executive Officer participates in the MTR MPF Scheme. Both the Company and the Chief Executive Officer each contribute to the MTR MPF Scheme at the mandatory levels as required by the MPF Ordinance.

Remuneration of Non-Executive and Executive Directors

(i) The total remuneration of the Members of the Board and the Executive Directorate (excluding share-based payments) is shown below and the remuneration details are set out in note 7 to the accounts.

in HK$ million	**2008**	2007
Fees	**4**	3
Base salaries, allowances and other benefits-in-kind	**37**	32
Variable remuneration related to performance	**26**	16
Retirement scheme contributions	**2**	1
	69	52

(ii) The gross remuneration of non-executive and executive Directors (excluding share-based payments) were within the following bands:

Remuneration	**2008 Number**	2007 Number
HK$0 – HK$500,000	**11**	13
HK$1,000,001 – HK$1,500,000	**1**	1
HK$4,500,001 – HK$5,000,000	**–**	1
HK$5,000,001 – HK$5,500,000	**–**	3
HK$5,500,001 – HK$6,000,000	**1**	2
HK$6,000,001 – HK$6,500,000	**–**	1
HK$6,500,001 – HK$7,000,000	**2**	–
HK$7,000,001 – HK$7,500,000	**3**	–
HK$8,000,001 – HK$8,500,000	**1**	–
HK$10,500,001 – HK$11,000,000	**–**	1
HK$15,000,001 – HK$15,500,000	**1**	–
	20	22

The information shown in the above table includes the five highest paid employees. The independent non-executive Directors' emoluments are included in the first remuneration band except the non-executive Chairman, whose emolument is included in the second remuneration band.

Edward Ho Sing-tin, *Chairman, Remuneration Committee*
MTR Corporation Limited
Hong Kong, 3 March 2009

Board and Executive Directorate

From Left to Right:
Ng Leung-sing
Abraham Shek Lai-him
T. Brian Stevenson
Alan Wong Chi-kong (Commissioner for Transport)
Eva Cheng (Secretary for Transport and Housing)
Professor Chan Ka-keung, Ceajer (Secretary for Financial Services and the Treasury)

Members of the Board

Dr. Raymond Ch'ien Kuo-fung 57, was appointed Non-Executive Chairman in July 2003. He has been a member of the Board since 1998. Dr. Ch'ien is chairman of CDC Corporation and its subsidiary, China.com Inc. He is also chairman and independent non-executive director of Hang Seng Bank Limited, as well as non-executive chairman of HSBC Private Equity (Asia) Limited. He serves on the boards of The Hongkong and Shanghai Banking Corporation Limited, Inchcape plc, Convenience Retail Asia Limited, The Wharf (Holdings) Limited and Swiss Reinsurance Company. Dr. Ch'ien is chairman of the Hong Kong/European Union Business Cooperation Committee, a Hong Kong member of the APEC Business Advisory Council, and a member of the Standing Committee of the Tianjin Municipal Committee of the Chinese People's Political Consultative Conference. In addition, Dr. Ch'ien is the honorary president and past chairman of the Federation of Hong Kong Industries. He was a member of the Executive Council of Hong Kong, then under British Administration, from 1992 to 1997, a member of the Executive Council of the Hong Kong SAR from 1 July 1997 to June 2002 and chairman of the Advisory Committee on Corruption of the Independent Commission Against Corruption from 1 January 1998 to 31 December 2006. Dr. Ch'ien was appointed a Justice of the Peace in 1993. He was made a Commander in the Most Excellent Order of the British Empire in 1994 and awarded the Gold Bauhinia Star medal in 1999. In 2008, he was awarded the honour of Chevalier de l'Ordre du Merite Agricole of France. Dr. Ch'ien received a doctoral degree in economics from the University of Pennsylvania in 1978 and became a Trustee of the University in 2006.

Chow Chung-kong 58, was appointed Chief Executive Officer on 1 December 2003. He was formerly chief executive officer of Brambles Industries Ltd, a global support services company. From 1997 to 2001, Mr. Chow was chief executive of GKN PLC, a leading engineering company based in the United Kingdom. Mr. Chow is a chartered engineer. He holds Bachelor of Science and Master of Science degrees in Chemical Engineering from The University of Wisconsin and The University of California respectively. He also holds a Master of Business Administration degree from The Chinese University of Hong Kong and was a graduate of the Advanced Management Program of Harvard Business School. He was awarded an Honorary Doctor of Engineering degree by The University of Bath. In 2000, Mr. Chow was knighted in the United Kingdom for his contribution to industry. Mr. Chow is the non-executive chairman of Standard Chartered Bank (Hong Kong) Limited and an independent non-executive director of Anglo American plc. He is a member of the Council of The Chinese University of Hong Kong and the General Committee of The Hong Kong General Chamber

From Left to Right:
Dr. Raymond Ch'ien Kuo-fung (Chairman)
CK Chow (Chief Executive Officer)
Professor Cheung Yau-kai
Christine Fang Meng-sang
Edward Ho Sing-tin

of Commerce. In public service, Mr. Chow is a board member of The Community Chest of Hong Kong, and a member of the Hong Kong Tourism Board, the Commission on Strategic Development, the Standing Committee on Directorate Salaries and Conditions of Service, as well as the Independent Commission on Remuneration for Members of the Executive Council and the Legislature, and Officials under the Political Appointment System of the HKSAR Government. Mr. Chow is also a member of the Standing Committee of the Shenzhen Municipal Committee of the Chinese People's Political Consultative Conference.

Professor Cheung Yau-kai 74, is an independent non-executive Director and has been a member of the Board since 1999. Professor Cheung is Honorary Professor of Engineering and Special Adviser to the Vice-Chancellor of The University of Hong Kong. He was Taikoo Professor of Engineering and Acting Deputy Vice-Chancellor of The University of Hong Kong until 30 June 2000. Professor Cheung began his academic research career at the University College of Swansea, Wales. He was appointed Professor of Civil Engineering at Calgary in 1970 and moved to the University of Adelaide in 1974 as Professor and Chairman of the Department of Civil Engineering. In 1977, he took up the Chair and Headship of the Department of Civil Engineering in The University of Hong Kong. In addition to his academic appointments, Professor Cheung was the former first Senior Vice-President of the Hong Kong Institution of Engineers and the Ex-Chairman of its Accreditation Board. He has been awarded several honorary degrees at educational institutions, including, an honorary Doctor of Science by The University of Hong Kong and an honorary Doctor of Laws by the University of Wales. He has also been elected a member of the Chinese Academy of Sciences, and is a fellow of the Royal Academy of Engineering, a fellow of the Royal Society of Canada and past President of the Hong Kong Academy of Engineering Sciences.

Christine Fang Meng-sang 50, is an independent non-executive Director and has been a member of the Board since 2004. Ms. Fang has been the chief executive of the Hong Kong Council of Social Service since 2001. Prior to joining the Hong Kong Council of Social Service, she worked for the Hong Kong Red Cross from 1989 to 2001 and held the position of Secretary General from 1993 to 2001. By training, Ms. Fang is a social worker and has a strong background in community service. She sits on various government advisory committees, including the Manpower Development Committee, the Sustainable Development Council and the Digital 21 Strategy Advisory Committee. She is also a member of the Commission on Strategic Development.

Board and Executive Directorate

From Left to right: Miranda Leung Chan Che-ming, Leonard Bryan Turk, William Chan Fu-keung, Lincoln Leong Kwok-kuen, CK Chow, Thomas Ho Hang-kwong, Jeny Yeung Mei-chun, Russell John Black, Andrew McCusker

Edward Ho Sing-tin 70, is an independent non-executive Director and has been a member of the Board since 1991. He is an architect and the Group Chairman of Wong Tung & Partners Limited. Mr. Ho was an elected member of the Legislative Council of Hong Kong from 1991 to 2000, representing the architectural, surveying and planning functional constituency. He was president of the Hong Kong Institute of Architects in 1983 and 1984 and was chairman of the Hong Kong Industrial Estates Corporation from 1992 to 2001. He was also a member of the Hong Kong Housing Authority, chairman of the Antiquities Advisory Board, chairman of the Hong Kong Philharmonic Society, and a member of the Town Planning Board and the Hospital Authority respectively.

Ng Leung-sing 59, joined the Board as an independent non-executive Director on 18 December 2007. Mr. Ng is vice chairman of Chiyu Banking Corporation, general manager, Bank-wide Operation Department of Bank of China (HK) Ltd and an independent non-executive director of SmarTone Telecommunications Holdings Limited. He is a director of the Bank of China (Hong Kong) Charitable Foundation and a Member of the Court of Lingnan University. Mr. Ng is also a Hong Kong Deputy to the 10th and 11th National People's Congress, People's Republic of China. Mr. Ng is a graduate of University of East Asia, Graduate College, Macau and holds a diploma in Chinese Law.

Abraham Shek Lai-him 63, joined the Board as an independent non-executive Director on 18 December 2007. Mr. Shek is an independent non-executive director and an audit committee member of each of Midas International Holdings Limited, Paliburg Holdings Limited, Lifestyle International Holdings Limited, Chuang's Consortium International Limited, NWS Holdings Limited, Regal Portfolio Management Limited, Titan Petrochemicals Group Limited, Eagle Asset Management (CP) Limited, ITC Corporation Limited, Country Garden Holdings Company Limited and SJM Holdings Limited. He is also an independent non-executive director of each of Hop Hing Group

Holdings Limited and Hsin Chong Construction Group Ltd as well as both the Chairman and an independent non-executive director of Chuang's China Investments Limited. Mr. Shek was appointed as Justice of the Peace in 1995 and was awarded the Silver Bauhinia Star in 2007. He is a Member of the Council of The Hong Kong University of Science & Technology and the Court of the University of Hong Kong. In addition, he is Vice Chairman of the Independent Police Complaints Council with effect from 1 January 2009. Mr. Shek is a graduate of the University of Sydney and holds a Bachelor of Arts degree and a Diploma in Education.

T. Brian Stevenson 64, is an independent non-executive Director and has been a member of the Board since October 2002. He is a non-executive director of The Hongkong and Shanghai Banking Corporation Limited, a member of the Asia Pacific Advisory Board of BT and a member of the Public Service Commission. He is Deputy Chairman of the Hong Kong Jockey Club with effect from 10 March 2008. Mr. Stevenson was previously the Senior Partner of Ernst & Young, Hong Kong from 1981 to 1999. He served on the Council of the Hong Kong Society of Accountants from 1991 to 1997 and was president of the Society in 1996. Mr. Stevenson is a chartered accountant and holds law degrees from Glasgow and Hong Kong Universities. He was awarded the Silver Bauhinia Star medal in 1998. He is also a Justice of the Peace.

Commissioner for Transport (Alan Wong Chi-kong 53, joined the Board as a non-executive Director appointed as an "additional director" under section 8 of the MTR Ordinance by virtue of his appointment to the post of the Commissioner for Transport of the Government of the Hong Kong SAR on 18 June 2005. Prior to that, Mr. Wong had served in various bureaux and departments of the Government of the Hong Kong SAR including the former Home Affairs Branch, the former Civil Service Branch, the former Urban Services Department, the former City and New Territories Administration, the former Health and Welfare Branch, the former Recreation and Culture Branch, the former Secretariat of the University and Polytechnic Grants Committee, the former Trade and Industry Branch, the Office of the Commissioner of Insurance from August 1996 to January 2000, the Mandatory Provident Fund Schemes Authority from January 2000 to June 2001, the former Information Technology Services Department from July 2001 to July 2004, and the Office of the Government Chief Information Officer from July 2004 to January 2005. As Commissioner for Transport, Mr. Wong is also a director of several transport-related companies, including The Kowloon Motor Bus Company (1933) Limited, Long Win Bus Company Limited, New World First Bus Services Limited, New Lantao Bus Company (1973) Limited, Citybus Limited, The Star Ferry Company Limited, The New Hong Kong Tunnel Company Limited, Western Harbour Tunnel Company Limited, Tate's Cairn Tunnel Company Limited and Route 3 (CPS) Company Limited.)

Secretary for Transport and Housing (Eva Cheng 48, joined the Board as a non-executive Director appointed as an "additional director" under section 8 of the MTR Ordinance on 1 July 2007 upon her appointment as the Secretary for Transport and Housing of the Government of the Hong Kong SAR. Ms. Cheng has served in various bureaux and departments of the Government of the HKSAR since 1983. Before joining the Transport and Housing Bureau, Ms. Cheng was the Permanent Secretary for Economic Development. She is a graduate of the University of Hong Kong and holds a Bachelor of Social Science degree.)

Professor Chan Ka-keung, Ceajer 52, joined the Board as a non-executive Director on 10 July 2007 after his appointment as the Secretary for Financial Services and the Treasury of the Government of the Hong Kong SAR with effect from 1 July 2007. He received his bachelor's degree in economics from Wesleyan University in the US and both his M.B.A. and Ph.D. in finance from the University of Chicago. Professor Chan sits on the boards of several public bodies including the Mandatory Provident Fund Schemes Authority and The Hong Kong Mortgage Corporation Limited and is the Chairman of the Kowloon-Canton Railway Corporation in his official capacity. Before joining the Government, Professor Chan was Dean of Business and Management of the Hong Kong University of Science and Technology from 1 July 2002. He was also an independent non-executive Director of Shui On Construction and Materials Limited from 1 June 2005 to 30 June 2007.

Members of the Executive Directorate

Chow Chung-kong Biographical details are set out on pages 108 and 109.

Russell John Black 62, has been the Projects Director of the Company since 1992. He is responsible for the planning and implementation of all major railway extension and upgrade projects, which have included the Airport Railway project and the Tseung Kwan O Extension project. Currently under construction is the Kowloon Southern Link, and under planning and design are the West Island Line, the South Island Line, the Guangzhou-Shenzhen-Hong Kong Express Rail Link, the Shatin to Central Line and the Kwun Tong Line Extension. He also provides project management expertise to the Company's railway projects in the Mainland of China. Mr. Black initially worked for the Company from 1976 to 1984 and, prior to rejoining the Company in 1992, he was the Project Director of London Underground's Jubilee Line Extension project. He also worked on Singapore's underground railway and on the Eastern Harbour Crossing. Mr. Black served on the Vocational Training Council from 1998 to 2002, the Construction Advisory Board from 1993 to 1999, the Provisional Construction Industry Coordination Board from 2001 to January 2007 and the Construction Industry Council since February 2007. Mr. Black holds an honours degree in civil engineering from the University of Canterbury in New Zealand. In 2006, he was elected an International Fellow of The Royal Academy of Engineering. He is also a Fellow of the Hong Kong Academy of Engineering Sciences, the Hong Kong Institution of Engineers and the Institution of Professional Engineers, New Zealand. He was awarded the Public Service medal (PBM) in Singapore in 1986 and the Bronze Bauhinia Star medal in 1999.

William Chan Fu-keung 60, has been the Human Resources Director since August 1998. He joined the Company as Human Resources Manager in 1989. He is responsible for human resource management, people development, organisation development, operations and management training, administration and security management. Prior to joining the Company, Mr. Chan held senior managerial positions both in the commerce and in the utility sectors in Hong Kong, including the Government, the Hong Kong Productivity Council, Hutchison Whampoa Limited and Hong Kong Telecommunications Limited. He is a fellow member of the Hong Kong Institute of Human Resource Management since 1985 and is also the Vice President of the Institute. He is a Council member of Employers' Federation of Hong Kong, a member of the Standing Committee on Disciplined Services Salaries and Conditions of Service, the Pensions Appeal Panel and the Career Development and Advisory Board for a number of universities. Mr. Chan received a Bachelor of Social Science degree from The University of Hong Kong in 1971, majoring in economics.

Thomas Ho Hang-kwong 58, has served as the Property Director since joining the Company in 1991. He is responsible for the development and management of all properties above and adjacent to MTR stations and depots. He leads a multi-disciplinary team of managers involved in the planning, design, construction and management of large-scale property developments. Between 1971 and 1990, Mr. Ho worked for the Hong Kong Government specialising in land administration and latterly held a directorate post in the Lands Department, responsible for formulating policies and procedures to make land available for the airport and the Airport Railway project. Mr. Ho was qualified in 1974 as a chartered surveyor in Hong Kong. He is serving The Community Chest of Hong Kong as a Member of the Campaign Organising Committee and a Co-Chairman of the Corporate and Employee Contribution Programme.

Lincoln Leong Kwok-kuen 48, has served as the Finance & Business Development Director since May 2008. Mr. Leong joined the Company in February 2002 as the Finance Director and is responsible for the financial management of all of the Company's affairs, including financial planning and control, budgeting, accounting and reporting and the treasury function. In addition, he has responsibility for the Company's information technology function and serves as chairman of both Octopus Holdings Limited and the board of trustees of the Company's retirement schemes. On 1 May 2008, he was re-titled the Finance & Business Development Director to reflect his additional role in overseeing growth business in the Mainland of China and overseas. Mr. Leong graduated from Cambridge University in 1982 and later qualified as a chartered accountant in England in 1985 and Canada in 1986. Prior to joining the Company as Finance Director, he worked in both the accountancy and investment banking industries. Mr. Leong had worked as an accountant in London and Vancouver, Canada and for a number of years as an investment banker in Hong Kong. Mr. Leong is the chairman of the executive committee of the Hong Kong Society for the Protection of Children, a member of the supervisory board of the Hong Kong Housing Society and a non-official member of the Family Council. He also serves on the Board of Governor of the Chinese International School and is a trustee of the Hospital Authority Pension Fund Scheme. Mr. Leong is also a non-executive director of both Hong Kong Aircraft Engineering Company Limited and Tai Ping Carpets International Limited.

Francois Lung Ka-kui 50, served as the China & International Business Director from September 2005 to 31 December 2008. He ceased to act as a Director of the Company from 1 January 2009. During the period of service, Dr. Lung was responsible for the Company's growth-business efforts, including investments in Mainland of China, operating franchises in Europe and international consultancy. Dr. Lung had held various positions in a number of Royal Dutch Shell affiliates since 1997 and joined the Company from Shell Eastern Petroleum (Pte) Ltd. He was the General Manager, China, with responsibility for strategy development, governance and business performance of Shell's gas and power business in China. From 1994 to 1997, he held positions at Duke Energy Asia Limited, an affiliate of Duke Energy International, becoming Vice-President in 1996. Prior to this, Dr. Lung spent approximately five years at PowerGen plc, a major generator, distributor and retailer of electricity in the United Kingdom, and three years at the Central Electricity Generating Board before the privatisation of the electricity industry in the United Kingdom. Dr. Lung holds a Bachelor of Science degree in Mechanical Engineering from the University of Hong Kong, a PhD in Combustion from the University of Leeds in the United Kingdom, a Master of Science degree in Management from the University of Southampton in the United Kingdom and a Bachelor of Law degree from the University of London. Dr. Lung was admitted to the Bar of the United Kingdom in 1992.

Andrew McCusker 63, has served as the Operations Director since December 2005. Mr. McCusker has more than 40 years of experience in the operating, engineering and projects fields in Defence, Power, Water and Rail Industries. He joined the Company as Operations Engineering Manager in 1987, and since then has been posted to other responsible positions, including Operations Engineering Design Manager, Project Manager (Operations) and General Manager (Operations). He was appointed Deputy Operations Director in March 2004 and Acting Operations Director in October 2005. Mr. McCusker holds a degree in Mechanical Engineering from the Kensington University in the United States and is a chartered member of both the Institution of Mechanical Engineers of the United Kingdom and the Chartered Institute of Personnel and Development (U.K.). In 2007, he was awarded the prestigious Steve Maxwell Leadership Award from the Australian Asset Management Council. Mr. McCusker is an Adjunct Professor for The Hong Kong Polytechnic University.

Leonard Bryan Turk 59, is a solicitor admitted to practise both in England and Wales and in Hong Kong. He joined the Company in 1981 and has been Legal Director & Secretary to the Board since 1988. Mr. Turk is responsible for legal advice, corporate secretarial services, insurance, procurement, enterprise risk management and corporate responsibility functions within the Company. His responsibilities include matters of corporate governance as well as construction contracts, contract administration and dispute resolution. Before joining the Company, Mr. Turk worked in England, concentrating particularly on commercial property development and the financing of large projects.

Members of the Executive Committee

The Executive Committee comprises all Members of the Executive Directorate (whose biographies are on pages 111 to 113), General Manager – Corporate Relations, and General Manager – Marketing & Station Commercial.

Miranda Leung Chan Che-ming 56, has served the Company since 1976 and was appointed Head of the Corporate Relations Department in 1994. As General Manager – Corporate Relations, she is responsible for formulating and directing the implementation of corporate relations strategy and policies to project, maintain and enhance the public image of the Company. Her responsibilities include corporate communications, community and customer engagement, stakeholder management and political lobbying. In 1985, Mrs. Leung qualified as a Chartered Member of The Chartered Institute of Transport (renamed as The Chartered Institute of Logistics and Transport) in UK. She is a Member of UK's Institute of Public Relations and a Chartered Fellow of The Chartered Institute of Logistics & Transport in Hong Kong. She is a member of the Public Relations Committee of The Community Chest of Hong Kong. Mrs. Leung has been appointed a member of the Council for Sustainable Development since March 2009.

Jeny Yeung Mei-chun 44, joined the Company in November 1999 as the Marketing Manager. Being the General Manager – Marketing & Station Commercial, Ms. Yeung is responsible for the marketing of the Company's railway services including fare management and promoting usage of railway services, advertising and shop rental businesses within the stations, and managing and enhancing the MTR Brand. Ms. Yeung graduated from the University of Hong Kong and holds a bachelor degree in Social Sciences majoring in Management Studies. She is a Fellow Member of the Chartered Institute of Marketing. Before joining the Company, she held various marketing and business development positions in Standard Chartered Bank (Hong Kong) Limited and Citibank in Hong Kong.

Key Corporate Management

Chow Chung-kong
Chief Executive Officer

Operations

Andrew McCusker
Operations Director

Li Yun-tai
Deputy Operations Director

Wilfred Lau Cheuk-man
Head of Operations

Jacob Kam Chak-pui
Head of Operations Engineering

William Leung Hon-wai
Head of Operations Strategic Business Management

David Leung Chuen-choi
General Manager – Technical & Engineering Services

Ronald Cheng Kin-wai
Deputy General Manager – Asset Engineering

Richard Keefe
General Manager – Infrastructure

Yuen Wah-hi
Rolling Stock Workshop Manager

Tony Lee Kar-yun
Rolling Stock Fleet Manager

George Lee Kai-wing
General Manager – Safety & Quality

Ho Chun-wing
Planning & Development Manager

Carmen Li Wai-ching
General Manager – Intercity & Freight

Choi Tak-tsan
Acting Head of Operations

Paul Chin Kam-wah
Operations Manager – KTL & TWL

Selwyn Lai Sau-heem
Operations Manager – EAL & MOL

Ivan Lai Ching-kai
Operations Manager – WRL & LR

Alan Cheng Kwan-hing
Operations Manager – AEL, TCL & DRL
(w.e.f. 1 January 2009)

Nelson Wong Sun-fat
Acting Operations Manager – ISL & TKL

China & International Business

Lincoln Leong Kwok-kuen
Finance and Business Development Director

Francois Lung Ka-kui
China & International Business Director
(up to 31 December 2008)

David Tang Chi-fai
General Manager – Central & Southern China

Richard Wong Shiu-ki
General Manager – Beijing & Tianjin

Adi Lau Tin-shing
General Manager – Shenzhen

Antonio Choi Fung-chung
Chief Project Manager – Shenzhen Line 4

Alvin Luk Wing-kwok
Chief Project Manager – Shanghai

Lee Tze-man
Project Manager – Beijing Line 4

Jeremy Long
Chief Executive Officer – European Business

Richard Drake
Finance Director – European Business

Jonathan Dring
Commercial Manager – European Business

Kelson Chan Chi-kun
Strategy & Planning Manager

David Yam Pak-nin
Head of International Consultancy (w.e.f. 1 January 2009)

Tommy Lam Choi-fung
Project Manager – Delhi

Projects

Russell Black
Projects Director

Lee Kang-kuen
Deputy Projects Director

Henry Lam Hing-cheung
General Manager – KSL/TKS

Paul Lo Po-hing
General Manager – XRL/MP

Roderic Hockin
General Manager – WIL/SIL

Barry Hill
Project Manager – WIL/SIL E&M

Julian Saunders
Project Manager – WIL Civil (w.e.f. 1 January 2009)

Joseph Choi Kin-hung
General Manager – SCL/KTE

David Sorton
Project Manager – SCL/KTE Civil

Malcolm Gibson
Head of Project Engineering

Wilfred Yeung Sze-wai
Chief Architect

Stephen Chik Wai-keung
Chief Civil & Planning Engineer

Leung Chi-lap
Chief E&M Engineer

Ringo Lo Tze-shut
Head of Corporate Efficiency

Glenn Frommer
Head of Sustainability Development

Property

Thomas Ho Hang-kwong
Property Director

Roger Poon Fat-chi
Head of Property Investment & Management

Victor Chan Hin-fu
Head of Property Development

Steve Yiu Chin
Head of Town Planning

Mingo Kwan Sze-ming
General Manager – Property Management

Betty Leong Sin-ling
General Manager – Investment Property

James Hor Wai-hong
Chief Development Manager

Emily Chan Sau-ching
Chief Development Manager

Melissa Pang mee-yuk
Chief Development Manager

Yan Chi-ming
Chief Development Manager – Shenzhen

Andy Tong Sze-hang
Chief Project Manager – Property

Edward Wong Koon-pong
Chief Project Manager – Property

Christine Yip Kee-ching
Chief Project Manager – Property

Simon Chan Shui-yan
Chief Project Manager – Property (w.e.f. 15 January 2009)

Candy Ng Chui-lok
Chief Shopping Centre Manager

Gary Lau Wai-keung
Chief Property Manager

Sammy Yu Ka-yin
Chief Property Manager

Maria S. Sze Mang-kwan
Chief Property Manager

Matthew Wong Siu-wing
Chief Technical Manager

Albert Lai Shu-ming
Chief Technical Manager

Rita Wong Lai-fan
Chief Resident Manager

Derek Pang Siu-fai
Chief Leasing Manager (w.e.f. 9 February 2009)

Finance

Lincoln Leong Kwok-kuen
Finance and Business Development Director

Jimmy Lau Chiu-chung
General Manager – Financial Control & Treasury

Herbert Hui Leung-wah
General Manager – Corporate Finance

Jeff Kwan Wai-hung
Treasurer

Daniel Lai Sik-cheung
Head of Information Technology

Denise Ng Kee Wing-man
Head of Investor Relations and Retirement Benefits

Leung Chi-choi
Stores Manager

Sunny Lui Siu-sun
Financial Controller – Property

Raymond Chan Wai-man
Financial Controller – Corporate Services

Lisa Seto Siu-wah
Financial Controller – Projects

Lena Kwok Lai-kay
Financial Controller – Railway Operations

Legal & Procurement

Leonard Turk
Legal Director & Secretary

David Fleming
Deputy Legal Director

Martin Dunn
General Manager – Procurement & Contracts

Teresa Tang Sui-ching
Procurement & Contracts Manager – Operations

Stephen Griffin
Procurement & Contracts Manager – HK Projects (E&M)

Scott Mackenzie
Procurement & Contracts Manager – HK Projects (Civil)

Lila Fong Man-lee
Legal Manager – Company Secretarial

Linda Li Sau-lin
Legal Manager – Property

Gillian Meller
Legal Manager – General

Nelson Ng Wai-hung
Enterprise Risk Manager

Carl Wu Ka-wah
Corporate Responsibility Development Manager

Human Resources & Administration

William Chan Fu-keung
Human Resources Director

Vincent Luk Kin-ping
General Manager – Human Resources

Cheung Kwok-choi
Human Resources Manager – Operations & Engineering

Stella Kan Chi-foon
Human Resources Manager – Staff Relations

Yolanda Law Sui-wah
Human Resources Manager – China & International Business

Chester Tsang Wing-cheong
Management Training & Development Manager

Steven Cho Yan-ming
Head of Operations Training

Lok Ka-sui
Administration & Security Manager

Alison Wong Yuen-fan
People Development Manager

Katy Lam Kwun-yi
Organisation Development Manager

Marketing

Jeny Yeung Mei-chun
General Manager – Marketing & Station Commercial

Eddie So Chung-tat
Senior Manager – Fare & Business Planning

Stella Kwan Mun-yee
Senior Manager – Media & Business Development

Annie Leung Ching-man
Senior Manager – Sales & Marketing

Margaret Chu Fung-kuen
Senior Manager – Station Retail

Victor Leung Wai-keung
Senior Manager – Special Projects

Corporate Relations

Miranda Leung Chan Che-ming
General Manager – Corporate Relations

May Wong May-kay
Deputy General Manager – Corporate Relations

Maggie So Man-kit
Senior Manager – Projects & Property Communications

Ida Leung Pik-fu
Senior Manager – External Affairs

Internal Audit

Stanley Woo Kam-ming
Head of Internal Audit

Nelson Hung Yat-keung
Chief Internal Audit Manager

Octopus Holdings Limited

Prudence Chan
Chief Executive Officer

TraxComm Limited

Kenneth Lau Kwai-hin
Chief Officer (w.e.f. 12 January 2009)

Ngong Ping 360 Limited

Morris Cheung Siu-wa
Managing Director

Report of the Members of the Board

The Members of the Board have pleasure in submitting their Report and the audited statement of Accounts for the financial year ended 31 December 2008.

Principal Activities of the Group

The principal activities of the Company and its subsidiaries are:

A the operation of a modern railway system with lines from Central to Tsuen Wan (Tsuen Wan Line), from Yau Ma Tei to Tiu Keng Leng (Kwun Tong Line), from Po Lam to North Point (Tseung Kwan O Line), from Chai Wan to Sheung Wan (Island Line), from Hong Kong to Tung Chung (Tung Chung Line), from Hong Kong to the Hong Kong International Airport and then AsiaWorld-Expo both at Chek Lap Kok (Airport Express Line), from Sunny Bay to Disneyland Resort (Disneyland Resort Line), from East Tsim Sha Tsui to the boundary at Lo Wu and Lok Ma Chau (East Rail Line), from Tai Wai to Wu Kai Sha (Ma On Shan Line), from Nam Cheong to Tuen Mun (West Rail Line), the North-west Railway (commonly known as Light Rail) in the North-West New Territories of Tuen Mun, Tin Shui Wai and Yuen Long, an intercity railway system between Hong Kong and some major cities in the Mainland of China, and a freight railway system along East Rail Line from the boundary at Lo Wu to Sheung Shui Abattoir and Hung Hom;

B property development, either as owner or as an agent for KCRC, at locations relating to the railway system including the Tseung Kwan O Line, the Ma On Shan Line, the East Rail Line, the Light Rail and the West Rail Line;

C related commercial activities, including the letting of advertising and retail space, bandwidth services on the railway telecommunication system, property management and leasing management of investment properties (including shopping centres, offices and residential units), and Octopus Card Building Access System services;

D the operation of the 7-year London Overground Concession, in which the Company has a 50% equity share, consisting of 107.2 route kilometres of commuter railway lines connecting London's suburbs into the London Underground network;

E the design and construction of a station at LOHAS Park (in Tseung Kwan O South) as an extension of the Tseung Kwan O Line;

F the project management for the Kowloon Southern Link as an extension of the West Rail Line;

G the planning and construction of future extensions to the railway system and other related infrastructure projects including the West Island Line, the South Island Line, the Kwun Tong Line Extension, the Shatin to Central Link and the Express Rail Link, as the major projects for which the Government has confirmed policy support;

H the operation of the Tung Chung to Ngong Ping Cable Car System and the Theme Village in Ngong Ping, Lantau Island, Hong Kong;

I worldwide consultancy services covering all areas of expertise required in the project management, planning, construction, operation, maintenance and up-grading of railways plus fare collection, property integration/development advice including other property related services and advice on generation of non-fare revenues;

J investment in Octopus Holdings Limited, a subsidiary of the Company, which has business activities both in Hong Kong and overseas including the operation of a smart card system by its subsidiary Octopus Cards Limited for the collection of payments for both transport and non-transport applications in Hong Kong;

K equity investments and long term operation and maintenance contracts outside of Hong Kong;

L property management, shopping centre investment and railway related property development business in the Mainland of China; and

M the investment in, and construction of, Beijing Metro Line 4, in which the Company has a 49% equity interest, for future operations under a 30 year concession agreement with the Beijing Municipal Government.

For Shenzhen Metro Line 4 project, approval has been obtained from the National Development and Reform Commission. The Company is now completing final regulatory procedures to sign the Concession Agreement in the next few months.

An Agreement in Principle has been entered into between Shenyang Municipal Government, Shenyang Metro Group Company Limited and the Company for the operation and maintenance of Shenyang Metro Line 1 and 2 for a term of 30 years.

A Principle Agreement for a Public-Private Partnership project has been entered into between Hangzhou Municipal Government, Hangzhou Metro Group Company Limited and the Company for the investment in and the construction of electrical and mechanical works, and the operation of the entire Hangzhou Metro Line 1 for a period of 25 years.

Dividend

The Directors have recommended a final dividend of HK$0.34 per Ordinary Share to be payable to shareholders whose names appear on the Register of Members of the Company on 14 April 2009. Subject to the passing of the necessary resolutions at the forthcoming Annual General Meeting, such dividend will be payable on or about 17 June 2009, in cash in Hong Kong dollars, with a scrip dividend alternative. The Company's majority shareholder, The Financial Secretary Incorporated, has agreed to elect to receive all or part of its entitlement to dividends in the form of scrip to the extent necessary to ensure that a maximum of 50% of the total dividend paid by the Company will be in the form of cash.

Members of the Board

Members of the Board who served during the year were Raymond Ch'ien Kuo-fung (non-executive Chairman), Chow Chung-kong (Chief Executive Officer), Cheung Yau-kai, David Gordon Eldon [resigned on 29 May 2008], Christine Fang Meng-sang, Edward Ho Sing-tin, Lo Chung-hing [retired by rotation on 29 May 2008], Ng Leung-sing, Abraham Shek Lai-him, T. Brian Stevenson, Chan Ka-keung, Ceajer, the Secretary for Transport and Housing (Eva Cheng) and the Commissioner for Transport (Alan Wong Chi-kong).

At the Annual General Meeting on 29 May 2008 and pursuant to the Articles of Association, Chan Ka-keung, Ceajer, Ng Leung-sing, Abraham Shek Lai-him, Edward Ho Sing-tin and Lo Chung-hing retired under the Articles of Association. Lo Chung-hing did not offer himself for re-election, and the other four Directors were re-elected as Members of the Board.

At the forthcoming Annual General Meeting and in accordance with the Articles of Association, Raymond Ch'ien Kuo-fung, Cheung Yau-kai and T. Brian Stevenson will retire by rotation. Cheung Yau-kai will not offer himself for re-election, and that Raymond Ch'ien Kuo-fung and T. Brian Stevenson will offer themselves for re-election at that Meeting.

Biographical details for Board Members are set out on pages 108 to 111.

Alternate Directors

The Alternate Directors in office during the year were:

- for Chan Ka-keung, Ceajer: Ying Yiu-hong and Leung Cheuk-man;
- for the office of the Secretary for Transport and Housing: (i) the Under Secretary for Transport and Housing (Yau Shing-mu [with effect from 28 November 2008]); (ii) the Permanent Secretary for Transport and Housing (Transport) (Ho Suen-wai); and (iii) the Deputy Secretary for Transport and Housing (Transport) (Chu Man Ling and Lee Lai-yee [who ceased to be Deputy Secretaries for Transport and Housing (Transport) and accordingly ceased to be alternate directors to the office of the Secretary for Transport and Housing, with effect from 10 June 2008 and 29 September 2008 respectively], Yung Wai-hung and Shirley Yuen [with effect from 10 June 2008]); and
- for the Commissioner for Transport: the Deputy Commissioner for Transport/Transport Services and Management (Carolina Yip Lai-ching).

Executive Directorate

The Members of the Executive Directorate who served during the year were Chow Chung-kong (Chief Executive Officer and a Member of the Board), Russell John Black, William Chan Fu-keung, Thomas Ho Hang-kwong, Lincoln Leong Kwok-kuen (retitled as Finance & Business Development Director with effect from 1 May 2008), Francois Lung Ka-kui (ceased to act as a Member of the Executive Directorate effective from 1 January 2009), Andrew McCusker and Leonard Bryan Turk.

Biographical details for Members of the Executive Directorate during the year are set out on pages 111 to 113.

Internal Audit

The Company's Internal Audit Department provides independent, objective assurance and consulting services designed to add value and improve the Company's operations. Key responsibilities of the Department include:

- Assessment of the adequacy and effectiveness of the Company's system of internal controls over its activities and risk management.
- Identification of opportunities for improving management control, resources utilisation and profitability.
- Special reviews and/or investigations as commissioned by Company management or the Audit Committee.

The Head of Internal Audit reports directly to the Chief Executive Officer and has direct access to the Audit Committee.

Business Ethics

Please refer to page 102.

Policies

The Board has adopted the following risk management strategies and policies:

A Construction and Insurance Risk Management Strategy;

B Finance Risk Management Strategy;

C Treasury Risk Management Strategy;

D Safety Risk Management Strategy;

E Enterprise Risk Management Strategy;

F Security Risk Management Policy; and

G Environmental Risk Management Policy.

Public Float

The Stock Exchange granted to the Company, at the time of its listing on the Main Board of the Stock Exchange in 2000, a waiver from strict compliance with Rule 8.08(1) of the Listing Rules ("Public Float Waiver"). Pursuant to the Public Float Waiver, the Company's prescribed minimum percentage of shares which must be in the hands of the public must not be less than 10% of the total issued share capital of the Company. Based on the information that is publicly available to the Company and within the knowledge of the Directors, the Company has maintained the prescribed amount of public float during the year and up to the date of this report as required by the Public Float Waiver.

Bank Overdrafts, Bank Loans and Other Borrowings

The total borrowings of the Group as at 31 December 2008 amounted to HK$31,289 million (2007: HK$34,050 million). Particulars of borrowings including bank overdrafts and bank loans are set out in note 38 to the accounts.

Accounts

The state of affairs of the Company and the Group as at 31 December 2008 and of the Group's results, changes in equity and cash flows for the year are set out in the accounts on pages 139 to 230.

Ten-Year Statistics

A summary of the results and of the assets and liabilities of the Group together with some major operational statistics for the last ten years are set out on pages 88 to 89.

Fixed Assets and Railway Construction in Progress

Movements in fixed assets and railway construction in progress during the year are set out in notes 18 to 20 and 22 to the accounts respectively.

Movements in Reserves

Movements in reserves during the year are set out in notes 45 and 46 to the accounts.

Share Capital

As at 31 December 2007, the authorised share capital of the Company was HK$6.5 billion, divided into 6.5 billion Ordinary Shares, 5,611,057,035 of which were issued and credited as fully paid.

During the year, the Company issued a total of 50,086,078 Ordinary Shares. Of this number:

A 1,644,500 Ordinary Shares were issued by the Company pursuant to the exercise of share options which had been granted under the Company's Pre-Global Offering Share Option Scheme (as referred in note 45 to the accounts). In respect of each Ordinary Share issued, the relevant exercise price per share of options is HK$8.44 to the Company;

B 635,500 Ordinary Shares were issued by the Company pursuant to the exercise of share options which had been granted under the Company's New Joiners Share Option Scheme (as referred in note 45 to the accounts). In respect of each Ordinary Share issued, the relevant exercise price per share of options are HK$15.45, HK$15.97, HK$18.30, HK$19.404, HK$20.66 and HK$21.00 to the Company;

C 32,071,954 Ordinary Shares were issued by the Company in order to satisfy shareholders' scrip dividend elections in respect of the final dividend of the Company for the year ended 31 December 2007 (for which the cash dividend was HK$0.31 per Ordinary Share); and

D 15,734,124 Ordinary Shares were issued by the Company in order to satisfy shareholders' scrip dividend elections in respect of the interim dividend of the Company for the six months ended 30 June 2008 (for which the cash dividend was HK$0.14 per Ordinary Share).

As at 31 December 2008, the authorised share capital of the Company was HK$6.5 billion, divided into 6.5 billion Ordinary Shares, 5,661,143,113 of which were issued and credited as fully paid.

Redemption of Listed Securities

Neither the Company nor any of its subsidiaries purchased, sold or redeemed any of its listed securities during the financial year 2008.

Properties

Particulars of the principal investment properties and properties held for sale of the Company are shown on pages 58 to 59.

Donations

During the year, the Company donated a total of HK$8.9 million to charitable organisations including the following:

A To show our care and concern, the Company donated HK$1 million to the Hong Kong Red Cross in February 2008 to provide clothing and emergency supplies for the victims of snow falls in Central China, and HK$1 million to the All-China Federation of Railway Trade Unions.

B The Sichuan earthquake was a natural disaster that evoked the deepest feelings of sympathy as well as a strong readiness to help in the hearts and minds of all in the Company, and indeed in Hong Kong as a whole. Following an initial early donation of HK$1 million by the Company in May 2008 to help the victims, MTR staff raised another HK$5.6 million, which was "dollar matched" in donation by the Company, bringing the total to HK$11.27 million. In addition, various MTR offices in the Mainland of China raised a further RMB300,000, while in our shopping centres in Hong Kong, customers contributed a further HK$2 million. Overall, donations from the Company, our employees and our customers topped more than HK$14.6 million for those struggling in the aftermath of the earthquake.

In addition, the MTR HONG KONG Race Walking 2008 raised over HK$1.3 million for the Hospital Authority Health InfoWorld health education campaign.

The Company helped raise funds for the Community Chest with a total cash donation of over HK$248,000 through different activities such as CARE Scheme, Green Day and Dress Special Day.

Reporting and Monitoring

There is a comprehensive budgeting system for all operational and business activities, with an annual budget approved by the Board. Monthly results of the Company's operations, businesses and projects are reported against the budget to the Board and updated forecasts for the year are prepared regularly.

Treasury Management

The Company's Treasury Department operates within approved guidelines from the Board. It manages the Company's debt profile with reference to the Preferred Financing Model which defines the preferred mix of financing instruments, fixed and floating rate debts, maturities, interest rate risks, currency exposure and financing horizon. The model is reviewed and refined periodically to reflect changes in the Company's financing requirements and market environment. Derivative financial instruments such as interest rate swaps and cross currency swaps are used only as hedging tools to manage the Group's exposure to interest rate and currency risks. Prudent guidelines and procedures are in place to control the Company's derivatives activities, including a comprehensive credit risk management system for monitoring counterparty credit exposure using the Value-at-Risk approach. There is also appropriate segregation of duties within the Company's Treasury Department.

Major financing transactions and guidelines for derivatives transactions including credit risk management framework are approved at the Board level.

Capital and Revenue Expenditure

There are defined procedures for the appraisal, review and approval of major capital and revenue expenditures. All project expenditure over 0.2% of the net assets of the Company and the employment of consultancy services over 0.1% of the net assets of the Company require the approval of the Board.

Bonds and Notes Issued

The Group issued bonds and notes during the year ended 31 December 2008, details of which are set out in note 38 to the accounts. Such bonds and notes were issued in order to meet the Group's general corporate funding requirements, including the financing of new capital expenditure and the refinancing of maturing debts.

Computer Processing

There are defined procedures, controls and regular quality reviews on the operation of computer systems to ensure the accuracy and completeness of financial records and efficiency of data processing. The Company's computer centre operation and support, help desk operation and support services, and also software development and maintenance, have been certified under ISO 9001:2000. Disaster recovery rehearsal on critical applications is conducted annually.

Interests in Contracts of Members of the Board and the Executive Directorate

There was no contract of significance, to which the Company or any of its subsidiaries was a party and in which a Member of the Board or a Member of the Executive Directorate had a material interest (whether direct or indirect), which subsisted at the end of the year or at any time during the year.

Board Members' and Executive Directorate's Interests in Shares

As at 31 December 2008, the interests or short positions of the Members of the Board and the Executive Directorate in the shares, underlying shares and debentures of the Company (within the meaning of Part XV of the Securities and Futures Ordinance (Cap. 571 of the Laws of Hong Kong) ("SFO")) as recorded in the register required to be kept under section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code were as follows:

Long Positions in Shares and Underlying Shares of the Company

	Number of Ordinary Shares held			Derivatives			
				Share Options	Other		
Member of the Board or the Executive Directorate	Personal* interests	Family† interests	Corporate interests	Personal* interests	Personal* interests	Total interests	Percentage of aggregate interests to total issued share capital
Raymond Ch'ien Kuo-fung	51,230	–	–	–	–	51,230	0.00090
Chow Chung-kong	–	–	–	1,190,000 (Note 1)	418,017 (Note 2)	1,608,017	0.02840
T. Brian Stevenson	4,871	–	–	–	–	4,871	0.00009
Christine Fang Meng-sang	1,712	–	–	–	–	1,712	0.00003
Russell John Black	56,095	–	–	340,000 (Note 1)	–	396,095	0.00700
William Chan Fu-keung	46,960	–	–	(i) 217,500 (Note 3) (ii) 340,000 (Note 1)	–	604,460	0.01068
Thomas Ho Hang-kwong	378,760	2,541	–	340,000 (Note 1)	–	721,301	0.01274
Lincoln Leong Kwok-kuen	23,000	–	23,000 (Note 4)	(i) 1,043,000 (Note 5) (ii) 340,000 (Note 1)	160,000 (Note 6)	1,589,000	0.02807
Francois Lung Ka-kui	346,500	2,500	–	(i) 355,500 (Note 5) (ii) 87,000 (Note 1)	–	791,500	0.01398
Andrew McCusker	–	–	–	340,000 (Note 1)	–	340,000	0.00601
Leonard Bryan Turk	–	–	–	340,000 (Note 1)	–	340,000	0.00601
Ho Suen-wai (Note 7)	691	1,393	–	–	–	2,084	0.00004

Notes

1 Further details of the above share options are set out in the table below showing details of the options to subscribe for ordinary shares granted under the 2007 Share Option Scheme.

2 Chow Chung-kong has a derivative interest in respect of 418,017 shares in the Company within the meaning of Part XV of the SFO. That derivative interest represents Mr. Chow's entitlement to receive an equivalent value in cash of 418,017 shares in the Company on completion of his three-year contract (on 30 November 2009).

3 Further details of the above share options are set out in the table below showing details of the options to subscribe for ordinary shares granted under the Pre-Global Offering Share Option Scheme.

4 The 23,000 shares are held by Linsan Investment Ltd., a private limited company beneficially wholly owned by Lincoln Leong Kwok-kuen.

5 Further details of the above share options are set out in the table below showing details of the options to subscribe for ordinary shares granted under the New Joiners Share Option Scheme.

6 Lincoln Leong Kwok-kuen has a derivative interest in respect of 160,000 shares in the Company within the meaning of Part XV of the SFO. That derivative interest represents Mr. Leong's entitlement to receive an equivalent value in cash of 160,000 shares in the Company on 9 April 2010.

7 The office of the Permanent Secretary for Transport and Housing (Transport) is an Alternate Director to the office of the Secretary for Transport and Housing (Eva Cheng). The Secretary for Transport and Housing is a non-executive Director of the Company. Ho Suen-wai is the holder of the post of the Permanent Secretary for Transport and Housing (Transport). Subsequent to 31 December 2008, all the shares were disposed of.

* Interests as beneficial owner

† Interests of spouse or child under 18 as beneficial owner

Options to Subscribe for Ordinary Shares Granted under the Pre-Global Offering Share Option Scheme, as Referred to in Notes 7B(i) and 47A(i) to the Accounts

Executive Directorate and eligible employees	Date granted	No. of options granted	Period during which rights exercisable (day/month/year)	Options outstanding as at 1 January 2008	Options vested during the year	Options lapsed during the year	Options exercised during the year	Exercise price per share of options (HK$)	Options outstanding as at 31 December 2008	Weighted average closing price of shares immediately before the date(s) on which options were exercised (HK$)
William Chan Fu-keung	20/9/2000	1,066,000	5/4/2001 – 11/9/2010	217,500	–	–	–	8.44	217,500	–
Thomas Ho Hang-kwong	20/9/2000	1,066,000	5/4/2001 – 11/9/2010	321,000	–	–	321,000	8.44	–	26.05
Other eligible employees	20/9/2000	41,409,000	5/4/2001 – 11/9/2010	4,728,500	–	17,000	1,323,500	8.44	3,388,000	25.07

Notes

1 The Pre-Global Offering Share Option Scheme ("Pre-IPO Option Scheme") is valid and effective for a period of ten years after 12 September 2000. No option may be offered to be granted under the Pre-IPO Option Scheme on or after the commencement of dealings in shares of the Company on Stock Exchange on 5 October 2000.

2 The number of shares to which the option granted to each participant under the Pre-IPO Option Scheme does not exceed 25% of the number of the shares issued and issuable under the Pre-IPO Option Scheme.

Options to Subscribe for Ordinary Shares Granted under the New Joiners Share Option Scheme, as Referred to in Notes 7B(ii) and 47A(ii) to the Accounts

Executive Directorate and eligible employees	Date granted	No. of options granted	Period during which rights exercisable (day/month/year)	Options outstanding as at 1 January 2008	Options granted during the year	Options vested during the year	Options lapsed during the year	Options exercised during the year	Exercise price per share of options (HK$)	Options outstanding as at 31 December 2008	Weighted average closing price of shares immediately before the date(s) on which options were exercised (HK$)
Lincoln Leong Kwok-kuen	1/8/2003	1,066,000	14/7/2004 – 14/7/2013	1,043,000	–	–	–	–	9.75	1,043,000	–
Francois Lung Ka-kui	22/3/2007	1,066,000	19/3/2008 – 19/3/2017	1,066,000	–	711,000	355,000	355,500	19.404	355,500	28.20
Other eligible employees	1/8/2003	495,200	14/7/2004 – 14/7/2013	202,200	–	–	–	–	9.75	202,200	–
	12/1/2006	94,000	9/1/2007 – 9/1/2016	62,500	–	31,500	31,000	31,500	15.45	–	31.35
	13/9/2005	94,000	9/9/2006 – 9/9/2015	94,000	–	31,000	–	45,000	15.97	49,000	27.05
	23/9/2005	213,000	9/9/2006 – 9/9/2015	213,000	–	71,000	–	–	15.97	213,000	–
	31/3/2006	94,000	20/3/2007 – 20/3/2016	94,000	–	31,500	–	–	18.05	94,000	–
	4/7/2006	94,000	19/6/2007 – 19/6/2016	94,000	–	–	62,500	31,500	18.30	–	29.55
	17/11/2006	94,000	13/11/2007 – 13/11/2016	62,500	–	–	62,500	–	19.104	–	–
	5/10/2006	94,000	29/9/2007 – 29/9/2016	94,000	–	31,500	–	–	19.732	94,000	–
	12/5/2006	266,500	25/4/2007 – 25/4/2016	266,500	–	89,000	–	–	20.66	266,500	–
	15/5/2006	213,000	25/4/2007 – 25/4/2016	213,000	–	71,000	–	30,000	20.66	183,000	31.60
	12/5/2006	213,000	2/5/2007 – 2/5/2016	213,000	–	71,000	71,000	142,000	21.00	–	25.13

Notes

1 No option may be exercised later than ten years after its date of offer and no option may be offered to be granted more than five years after the adoption of the New Joiners Share Option Scheme ("New Option Scheme") on 16 May 2002.

2 Unless approved by shareholders in the manner as required by the Listing Rules, the total number of shares issued and issuable upon exercise of the options granted to any eligible employee under the New Option Scheme together with the total number of shares issued and issuable upon the exercise of any option granted to such eligible employee under any other share option scheme of the Company (including, in each case, both exercised and outstanding options) in any 12-month period must not exceed 1% of the shares of the Company in issue at the date of offer in respect of such option under the New Option Scheme.

Options to Subscribe for Ordinary Shares Granted under the 2007 Share Option Scheme, as Referred to in Notes 7B(iii) and 47A(iii) to the Accounts

Executive Directorate and eligible employees	Date granted	No. of options granted	Period during which rights exercisable (day/month/year)	Options outstanding as at 1 January 2008	Options granted during the year	Options vested during the year	Options lapsed during the year	Options exercised during the year	Exercise price per share of options (HK$)	Options outstanding as at 31 December 2008	Weighted average closing price of shares immediately before the date(s) on which options were exercised (HK$)
Chow Chung-kong	13/12/2007	720,000	10/12/2008 – 10/12/2014	720,000	–	240,000	–	–	27.60	720,000	–
	9/12/2008	470,000	8/12/2009 – 8/12/2015	–	470,000	–	–	–	18.30	470,000	–
Russell John Black	12/12/2007	170,000	10/12/2008 – 10/12/2014	170,000	–	57,000	–	–	27.60	170,000	–
	9/12/2008	170,000	8/12/2009 – 8/12/2015	–	170,000	–	–	–	18.30	170,000	–
William Chan Fu-keung	13/12/2007	170,000	10/12/2008 – 10/12/2014	170,000	–	57,000	–	–	27.60	170,000	–
	9/12/2008	170,000	8/12/2009 – 8/12/2015	–	170,000	–	–	–	18.30	170,000	–
Thomas Ho Hang-kwong	12/12/2007	170,000	10/12/2008 – 10/12/2014	170,000	–	57,000	–	–	27.60	170,000	–
	11/12/2008	170,000	8/12/2009 – 8/12/2015	–	170,000	–	–	–	18.30	170,000	–
Lincoln Leong Kwok-kuen	12/12/2007	170,000	10/12/2008 – 10/12/2014	170,000	–	57,000	–	–	27.60	170,000	–
	9/12/2008	170,000	8/12/2009 – 8/12/2015	–	170,000	–	–	–	18.30	170,000	–
Francois Lung Ka-kui	12/12/2007	130,000	10/12/2008 – 10/12/2014	130,000	–	87,000	43,000	–	27.60	87,000	–
Andrew McCusker	12/12/2007	170,000	10/12/2008 – 10/12/2014	170,000	–	57,000	–	–	27.60	170,000	–
	12/12/2008	170,000	8/12/2009 – 8/12/2015	–	170,000	–	–	–	18.30	170,000	–
Leonard Bryan Turk	12/12/2007	170,000	10/12/2008 – 10/12/2014	170,000	–	57,000	–	–	27.60	170,000	–
	9/12/2008	170,000	8/12/2009 – 8/12/2015	–	170,000	–	–	–	18.30	170,000	–
Other eligible employees	11/12/2007	45,000	10/12/2008 – 10/12/2014	45,000	–	15,000	–	–	27.60	45,000	–
	12/12/2007	1,750,000	10/12/2008 – 10/12/2014	1,750,000	–	573,000	45,000	–	27.60	1,705,000	–
	13/12/2007	915,000	10/12/2008 – 10/12/2014	915,000	–	309,000	–	–	27.60	915,000	–
	14/12/2007	1,005,000	10/12/2008 – 10/12/2014	1,005,000	–	339,000	–	–	27.60	1,005,000	–
	15/12/2007	435,000	10/12/2008 – 10/12/2014	435,000	–	124,500	65,000	–	27.60	370,000	–
	17/12/2007	835,000	10/12/2008 – 10/12/2014	835,000	–	283,000	–	–	27.60	835,000	–
	18/12/2007	445,000	10/12/2008 – 10/12/2014	445,000	–	128,000	65,000	–	27.60	380,000	–
	19/12/2007	115,000	10/12/2008 – 10/12/2014	115,000	–	39,000	–	–	27.60	115,000	–
	20/12/2007	190,000	10/12/2008 – 10/12/2014	190,000	–	63,500	–	–	27.60	190,000	–
	21/12/2007	45,000	10/12/2008 – 10/12/2014	45,000	–	15,000	–	–	27.60	45,000	–
	22/12/2007	35,000	10/12/2008 – 10/12/2014	35,000	–	12,000	–	–	27.60	35,000	–
	24/12/2007	118,000	10/12/2008 – 10/12/2014	118,000	–	39,500	–	–	27.60	118,000	–
	28/12/2007	35,000	10/12/2008 – 10/12/2014	35,000	–	12,000	–	–	27.60	35,000	–
	31/12/2007	130,000	10/12/2008 – 10/12/2014	130,000	–	43,500	–	–	27.60	130,000	–
	2/1/2008	75,000	10/12/2008 – 10/12/2014	–	75,000	25,500	–	–	27.60	75,000	–
	3/1/2008	40,000	10/12/2008 – 10/12/2014	–	40,000	13,500	–	–	27.60	40,000	–
	4/1/2008	65,000	10/12/2008 – 10/12/2014	–	65,000	65,000	–	–	27.60	65,000	–
	7/1/2008	125,000	10/12/2008 – 10/12/2014	–	125,000	42,000	–	–	27.60	125,000	–
	28/3/2008	255,000	26/03/2009 – 26/03/2015	–	255,000	–	–	–	26.52	255,000	–
	31/3/2008	379,000	26/03/2009 – 26/03/2015	–	379,000	–	–	–	26.52	379,000	–
	1/4/2008	261,000	26/03/2009 – 26/03/2015	–	261,000	–	–	–	26.52	261,000	–
	2/4/2008	296,000	26/03/2009 – 26/03/2015	–	296,000	–	–	–	26.52	296,000	–
	3/4/2008	171,000	26/03/2009 – 26/03/2015	–	171,000	–	–	–	26.52	171,000	–
	4/4/2008	23,000	26/03/2009 – 26/03/2015	–	23,000	–	–	–	26.52	23,000	–

Options to Subscribe for Ordinary Shares Granted under the 2007 Share Option Scheme, as Referred to in Notes 7B(iii) and 47A(iii) to the Accounts *(Continued)*

Executive Directorate and eligible employees	Date granted	No. of options granted	Period during which rights exercisable (day/month/year)	Options outstanding as at 1 January 2008	Options granted during the year	Options vested during the year	Options lapsed during the year	Options exercised during the year	Exercise price per share of options (HK$)	Options outstanding as at 31 December 2008	Weighted average closing price of shares immediately before the date(s) on which options were exercised (HK$)
Other eligible employees	5/4/2008	17,000	26/03/2009 – 26/03/2015	–	17,000	–	–	–	26.52	17,000	–
	7/4/2008	390,000	26/03/2009 – 26/03/2015	–	390,000	–	32,000	–	26.52	358,000	–
	8/4/2008	174,000	26/03/2009 – 26/03/2015	–	174,000	–	19,000	–	26.52	155,000	–
	9/4/2008	85,000	26/03/2009 – 26/03/2015	–	85,000	–	–	–	26.52	85,000	–
	10/4/2008	58,000	26/03/2009 – 26/03/2015	–	58,000	–	–	–	26.52	58,000	–
	11/4/2008	134,000	26/03/2009 – 26/03/2015	–	134,000	–	17,000	–	26.52	117,000	–
	12/4/2008	48,000	26/03/2009 – 26/03/2015	–	48,000	–	–	–	26.52	48,000	–
	14/4/2008	40,000	26/03/2009 – 26/03/2015	–	40,000	–	–	–	26.52	40,000	–
	15/4/2008	34,000	26/03/2009 – 26/03/2015	–	34,000	–	–	–	26.52	34,000	–
	16/4/2008	57,000	26/03/2009 – 26/03/2015	–	57,000	–	17,000	–	26.52	40,000	–
	17/4/2008	147,000	26/03/2009 – 26/03/2015	–	147,000	–	23,000	–	26.52	124,000	–
	18/4/2008	32,000	26/03/2009 – 26/03/2015	–	32,000	–	–	–	26.52	32,000	–
	19/4/2008	25,000	26/03/2009 – 26/03/2015	–	25,000	–	–	–	26.52	25,000	–
	20/4/2008	23,000	26/03/2009 – 26/03/2015	–	23,000	–	–	–	26.52	23,000	–
	21/4/2008	66,000	26/03/2009 – 26/03/2015	–	66,000	–	–	–	26.52	66,000	–
	23/4/2008	34,000	26/03/2009 – 26/03/2015	–	34,000	–	15,000	–	26.52	19,000	–
	8/12/2008	155,000	8/12/2009 – 8/12/2015	–	155,000	–	–	–	18.30	155,000	–
	9/12/2008	313,000	8/12/2009 – 8/12/2015	–	313,000	–	–	–	18.30	313,000	–
	10/12/2008	2,176,400	8/12/2009 – 8/12/2015	–	2,176,400	–	–	–	18.30	2,176,400	–
	11/12/2008	2,294,200	8/12/2009 – 8/12/2015	–	2,294,200	–	–	–	18.30	2,294,200	–
	12/12/2008	1,311,500	8/12/2009 – 8/12/2015	–	1,311,500	–	–	–	18.30	1,311,500	–
	13/12/2008	84,500	8/12/2009 – 8/12/2015	–	84,500	–	–	–	18.30	84,500	–
	14/12/2008	88,200	8/12/2009 – 8/12/2015	–	88,200	–	–	–	18.30	88,200	–
	15/12/2008	1,084,700	8/12/2009 – 8/12/2015	–	1,084,700	–	–	–	18.30	1,084,700	–
	16/12/2008	581,500	8/12/2009 – 8/12/2015	–	581,500	–	–	–	18.30	581,500	–
	17/12/2008	513,500	8/12/2009 – 8/12/2015	–	513,500	–	–	–	18.30	513,500	–
	18/12/2008	611,500	8/12/2009 – 8/12/2015	–	611,500	–	–	–	18.30	611,500	–
	19/12/2008	198,000	8/12/2009 – 8/12/2015	–	198,000	–	–	–	18.30	198,000	–
	20/12/2008	19,000	8/12/2009 – 8/12/2015	–	19,000	–	–	–	18.30	19,000	–
	22/12/2008	772,500	8/12/2009 – 8/12/2015	–	772,500	–	–	–	18.30	772,500	–
	23/12/2008	306,000	8/12/2009 – 8/12/2015	–	306,000	–	–	–	18.30	306,000	–
	24/12/2008	500,500	8/12/2009 – 8/12/2015	–	500,500	–	–	–	18.30	500,500	–
	25/12/2008	45,000	8/12/2009 – 8/12/2015	–	45,000	–	–	–	18.30	45,000	–
	29/12/2008	148,000	8/12/2009 – 8/12/2015	–	148,000	–	–	–	18.30	148,000	–
	30/12/2008	19,000	8/12/2009 – 8/12/2015	–	19,000	–	–	–	18.30	19,000	–

Notes

1 No option may be exercised later than seven years after its date of offer and no option may be offered to be granted more than seven years after the adoption of the 2007 Share Option Scheme ("2007 Option Scheme") on 7 June 2007.

2 Unless approved by shareholders in the manner as required by the Listing Rules, the total number of shares issued and issuable upon exercise of the options granted to any eligible employee under the 2007 Option Scheme together with the total number of shares issued and issuable upon the exercise of any option granted to such eligible employee under any other share option scheme of the Company (including, in each case, both exercised and outstanding options) in any 12-month period must not exceed 0.2% of the shares of the Company in issue at the date of offer in respect of such option under the 2007 Option Scheme.

During the year ended 31 December 2008, 1,490,000 and 14,276,000 options to subscribe for shares of the Company were granted to 7 Members of the Executive Directorate and 358 employees respectively under the 2007 Share Option Scheme during the period from 2 January 2008 to 30 December 2008. Details of the grant are set out in the tables above. The respective closing price per share immediately before the respective date of grant of the options are set out below.

Pursuant to the terms of the Scheme, each grantee undertakes to pay HK$1.00, on demand, to the Company, in consideration for the grant of the options. The share options granted are recognised on an accrued vesting basis in the accounts. The weighted average value per option granted, estimated at the respective date of grant using the Black-Scholes pricing model is as follows:

Date granted	Closing price per share immediately before the date of grant (HK$)	Estimated risk-free interest rate (%)	Expected life (Years)	Estimated Volatility	Expected dividend per share (HK$)	Weighted average value per option granted (HK$)
2/1/2008	28.70	2.82	3.5	0.22	0.45	5.49
3/1/2008	30.80	2.71	3.5	0.22	0.45	6.88
4 /1/2008	31.80	2.77	3.5	0.22	0.45	7.65
7/1/2008	32.00	2.77	3.5	0.22	0.45	7.79
28/3/2008	25.90	1.69	3.5	0.22	0.45	3.80
31/3/2008	26.10	1.68	3.5	0.22	0.45	3.90
1/4/2008	26.70	1.66	3.5	0.23	0.45	4.39
2/4/2008	26.70	1.75	3.5	0.23	0.45	4.42
3/4/2008	27.35	1.83	3.5	0.23	0.45	4.84
4/4/2008	27.25	1.83	3.5	0.23	0.45	4.78
5/4/2008	27.25	1.83	3.5	0.23	0.45	4.78
7/4/2008	27.25	1.79	3.5	0.23	0.45	4.76
8/4/2008	27.10	1.84	3.5	0.23	0.45	4.69
9/4/2008	27.20	1.76	3.5	0.23	0.45	4.72
10/4/2008	26.90	1.65	3.5	0.23	0.45	4.49
11/4/2008	26.90	1.72	3.5	0.23	0.45	4.52
12/4/2008	27.10	1.72	3.5	0.23	0.45	4.63
14/4/2008	27.10	1.65	3.5	0.23	0.45	4.60
15/4/2008	26.65	1.74	3.5	0.23	0.45	4.37
16/4/2008	27.05	1.81	3.5	0.23	0.45	4.63
17/4/2008	26.65	1.88	3.5	0.23	0.45	4.42
18/4/2008	26.80	1.91	3.5	0.23	0.45	4.52
19/4/2008	26.85	1.91	3.5	0.23	0.45	4.54
20/4/2008	26.85	1.91	3.5	0.23	0.45	4.54
21/4/2008	26.85	1.91	3.5	0.23	0.45	4.54
23/4/2008	27.35	1.99	3.5	0.23	0.45	4.88
8/12/2008	16.90	1.35	3.5	0.27	0.45	2.31

Date granted	Closing price per share immediately before the date of grant (HK$)	Estimated risk-free interest rate (%)	Expected life (Years)	Estimated Volatility	Expected dividend per share (HK$)	Weighted average value per option granted (HK$)
9/12/2008	18.30	1.28	3.5	0.27	0.45	3.03
10/12/2008	18.02	1.26	3.5	0.27	0.45	2.87
11/12/2008	18.98	1.22	3.5	0.27	0.45	3.41
12/12/2008	18.68	1.17	3.5	0.27	0.45	3.22
13/12/2008	18.00	1.17	3.5	0.27	0.45	2.84
14/12/2008	18.00	1.17	3.5	0.27	0.45	2.84
15/12/2008	18.00	1.20	3.5	0.27	0.45	2.84
16/12/2008	18.50	1.21	3.5	0.27	0.45	3.12
17/12/2008	18.48	1.04	3.5	0.27	0.45	3.07
18/12/2008	18.90	1.05	3.5	0.27	0.45	3.32
19/12/2008	19.06	1.01	3.5	0.27	0.45	3.40
20/12/2008	18.36	1.01	3.5	0.27	0.45	3.00
22/12/2008	18.36	0.99	3.5	0.27	0.45	2.99
23/12/2008	17.86	1.01	3.5	0.27	0.45	2.72
24/12/2008	17.64	0.98	3.5	0.27	0.45	2.60
25/12/2008	17.96	0.98	3.5	0.27	0.45	2.77
29/12/2008	17.96	0.97	3.5	0.27	0.45	2.76
30/12/2008	18.16	0.92	3.5	0.27	0.45	2.86

The Black-Scholes option pricing model was developed for use in estimating the fair value of traded options and requires input of highly subjective assumptions, including the expected life and stock price volatility. Since the Company's share options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimates, the Black-Scholes option pricing model does not necessarily provide a reliable measure of the fair value of the share options.

Save as disclosed above:

A none of the Members of the Board or the Executive Directorate of the Company had any interest or short position in the shares, underlying shares or debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO); and

B during the year ended 31 December 2008, no Member of the Board or the Executive Directorate nor any of their spouses or children under 18 years of age held any rights to subscribe for equity or debt securities of the Company nor had there been any exercises of any such rights by any of them,

as recorded in the register kept by the Company under section 352 of the SFO or otherwise notified to the Company and the HKSE pursuant to the Model Code.

Directors' Service Contracts

No director proposed for re-election at the forthcoming Annual General Meeting has a service contract which is not determinable by the Company or any of its subsidiaries within one year without payment of compensation, other than statutory compensation.

No Director has a service contract with the Company or any of its subsidiaries which is for a duration which may exceed three years or which requires the Company to, in order to terminate such contract, give a notice period in excess of one year or pay or make other payments equivalent to more than one year's emoluments.

Substantial Shareholders' Interests

Set out below is the name of the party which was interested in 5% or more of the nominal value of the share capital of the Company and the number of shares in which it was interested as at 31 December 2008 as recorded in the register kept by the Company under section 336 of the SFO:

Name	No. of Ordinary Shares	Percentage of Ordinary Shares to total issued share capital
The Financial Secretary Incorporated (in trust on behalf of the Government)	4,344,710,490	76.75

The Company has been informed by the Government that, as at 31 December 2008, approximately 0.77% of the shares of the Company were held for the account of the Exchange Fund. The Exchange Fund is a fund established under the Exchange Fund Ordinance (Cap. 66 of the Laws of Hong Kong) under the control of the Financial Secretary.

Loan Agreements with Covenant Relating to Specific Performance of the Controlling Shareholder

As at 31 December 2008, the Group had borrowings of HK$29,009 million with maturities ranging 2009 to 2020 and undrawn committed and uncommitted banking and other facilities of HK$20,659 million, which were subject to the condition that the Government, being the Company's controlling shareholder, owns more than half in nominal value of the voting share capital of the Company during the lives of the borrowings and the undrawn facilities. Otherwise, immediate repayment of borrowings may be demanded and cancellation of the undrawn facilities may result.

Major Suppliers and Customers

Less than 30% in value of supplies (which were not of a capital nature) purchased during the year ended 31 December 2008 was attributable to the Company's five largest suppliers. Less than 30% in value of the Company's turnover during the year ended 31 December 2008 was attributable to the Company's five largest customers combined by value.

Going Concern

The accounts on pages 139 to 230 have been prepared on a going concern basis. The Board has reviewed the Company's budget for 2009, together with the longer-term forecast for the following five years and is satisfied that the Company has sufficient resources to continue as a going concern for the foreseeable future.

Connected Transactions

During the year under review, the following transactions and arrangements described below were entered into with the Government which is a substantial shareholder of the Company as defined in the Listing Rules. The Government is therefore a "connected person" of the Company for the purposes of the Listing Rules, and the transactions described below are connected transactions for the Company under the Listing Rules.

As disclosed in the announcement of the Company dated 13 January 2005, the Stock Exchange has granted a waiver to the Company from strict compliance with the requirements under Chapter 14A of the Listing Rules which would otherwise apply to connected transactions and continuing connected transactions between the Company and Government, subject to certain conditions (the "Waiver").

Consequently, the Company makes the disclosures below in accordance with Rule 14A.45 of the Listing Rules and in accordance with paragraph (B)(I)(i) of the Waiver.

I Preliminary Project Agreement for the Pre-Authorisation Activities of the West Island Line ("Preliminary Project Agreement")

The Preliminary Project Agreement was entered into on 6 February 2008 between the Permanent Secretary for Transport and Housing (Transport) for and on behalf of the Government and the Company.

The Preliminary Project Agreement contains provisions for the carrying out of the various activities which are required prior to the authorisation of the West Island Line scheme under the

Railways Ordinance (Cap. 519 of the Laws of Hong Kong), to enable the construction of the West Island Line to commence promptly after the authorisation including in relation to:

- payment by the Government of HK$400 million to the Company in respect of the Company's obligations under the Preliminary Project Agreement;
- the standard of skill and care with which the pre-authorisation activities will be carried out and an obligation on the Company to procure consultants to effect and maintain professional indemnity insurance;
- arrangements in relation to consultation sessions for the review of progress;
- land issues and environmental protection;
- arrangements in relation to project monitoring by the Government;
- should the railway scheme for the West Island Line be authorised under the Railways Ordinance (Cap. 519), the execution of a project agreement by the Government and the Company setting out each of their rights, obligations, duties and powers with respect to the financing, design, construction, completion, testing, commissioning and putting into service the works necessary for the construction and operation of the West Island Line; and
- arrangements in relation to certain intellectual property rights.

II Land Agreements

A The Company entered into a Further Modification Letter dated 19 March 2008 (the "Further Modification Letter") with the Government in relation to New Grant No.9689 relating to the arrangements for the implementation of the proposed development on Site E and also on Tseung Kwan O Town Lot No.70 generally. The Further Modification Letter also amends the building covenant period for Site E from "the later of on or before the 30th day of September, 2013 or 66 calendar months from the date of payment of the Site E premium" to on or before the 30 September 2014, defines the development parameters and the site boundary of Site E, increases the allowable building height for all Sites except that of Site F, Site AB and Site M, reduces the number of school sites and kindergarten classrooms, increases the minimum local open space and requires permitted works to be carried out within The Remaining Portion of Tseung Kwan O Town Lot No.70 with a total consideration or value of HK$3,335,000,000.

B New Grant No.20605 dated 22 July 2008, of Sha Tin Town Lot No.519 for the development at Che Kung Temple Station (building covenant period expiry date 31 March 2014) with a total consideration or value of HK$3,662,461,000.

C By an Approval Letter dated 26 September 2008 the Government approved the Company's proposal to vary the Fixed Boundaries of Site E, Site F, Site G and Site M; to amend the Master Layout Plan; and to relocate the accommodation and facilities to be provided within Site E, Site F and Site G and to vary the total minimum and the total maximum gross floor areas of Site E, Site F and Site G as stipulated in Special Condition Nos. (18)(b)(v), (18)(b)(vi) and (18)(b)(vii) of the Conditions of Grant No.UB12397 in respect of Kowloon Inland Lot No.11080 with a total consideration or value of HK$1,265,480,000.

D In respect of the Remaining Portion of Mass Transit Railway Lot No. 1 :

A Supplemental Lease was signed on 11 February 2002 between Government and the Company in which the Government leased to the Company land occupied by the Quarry Bay Congestion Relief Works or the Quarry Bay Relief Works connecting Quarry Bay Station to North Point Station at an annual rent of 3% of the rateable value of the leased area for a term commencing 1 October 2001 to 29 June 2050 on terms and conditions substantially similar to the lease for the Mass Transit Railway Lot No. 1. By a Modification Letter dated 13 May 2002 entered into between Government and the Company, the lease for the Remaining Portion of Mass Transit Railway Lot No. 1 was modified in areas indicated in the lease plans attached to the Modification Letter at an administration fee of HK$16,200. By a Modification Letter dated 20 December 2003 entered into between Government and the Company, the lease for the Remaining Portion of Mass Transit Railway Lot No. 1 was modified in areas indicated in the lease plans attached to the Modification Letter in the consideration of a premium of HK$1,000 and an administration fee of HK$16,200. By a Modification Letter executed by the Government and the Company dated 31 May 2004, the lease for the Remaining Portion of Mass Transit Railway Lot No. 1 was modified in areas indicated in the lease plans attached to the Modification

Letter in the consideration of a premium of HK$1,000 and an administrative fee of HK$16,200. By a modification letter dated 1 March 2005 entered into between Government and the Company, the lease for the Remaining Portion of Mass Transit Railway Lot No.1 was modified in areas indicated in the lease plans attached to the Modification Letter in the consideration of a premium of HK$1,000 and an administrative fee of HK$16,200. By a Modification Letter dated 9 March 2007 entered into between Government and the Company, the lease for the Remaining Portion of Mass Transit Railway Lot No.1 was modified in areas indicated in the lease plans attached to the Modification Letter in the consideration of a premium of HK$1,000 and an administrative fee of HK$18,650. By a Modification Letter which was effective from 1 January 2009 entered into between Government and the Company, the lease for the Remaining Portion of Mass Transit Railway Lot No.1 was modified in areas indicated in the lease plans attached to the Modification Letter in the consideration of a premium of HK$1,000 and an administrative fee of HK$21,450.

Continuing Connected Transactions

During the year under review, the following transactions and arrangements described below involved the provision of goods or services on an ongoing basis with the Government and/or KCRC. As noted above under the section headed "Connected Transactions", the Government is a substantial shareholder of the Company. KCRC and the Airport Authority (the "AA") are both associates of the Company as defined in the Listing Rules. Government, KCRC and the AA are therefore each "connected persons" for the purposes of the Listing Rules and each transaction set out at paragraph I and II below constitutes a continuing connected transaction for the Company under the Listing Rules.

I Merger-related Continuing Connected Transactions

Each of the transactions listed in paragraphs A to F below was approved by the independent shareholders of the Company at an Extraordinary General Meeting held on 9 October 2007. These paragraphs should be read in conjunction with the paragraphs contained in the section below headed "Additional Information in respect of the Rail Merger".

As disclosed in the circular issued by the Company on 3 September 2007 in connection with the Rail Merger, the Stock Exchange granted a waiver to the Company from strict compliance with the requirements under Chapter 14A of the Listing Rules which would otherwise apply to continuing connected transactions between the Company, the Government and/or KCRC arising as a result of the Rail Merger, subject to certain conditions (the "Merger-related Waiver").

A Merger Framework Agreement

The Merger Framework Agreement was entered into on 9 August 2007 between the Company, KCRC and the Secretary for Transport and Housing and the Secretary for Financial Services and the Treasury for and on behalf of the Government.

The Merger Framework Agreement contains provisions for the overall structure and certain specific aspects of the Rail Merger, including in relation to:

- a seamless interchange programme;
- corporate governance of the Company post-Rail Merger;
- payments relating to property enabling works;
- arrangements relating to the establishment of a rolling programme on the level of flat production arising from tenders for railway property development;
- arrangements in relation to the assessment of land premium amounts;
- arrangements in relation to the employees of the Company and KCRC, including provisions preventing the Company from terminating the employment of relevant frontline staff for any reason that relates to the process of integrating the operations of the Company and KCRC;
- the implementation of certain fare reductions;
- arrangements in relation to the proposed Shatin to Central Link;
- KCRC's continuing responsibility for its existing financial arrangements;
- treatment of KCRC's cross border leases ("CBLs");
- the payment of HK$7.79 billion in respect of the Property Package (as described on pages 130 to 131 and in paragraph F below);
- the allocation of liability for any pre-Rail Merger and post-Rail Merger claims by third parties; and
- the Company's retention of its English name and (pursuant to the MTR Ordinance) the change of its Chinese name to "香港鐵路有限公司".

B KSL Project Management Agreement

The KSL Project Management Agreement was entered into between the Company and KCRC on 9 August 2007.

Pursuant to the terms of the KSL Project Management Agreement (as amended), the Company is appointed:

- to manage the performance of KCRC's principal obligations to the Government in relation to the design and construction of the Kowloon Southern Link ("KSL") (other than obligations relating to payment);
- to act as the engineer under the various KSL construction contracts;
- to act as KCRC's representative under the various KSL consultancy agreements; and
- to act as KCRC's agent in connection with the KSL under certain circumstances.

The Company itself will not construct, nor be responsible for the costs of, the KSL works.

In return for the performance of these services, the Company will receive a project management fee of approximately HK$710.8 million and, if the construction of the KSL is completed ahead of time and under budget, an incentive payment (calculated with reference to the amount by which the final outturn cost of the project is under budget) of up to HK$110 million. The internal KCRC budget for project management costs was analysed in detail and formed the basis of the fee to be received by the Company.

C West Rail Agency Agreement

The West Rail Agency Agreement and related agreements were entered into on 9 August 2007 between the Company, KCRC and certain KCRC subsidiary companies ("West Rail Subsidiaries"). Pursuant to the terms of the West Rail Agency Agreement, the Company was appointed:

- to act as KCRC's agent, and donee under powers of attorney, to exercise certain rights and perform certain obligations relating to specified development sites along West Rail; and
- to act as agent for, and donee under powers of attorney from, each of the West Rail Subsidiaries to exercise certain rights and perform certain obligations relating to specified development sites along West Rail.

The Company will receive an agency fee of 0.75% of the gross sale proceeds in respect of the unawarded West Rail development sites and 10% of the net profits accrued to the West Rail Subsidiaries under the development agreements in respect of the awarded West Rail development sites. The Company will also recover from the West Rail Subsidiaries its costs (including internal costs) incurred in respect of the West Rail development sites plus 16.5% on-cost, together with interest accrued thereon.

D Outsourcing Agreement

The Outsourcing Agreement was entered into on 9 August 2007 between the Company and KCRC. For the period from 2 December 2007 to 2 December 2009, KCRC, pursuant to the terms of the Outsourcing Agreement, has outsourced certain financial and administrative functions to the Company.

Pursuant to the terms of the Outsourcing Agreement, the Company:

- provides a number of financial and administrative services to KCRC;
- provides certain staff to enable KCRC to operate after the Rail Merger; and
- receives an annual fee of not more than HK$20 million from KCRC.

The scope of the services to be provided by the Company includes services relating to treasury, financial control, information technology, company secretarial, legal and other corporate functions, human resources, office administration and management of claims.

E KCRC Cross Border Lease Agreements

US CBL Assumption Agreements

Separate US CBL Assumption Agreements were entered into on 30 November 2007 between the Company, KCRC and, variously, Wilmington Trust Company, Buoyant Asset Limited, BA Leasing & Capital Corporation, Utrecht-America Finance Co., Cooperatieve Cenrale Raiffeisen-Boerenleenbank B.A., Advanced Asset Limited, Washoe Asset Management Company, Quality Asset Limited, Kasey Asset Limited, Key Equipment Finance Inc., Mercantile Leasing Company (No. 132) Limited, Landesbank Sachsen Aktiengesellschaft, Barclays Bank PLC, Bayerische Landesbank Girozentrale, U.S. Bank National Association, Circuit Asset Limited, Citicorp USA Inc., Shining Asset Limited, Banc of America FSC Holdings Inc., Fluent Asset Limited, Anzef Limited, Societe Generale, Australia and New Zealand Banking Group Limited, Statesman Asset Limited, State Street Bank and Trust Company and Bowman Asset Limited and became effective on 3 December 2007, with respect to each of the US cross border leases originally entered into between KCRC and certain counterparties (each, a "CBL"). Pursuant to each US CBL Assumption Agreement, the Company undertakes to perform, on a joint and several basis with KCRC, the obligations of KCRC under the respective CBLs. As a result thereof, the Company is generally liable to the CBL counterparties in respect of KCRC's obligations under the CBLs and has the right to exercise certain of KCRC's rights under the CBLs.

US CBL Allocation Agreement

The US CBL Allocation Agreement was entered into between the Company, KCRC and the subsidiaries of KCRC (the "KCRC Subsidiaries") on 2 December 2007. Pursuant to the US CBL Allocation Agreement, rights, obligations and responsibility for risks relating to the CBLs are delineated and allocated between KCRC and the Company (each of which is jointly and severally liable to specified CBL counterparties, as referred to in the paragraph above headed "US CBL Assumption Agreements"). Under the terms of the US CBL Allocation Agreement, as between the Company and KCRC, the Company is responsible for specified obligations. The Company and KCRC each made representations under the US CBL Allocation Agreement, which include, in the case of those made by KCRC, representations with respect to the status of the CBLs. The Company and KCRC agreed to indemnify each other for certain losses in relation to the CBLs.

F Property Package Agreements

Category 2A Properties

On 9 August 2007, the Government entered into an undertaking that it would, within twelve months of the Merger Date or such further period of time as the Government and the Company may agree, issue to KCRC an offer for the grant at nil premium of Government leases in respect of the land upon which certain properties (the "Category 2A Properties") are situate. The Category 2A Properties are currently held by KCRC as vested land under the Kowloon-Canton Railway Corporation Ordinance (Cap. 372 of the Laws of Hong Kong) ("KCRC Ordinance"). On 9 August 2007, KCRC entered into an undertaking that it would, immediately after the grant of the Government leases referred to in the preceding sentence, enter into an agreement for sale and purchase to sell the Category 2A Properties to the Company. Assignment of the Category 2A Properties to the Company shall then take place pursuant to the agreement for sale and purchase. Pursuant to the KCRC undertaking and as interim arrangements until the grant of the Government leases, on 9 August 2007 the following agreements were entered into between KCRC and the Company:

- an agreement that KCRC (as lessor) shall enter into tenancy agreements with the Company (as lessee) at market rent in respect of the Category 2A Properties' vacant units (with the intention that the Company will then sub-let the vacant units to sub-tenants);
- two licence agreements in respect of the common areas within the Category 2A Properties, pursuant to which KCRC granted the Company the right to use certain common areas until the execution of the Category 2A Properties assignment referred to above;
- a lease enforcement agency agreement appointing the Company as its enforcement agent to enforce KCRC's current Category 2A Properties tenancy agreements against tenants; and
- an assignment of rental proceeds whereby the proceeds received under KCRC's current Category 2A Properties tenancy agreements with tenants are assigned to the Company.

Category 2B Property

On 9 August 2007, the Government entered into an undertaking that it would, within twenty four months of the Merger Date or such further period of time as the Government and the Company may agree, issue to the Company an offer for the grant of a Government Lease of a certain property (the "Category 2B Property") on terms to be agreed. The Category 2B Property is currently held by KCRC as vested land under the KCRC Ordinance for use as staff quarters and a recreational club.

On 9 August 2007, KCRC entered into an undertaking relating to interim arrangements to ensure that, as from the Merger Date, the Company shall be responsible for KCRC's obligations under licence agreements relating to the Category 2B Property, and for enforcing such agreements. The Company is entitled to proceeds received by KCRC in respect of those licence agreements. The interim arrangements include, inter alia, as from the Merger Date:

- an agreement that KCRC (as licensor) shall grant to the Company (as licensee) possession of the Category 2B Property (without payment of any licence fee or premium), subject to existing licences and the Second Schedule of the KCRC Ordinance, with the right of the Company to sub-license all or any part of the Category 2B Property (subject to it being used as staff quarters and a recreation club);
- until the grant of the Government lease of the Category 2B Property, KCRC has appointed the Company as its enforcement agent to enforce KCRC's current Category 2B Property licence agreements against licensees; and
- KCRC has assigned to the Company the proceeds received under KCRC's current Category 2B Property licence agreements with licensees.

Category 3 Properties

On 9 August 2007, the Company entered into three agreements (the "Category 3 Agreements") and related powers of attorney with KCRC. Each Category 3 Agreement relates to a certain property (each a "Category 3 Property"). KCRC has previously entered into a development agreement in respect of each Category 3 Property. None of the rights and obligations granted to or undertaken by the Company under the Category 3 Agreements may be exercised or performed by the Company if they relate exclusively to concession property situate on any Category 3 Property. Matters affecting the concession property situate on any Category 3 Property are dealt with under the terms of the Service Concession Agreement (as defined and summarised on pages 134 to 135).

Pursuant to the terms of each Category 3 Agreement, the Company has been appointed to act as KCRC's agent, and donee under powers of attorney, to exercise rights and to perform obligations of KCRC which relate to the Category 3 Property (but excluding the right or obligation to dispose of the relevant Category 3 Property).

The Company is required at all times to comply with statutory restrictions and obligations binding on KCRC which relate to the Category 3 Property, and shall pay all amounts due and payable from KCRC which have been incurred by KCRC as a result of the Company's actions.

In acting as KCRC's agent, the Company is required to act according to prudent commercial principles, and aim to maximise gross profits under the Category 3 Property and to run a safe and efficient railway. In order to assist the Company in performing its agency functions, KCRC has granted powers of attorney to the Company. The Company may only use the powers of attorney to exercise rights and perform obligations conferred or undertaken by it under the relevant Category 3 Agreement. As well as acting as KCRC's agent, the Company has the right to give KCRC instructions in respect of any action or matter relating to each Category 3 Property (including its related development agreement) which the Company is unable to take by reason of the limitation of the scope of its agency powers. KCRC is required to comply promptly with those instructions provided that it is permitted under law, and under the relevant Government grant, to carry out those instructions.

KCRC is required to account for revenue received in respect of a Category 3 Property by way of balance sheet movement (rather under its profit and loss account), provided that such treatment is permitted under law and accounting principles and practices.

KCRC shall not take any action in respect of a Category 3 Property which is not carried out by the Company (acting as KCRC's agent), or according to the Company's instructions, or otherwise in accordance with the terms of the Category 3 Agreement.

As consideration for acting as KCRC's agent, the Company shall be paid a fee which is expected to be similar in quantum to the profits made by KCRC in respect of the relevant Category 3 Property (after deducting certain initial and upfront payments and consultant contribution costs, in each case paid or to be paid by the relevant developer to KCRC). Generally, the Company's fee shall be payable in instalments promptly following receipt of relevant funds by KCRC (but subject to specified deductions of amounts due from KCRC to the relevant Category 3 Property developer).

The Company has agreed to give certain indemnities to KCRC in respect of each Category 3 Property.

The Company shall be the first manager, or shall ensure that a manager is appointed in respect of, each Category 3 Property (once developed).

The Company's appointment as agent shall terminate when KCRC ceases to have any undivided share in the relevant Category 3 Property, other than concession property, and neither KCRC nor the developer nor the guarantors have any further rights to exercise, or obligations to perform, under the development agreement relating to the relevant Category 3 Property.

In relation to the Merger Framework Agreement, the KSL Project Management Agreement, the West Rail Agency

Agreement (and related powers of attorney), the US CBL Assumption Agreements, the US CBL Allocation Agreement, the Outsourcing Agreement and the agreements in relation to Category 2A, Category 2B and Category 3 Properties (together the "Merger-related Continuing Connected Transactions") and in accordance with paragraph B(I)(i) of the Merger-related Waiver, the Company confirms that the Independent Non-executive Directors of the Company have reviewed each of the Merger-related Continuing Connected Transactions and confirmed that the Merger-related Continuing Connected Transactions were entered into:

(1) in the ordinary and usual course of business of the Company;

(2) on normal commercial terms or on terms which are no less favourable to the Company than terms available to or from independent third parties; and

(3) in accordance with the relevant agreement governing them on terms that are fair and reasonable and in the interests of the shareholders of the Company as a whole.

The Company has engaged the auditors of the Company to carry out a review of each of the Merger-related Continuing Connected Transactions in accordance with Hong Kong Standard on Related Services 4400 "Engagements to Perform Agreed-Upon Procedures Regarding Financial Information" issued by the Hong Kong Institute of Certified Public Accountants. In accordance with paragraph B(I)(ii) of the Merger-related Waiver, the auditors have provided a letter to the Board of Directors confirming that each of the Merger-related Continuing Connected Transactions:

(a) has been approved by the Board of Directors of the Company; and

(b) has been entered into in accordance with the relevant agreement governing the relevant transaction.

II Non Merger-related Continuing Connected Transactions

The following disclosures are made in accordance with paragraph (B)(I)(i) of the Waiver and Rule 14A.46 of the Listing Rules.

II(i) Entrustment Agreement for Design and Site Investigation in Relation to the Shatin to Central Link

The Entrustment Agreement for Design and Site Investigation in Relation to the Shatin to Central Link (the "SCL Agreement") was entered into on 24 November 2008 between the Company and the Secretary for Transport and Housing for and on behalf of the Government.

The SCL Agreement contains provisions for the design of and site investigation and procurement activities in relation to the proposed Shatin to Central Link, including in relation to:

- the Government's obligation to pay the Company up to a maximum aggregate amount of HK$1,500,000,000 in respect of certain costs incurred by the Company pursuant to the SCL Agreement, including the Company's in-house design costs and certain on-costs and preliminary costs;
- the Government's obligation to bear and finance the total cost of the design and site investigation activities under the SCL Agreement (subject to the limit noted above in respect of payments to the Company) and arrangements for the payment of these costs directly by the Government;
- the Company's obligation to carry out or procure the carrying out of the design and site investigation activities in relation to the proposed Shatin to Central Link;
- the limitation of the Company's liability to the Government under the SCL Agreement, except in respect of death or personal injury caused by the negligence of the Company, to HK$600,000,000; and
- should the railway scheme for the Shatin to Central Link be authorised under the Railways Ordinance (Cap. 519 of the Laws of Hong Kong), the execution of a further agreement by the Government and the Company setting out each of their rights, obligations, duties and powers with respect to the financing, construction, completion, testing, commissioning and putting into service the works necessary for the construction and operation of the Shatin to Central Link.

II(ii) Entrustment Agreement for Design and Site Investigation in Relation to the Express Rail Link

The Entrustment Agreement for Design and Site Investigation in Relation to the Express Rail Link (the "XRL Agreement") was entered into on 24 November 2008 between the Company and the Secretary for Transport and Housing for and on behalf of the Government.

The XRL Agreement contains provisions for the design of and site investigation and procurement activities in relation to the proposed Express Rail Link, including in relation to:

- the Government's obligation to pay the Company, up to a maximum aggregate amount of HK$1,500,000,000, in respect of certain costs incurred by the Company pursuant to the XRL Agreement, including the Company's in-house design costs and certain on-costs, preliminary costs and recruited staff costs;
- the Government's obligation to bear and finance the total cost of the design and site investigation activities under the XRL Agreement (subject to the limit noted above in respect of payments to the Company) and arrangements for the payment of these costs directly by the Government;
- the Company's obligation to carry out or procure the carrying out of the design and site investigation activities in relation to the proposed Express Rail Link;
- the limitation of the Company's liability to the Government under the XRL Agreement, except in respect of death or personal injury caused by the negligence of the Company, to HK$700,000,000; and
- should the railway scheme for the Express Rail Link be authorised under the Railways Ordinance (Cap. 519 of the Laws of Hong Kong), the execution of a further agreement by the Government and the Company setting out each of their rights, obligations, duties and powers with respect to the financing, construction, completion, testing, commissioning and putting into service the works necessary for the construction and operation of the Express Rail Link.

II(iii) Renewal of the existing Maintenance Agreement of the Automated People Mover System at the Hong Kong International Airport

The Company has had entered into a Maintenance Agreement with the AA for the maintenance of the Automated People Mover system at the Hong Kong International Airport since 2002. It was signed on 18 March 2002 for a period of three years, which expired on 6 July 2005. A Supplemental Agreement was agreed with the AA, and approved by the Board in June 2005, to extend the Maintenance Agreement for another three years until 6 July 2008, which also included options for the Automated People Mover serving the Sky Plaza and Sky Pier terminal buildings.

On 21 August 2008, the Company entered into a new Maintenance Agreement with the AA, for the renewal of the then expired Maintenance Agreement for the Automated People Mover system for a five year period (the "New Maintenance Agreement"), effective from 6 July 2008. It is expected that the highest amount per year receivable from the AA under the New Maintenance Agreement will be HK$37 million.

The New Maintenance Agreement contains provisions relating to the operation and maintenance by the Company of the automated people mover system installed at Hong Kong International Airport (the "System") and the carrying out by the Company of certain specified services in respect of the System, they including the following:

- provisions stating that the duration of the New Maintenance Agreement shall be five years from 6 July 2008 up to and including 5 July 2013;
- provisions relating to the performance of scheduled maintenance works and overhaul of the System by the Company;
- provisions relating to monitoring the System for any breakdown and the Company providing repair services where necessary;
- provisions relating to the standards to which the Company must operate the System; and
- provisions relating to the carrying out by the Company (as additional services), in certain circumstances, of upgrade work on the System.

In relation to the SCL Agreement, the XRL Agreement and the New Maintenance Agreement (together the "Non Merger-related Continuing Connected Transactions") and in accordance with paragraph B(I)(iii)(a) of the Waiver, the Company confirms that the Independent Non-executive Directors of the Company have reviewed each of the Non Merger-related Continuing Connected Transactions and confirmed that the Non Merger-related Continuing Connected Transactions were entered into:

(1) in the ordinary and usual course of business of the Company;

(2) on normal commercial terms or on terms which are no less favourable to the Company than terms available to or from independent third parties; and

(3) in accordance with the relevant agreement governing them on terms that are fair and reasonable and in the interests of the shareholders of the Company as a whole.

The Company has engaged the auditors of the Company to carry out a review of each of the Non Merger-related Continuing Connected Transactions in accordance with Hong Kong Standard on Related Services 4400 "Engagements to Perform Agreed-Upon Procedures Regarding Financial Information" issued by the Hong Kong Institute of Certified Public Accountants. In accordance with paragraph B(I)(iii)(b) of the Waiver, the auditors have provided a letter to the Board of Directors confirming that each of the Non Merger-related Continuing Connected Transactions:

(a) has been approved by the Board of Directors of the Company; and

(b) has been entered into in accordance with the relevant agreement governing the relevant transaction.

Additional Information in Respect of the Rail Merger

The Rail Merger consisted of a number of separate agreements, each of which was detailed in the circular issued by the Company on 3 September 2007 in connection with the Rail Merger, and which together formed a complete package deal which was approved by the independent shareholders of the Company at an Extraordinary General Meeting held on 9 October 2007. The information set out at paragraph A below describes the payment framework adopted in respect of the Rail Merger and paragraphs B to F below set out, summaries of the various agreements entered into by the Company in respect of the Rail Merger in addition to those agreements disclosed above under the heading "Merger-related Continuing Connected Transactions".

A Payments in Connection with Merger-related Agreements

In connection with the Rail Merger, the following initial payments were made by the Company to KCRC on 2 December 2007 (being the Merger Date):

- an upfront payment of HK$4.25 billion, payable under the Service Concession Agreement (as described in paragraph B below), being the upfront fee for the right to operate the Service Concession (as defined in paragraph B below) and the consideration for the purchased rail assets; and
- an upfront payment of HK$7.79 billion payable under the Merger Framework Agreement (as described on page 128) in consideration for the execution of the Property Package Agreements (as described on pages 135 to 136 and in paragraph E below) and the sale of the shares in the KCRC Subsidiaries (as defined on page 130) that were transferred to the Company under the Sale and Purchase Agreement which was entered into on 9 August 2007 between the Company and KCRC.

In addition to the initial payments above, the Company is also required to make the following payments to KCRC going forward:

- fixed annual payments of HK$750 million payable under the Service Concession Agreement, for the right to use and operate the concession property for the operation of the service concession, in arrears on the day immediately preceding each anniversary of the Merger Date which falls during the concession period in respect of the 12 month period up to and including the date on which such payment falls due; and
- variable annual payments payable under the Service Concession Agreement, for the right to use and operate the concession property for the operation of the service concession, in each case, calculated on a tiered basis by reference to the amount of revenue from the KCRC system (as determined in accordance with the Service Concession Agreement) for each financial year of the Company. No variable annual payment is payable in respect of the first 36 months following the Merger Date.

As a complete package deal, other than the payment elements described above and unless stated otherwise in the relevant paragraph below, no specific allocation was made between the various elements of the Rail Merger.

B Service Concession Agreement

The Service Concession Agreement was entered into on 9 August 2007 between the Company and KCRC.

The Service Concession Agreement contains provisions in relation to the grant and operation of a service concession and licence granted by KCRC to the Company ("Service Concession"), including in relation to:

- the grant of the Service Concession to the Company to access, use and operate the concession property (other than KCRC railway land referred to immediately below) to certain specified standards;

- the grant of a licence to access and use certain KCRC railway land;
- the term (being an initial period of 50 years from the Merger Date) of the Service Concession and redelivery of the KCRC system upon expiry or termination of the concession period. The Service Concession will end if the Company's franchise relating to the KCRC railway is revoked;
- the payments of an upfront payment of HK$4.25 billion and fixed annual payments and variable annual payments (as described in paragraph A above);
- KCRC remaining the legal and beneficial owner of the concession property as at the Merger Date and the Company being the legal and beneficial owner of certain future concession property ("Additional Concession Property");
- the regime for compensation payable by KCRC to the Company if Additional Concession Property is returned to KCRC at the end of the concession period;
- the rights and restrictions of the Company and KCRC in relation to the concession property; and
- subject to certain conditions, the Company bearing all risks, liabilities and/or costs whatsoever associated with or arising from the concession property and the land on which any of the concession property is located during the concession period.

C Sale and Purchase Agreement

The Sale and Purchase Agreement was entered into on 9 August 2007 between the Company and KCRC.

The Sale and Purchase Agreement provides the terms pursuant to which the Company acquired certain assets and contracts (the "Purchased Rail Assets") from KCRC.

The consideration for the sale of the Purchased Rail Assets (excluding the shares in the KCRC Subsidiaries) formed part of the upfront payment of HK$4.25 billion. The consideration for the sale of the shares in the KCRC Subsidiaries (which own the Category 1A Properties referred to at paragraph E below and act as property managers) formed part of the payment of HK$7.79 billion for the property package (as described in paragraph A above and in paragraph E below).

D Operating Agreement

The Operating Agreement was entered into on 9 August 2007 between the Company and the Secretary for Transport and Housing for and on behalf of the Government as contemplated in the MTR Ordinance.

The Operating Agreement is based on the previous Operating Agreement which was signed on 30 June 2000. The Operating Agreement differs from the previous Operating Agreement to provide for, amongst other things, the nature of the combined MTRC railway and KCRC railway. The Operating Agreement includes terms relating to:

- the extension of the Company's franchise under the MTR Ordinance;
- the design, construction and maintenance of the railway;
- passenger services;
- a framework for the award of new projects and the operation and ownership structure of new railways;
- the adjustment mechanism to be applied to certain of the Company's fares; and
- compensation which may be payable under the MTR Ordinance to the Company in relation to a suspension, expiry or termination of the franchise.

E Additional Property Package Agreements

Category 1A Properties

The Category 1A Properties are held by the KCRC Subsidiaries. Under the terms of the Sale and Purchase Agreement, the Company acquired from KCRC the shares in the KCRC Subsidiaries (and thereby indirectly acquired the "Category 1A Properties").

Category 1B Properties

On 9 August 2007, KCRC and the Company entered into an agreement for sale of purchase under which KCRC agreed to assign certain properties (the "Category 1B Properties") to the Company on the Merger Date. The relevant assignment was executed between KCRC and the Company on 2 December 2007.

Category 4 Properties

On 9 August 2007, the Government entered into an undertaking that it would, within periods to be agreed between the Company and the Government, offer to the Company a private treaty grant in respect of certain development sites ("Category 4 Properties"). The terms of each private treaty grant shall generally be determined by the Government, and the premium for each private treaty grant shall be assessed on a full market value basis ignoring the presence of the railway other than the Tin Shui Wai Terminus, Light Rail, Yuen Long, New Territories.

On 9 August 2007, the Company issued a letter to KCRC confirming that, if there should be any railway premises on the Category 4 Properties, the Company would assign the railway premises to KCRC.

Metropolis Equity Sub-participation Agreement

The Metropolis Equity Sub-participation Agreement was entered into on 9 August 2007 between KCRC and the Company. KCRC is obliged to act on the Company's instructions, and pay to the Company any distributions, or proceeds of sale, relating to its shareholding in the property management company The Metropolis Management Company Limited ("Metropolis"). The issued share capital of Metropolis is 25,500 A shares (which are held by KCRC) and 24,500 B shares (which are held by Cheung Kong Property Management Limited). Metropolis' business is property management.

F Liaison Committee Letter

The Liaison Committee Letter was issued on 9 August 2007 by KCRC, the terms of which were acknowledged and agreed to by the Company and the Government.

The letter sets out the agreement between the parties regarding a "Liaison Committee" established for the purposes of governing certain matters of KCRC between 9 August 2007 and the Merger Date. Upon the completion of the Rail Merger the Liaison Committee was dissolved.

G Application of Merger-related Waiver

In relation to the Operating Agreement and the Service Concession Agreement, pursuant to paragraph A of the Merger-related Waiver, the Stock Exchange granted a waiver to the Company from strict compliance with all the continuing connected transaction requirements of Chapter 14A of the Listing Rules.

Auditors

The retiring auditors, KPMG, have signified their willingness to continue in office. A resolution will be proposed at the Annual General Meeting to reappoint them and to authorise the Directors to fix their remuneration.

By order of the Board

Leonard Bryan Turk
Secretary to the Board
Hong Kong, 10 March 2009

Contents of Accounts and Notes

Independent Auditor's Report to the Shareholders of MTR Corporation Limited *(Incorporated in Hong Kong with limited liability)*

We have audited the consolidated accounts of MTR Corporation Limited (the "Company") set out on pages 139 to 230, which comprise the consolidated and company balance sheets as at 31 December 2008, and the consolidated profit and loss account, the consolidated statement of changes in equity and the consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Directors' Responsibility for the Accounts

The directors of the company are responsible for the preparation and the true and fair presentation of these accounts in accordance with Hong Kong Financial Reporting Standards issued by the Hong Kong Institute of Certified Public Accountants and the Hong Kong Companies Ordinance. This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and the true and fair presentation of accounts that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility

Our responsibility is to express an opinion on these accounts based on our audit. This report is made solely to you, as a body, in accordance with section 141 of the Hong Kong Companies Ordinance, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

We conducted our audit in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance as to whether the accounts are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the accounts. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the accounts, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and true and fair presentation of the accounts in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the accounts.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated accounts give a true and fair view of the state of affairs of the Company and of the Group as at 31 December 2008 and of the Group's profit and cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards and have been properly prepared in accordance with the Hong Kong Companies Ordinance.

KPMG

Certified Public Accountants

8th Floor, Prince's Building
10 Chater Road
Central, Hong Kong
10 March 2009

Consolidated Profit and Loss Account

for the year ended 31 December in HK$ million	Note	2008	2007
Fare revenue	4	**11,467**	7,115
Station commercial and rail related revenue	5A	**3,449**	1,741
Rental, management and other revenue	5B	**2,712**	1,834
Turnover		**17,628**	10,690
Staff costs and related expenses	6A	**(3,358)**	(1,802)
Energy and utilities		**(1,020)**	(576)
Operational rent and rates		**(179)**	(99)
Stores and spares consumed		**(411)**	(130)
Repairs and maintenance	6B	**(856)**	(521)
Railway support services		**(121)**	(86)
Expenses relating to station commercial and rail related businesses		**(822)**	(410)
Expenses relating to property ownership, management and other businesses		**(785)**	(540)
Project study and business development expenses	6C	**(198)**	(268)
General and administration expenses	6D	**(342)**	(183)
Other expenses	6D	**(211)**	(163)
Operating expenses before depreciation and amortisation		**(8,303)**	(4,778)
Operating profit from railway and related businesses before depreciation and amortisation		**9,325**	5,912
Profit on property developments	8	**4,670**	8,304
Operating profit before depreciation and amortisation		**13,995**	14,216
Depreciation and amortisation	9	**(2,930)**	(2,739)
Merger related expenses	10	**(53)**	(193)
Operating profit before interest and finance charges		**11,012**	11,284
Interest and finance charges	11	**(1,998)**	(1,316)
Change in fair value of investment properties	18	**(146)**	8,011
Net gain on acquisition of subsidiaries		**–**	187
Share of profits of non-controlled subsidiaries and associates	12	**159**	99
Profit before taxation		**9,027**	18,265
Income tax	13A	**(747)**	(3,083)
Profit for the year		**8,280**	15,182
Attributable to:			
– Equity shareholders of the Company	14	**8,284**	15,180
– Minority interests		**(4)**	2
Profit for the year		**8,280**	15,182
Dividends paid and proposed to equity shareholders of the Company attributable to the year:	15		
– Interim dividend declared and paid during the year		**790**	782
– Final dividend proposed after the balance sheet date		**1,925**	1,740
		2,715	2,522
Earnings per share:	16		
– Basic		**HK$1.47**	HK$2.72
– Diluted		**HK$1.47**	HK$2.72

The notes on pages 144 to 230 form part of the accounts

Consolidated Balance Sheet

at 31 December in HK$ million	Note	2008	2007
Assets			
Fixed assets			
– Investment properties	18	**37,737**	37,723
– Other property, plant and equipment	19	**77,804**	79,444
– Service concession assets	20	**15,463**	15,250
		131,004	132,417
Property management rights	21	**35**	40
Railway construction in progress	22	**658**	424
Property development in progress	23A	**7,895**	9,066
Deferred expenditure	24	**1,988**	825
Prepaid land lease payments	25	**567**	581
Interests in non-controlled subsidiaries	26	**381**	268
Interests in associates	28	**743**	205
Deferred tax assets	44B	**11**	4
Investments in securities	29	**471**	333
Staff housing loans	30	**10**	15
Properties held for sale	31	**2,228**	756
Derivative financial assets	32	**528**	273
Stores and spares	33	**690**	642
Debtors, deposits and payments in advance	34	**7,190**	5,167
Loan to a property developer	35	**3,720**	3,532
Amounts due from the Government and other related parties	36	**426**	544
Cash and cash equivalents	37	**793**	576
		159,338	155,668
Liabilities			
Bank overdrafts	38A	**59**	2
Short-term loans	38A	**1,646**	507
Creditors, accrued charges and provisions	39	**5,334**	5,412
Current taxation	44A	**450**	3
Contract retentions	40	**224**	225
Amounts due to related parties	41	**882**	975
Loans and other obligations	38A	**29,584**	33,541
Obligations under service concession	42	**10,656**	10,685
Derivative financial liabilities	32	**305**	192
Deferred income	43	**156**	515
Deferred tax liabilities	44B	**12,220**	12,574
		61,516	64,631
Net assets		**97,822**	91,037
Capital and reserves			
Share capital, share premium and capital reserve	45A	**41,119**	39,828
Other reserves	46	**56,682**	51,186
Total equity attributable to equity shareholders of the Company		**97,801**	91,014
Minority interests		**21**	23
Total equity		**97,822**	91,037

Approved and authorised for issue by the Members of the Board on 10 March 2009

Raymond K F Ch'ien
C K Chow
Lincoln K K Leong

The notes on pages 144 to 230 form part of the accounts

Balance Sheet

at 31 December in HK$ million	Note	2008	2007
Assets			
Fixed assets			
– Investment properties	18	**36,618**	36,562
– Other property, plant and equipment	19	**77,613**	79,270
– Service concession assets	20	**15,463**	15,250
		129,694	131,082
Property management rights	21	**35**	40
Railway construction in progress	22	**658**	424
Property development in progress	23A	**7,895**	9,066
Deferred expenditure	24	**338**	155
Prepaid land lease payments	25	**567**	581
Investments in subsidiaries	27	**1,150**	1,150
Investments in securities	29	**90**	–
Staff housing loans	30	**10**	15
Properties held for sale	31	**2,228**	756
Derivative financial assets	32	**528**	273
Stores and spares	33	**667**	640
Debtors, deposits and payments in advance	34	**7,000**	5,057
Loan to a property developer	35	**3,720**	3,532
Amounts due from the Government and other related parties	36	**2,128**	1,315
Cash and cash equivalents	37	**262**	184
		156,970	154,270
Liabilities			
Bank overdrafts	38A	**59**	2
Short-term loans	38A	**624**	186
Creditors, accrued charges and provisions	39	**4,666**	4,856
Current taxation	44A	**441**	1
Contract retentions	40	**166**	197
Amounts due to related parties	41	**14,121**	12,962
Loans and other obligations	38A	**16,628**	21,771
Obligations under service concession	42	**10,656**	10,685
Derivative financial liabilities	32	**305**	192
Deferred income	43	**156**	515
Deferred tax liabilities	44B	**12,219**	12,574
		60,041	63,941
Net assets		**96,929**	90,329
Capital and reserves			
Share capital, share premium and capital reserve	45A	**41,119**	39,828
Other reserves	46	**55,810**	50,501
Total equity		**96,929**	90,329

Approved and authorised for issue by the Members of the Board on 10 March 2009

Raymond K F Ch'ien

C K Chow

Lincoln K K Leong

The notes on pages 144 to 230 form part of the accounts

Consolidated Statement of Changes in Equity

for the year ended 31 December in HK$ million	Note	2008	2008	2007	2007
Total equity as at 1 January					
– Attributable to equity shareholders of the Company		**91,014**		76,767	
– Minority interests		**23**		19	
Total equity as at 1 January			**91,037**		76,786
Cash flow hedges:	46				
Effective portion of changes in fair value, net of deferred tax		**(151)**		(13)	
Transfer from equity					
– to profit and loss account		**41**		–	
– to initial carrying amount of non-financial hedged items		**(14)**		(2)	
– to deferred tax		**(5)**		–	
		(129)		(15)	
(Deficit)/surplus on revaluation of self-occupied land and buildings, net of deferred tax	46	**(189)**		202	
Release of revaluation reserve on disposal, net of deferred tax		**7**		–	
Effect on deferred tax balances resulting from a change in tax rate		**14**		–	
Exchange difference on translation of accounts of overseas subsidiaries	46	**21**		25	
Net (expense)/income recognised directly in equity		**(276)**		212	
Net profit for the year		**8,280**		15,182	
Total recognised income and expense for the year			**8,004**		15,394
Dividends declared or approved during the year	15				
– 2007/2006 final dividend		**(1,740)**		(1,554)	
– 2008/2007 interim dividend		**(790)**		(782)	
			(2,530)		(2,336)
Shares issued during the year	45A				
– Employee Share Option Scheme		**27**		23	
– Scrip Dividend Scheme		**1,262**		1,166	
		1,289		1,189	
Employee share-based payments	46	**20**		2	
Movements in equity arising from capital transactions			**1,309**		1,191
Exchange difference on translation of minority interests			**2**		2
Total equity as at 31 December			**97,822**		91,037
Total recognised income and expense for the year attributable to:					
– Equity shareholders of the Company			**8,008**		15,392
– Minority interests			**(4)**		2
			8,004		15,394

The notes on pages 144 to 230 form part of the accounts

Consolidated Cash Flow Statement

for the year ended 31 December in HK$ million	2008	2007
Cash flows from operating activities		
Operating profit from railway and related businesses before depreciation and amortisation	**9,325**	5,912
Adjustments for:		
Decrease in provision for obsolete stock	**(14)**	(3)
Loss on disposal of fixed assets	**30**	36
Amortisation of deferred income from lease transaction	**–**	(5)
Amortisation of prepaid land lease payments	**14**	13
Decrease in fair value of derivative instruments	**11**	1
Unrealised (gain)/loss on revaluation of investment in securities	**(2)**	4
Employee share-based payment expenses	**22**	7
Exchange gain	**(1)**	(1)
Operating profit from railway and related businesses before working capital changes	**9,385**	5,964
Decrease/(increase) in debtors, deposits and payments in advance	**113**	(421)
Increase in stores and spares	**(34)**	(10)
Increase in creditors, accrued charges and provisions	**34**	442
Cash generated from operations	**9,498**	5,975
Current tax paid		
Hong Kong Profits Tax paid	**(575)**	–
Overseas tax paid	**(2)**	(1)
Net cash generated from operating activities	**8,921**	5,974
Cash flows from investing activities		
Capital expenditure		
– Purchase of operational railway assets	**(1,624)**	(944)
– LOHAS Park Station Project	**(230)**	(203)
– Disneyland Resort Line Project	**(16)**	(25)
– Tung Chung Cable Car Project	**(43)**	(82)
– West Island Line Project	**(306)**	(45)
– Tseung Kwan O property development projects	**(204)**	(197)
– East Rail/Light Rail/Kowloon Southern Link property development projects	**(1,962)**	(2)
– Property fitting out works and other development projects	**(431)**	(641)
– Other capital projects	**(991)**	(342)
Net payments in respect of Shatin to Central Link and Express Rail Link	**(89)**	(8)
Fixed annual payment on service concession assets	**(750)**	–
Payments in respect of the Rail Merger		
– Upfront payment for the service concession	**–**	(4,250)
– Upfront payment for property package	**–**	(7,790)
– Cash received for the assumption of assets and liabilities of KCRC	**–**	786
– Staff voluntary separation payments	**(174)**	(1)
– Other payments directly attributable to the Rail Merger	**(142)**	(354)
Receipts in respect of property development	**4,448**	5,824
Receipts of Government grant for West Island Line Project	**400**	–
Purchase of investment in securities	**(147)**	(266)
Proceeds from sale of investment in securities	**100**	202
Loan repayments from/(drawdown to) non-controlled subsidiaries and associates	**109**	(62)
Investment in an associate	**(515)**	(103)
Dividend received from non-controlled subsidiaries	**23**	–
Principal repayments under Staff Housing Loan Scheme	**5**	10
Net cash used in investing activities	**(2,539)**	(8,493)
Cash flows from financing activities		
Proceeds from shares issued under share option schemes	**26**	23
Drawdown of loans	**6,150**	11,391
Proceeds from issuance of capital market instruments	**1,750**	–
Repayment of loans	**(10,438)**	(5,849)
Repayment of capital market instruments	**(1,000)**	–
Reduction in capital element of finance lease	**–**	(141)
Interest paid	**(1,442)**	(1,500)
Interest received	**14**	50
Interest element of finance lease rental payments	**–**	(9)
Finance charges paid	**(17)**	(9)
Dividends paid	**(1,265)**	(1,168)
Net cash (used in)/generated from financing activities	**(6,222)**	2,788
Net increase in cash and cash equivalents	**160**	269
Cash and cash equivalents at 1 January	**574**	305
Cash and cash equivalents at 31 December	**734**	574
Analysis of the balances of cash and cash equivalents		
Cash and cash equivalents	**793**	576
Bank overdrafts	**(59)**	(2)
	734	574

The notes on pages 144 to 230 form part of the accounts

Notes to the Accounts

1 Statement of Compliance

These accounts have been prepared in compliance with the Hong Kong Companies Ordinance and the applicable disclosure provisions of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules"). These accounts have also 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"), and accounting principles generally accepted in Hong Kong. The HKFRSs have been fully converged with International Financial Reporting Standards in all material respects. A summary of the principal accounting policies adopted by the Group is set out in note 2.

The HKICPA has issued certain new and revised HKFRSs that are effective for accounting periods beginning on or after 1 January 2008. Changes in accounting policies resulting from initial application of these developments to the extent that they are relevant to the Group for the current and prior accounting periods reflected in these accounts are disclosed in note 2A(iii).

2 Principal Accounting Policies

A Basis of Preparation of the Accounts

(i) The measurement basis used in the preparation of the accounts is historical cost basis except that the following assets and liabilities are stated at their fair value as explained in the accounting policies set out below:

- investment properties (see note 2F(i));
- other leasehold land and buildings, for which the fair values cannot be measured separately at inception of the lease and the entire lease is classified as a finance lease (see note 2F(ii));
- financial instruments classified as investments in securities other than those intended to be held to maturity (see note 2M); and
- derivative financial instruments (see note 2U).

(ii) The preparation of the accounts 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 and estimations 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 accounts and estimates are discussed in note 53.

(iii) The HKICPA has issued the following interpretations and amendments to HKFRSs that are first effective for the current accounting period of the Group and the Company:

- HK(IFRIC) 11, HKFRS 2 – Group and treasury share transactions
- HK(IFRIC) 12, Service concession arrangements
- HK(IFRIC) 14, HKAS 19 – The limit on a defined benefit asset, minimum funding requirements and their interaction
- Amendments to HKAS 39, Financial instruments: Recognition and measurement, and HKFRS 7, Financial instruments: Disclosures – Reclassification of financial assets

The Company early adopted HK(IFRIC) 12 in the 2007 accounts. As a result, the merger of the Company's operations with Kowloon-Canton Railway Corporation ("KCRC") on 2 December 2007 was considered as a service concession arrangement under this interpretation. Except for HK(IFRIC) 12, the other HKFRS developments listed above have no material impact on the Group's and the Company's financial statements.

The Group has not applied any new standard or interpretation that is not yet effective for the current accounting period (see note 54).

B Basis of Consolidation

The consolidated accounts include the accounts of the Company and its subsidiaries (together referred to as the "Group") and the Group's interest in non-controlled subsidiaries (see note 2D) and associates (see note 2E) made up to 31 December each year. The results of subsidiaries acquired or disposed of during the year are included in the consolidated profit and loss account from or to the date of their acquisition or disposal, as appropriate.

2 Principal Accounting Policies *(continued)*

C Subsidiaries

A subsidiary in accordance with the Hong Kong Companies Ordinance is a company in which the Group, directly or indirectly, holds more than half of the issued share capital, or controls more than half of the voting power, or controls the composition of the board of directors. Subsidiaries are considered to be controlled if the Company has the power, directly or indirectly, to govern the financial and operating policies, so as to obtain benefits from their activities.

Intra-group balances and transactions, and any unrealised profits arising from intra-group transactions, are eliminated in full in preparing the consolidated accounts. 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.

Minority interests at the balance sheet date, being the portion of the net assets of subsidiaries attributable to equity interests that are not owned by the Company, whether directly or indirectly through subsidiaries, are presented in the consolidated balance sheet and statement of changes in equity within equity, separately from equity attributable to the equity shareholders of the Company. Minority interests in the results of the Group are presented on the face of the consolidated profit and loss account as an allocation of the total profit or loss for the year between minority interests and the equity shareholders of the Company.

Where losses attributable to the minority exceed the minority interest in the equity of a subsidiary, the excess, and any further losses attributable to the minority, are charged against the Group's interest except to the extent that the minority has a binding obligation to, and is able to, make good the losses. All subsequent profits of the subsidiary are allocated to the Group until the minority's share of losses previously absorbed by the Group has been recovered.

Investments in subsidiaries are carried in the Company's balance sheet at cost less any impairment losses (see note 2H(ii)).

D Non-controlled Subsidiaries

Non-controlled subsidiaries are not consolidated in the accounts as the Group does not have effective control over their Boards. The investments in non-controlled subsidiaries are accounted for in the consolidated accounts of the Company using the equity method and are initially recorded at cost and adjusted thereafter for the post acquisition change in the Group's share of their net assets. The consolidated profit and loss account reflects the Group's share of the results of those non-controlled subsidiaries for the year.

Unrealised profits and losses resulting from transactions between the Group and the non-controlled subsidiaries are eliminated to the extent of the Group's interest in those subsidiaries, except where unrealised losses provide evidence of an impairment of the asset transferred, in which case they are recognised immediately in the profit and loss account.

In the Company's balance sheet, its investments in non-controlled subsidiaries are stated at cost less impairment losses (see note 2H(ii)).

E Associates and Jointly Controlled Entities

An associate is an entity over which the Group or the 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 the Company and other parties, where the contractual arrangement establishes that the Group or the 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 accounts of the Company using 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 reflects the Group's share of the post acquisition results of the associates and jointly controlled entities for the year.

When the Group's share of losses equals or 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 and 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 associates and jointly controlled entities, except where unrealised losses provide evidence of an impairment of the asset transferred, in which case they are recognised immediately in the profit and loss account.

In the Company's balance sheet, its investments in associates and jointly controlled entities are stated at cost less impairment losses (see note 2H(ii)).

2 Principal Accounting Policies *(continued)*

F Fixed Assets

(i) Investment properties are land and/or buildings which are owned or held under a leasehold interest to earn rental income and/or for capital appreciation.

Investment properties are stated in the balance sheet at fair value as determined semi-annually by independent professionally qualified valuers. Gains or losses arising from changes in the fair value are recognised as profit or loss in the year in which they arise.

Property that is being constructed or developed for future use as investment property is classified as asset under construction within property, plant and equipment and stated at cost until construction or development is complete, at which time it is reclassified as investment property at fair value. Any difference between the fair value of the property at that date and its previous carrying amount is recognised in the profit and loss account.

(ii) Land held for own use under operating leases and buildings thereon, where the fair values of the leasehold interest in the land and buildings cannot be measured separately at inception of the lease are accounted for as being held under a finance lease, unless the buildings are also clearly held under an operating lease. The self-occupied land and buildings are stated in the balance sheet at their fair values on the basis of their existing use at the date of revaluation less any subsequent accumulated depreciation. Revaluations are performed by independent qualified valuers semi-annually, with changes in the value arising on revaluations treated as movements in the fixed asset revaluation reserve, except:

(a) where the balance of the fixed asset revaluation reserve relating to a self-occupied land and building is insufficient to cover a revaluation deficit of that property, the excess of the deficit is charged to the profit and loss account; and

(b) where a revaluation deficit had previously been charged to the profit and loss account and a revaluation surplus subsequently arises, this surplus is firstly credited to the profit and loss account to the extent of the deficit previously charged to the profit and loss account, and is thereafter taken to the fixed asset revaluation reserve.

(iii) Civil works and plant and equipment are stated at cost less accumulated depreciation and impairment losses (see note 2H(ii)).

(iv) Assets under construction are stated at cost less impairment losses (see note 2H(ii)). Cost comprises direct costs of construction, such as materials, staff costs and overheads, together with interest expense capitalised during the period of construction or installation and testing. Capitalisation of these costs ceases and the asset concerned is transferred to the appropriate fixed assets category when substantially all the activities necessary to prepare the asset for its intended use are completed.

(v) Leased assets
(a) Leases of assets under which the lessee assumes substantially all the risks and rewards of ownership are classified as finance leases. Where the Group acquires the use of assets under finance leases, the amounts representing the fair value of the leased asset, or, if lower, the present value of the minimum lease payments (computed using the rate of interest implicit in the lease), of such assets are included in fixed assets and the corresponding liabilities, net of finance charges, are recorded as obligations under finance leases. Depreciation and impairment losses are accounted for in accordance with the accounting policy as set out in notes 2I(iv) and 2H(ii) respectively. Finance charges implicit in the lease payments are charged to the profit and loss account over the period of the leases so as to produce an approximately constant periodic rate of charge on the remaining balance of the obligations for each accounting period.

(b) Leases of assets, other than that mentioned in note 2F(v)(c) below, under which the lessor has not transferred substantially all the risks and rewards of ownership are classified as operating leases. Where the Group leases out assets under operating leases, the assets are included in the balance sheet according to their nature and, where applicable, are depreciated in accordance with the Group's depreciation policies. Impairment losses are accounted for in accordance with the accounting policies on impairment of assets (see note 2H(ii)). Revenue arising from operating leases is recognised in accordance with the Group's revenue recognition policies as set out in note 2AA(iv).

(c) Land held for own use under an operating lease where its fair value cannot be measured separately from the fair value of a building situated thereon at inception of the lease, is accounted for as being held under a finance lease, unless the building is also clearly held under an operating lease (see note 2F(ii)). For these purposes, inception of the lease is the time that the lease was first entered into by the Group, or taken over from the previous lessee, or at the date of construction of those buildings, if later.

(vi) Subsequent expenditure relating to the replacement of certain parts of an existing fixed asset is recognised in the carrying amount of the asset if it is probable that future economic benefit will flow to the Group and the cost of the item can be measured reliably. The carrying amount of those parts that are replaced is derecognised, with gain or loss arising therefrom dealt with in the profit and loss account.

Expenditure on repairs or maintenance of an existing fixed asset to restore or maintain the originally assessed standard of performance of that asset is charged as an expense when incurred.

Gains or losses arising from the retirement or disposal of a fixed asset or an investment property are determined as the difference between the net disposal proceeds and the carrying amount of the asset. Such gains or losses are recognised as income or expense in the profit and loss account on the date of retirement or disposal. Any related revaluation surplus is transferred from the fixed asset revaluation reserve to retained profits.

2 Principal Accounting Policies *(continued)*

F Fixed Assets *(continued)*

(vii) Service concession assets
Where the Group enters into service concession arrangements under which the Group acquires the right to access, use and operate certain assets for the provision of public services:

- Upfront payments at inception of the service concession are capitalised and amortised on a straight-line basis over the period of the service concession;
- Annual payments over the period of the service concession with the amounts fixed at inception are capitalised at the present value of the total fixed annual payments discounted at the incremental long-term borrowing rate determined at inception, and amortised on a straight-line basis over the period of the service concession with a corresponding liability recognised as obligations under service concession;
- Annual payments for the service concession which are not fixed or determinable at inception and which are contingent on future revenues generated from the service concession over certain thresholds are charged to the profit and loss account in the period when incurred;
- Expenditure directly attributable to the acquisition of the service concession up to inception, including the assumption of certain obligations of the grantor of the service concession, are capitalised and amortised on a straight-line basis over the period of the service concession; and
- Payments for the replacement and/or upgrade of assets subject to the service concession arrangement are capitalised and amortised on a straight-line basis over the shorter of the assets' useful lives and the remaining period of the service concession.

The service concession asset is carried on the balance sheet, as an intangible asset, at cost less accumulated amortisation and impairment losses, if any (see note 2H(ii)).

Income and expenditure and assets and liabilities in relation to the operation of the service concession are accounted for in the respective line items of the Group's and the Company's profit and loss accounts and balance sheets.

G Property Management Rights

Where the Group makes payments for acquisition of property management rights, the amounts paid are capitalised as intangible assets and stated in the balance sheet at cost less accumulated amortisation and impairment losses (see note 2H(ii)). The intangible asset is amortised to the profit and loss account on a straight-line basis over the terms of the management rights.

H Impairment of Assets

(i) Impairment of Debtors and Other Receivables
Debtors and other current and non-current receivables are reviewed at each balance sheet date to determine whether there is objective evidence of impairment. If any such evidence exists, 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 these assets) where the effect of discounting is material.

If in a subsequent period the amount of an impairment loss decreases, the impairment loss is reversed through the profit and loss account.

(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 an impairment loss previously recognised no longer exists or may have decreased:

- fixed assets (other than properties carried at revalued amounts);
- service concession assets;
- property management rights;
- railway construction in progress;
- property development in progress;
- prepaid land lease payments;
- deferred expenditure;
- investments in held-to-maturity securities; and
- investments in subsidiaries, non-controlled subsidiaries, associates and jointly controlled entities.

If any such indication exists, the asset's recoverable amount is estimated.

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 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).

2 Principal Accounting Policies *(continued)*

H Impairment of Assets *(continued)*

(ii) Impairment of Other Assets *(continued)*

An impairment loss is recognised in the profit and loss account whenever the carrying amount of an asset, or the cash-generating unit to which it belongs, exceeds its recoverable amount.

An impairment loss is reversed if there has been a favourable change in the estimates used to determine the recoverable amount of the asset.

A reversal of impairment losses 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 the profit and loss account in the year in which the reversals are recognised.

I Depreciation

(i) Investment properties are not depreciated.

(ii) Fixed assets other than investment properties and assets under construction are depreciated on a straight-line basis at rates sufficient to write off their cost or valuation, less their estimated residual value, if any, over their estimated useful lives as follows:

Land and Buildings

Self-occupied land and buildings	the shorter of 50 years and the unexpired term of the lease

Civil Works

Excavation and boring	Indefinite
Tunnel linings, underground civil structures, overhead structures and immersed tubes	100 years
Station building structures	100 years
Depot structures	80 years
Concrete kiosk structures	20 years
Cableway station tower and theme village structures	27 years

Plant and Equipment

Rolling stock and components	4 – 50 years
Platform screen doors	35 years
Rail track	7 – 30 years
Environmental control systems, lifts and escalators, fire protection and drainage system	7 – 30 years
Power supply systems	7 – 40 years
Aerial ropeway and cabin	5 – 27 years
Automatic fare collection systems, metal station kiosks, and other mechanical equipment	20 years
Train control and signalling equipment, station announcement systems, telecommunication systems and advertising panels	5 – 20 years
Station architectural finishes	20 – 30 years
Fixtures and fittings	10 – 15 years
Maintenance equipment	4 – 10 years
Office furniture and equipment	5 – 15 years
Computer software licences and applications	5 – 7 years
Computer equipment	4 – 5 years
Cleaning equipment and tools	5 years
Motor vehicles	4 years

Where parts of an item of property, plant and equipment have different useful lives, each part is depreciated separately. The useful lives of the various categories of fixed assets are reviewed annually in the light of actual asset condition, usage experience and the current asset replacement programme.

(iii) No depreciation is provided on assets under construction until construction is completed and the assets are ready for their intended use.

(iv) Depreciation on assets held under finance leases is provided at rates designed to write off the cost of the asset in equal annual amounts over the shorter of the lease term or the anticipated useful life of the asset as set out above, except in cases where title to the asset will be acquired by the Group at the end of the lease where depreciation is provided at rates designed to write off the cost of the asset in equal amounts over the anticipated useful life of the asset.

2 Principal Accounting Policies *(continued)*

J Construction Costs

(i) Costs incurred by the Group in respect of feasibility studies on proposed railway related construction projects (including consultancy fees, in-house staff costs and overheads) are dealt with as follows:

- where the proposed projects are at a preliminary review stage with no certainty of materialising, the costs concerned are written off to the profit and loss account; and
- where the proposed projects are at a detailed study stage, having been agreed in principle by the Members of the Board based on a feasible financial plan, the costs concerned are dealt with as deferred expenditure until such time as a project agreement is reached, whereupon the costs are transferred to railway construction in progress.

(ii) After entering into a project agreement, all costs incurred in the construction of the railway are dealt with as railway construction in progress until commissioning of the railway line, whereupon the relevant construction costs are transferred to fixed assets.

K Property Development

(i) Costs incurred by the Group in respect of site preparation, land costs and acquisition of development rights for as well as interest in connection with loans to property developers are dealt with as property development in progress.

(ii) Payments received from developers in respect of developments are offset against the amounts in property development in progress attributable to that development. Any surplus amounts of payments received from developers in excess of the balance in property development in progress are transferred to deferred income. In these cases, further costs subsequently incurred by the Group in respect of that development are charged against deferred income.

(iii) Expenditure incurred on the development of properties for self-occupation by the Group is transferred to fixed assets when the occupation permits are issued and the properties are put into use.

(iv) When agreement is reached with a developer to redevelop an existing self-occupied property, the relevant property is revalued on an existing use basis prior to commencement of redevelopment. The surplus arising on revaluation is credited to fixed asset revaluation reserve. On commencement of redevelopment, the net book value of the property is transferred to property development in progress.

(v) Where an interest-free loan is provided to a developer as one of the terms of the development contract, such loan is initially stated at fair value which is its present value discounted at the prevailing market rates of interest at inception. The difference between the fair value and the face value of the loan is dealt with as property development in progress during construction and transferred to the profit and loss account upon completion of the development. Notional interest income is credited to the profit and loss account and debited to the loan over the period of the loan so that the fair value of the loan at maturity equates to its face value.

(vi) Profits arising from the development of properties undertaken in conjunction with property developers are recognised in the profit and loss account as follows:

- where the Group receives payments from developers at the commencement of the project, profits arising from such payments are recognised when the foundation and site enabling works are complete and acceptable for development, and after taking into account the outstanding risks and obligations, if any, retained by the Group in connection with the development;
- where the Group receives a right to a share of the net surplus from sale of the development, income is initially recognised by the Group upon the issue of occupation permits provided the amounts of revenue and costs can be estimated reliably. The interest in any unsold properties is subsequently remeasured on a basis consistent with the policy set out in note 2K(viii); and
- where the Group receives a distribution of the assets of the development, profit is recognised based on the fair value of such assets at the time of receipt and after taking into account any outstanding risks and obligations retained by the Group in connection with the development.

Upon recognition of profit, the balance of deferred income or property development in progress related to that development is credited or charged to the profit and loss account, as the case may be.

(vii) Where the Group is liable to pay the developer consideration for the retention of part of a property to be redeveloped, profit attributable to the Group in respect of the redevelopment (including any payment received from the developer) will be recognised in the profit and loss account when the quantum of the obligation of the Group and the amount of realised profit can be determined with reasonable accuracy.

(viii) Where properties are received as a profit distribution upon completion of development and are held for sale, those properties are stated at cost represented by their estimated net realisable value upon receipt. Net realisable value represents the estimated selling price less costs to be incurred in selling the properties. When properties are sold, the carrying amount of those properties is recognised as cost of properties sold in the period in which the related revenue is recognised. The amount of any write-down of properties to net realisable value is recognised as an expense in the period the write-down occurs. The amount of any reversal of any write-down of properties, arising from an increase in net realisable value, is recognised as a reduction in the cost of properties sold in the period in which the reversal occurs.

(ix) Where properties under construction are received as a sharing in kind from a development, these properties are initially recognised in assets under construction at fair value. Further costs incurred in the construction of those assets are capitalised into the assets under construction, which are transferred to fixed assets when substantially all the activities necessary to prepare the assets for their intended use have been completed.

2 Principal Accounting Policies *(continued)*

L Jointly Controlled Operations

The arrangements entered into by the Group with developers for property developments without establishing separate entities are considered to be jointly controlled operations pursuant to HKAS 31 "Investments in joint ventures". Under the development arrangements, the Group is normally responsible for its own costs, including in-house staff costs and the costs of enabling works, and the developers normally undertake to pay for all other project costs such as land premium, construction costs, professional fees, etc. Such costs are deductible from the proceeds of sale before surplus proceeds are shared. In respect of its interests in such operations, the Group accounts for the costs of enabling works and land costs paid net of up-front payments received as property development in progress. In cases where up-front payments received from developers exceed the related expenditures incurred by the Group, such excess is recorded as deferred income. Expenses incurred by the Group on staff, overhead and consultancy fees in respect of these developments are also capitalised as property development in progress. The Group's share of income earned from such operations is recognised in the profit and loss account on the basis of note 2K(vi) after netting off any related balance in property development in progress at that time.

M Investments in Securities

The Group's policies for investments in securities (other than investments in its subsidiaries, non-controlled subsidiaries, associates and jointly controlled entities) are as follows:

(i) Investments in securities held for trading purpose are initially stated at fair value. At each balance sheet date the fair value is remeasured, with any resultant unrealised gain or loss being recognised in the profit and loss account.

(ii) Investments in debt securities on which the Company has the ability and intention to hold to maturity are classified as held-to-maturity securities, which are stated at amortised cost less impairment losses (see note 2(H)(ii)).

(iii) Investments are recognised/derecognised on the date the Group commits to purchase / sell the investments.

(iv) Profit or loss on disposal of investments in securities are determined as the difference between the estimated net disposal proceeds and the carrying amount of the investments and are accounted for in the profit and loss account as they arise.

N Defeasance of Long-term Lease Payments

Where obligations to make long-term lease payments have been defeased by the placement of securities, those obligations and securities (and income and charges arising therefrom) have been netted off in order to reflect the overall commercial effect of the arrangements. These transactions are not accounted for as leases and these liabilities and investment in securities are not recognised as liabilities and assets.

O Stores and Spares

Stores and spares used for railway and business operation are categorised as either revenue or capital. Revenue spares are stated in the balance sheet at cost, using the weighted average cost method and are recognised in the year in which the consumption occurred. Provision is made for obsolescence where appropriate. Capital items are included in fixed assets and stated at cost less aggregate depreciation and impairment losses. Depreciation is charged at the rates applicable to the relevant fixed assets against which the capital spares are held in reserve.

P Long-term Consultancy Contracts

The accounting policy for contract revenue is set out in note 2AA(iii). When the outcome of a fixed-price consultancy contract can be estimated reliably, contract costs are recognised as expenses by reference to the stage of completion of the contract activity at the balance sheet date. When it is probable that total contract costs will exceed total contract revenue, the expected loss is recognised as an expense immediately. When the outcome of a consultancy contract cannot be estimated reliably, contract costs are recognised as expenses in the period in which they are incurred.

Consultancy contracts in progress at the balance sheet date are recorded in the balance sheet at the net amount of costs incurred plus recognised profits less recognised losses and progress billings, and are presented in the balance sheet as the "Gross amount due from customers for contract work" (as an asset) or the "Gross amount due to customers for contract work" (as a liability), as applicable. Progress billings not yet paid by the customer are included in the balance sheet under "Debtors, deposits and payments in advance". Amounts received before the related work is performed are included in the balance sheet, as a liability, under "Creditors, accrued charges and provisions".

Q Cash and Cash Equivalents

Cash and cash equivalents comprise cash at banks 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. Bank overdrafts that are repayable on demand and form an integral part of the Group's cash management are also included as a component of cash and cash equivalents for the purpose of the consolidated cash flow statement.

R Debtors, Deposits and Payments in Advance

Debtors, deposits and payments in advance are initially recognised at fair value and thereafter stated at amortised cost less impairment losses for bad and doubtful debts (see note 2H(i)), except where the effect of discounting would be immaterial or the discount is not measurable as the receivables are interest-free loans made to related parties without any fixed repayment terms. In such cases, the receivables are stated at cost less impairment losses for bad and doubtful debts.

2 Principal Accounting Policies *(continued)*

S Interest-bearing Borrowings

Interest-bearing borrowings are recognised initially at fair value, net of transaction costs incurred. The unhedged portion of interest-bearing borrowings are subsequently stated at amortised costs; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the profit and loss account over the period of the borrowings using the effective interest method.

Subsequent to initial recognition, the carrying amount of the hedged portion of interest-bearing borrowings is remeasured and the change in fair value attributable to the risk being hedged is recognised in the profit and loss account to offset the effect of the gain or loss on the related hedging instrument.

T Creditors, Accrued Charges and Provisions

Creditors, accrued charges and provisions are stated at amortised cost if the effect of discounting would be material, otherwise they are stated at cost.

U Derivative Financial Instruments and Hedging Activities

The Group uses derivative financial instruments such as interest rate swaps and currency swaps to manage its interest rate and foreign exchange exposure. Based on Group policy, these instruments are used solely for reducing or eliminating financial risks associated with the Group's liabilities and not for trading or speculation purposes.

Derivatives are initially recognised at fair value and are subsequently remeasured at their fair value at each balance sheet date. The method of recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument and the nature of the item being hedged.

Where hedge accounting applies, the Group designates derivatives employed as either: (1) a fair value hedge: to hedge the fair value of recognised liabilities; or (2) a cash flow hedge: to hedge the variability in cash flows of a recognised liability or the foreign currency risk of a firm commitment.

(i) Fair Value Hedge

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

(ii) Cash Flow Hedge

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised directly in equity. The gain or loss relating to the ineffective portion is recognised immediately in the profit and loss account.

Amounts accumulated in equity are transferred to the profit and loss account in the periods when the hedged liability affects earning. However, when the firm commitment that is hedged results in the recognition of a non-financial asset, the associated gains and losses that were recognised in equity are transferred from equity and included in the initial cost or carrying amount of the asset.

When a hedging instrument expires or is sold, terminated or exercised, or when a hedge no longer meets the criteria for hedge accounting, the cumulative gain or loss existing in equity at that time shall remain in equity and is recognised when the hedged liability affects profit or loss, or when the firm commitment is recognised as a non-financial asset, in accordance with the above policy. However, when a hedged liability is no longer expected to take place or a firm commitment is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the profit and loss account.

(iii) Derivatives That Do Not Qualify for Hedge Accounting

Changes in the fair value of any derivative instruments that do not qualify for hedge accounting are recognised immediately in the profit and loss account.

V Employee Benefits

(i) Salaries, annual leave, leave passage allowance and other costs of non-monetary benefits are accrued and recognised as an expense in the year in which the associated services are rendered by employees of the Group, except those benefits incurred for project staff in respect of construction projects and capital works, which are capitalised as part of the cost of the qualifying assets.

(ii) Contributions to defined contribution retirement plans, including contributions to Mandatory Provident Funds ("MPF") as required under the Hong Kong Mandatory Provident Fund Schemes Ordinance, are recognised as an expense in the profit and loss account as incurred, except those contributions for project staff incurred in respect of construction projects and capital works, which are capitalised as part of the cost of the qualifying assets.

(iii) The Group's net obligation in respect of defined benefit retirement plans is calculated separately for each plan by estimating the amount of future benefit that employees have earned in return for their service in the current and prior years; that benefit is discounted to determine the present value, and the fair value of any plan assets is deducted. The discount rate is the yield at balance sheet date on high quality corporate bonds that have maturity dates approximating the terms of the Group's obligations. If there is no deep market in such bonds, the market yield on government bonds would be used. The calculation is performed by a qualified actuary using the projected unit credit method.

2 Principal Accounting Policies *(continued)*

V Employee Benefits *(continued)*

When the benefits of a plan are improved, the portion of the increased benefit relating to past service by employees is recognised either as an expense in the profit and loss account, or capitalised as part of the cost of the relevant construction projects or capital works in the case of project related employees, as the case may be, on a straight-line basis over the average period until the benefits become vested. To the extent that the benefits vest immediately, the expense is recognised immediately in a similar manner.

In calculating the Group's obligation in respect of a plan, to the extent that any cumulative unrecognised actuarial gain or loss exceeds ten percent of the greater of the present value of the defined benefit obligation and the fair value of plan assets, that portion is recognised in the profit and loss account over the expected average remaining working lives of the employees participating in the plan. Otherwise, the actuarial gain or loss is not recognised.

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 net actuarial losses and past service costs and the present value of any future refunds from the plan or reductions in future contributions to the plan.

(iv) Equity-settled share-based payments are measured at fair value at the date of grant. The fair value determined at the grant date is recognised as a staff cost, unless the relevant employee expenses qualify for recognition as an asset, on a straight-line basis over the vesting period and taking into account the probability that the options will vest, with a corresponding increase in the employee share-based capital reserve within equity. Fair value is measured by use of a Black-Scholes model, taking into account the terms and conditions upon which the options are granted. The expected life used in the model is adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions, and behavioural considerations.

During the vesting period, the number of share options that is expected to vest is reviewed. Any adjustment to the cumulative fair value recognised in prior years is charged / credited to the profit and loss account for the year of the review, unless the original employee expenses qualify for recognition as an asset, with a corresponding adjustment to the capital reserve. On vesting date, the amount recognised as an expense is adjusted to reflect the actual number of share options that vest (with a corresponding adjustment to the capital reserve). The equity amount is recognised in the capital reserve until either the option is exercised (when it is transferred to the share premium account) or the option expires (when it is released directly to retained profits).

For cash-settled share-based payments, a liability equal to the portion of the services received is recognised at the fair value of the shares determined at each balance sheet date.

(v) Termination benefits are recognised when, and only when, the Group demonstrably commits itself to terminate employment or to provide benefits as a result of voluntary redundancy by having a detailed formal plan which is without realistic possibility of withdrawal.

W Retirement Schemes

The Group operates both defined contribution and defined benefit retirement schemes.

Employer's contributions to defined contribution retirement schemes including MPF Schemes are recognised in the accounts in accordance with the policy set out in note 2V(ii).

Employer's contributions paid and payable in respect of employees of defined benefit retirement schemes as calculated annually by independent actuaries in accordance with the Retirement Scheme Rules and provisions of the Occupational Retirement Schemes Ordinance, are used to satisfy the pension expenses recognised in the accounts according to note 2V(iii). Any deficit or surplus thereof will be dealt with in the balance sheet as accrued or prepaid benefit expenses, as the case may be.

X Income Tax

(i) Income tax for the year comprises current tax and movements in deferred tax assets and liabilities. Income tax is recognised in the profit and loss account except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

(ii) 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.

(iii) Deferred tax assets and liabilities arise from deductible and taxable temporary 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. Future taxable profits that may support the recognition of deferred tax assets arising from deductible temporary differences include those that will arise from the reversal of existing taxable temporary differences, provided those differences relate to the same taxation authority and the same taxable entity, and are expected to reverse either in the same period as the expected reversal of the deductible temporary difference or in periods into which a tax loss arising from the deferred tax asset can be carried back or forward. The same criteria are adopted when determining whether existing taxable temporary differences support the recognition of deferred tax assets arising from unused tax losses and credits, that is, those differences are taken into account if they relate to the same taxation authority and the same taxable entity, and are expected to reverse in a period, or periods, in which the tax loss or credit can be utilised.

2 Principal Accounting Policies *(continued)*

X Income Tax *(continued)*

The limited exceptions to recognition of deferred tax assets and liabilities are those temporary differences arising from the initial recognition of assets or liabilities that affect neither accounting nor taxable profit (provided they are not part of a business combination) and investments in subsidiaries to the extent that, in the case of taxable differences, the Group controls the timing of the reversal and it is probable that the differences will not reverse in the foreseeable future, or in the case of deductible differences, unless it is probable that they will reverse in the future.

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.

(iv) Current tax balances and deferred tax balances, and movements therein, are presented separately from each other and are not offset. Current tax assets are offset against current tax liabilities, and deferred tax assets against deferred tax liabilities if, and only if, the Company or the Group has the legally enforceable right to set off current tax assets against current tax liabilities and the following additional conditions are met:

- in the case of current tax assets and liabilities, the Company or the Group intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously; or
- in the case of deferred tax assets and liabilities, if they relate to income taxes levied by the same taxation authority on either:
  - the same taxable entity; or
  - different taxable entities, which, in each future period in which significant amounts of deferred tax liabilities or assets are expected to be settled or recovered, intend to realise the current tax assets and settle the current tax liabilities on a net basis or realise and settle simultaneously.

Y Financial Guarantee Contracts

Financial guarantees are contracts that require the issuer to make specified payments to reimburse the holder of the guarantee for a loss it incurs because a specified debtor fails to make payment to the holder when due in accordance with the original or modified terms of a debt instrument.

When the Group issues a financial guarantee, where the effect is material, the fair value of the guarantee (being the transaction price, unless the fair value can otherwise be reliably estimated) after netting off any consideration received or receivable at inception is initially debited to the profit and loss account and recognised as deferred income within creditors, accrued charges and provisions.

The amount of the guarantee initially recognised as deferred income is amortised in the profit and loss account over the term of the guarantee as income from financial guarantees issued. In addition, provisions are recognised in accordance with note 2Z 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 creditors, accrued charges and provisions in respect of that guarantee, i.e. the amount initially recognised less accumulated amortisation.

Z Provisions and Contingent Liabilities

Provisions are recognised for liabilities of uncertain timing or amount when the Company or Group 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.

2 Principal Accounting Policies *(continued)*

AA Revenue Recognition

Provided it is probable that the economic benefits associated with the transactions will flow to the Group and the amount of revenue can be measured reliably, revenue is recognised in the profit and loss account as follows:

(i) Fare revenue is recognised when the journey is provided.

(ii) Advertising income and service fees from telecommunication services provided within the railway are recognised when the services are provided.

(iii) Contract revenue is recognised when the outcome of a consultancy or service contract can be estimated reliably. Contract revenue is recognised using the percentage of completion method, measured by reference to the percentage of contract costs incurred to date to estimated total contract costs for the contract. When the outcome of a consultancy contract cannot be estimated reliably, revenue is recognised only to the extent of contract costs incurred that it is probable will be recoverable.

(iv) Rental income from investment properties, station kiosks and other railway premises under operating leases is accounted for in accordance with the terms of the leases. Lease incentives granted are recognised in the profit and loss account as an integral part of the aggregate net lease payments receivable. Contingent rentals are recognised as income in the accounting period in which they are earned. Property management income is recognised when the services are provided.

BB Operating Lease Charges

(i) Rentals payable under operating leases are charged on a straight-line basis over the period of the lease to the profit and loss account, except for rentals payable in respect of railway construction, property development in progress and proposed capital projects which are capitalised as part of railway construction in progress, property development in progress and deferred expenditure respectively.

(ii) Prepaid land lease payments for land are stated at cost and are amortised on a straight-line basis over the period of the lease terms to the profit and loss account as land lease expenses.

CC Interest and Finance Charges

Interest expense directly attributable to the financing of capital projects prior to their completion or commissioning is capitalised. Exchange differences arising from foreign currency borrowings related to the acquisition of assets are capitalised to the extent that they are regarded as an adjustment to capitalised interest costs. Interest expense attributable to other purposes is charged to the profit and loss account.

Finance charges implicit in the lease payments on assets held under finance leases are charged to the profit and loss account over the period of the lease so as to produce an approximately constant periodic rate of charge on the remaining balance of the obligations for each accounting period.

DD Foreign Currency Translation

Foreign currency transactions during the year are translated into Hong Kong dollars and recorded at exchange rates ruling at the transaction dates. Foreign currency monetary assets and liabilities are translated into Hong Kong dollars at the exchange rates ruling at the balance sheet date. Exchange gains and losses are recognised in the profit and loss account.

The results of foreign enterprises are translated into Hong Kong dollars at the average exchange rates for the year; balance sheet items are translated into Hong Kong dollars at the rates of exchange ruling at the balance sheet date. The resulting exchange differences are dealt with as a movement in reserves.

EE 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 system, the Group has chosen business segment information as the primary reporting format. As substantially all the principal operating activities of the Group are carried out in Hong Kong, no geographical segment information is provided.

Segment revenue, expenses, results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis to that segment. Segment revenue, expenses, assets and liabilities are determined before intra-group balances and intra-group transactions are eliminated as part of the consolidation process, except to the extent that such intra-group balances and transactions are between group enterprises within a single segment.

Segment capital expenditure is the total cost incurred during the year to acquire segment assets that are expected to be used for more than one year.

Unallocated items mainly comprise derivative financial assets and liabilities, corporate assets, interest-bearing loans, borrowings, share of results of non-controlled subsidiaries, associates and jointly controlled entities, corporate and financing expenses and minority interests.

2 Principal Accounting Policies *(continued)*

FF Related Parties

For the purposes of these accounts, parties are considered to be related to the Group if the Group has the ability, directly or indirectly, to control the party or exercise significant influence over the party in making financial and operating decisions, or vice versa, or where the Group and the party are subject to common control or common significant influence. Related parties may be individuals (being members of key management personnel, significant shareholders and/or their close family members) or other entities including entities which are under the significant influence of related parties of the Group where those parties are individuals, and post-employment benefit plans which are for the benefit of employees of the Group or of any entity that is a related party of the Group.

GG Government Grants

Government grants are assistance by Government in the form of transfer of resources in return for the Group's compliance to the conditions attached thereto. Government grants which represent compensation for the cost of an asset will be deducted from the cost of the asset in arriving at its carrying value to the extent of the amounts received and receivable as at the date of the balance sheet. Any excess of the amount of grant received or receivable over the cost of the asset at the balance sheet date will be carried forward as advance receipts to set off against the future cost of the asset.

3 Rail Merger with Kowloon-Canton Railway Corporation

A On 2 December 2007 (the "Appointed Day"), the Company's operations merged with those of KCRC ("Rail Merger"). The structure and key terms of the Rail Merger were set out in a series of transaction agreements entered into between, inter alia, the Government of the Hong Kong Special Administrative Region, KCRC and the Company including the Service Concession Agreement, Property Package Agreements and Merger Framework Agreement. Key elements of the Rail Merger include the following:

- The expansion of the Company's existing franchise under the Mass Transit Railway Ordinance ("MTR Ordinance") to cover the construction, operation and regulation of railways in addition to the MTRC railway for an initial period of 50 years from the Appointed Day ("Franchise Period"), which may be extended pursuant to the provisions of the MTR Ordinance (note 51I);
- The Service Concession Agreement ("SCA") pursuant to which KCRC granted the Company the right to access, use and operate the KCRC system for an initial term of 50 years (the "Concession Period"), which will be extended if the Franchise Period (as it relates to the KCRC railway) is extended. The SCA also sets out the basis on which the KCRC system will be returned at the end of the Concession Period. In accordance with the terms of the SCA, the Company paid an upfront lump sum to KCRC on the Appointed Day and is obliged to pay an annual fixed payment to KCRC for the duration of the Concession Period. Additionally, commencing after three years from the Appointed Day, the Company is obliged to pay an annual variable fee to KCRC based on the revenue generated from the KCRC system above certain thresholds;
- Under the SCA, the Company is responsible for the expenditure incurred in relation to the maintenance, repair, replacement and upgrade of the KCRC system (with any new assets acquired being classified as "additional concession property"). To the extent that such expenditure exceeds an agreed threshold ("Capex Threshold"), the Company will be reimbursed for any above threshold expenditure at the end of the Concession Period with such reimbursement to be on the basis of depreciated book value;
- In the event that the Concession Period is extended, the fixed annual payment and the variable annual payment will continue to be payable by the Company. On such extension, the Capex Threshold may also be adjusted;
- With effect from the Appointed Day, staff of the Company and KCRC have been employed by the Company on their prevailing terms and conditions of employment. In connection with the Rail Merger, a Staff Voluntary Separation Scheme has been offered to eligible staff (note 10);
- Property Package Agreements whereby property assets comprising certain investment and own-used properties, property management rights and property development rights were acquired by the Company;
- Merger Framework Agreement setting out the framework for the Rail Merger including the implementation of the Fare Adjustment Mechanism whereby the extent to which fares may be adjusted is linked to certain public indices, the provision of a fare reduction starting from the Appointed Day and the guarantee of job security for front line staff employed at the time of the Rail Merger;
- Pursuant to the above and the vesting and novation of certain contracts, the Company assumed certain assets and liabilities of KCRC on the Appointed Day. The assumption of the liabilities of deposits refundable to third parties was subject to compensation by KCRC on the Appointed Day; and
- Other post-Appointed Day arrangements between the Company and KCRC such as the arrangements documented by the Kowloon Southern Link ("KSL") Project Management Agreement, the West Rail Agency Agreement and the Outsourcing Agreement.

3 Rail Merger with Kowloon-Canton Railway Corporation *(continued)*

B The principal financial terms of the Rail Merger and their financial impact on the accounts are described in the following paragraphs.

For the acquisition of the service concession, the Company has settled or is liable to settle the following payments to KCRC in respect of the service concession:

- Upfront payment of HK$4,250 million was paid on the Appointed Day, of which HK$326 million was in respect of stores and spares, with the balance of HK$3,924 million for the right to access, use and operate the KCRC system ("initial concession property"), which is capitalised as a service concession asset on the balance sheet and amortised on a straight-line basis over the Concession Period;
- Fixed annual payments of HK$750 million are payable by the Company to KCRC throughout the Concession Period. The present value of the total fixed annual payments discounted at the Company's estimated long-term incremental borrowing rate at inception of 6.75% amounting to HK$10,687 million was capitalised as a service concession asset on the balance sheet and amortised on a straight-line basis over the Concession Period with a corresponding liability for obligations under the service concession recognised on the balance sheet; and
- Variable annual payments are payable by the Company to KCRC commencing after the third year from the Appointed Day to the end of the Concession Period. The payments are calculated on a tiered basis by reference to the revenues generated from the operation of the service concession over certain thresholds.

The assumption of the liability of deposits refundable to third parties and other liabilities subject to cash compensation by KCRC on the Appointed Day amounted to HK$663 million. The assumption of other assets and liabilities not subject to compensation by KCRC on the Appointed Day amounted to a net liability amount of HK$226 million (note 20), formed part of the cost of acquiring the service concession and was capitalised accordingly.

On the Appointed Day, the Company paid a total consideration of HK$7,790 million for the transfer of the economic benefits of the property package from KCRC as follows:

- Acquisition of certain properties or property holding subsidiaries from KCRC at a consideration of HK$2,840 million;
- Acquisition of property development rights for eight development sites for a consideration of HK$4,910 million, which was recognised at cost as property development in progress on the balance sheet. Pursuant to the transaction agreements, when the development sites which have not been awarded as at the Appointed Day are subsequently awarded, the Company is obliged to pay KCRC an agreed amount of HK$875 million in respect of enabling works carried out by KCRC for such sites, which are to be settled by the receipt of mandatory payments from property developers when the sites are awarded;
- Acquisition of certain property management rights from KCRC in respect of existing and future managed properties at a consideration of HK$40 million. The amount was capitalised and subject to amortisation on a straight-line basis over the period of the management rights;
- Assumption of certain assets and liabilities with a net liability amount of HK$123 million relating to the property package with corresponding cash settlement from KCRC; and
- Acquisition of certain other subsidiaries of KCRC.

The Rail Merger also gave rise to the following:

- The Company obtained a new loan financing facility of HK$10 billion in 2007 as part of the financing for the above arrangements; and
- Deferred expenditure of HK$492 million incurred in connection with the acquisition of the respective assets was capitalised on the Appointed Day.

Income and expenditure and assets and liabilities in relation to the operation of the service concession are accounted for in the respective line items of the Group's and the Company's profit and loss accounts and balance sheets. Accordingly, the profit and loss accounts for the year ended 31 December 2008 reflect a full year of the Rail Merger whereas the comparatives reflect one month.

4 Fare Revenue

Fare revenue comprises:

in HK$ million	2008	2007
Domestic Service	**7,930**	6,213
Cross-boundary Service	**2,283**	201
Airport Express	**673**	655
Light Rail, Bus and Intercity	**581**	46
	11,467	7,115

The Domestic Service comprises the Kwun Tong, Tsuen Wan, Island, Tung Chung, Tseung Kwan O and Disneyland Resort lines, and additional services of the East Rail excluding Cross-boundary Service, West Rail and Ma On Shan lines after the Rail Merger. The Cross-boundary Service, Light Rail, Bus and Intercity are also KCRC transport services provided by the Company after the Rail Merger.

5 Non-fare Revenue

A Station Commercial and Rail Related Revenue

Station commercial and rail related revenue comprises:

in HK$ million	2008	2007
Advertising	**741**	593
Duty free shops and kiosk rental	**1,546**	499
Telecommunication income	**356**	239
Consultancy income	**158**	193
Miscellaneous business revenue	**648**	217
	3,449	1,741

B Rental, Management and Other Revenue

in HK$ million	2008	2007
Property rental income:		
– Telford Plaza	**571**	524
– Luk Yeung Galleria	**146**	118
– Paradise Mall	**115**	111
– Maritime Square	**330**	300
– International Finance Centre	**211**	147
– Ginza Mall – Beijing	**109**	90
– Elements	**395**	93
– Citylink Plaza	**112**	8
– Other properties	**357**	190
	2,346	1,581
Property management income	**210**	168
	2,556	1,749
Ngong Ping 360 business revenue	**156**	85
	2,712	1,834

5 Non-fare Revenue *(continued)*

B Rental, Management and Other Revenue *(continued)*

Included in rental income is HK$107 million (2007: HK$72 million) in respect of the provision of air conditioning services. Phase 1 and Phase 2A of Elements commenced operations in October 2007 and November 2008 respectively. Rental income from other properties includes income in respect of investment properties, other than Citylink Plaza, that were acquired from KCRC upon the Rail Merger of HK$163 million (2007: HK$13 million).

Ngong Ping 360 business revenue comprises revenue generated from the Tung Chung cable car operations and related businesses at the Ngong Ping Theme Village.

6 Operating Expenses

A Staff costs comprise:

in HK$ million	2008	2007
Amount charged to profit and loss account under:		
– staff costs and related expenses	**3,358**	1,802
– repairs and maintenance	**45**	59
– expenses relating to station commercial and rail related businesses	**454**	162
– expenses relating to property ownership, management and other businesses	**141**	55
– project study and business development expenses	**83**	136
– staff voluntary separation payments	**–**	175
– other line items	**47**	21
Amount capitalised in:		
– railway construction in progress	**46**	49
– property development in progress	**102**	83
– assets under construction and other projects	**482**	318
– service concession assets	**24**	23
Amount recoverable	**418**	233
Total staff costs	**5,200**	3,116

Amount recoverable relates to property management, entrustment works and other agreements.

The following expenditures are included in staff costs:

in HK$ million	2008	2007
Share-based payments	**22**	7
Contributions to defined contribution plans and Mandatory Provident Fund	**156**	38
Expense recognised in respect of defined benefit plans (note 49E)	**80**	98
	258	143

6 Operating Expenses *(continued)*

B Repairs and maintenance costs relate mainly to contracted maintenance and revenue works. Other routine repairs and maintenance works are performed by in-house operations, the costs of which are included under staff costs and stores and spares consumed.

C Project study and business development expenses comprise:

in HK$ million	**2008**	2007
Business development expenses	**182**	239
Miscellaneous project study expenses	**16**	29
	198	268

Business development expenses relate mainly to studies on business opportunities in China and Europe in line with the Group's business strategy.

D Included in general and administration expenses and other expenses are the following charges/(credits):

in HK$ million	**2008**	2007
Auditors' remuneration		
– audit services	**7**	5
– tax services	**1**	1
– other services	**1**	–
	9	6
Loss on disposal of fixed assets	**30**	36
Derivative financial instruments:		
– foreign exchange contracts – ineffective portion of cash flow hedges	**8**	(1)
– transfer from hedging reserve	**3**	2
Amortisation of land lease expenses (note 25)	**14**	13
Unrealised (gain)/loss on revaluation of investment in securities	**(2)**	4

In 2007, in addition to the amounts of auditors remuneration charged to general and administration expense, HK$5 million was incurred on audit and tax related services in respect of the Rail Merger.

E Operating lease expenses charged to the profit and loss account comprise:

in HK$ million	**2008**	2007
Shopping centre, office building, staff quarters and bus depot	**79**	59
Amount capitalised	**(13)**	(1)
	66	58

7 Remuneration of Members of the Board and the Executive Directorate

A Remuneration of Members of the Board and the Executive Directorate

(i) The emoluments of the Members of the Board and the Executive Directorate of the Company were as follows:

in HK$ million	Fees	Base pay, allowances and benefits in kind	Retirement scheme contribution	Variable remuneration related to performance	Total
2008					
Members of the Board					
– Raymond Ch'ien Kuo-fung	1.2	–	–	–	1.2
– Cheung Yau-kai	0.3	–	–	–	0.3
– David Gordon Eldon (retired on 29 May 2008)	0.1	–	–	–	0.1
– Christine Fang Meng-sang	0.3	–	–	–	0.3
– Edward Ho Sing-tin	0.4	–	–	–	0.4
– Lo Chung-hing (retired on 29 May 2008)	0.2	–	–	–	0.2
– Ng Leung-sing	0.3	–	–	–	0.3
– Abraham Shek Lai–him	0.3	–	–	–	0.3
– T. Brian Stevenson	0.4	–	–	–	0.4
– Ceajer Chan Ka–keung	0.3	–	–	–	0.3
– Eva Cheng	0.3	–	–	–	0.3
– Alan Wong Chi-kong	0.3	–	–	–	0.3
Members of the Executive Directorate					
– Chow Chung-kong	–	6.7	–*	8.6	15.3
– Russell John Black	–	4.3	0.2	2.7	7.2
– William Chan Fu-keung	–	4.4	0.2	2.6	7.2
– Thomas Ho Hang-kwong	–	4.4	0.2	2.6	7.2
– Lincoln Leong Kwok-kuen	–	4.8	0.7	2.7	8.2
– Francois Lung Ka-kui (left service on 31 December 2008)	–	3.6	0.5	1.7	5.8
– Andrew McCusker	–	4.4	0.2	2.3	6.9
– Leonard Bryan Turk	–	4.2	0.2	2.6	7.0
	4.4	36.8	2.2	25.8	69.2

* C K Chow participates in the Company's Mandatory Provident Fund Scheme. The total contributions paid by the Company in each of the years 2007 and 2008 were HK$12,000.

7 Remuneration of Members of the Board and the Executive Directorate *(continued)*

A Remuneration of Members of the Board and the Executive Directorate *(continued)*

in HK$ million	Fees	Base pay, allowances and benefits in kind	Retirement scheme contribution	Variable remuneration related to performance	Total
2007					
Members of the Board					
– Raymond Ch'ien Kuo-fung	1.0	–	–	–	1.0
– Cheung Yau-kai	0.2	–	–	–	0.2
– David Gordon Eldon	0.2	–	–	–	0.2
– Christine Fang Meng-sang	0.2	–	–	–	0.2
– Edward Ho Sing-tin	0.3	–	–	–	0.3
– Lo Chung-hing	0.2	–	–	–	0.2
– Ng Leung-sing (appointed on 18 December 2007)	–	–	–	–	–
– Abraham Shek Lai-him (appointed on 18 December 2007)	–	–	–	–	–
– T. Brian Stevenson	0.3	–	–	–	0.3
– Ceajer Chan Ka-keung (appointed on 10 July 2007)	0.1	–	–	–	0.1
– Eva Cheng (appointed on 1 July 2007)	0.1	–	–	–	0.1
– Sarah Liao Sau-tung (retired on 1 July 2007)	0.1	–	–	–	0.1
– Frederick Ma Si-hang (retired on 10 July 2007)	0.1	–	–	–	0.1
– Alan Wong Chi-kong	0.2	–	–	–	0.2
Members of the Executive Directorate					
– Chow Chung-kong	–	5.9	–*	5.1	11.0
– Russell John Black	–	3.8	0.1	1.7	5.6
– William Chan Fu-keung	–	3.7	0.1	1.7	5.5
– Thomas Ho Hang-kwong	–	3.8	0.1	1.6	5.5
– Lincoln Leong Kwok-kuen	–	3.8	0.5	1.7	6.0
– Francois Lung Ka-kui	–	3.5	0.5	0.8	4.8
– Andrew McCusker	–	3.7	0.1	1.4	5.2
– Leonard Bryan Turk	–	3.7	0.1	1.7	5.5
	3.0	31.9	1.5	15.7	52.1

The above emoluments do not include the fair value of share options, as estimated at the date of grant which is defined as the date of acceptance of the offer to grant the option. The fair values of the share options awarded to Members of the Executive Directorate are as follows:

(a) Options vested under the New Joiners Share Option Scheme (the "New Option Scheme") in 2007 and 2008

Francois K K Lung was granted options in respect of 1,066,000 shares under the New Option Scheme on 22 March 2007, of which 711,000 options were vested in 2008 (2007: nil), and the respective fair value of the share-based payments recognised for the year ended 31 December 2008 was HK$1.6 million (2007: HK$1.1 million).

7 Remuneration of Members of the Board and the Executive Directorate *(continued)*

A Remuneration of Members of the Board and the Executive Directorate *(continued)*

(b) Options vested under the 2007 Share Option Scheme (the "2007 Option Scheme") in 2007 and 2008

Share options were granted to Members of the Executive Directorate under the Company's 2007 Option Scheme, which were offered to them on 10 December 2007 and 8 December 2008. The entitlements of each of the Members are as follows:

- C K Chow was granted options in respect of 720,000 shares on 13 December 2007 and 470,000 shares on 9 December 2008, of which 240,000 options were vested in 2008 (2007: nil), and the respective fair value of the share-based payments recognised for the year ended 31 December 2008 was HK$1.2 million (2007: HK$0.071 million);
- Russell J Black, Lincoln K K Leong and Leonard B Turk were each granted options in respect of 170,000 shares on both 12 December 2007 and 9 December 2008, of which 57,000 options were vested in 2008 (2007: nil), and the respective fair value of the share-based payments recognised for the year ended 31 December 2008 was HK$0.3 million (2007: HK$0.017 million) for each of them;
- Thomas H K Ho was granted options in respect of 170,000 shares on both 12 December 2007 and 11 December 2008, of which 57,000 were vested in 2008 (2007: nil), and the respective fair value of the share-based payments recognised for the year ended 31 December 2008 was HK$0.3 million (2007: HK$0.017 million);
- Andrew McCusker was granted options in respect of 170,000 shares on both 12 December 2007 and 12 December 2008, of which 57,000 options were vested in 2008 (2007: nil), and the respective fair value of the share-based payments recognised for the year ended 31 December 2008 was HK$0.3 million (2007: HK$0.017 million);
- William F K Chan was granted options in respect of 170,000 shares on both 13 December 2007 and 9 December 2008, of which 57,000 options were vested in 2008 (2007: nil), and the respective fair value of the share-based payments recognised for the year ended 31 December 2008 was HK$0.3 million (2007: HK$0.017 million); and
- Francois K K Lung was granted options in respect of 130,000 shares on 12 December 2007, of which 87,000 options were vested in 2008 (2007: nil), and the respective fair value of the share-based payments recognised for the year ended 31 December 2008 was HK$0.4 million (2007: HK$0.013 million).

The details of directors' interest in the Company's shares are disclosed under the paragraph "Board Members' and Executive Directorate's Interests in Shares" of the Report of the Members of the Board and note 47.

(ii) C K Chow has a derivative interest in respect of 418,017 shares within the meaning of Part XV of the Securities and Futures Ordinance ("SFO"). The derivative interest represents C K Chow's entitlement to receive an equivalent value in cash of 418,017 shares on completion of his three-year contract ending on 30 November 2009.

On 12 April 2007, Lincoln K K Leong was granted a derivative interest in respect of 160,000 shares in the Company within the meaning of Part XV of the SFO. The derivative interest represents Lincoln K K Leong's entitlement to receive an equivalent value in cash of 160,000 shares on 9 April 2010.

The arrangements were offered to C K Chow and Lincoln K K Leong in order to provide a competitive level of compensation which is also closely tied to the performance of the Company.

(iii) The aggregate emoluments of Members of the Board and the Executive Directorate for the year pursuant to section 161 of the Hong Kong Companies Ordinance was HK$74.2 million (2007: HK$53.4 million).

(iv) Non-executive directors of the Company are not appointed for a specific term but are subject (save for those appointed pursuant to Section 8 of the Mass Transit Railway Ordinance (Chapter 556 of the Laws of Hong Kong)) to retirement by rotation and re-election at the Company's annual general meetings in accordance with Articles 87 and 88 of the Company's Articles of Association. Dr. Raymond Ch'ien Kuo-fung, a Member of the Board, was appointed as the non-executive Chairman of the Company with effect from 21 July 2003 for a term of three years. In July 2006, he was re-appointed as the non-executive Chairman of the Company until 31 July 2007. In July 2007, Dr. Ch'ien was re-appointed as the non-executive Chairman of the Company with effect from 1 August 2007 for a term up to 31 December 2007 or the day to be appointed by the Secretary for Transport and Housing by notice published in the Gazette under the Rail Merger Ordinance, whichever was the earlier. On 8 August 2007, he was appointed as the non-executive Chairman of the Company after the Rail Merger for a term of two years commencing from 2 December 2007. All of the five individuals with the highest emoluments are Members of the Executive Directorate whose emoluments are disclosed above.

7 Remuneration of Members of the Board and the Executive Directorate *(continued)*

B Share Options

Options exercised and outstanding in respect of each Member of the Executive Directorate as at 31 December 2008 are set out under the paragraph "Board Members' and Executive Directorate's Interests in Shares" of the Report of the Members of the Board. Details of the options granted to Members of the Executive Directorate are as follows:

(i) Pre-Global Offering Share Option Scheme

Under the Company's Pre-Global Offering Share Option Scheme (the "Pre-IPO Option Scheme") described in note 47A(i), each Member of the Executive Directorate, except C K Chow, Lincoln K K Leong, Francois K K Lung and Andrew McCusker, was granted options on 20 September 2000 to acquire 1,066,000 shares. C K Chow, Lincoln K K Leong and Francois K K Lung joined the Company on 1 December 2003, 1 February 2002 and 26 September 2005 respectively, and are not beneficiaries of the Pre-IPO Option Scheme. Andrew McCusker was granted 266,500 options on 20 September 2000 under the Pre-IPO Option Scheme and no additional share options were granted upon his appointment as a Member of the Executive Directorate on 1 October 2005.

Under the vesting terms of the Pre-IPO Option Scheme, each eligible Member of the Executive Directorate must continue to beneficially own (i) at all times after 26 October 2001, at least 23,000 shares; and (ii) at all times after 26 October 2002, at least 46,000 shares, in each case, up to and including the date on which he has exercised his option in full or the date on which his option lapses (whichever is earlier).

(ii) New Joiners Share Option Scheme

Under the New Joiners Share Option Scheme (the "New Option Scheme") as described in note 47A(ii), Lincoln K K Leong and Francois K K Lung, Members of the Executive Directorate, were granted options to acquire 1,066,000 shares on 1 August 2003 and 27 September 2005 respectively.

Under the vesting terms of the New Option Scheme, Lincoln K K Leong must continue to beneficially own (i) at all times on and after 4 August 2004, at least 23,000 shares; and (ii) at all times on and after 4 August 2005, at least 46,000 shares, up to and including the date on which he has exercised his option in full or the date on which his option lapses (whichever is earlier).

Under the vesting terms of the New Option Scheme, Francois K K Lung was required to beneficially own at all times on and after 17 October 2006, at least 23,000 shares up to and including the date on which he has exercised his option in full or the date on which his option lapses (whichever is earlier). Francois K K Lung's options lapsed on 17 October 2006 in accordance with the terms of the New Option Scheme.

On 22 March 2007, Francois K K Lung was granted options to acquire 1,066,000 shares under the New Option Scheme. Under the vesting terms of the New Option Scheme, Francois K K Lung was required to beneficially own at all times on and after 9 April 2008, at least 23,000 shares up to and including the date on which he has exercised his options in full or the date on which his options lapse (whichever is earlier). In connection with the termination of his employment with the Company on 31 December 2008 and in accordance with the terms of the New Option Scheme, 711,000 options granted to Francois K K Lung under the New Option Scheme were vested and 355,000 options lapsed as at 31 December 2008.

(iii) 2007 Share Option Scheme

Under the 2007 Share Option Scheme (the "2007 Option Scheme") as described in note 47A(iii), all Members of the Executive Directorate were granted options to acquire shares in December 2007 and December 2008. C K Chow was granted options to acquire 720,000 shares in 2007 and 470,000 shares in 2008; Russell J Black, William F K Chan, Thomas H K Ho, Lincoln K K Leong, Andrew McCusker and Leonard B Turk were each granted options to acquire 170,000 shares in both 2007 and 2008; and Francois K K Lung was granted options to acquire 130,000 shares in 2007.

Under the vesting terms of the options granted in December 2007 and December 2008, options granted will be evenly vested in respect of their underlying shares over a period of three years from 10 December 2007 and 8 December 2008 respectively. However, in connection with the termination of his employment with the Company on 31 December 2008 and in accordance with the terms of the 2007 Option Scheme, 87,000 options granted to Francois K K Lung under the 2007 Option Scheme were vested and 43,000 options lapsed as at 31 December 2008.

8 Profit on Property Developments

Profit on property developments comprises:

in HK$ million	**2008**	2007
Transfer from deferred income on		
– up-front payments (note 23B(i))	**139**	861
– sharing in kind (note 23B(ii))	**61**	363
Share of surplus from development	**4,505**	7,077
Income recognised from sharing in kind	**–**	21
Other overhead costs	**(35)**	(18)
	4,670	8,304

9 Depreciation and Amortisation

Depreciation and amortisation comprise:

in HK$ million	2008	2007
Depreciation charge on:		
Railway operations		
– on fixed assets held under finance leases	**19**	19
– on other railway fixed assets	**2,388**	2,501
Assets relating to station commercial and rail related businesses	**76**	73
Assets relating to property ownership, management and other businesses	**71**	68
Unallocated corporate assets	**61**	53
	2,615	2,714
Amortisation charge on:		
Service concession assets	**310**	25
Property management rights	**5**	–
	315	25
	2,930	2,739

10 Merger Related Expenses

Merger related expenses comprise:

in HK$ million	2008	2007
Staff Voluntary Separation Scheme payments (i)	**–**	175
Merger expenses (ii)	**53**	18
	53	193

(i) In 2007, a Staff Voluntary Separation Scheme ("VSS") was offered to eligible staff affected by the Rail Merger with compensation determined according to individual staff's year of services. 384 staff terminated their employment under the VSS and the resulting compensation was charged to the profit and loss account of 2007.

(ii) After the Rail Merger, other merger related expenses not eligible for capitalisation are charged to the profit and loss account.

11 Interest and Finance Charges

in HK$ million	2008		2007	
Interest expenses in respect of:				
Bank loans, overdrafts and capital market instruments wholly repayable within 5 years	**1,046**		1,004	
Bank loans and capital market instruments not wholly repayable within 5 years	**396**		498	
Obligations under finance leases	**–**		4	
Obligations under service concession	**721**		60	
Other obligations (note 19E)	**100**		–	
Finance charges	**31**		19	
Exchange gain	**(8)**		(5)	
		2,286		1,580
Derivative financial instruments:				
Fair value hedges	**34**		62	
Cash flow hedges:				
– transfer to/(from) hedging reserve	**39**		(2)	
– ineffective portion	**(1)**		–	
Derivatives not qualified for hedge accounting	**(2)**		(3)	
		70		57
Interest expenses capitalised		**(149)**		(93)
		2,207		1,544
Interest income in respect of:				
Deposits with banks and other financial institutions	**(8)**		(43)	
Investments in debt securities	**(7)**		–	
Loan to non-controlled subsidiary and associate	**(5)**		(7)	
Staff housing loans	**(1)**		(1)	
		(21)		(51)
Accreted interest on loan to a property developer		**(188)**		(177)
		1,998		1,316

Interest expenses capitalised were calculated at the average cost of borrowings to the Group on a monthly basis. The average interest rates for each month varied from 4.5% to 5.1% per annum during the year (2007: 5.3% to 5.8% per annum).

During the year, fair value gain on fair value hedges comprising interest rate and cross currency swaps was HK$368 million (gain in 2007: HK$414 million) whereas the fair value loss on the underlying financial assets and liabilities being hedged was HK$402 million (loss in 2007: HK$476 million), resulting in a net loss of HK$34 million (loss in 2007: HK$62 million).

12 Share of Profits of Non-controlled Subsidiaries and Associates

Share of profits of non-controlled subsidiaries and associates comprises:

in HK$ million	2008	2007
Share of profit before taxation of non-controlled subsidiaries (note 26)	**152**	125
Share of profit before taxation of associates (note 28)	**32**	3
	184	128
Share of income tax of non-controlled subsidiaries (note 26)	**(16)**	(28)
Share of income tax of associates (note 28)	**(9)**	(1)
	159	99

13 Income Tax

A Income tax in the consolidated profit and loss account represents:

in HK$ million	2008	2007
Current tax		
– Provision for Hong Kong Profits Tax at 16.5% (2007: 17.5%) for the year	**1,021**	1
– Overseas tax for the year	**3**	2
	1,024	3
Deferred tax		
– Origination and reversal of temporary differences on:		
– change in fair value of investment properties	**(24)**	1,402
– utilisation of tax losses	**532**	1,608
– others	**(81)**	70
	427	3,080
– Effect on deferred tax balances resulting from a change in tax rate	**(704)**	–
	(277)	3,080
	747	3,083

In February 2008, the Hong Kong Government announced a decrease in the Hong Kong Profits Tax rate from 17.5% to 16.5% applicable to the Group's operations in Hong Kong as from the year ended 31 December 2008. This decrease has been taken into account in the preparation of the Group's and the Company's 2008 accounts. Accordingly, the provision for Hong Kong Profits Tax for 2008 is calculated at 16.5% (2007: 17.5%) of the estimated assessable profits for the year after deducting accumulated tax losses brought forward and the deferred tax has been re-estimated accordingly.

Current tax for overseas subsidiaries is charged at the appropriate current rates of taxation ruling in the relevant countries.

For the year ended 31 December 2007, no provision for current Hong Kong Profits Tax was made in the consolidated profit and loss account in respect of the Company and most of its subsidiaries, as the Company and these subsidiaries either had accumulated tax losses brought forward which were available for setting off against the assessable profits for the year or had sustained tax losses.

Provision for deferred tax on temporary differences arising in Hong Kong is calculated at Hong Kong Profits Tax rate at 16.5% (2007: 17.5%).

13 Income Tax *(continued)*

B Reconciliation between tax expense and accounting profit at applicable tax rates:

	2008		2007	
	HK$ million	%	HK$ million	%
Profit before taxation	**9,027**		18,265	
Notional tax on profit before taxation, calculated at the rates applicable to profits in the tax jurisdictions concerned	**1,472**	**16.3**	3,186	17.4
Tax effect of non-deductible expenses	**95**	**1.1**	53	0.3
Tax effect of non-taxable revenue	**(121)**	**(1.3)**	(162)	(0.9)
Tax effect of unused tax losses not recognised	**5**	**0.1**	6	0.0
Effect on deferred tax balances resulting from a change in tax rate	**(704)**	**(7.8)**	–	0.0
Actual tax expenses	**747**	**8.4**	3,083	16.8

14 Profit Attributable to Equity Shareholders

The consolidated profit attributable to equity shareholders includes a profit of HK$8,118 million (2007: HK$14,883 million) which has been dealt with in the accounts of the Company.

15 Dividends

During the year, dividends paid and proposed to equity shareholders of the Company comprised:

in HK$ million	2008	2007
Dividends paid and payable attributable to the year		
– Interim dividend of 14 cents (2007: 14 cents) per share	**790**	782
– Final dividend proposed after the balance sheet date of 34 cents (2007: 31 cents) per share	**1,925**	1,740
	2,715	2,522
Dividends payable attributable to the previous year		
– Final dividend of 31 cents (2006: 28 cents) per share approved and paid during the year	**1,740**	1,554

The final dividend proposed after the balance sheet date has not been recognised as a liability at the balance sheet date.

During the year, scrip dividend elections were offered to all shareholders except shareholders with registered addresses in the United States of America or any of its territories or possessions. The Company's majority shareholder, The Financial Secretary Incorporated ("FSI"), had elected to receive part of its entitlement to dividends in the form of scrip to the extent necessary to ensure that the amount payable in cash would not exceed 50% of the total dividend payable. Details of dividends paid to the FSI are disclosed in note 51V. On 8 November 2006, the FSI agreed to extend the scrip dividend arrangement for another three financial years until the financial year ending 31 December 2009.

16 Earnings Per Share

A Basic earnings per share

The calculation of basic earnings per share is based on the profit for the year attributable to equity shareholders of HK$8,284 million (2007: HK$15,180 million) and the weighted average number of ordinary shares of 5,632,895,671 in issue during the year (2007: 5,573,736,592), calculated as follows:

	2008	2007
Issued ordinary shares at 1 January	**5,611,057,035**	5,548,613,951
Effect of scrip dividends issued	**20,529,968**	24,065,067
Effect of share options exercised	**1,308,668**	1,057,574
Weighted average number of ordinary shares at 31 December	**5,632,895,671**	5,573,736,592

16 Earnings Per Share *(continued)*

B Diluted earnings per share

The calculation of diluted earnings per share is based on the profit for the year attributable to equity shareholders of HK$8,284 million (2007: HK$15,180 million) and the weighted average number of ordinary shares of 5,636,941,336 in issue during the year (2007: 5,578,838,104) after adjusting for the number of dilutive potential ordinary shares under the employee share option schemes, calculated as follows:

	2008	2007
Weighted average number of ordinary shares at 31 December	**5,632,895,671**	5,573,736,592
Number of ordinary shares deemed to be issued for no consideration	**4,045,665**	5,101,512
Weighted average number of ordinary shares (diluted) at 31 December	**5,636,941,336**	5,578,838,104

C Both basic and diluted earnings per share would have been HK$1.45 (2007: HK$1.54) if the calculation is based on profit from underlying businesses attributable to equity shareholders, i.e. excluding change in fair value of investment properties net of related deferred tax, adjusted as follows:

in HK$ million	**2008**	2007
Profit attributable to equity shareholders	**8,284**	15,180
Change in fair value of investment properties	**146**	(8,011)
Deferred tax on change in fair value of investment properties		
– Effect of the change during the year (note 13A)	**(24)**	1,402
– Effect on deferred tax balances resulting from a change in tax rate	**(221)**	–
Profit from underlying businesses attributable to equity shareholders	**8,185**	8,571

17 Segmental Information

Segmental information is presented in accordance with the Group's business segments, which comprise the following:

Railway operations: The operation of an urban mass transit railway system within Hong Kong and an Airport Express serving both the Hong Kong International Airport and the AsiaWorld-Expo at Chek Lap Kok and following the Rail Merger, with effect from 2 December 2007, the KCR System consisting of KCR Lines (comprising the East Rail excluding Cross-boundary Service, West Rail and Ma On Shan lines), Cross-boundary Service, Light Rail, Bus and Intercity passenger services.

Station commercial and rail related businesses: Commercial activities including letting of advertising and retail space, bandwidth services on the railway telecommunication system, railway consultancy services, freight and rail related subsidiaries' businesses.

Property ownership, management and other businesses: Property rental, property management and operations relating to Ngong Ping 360.

Property developments: Property development at locations relating to the railway system.

17 Segmental Information *(continued)*

The results of major business activities are summarised below:

in HK$ million	Railway operations	Station commercial and rail related businesses	Property ownership, management and other businesses	**Total railway operations and related activities**	Property developments	Total
2008						
Revenue	11,467	3,449	2,712	17,628	–	17,628
Operating expenses before depreciation and amortisation	(5,969)	(822)	(785)	(7,576)	–	(7,576)
	5,498	2,627	1,927	10,052	–	10,052
Profit on property developments	–	–	–	–	4,670	4,670
Operating profit before depreciation and amortisation	5,498	2,627	1,927	10,052	4,670	14,722
Depreciation and amortisation	(2,722)	(76)	(71)	(2,869)	–	(2,869)
	2,776	2,551	1,856	7,183	4,670	11,853
Unallocated corporate expenses						(788)
Merger related expenses						(53)
Operating profit before interest and finance charges						11,012
Interest and finance charges						(1,998)
Change in fair value of investment properties			(146)			(146)
Share of profits of non-controlled subsidiaries and associates						159
Income tax						(747)
Profit for the year ended 31 December 2008						8,280
Assets						
Operational assets *	74,025	1,281	39,589	114,895	5,899	120,794
Assets under construction	1,038	10	–	1,048	352	1,400
Service concession assets	15,463	–	–	15,463	–	15,463
Property management rights	–	–	35	35	–	35
Railway construction in progress	658	–	–	658	–	658
Property development in progress	–	–	–	–	7,895	7,895
Deferred expenditure	1,975	–	–	1,975	13	1,988
Prepaid land lease payments	567	–	–	567	–	567
Deferred tax assets	–	3	8	11	–	11
Investments in securities	471	–	–	471	–	471
Properties held for sale	–	–	–	–	2,228	2,228
Loan to a property developer	–	–	–	–	3,720	3,720
	94,197	1,294	39,632	135,123	20,107	155,230
Interests in non-controlled subsidiaries						381
Interests in associates						743
Unallocated assets						2,984
Total assets						159,338

17 Segmental Information *(continued)*

in HK$ million	Railway operations	Station commercial and rail related businesses	Property ownership, management and other businesses	**Total railway operations and related activities**	Property developments	**Total**
2008						
Liabilities						
Segment liabilities	**2,832**	**964**	**1,119**	**4,915**	**1,470**	**6,385**
Obligations under service concession	**10,656**	**–**	**–**	**10,656**	**–**	**10,656**
Deferred income	**–**	**–**	**–**	**–**	**156**	**156**
	13,488	**964**	**1,119**	**15,571**	**1,626**	**17,197**
Unallocated liabilities						**44,319**
Total liabilities						**61,516**
Other Information						
Capital expenditure on:						
Operational assets	**59**	**2**	**14**	**75**	**–**	**75**
Assets under construction	**1,153**	**137**	**–**	**1,290**	**61**	**1,351**
Investment properties	**–**	**–**	**108**	**108**	**–**	**108**
Service concession assets	**523**	**–**	**–**	**523**	**–**	**523**
Railway construction in progress	**234**	**–**	**–**	**234**	**–**	**234**
Property development in progress	**–**	**–**	**–**	**–**	**2,331**	**2,331**
Non-cash expenses other than depreciation and amortisation	**19**	**11**	**–**	**30**	**–**	**30**

* Operational assets include property, plant and equipment and other assets employed in the operations of individual business segments.

17 Segmental Information *(continued)*

in HK$ million	Railway operations	Station commercial and rail related businesses	Property ownership, management and other businesses	**Total railway operations and related activities**	Property developments	**Total**
2007						
Revenue	7,115	1,741	1,834	10,690	–	10,690
Operating expenses before depreciation and amortisation	(3,215)	(410)	(540)	(4,165)	–	(4,165)
	3,900	1,331	1,294	6,525	–	6,525
Profit on property developments	–	–	–	–	8,304	8,304
Operating profit before depreciation and amortisation	3,900	1,331	1,294	6,525	8,304	14,829
Depreciation and amortisation	(2,545)	(73)	(68)	(2,686)	–	(2,686)
	1,355	1,258	1,226	3,839	8,304	12,143
Unallocated corporate expenses						(666)
Merger related expenses						(193)
Operating profit before interest and finance charges						11,284
Interest and finance charges						(1,316)
Change in fair value of investment properties			8,011			8,011
Net gain on acquisition of subsidiaries						187
Share of profits of non-controlled subsidiaries and associates						99
Income tax						(3,083)
Profit for the year ended 31 December 2007						15,182
Assets						
Operational assets *	75,304	1,528	39,628	116,460	3,774	120,234
Assets under construction	640	8	–	648	389	1,037
Service concession assets	15,250	–	–	15,250	–	15,250
Property management rights	–	–	40	40	–	40
Railway construction in progress	424	–	–	424	–	424
Property development in progress	–	–	–	–	9,066	9,066
Deferred expenditure	825	–	–	825	–	825
Prepaid land lease payments	581	–	–	581	–	581
Deferred tax assets	–	4	–	4	–	4
Investments in securities	333	–	–	333	–	333
Properties held for sale	–	–	–	–	756	756
Loan to a property developer	–	–	–	–	3,532	3,532
	93,357	1,540	39,668	134,565	17,517	152,082
Interests in non-controlled subsidiaries						268
Interests in associates						205
Unallocated assets						3,113
Total assets						155,668
Liabilities						
Segment liabilities	2,764	1,034	1,128	4,926	1,614	6,540
Obligations under service concession	10,685	–	–	10,685	–	10,685
Deferred income	115	–	–	115	400	515
	13,564	1,034	1,128	15,726	2,014	17,740
Unallocated liabilities						46,891
Total liabilities						64,631

17 Segmental Information *(continued)*

in HK$ million	Railway operations	Station commercial and rail related businesses	Property ownership, management and other businesses	**Total railway operations and related activities**	Property developments	**Total**
2007						
Other Information						
Capital expenditure on:						
Operational assets	31	2	11	44	–	44
Assets under construction	625	123	19	767	620	1,387
Investment properties	–	–	3,204	3,204	–	3,204
Service concession assets	14,886	–	–	14,886	–	14,886
Property management rights	–	–	40	40	–	40
Railway construction in progress	263	–	–	263	–	263
Property development in progress	–	–	–	–	6,239	6,239
Non-cash expenses other than depreciation and amortisation	36	3	1	40	–	40

As substantially all of the principal operating activities of the Group were carried out in Hong Kong throughout the reporting periods, no geographical analysis is provided.

18 Investment Properties

Movements and analysis of the Group's and the Company's investment properties, all of which are held in Hong Kong and carried at fair value, are as follows:

	The Group		The Company	
in HK$ million	**2008**	2007	**2008**	2007
Valuation				
At 1 January	**37,723**	22,539	**36,562**	22,539
Additions through Rail Merger	**–**	2,840	**–**	1,874
Other additions	**108**	364	**104**	169
Change in fair value	**(146)**	8,011	**(100)**	8,011
Transfer from assets under construction (note 19)	**98**	4,027	**98**	4,027
Transfer to self-occupied land and buildings (note 19)	**(46)**	(58)	**(46)**	(58)
At 31 December	**37,737**	37,723	**36,618**	36,562
Long leases	**1,575**	1,609	**1,575**	1,609
Medium-term leases	**36,162**	36,114	**35,043**	34,953
	37,737	37,723	**36,618**	36,562

Phase 1 and Phase 2A of Elements were completed in October 2007 and November 2008 respectively. Upon completion, the respective values of the shell and costs of fitting-out works, which were carried as assets under construction in other property, plant and equipment, were transferred to investment properties.

All investment properties of the Group were revalued at open market value at 31 December 2008 by an independent firm of surveyors, Jones Lang LaSalle Limited, who have among their staff Members of the Hong Kong Institute of Surveyors. The valuations are based on a "term and reversion basis", which capitalises the existing and reversionary net rental income having regard to market valuation checks on comparable sale and yields. The net decrease in fair value of HK$146 million (2007: increase of HK$8,011 million) arising from the revaluation has been charged to the profit and loss account.

The Group's future minimum lease receipts in respect of investment properties under non-cancellable operating leases are disclosed together with those in respect of other properties under note 19D.

19 Other Property, Plant and Equipment

The Group

in HK$ million	Self–occupied land and buildings	Civil works	Plant and equipment	Assets under construction	Total
Cost or Valuation					
At 1 January 2008	**2,240**	**46,471**	**58,820**	**1,037**	**108,568**
Additions	**–**	**–**	**75**	**1,351**	**1,426**
Capitalisation adjustments *	**–**	**(96)**	**5**	**–**	**(91)**
Disposals/Write-offs	**(36)**	**(15)**	**(316)**	**(2)**	**(369)**
Deficit on revaluation (note 46)	**(285)**	**–**	**–**	**–**	**(285)**
Reclassification	**–**	**(4)**	**4**	**–**	**–**
Transfer from / (to) investment properties (note 18)	**46**	**–**	**–**	**(98)**	**(52)**
Other assets commissioned	**–**	**3**	**885**	**(888)**	**–**
At 31 December 2008	**1,965**	**46,359**	**59,473**	**1,400**	**109,197**
At Cost	**–**	**46,359**	**59,473**	**1,400**	**107,232**
At 31 December 2008 Valuation	**1,965**	**–**	**–**	**–**	**1,965**
Aggregate depreciation					
At 1 January 2008	**–**	**4,236**	**24,888**	**–**	**29,124**
Charge for the year	**58**	**389**	**2,174**	**–**	**2,621**
Capitalisation adjustments *	**–**	**(6)**	**–**	**–**	**(6)**
Written back on disposal	**–**	**(7)**	**(281)**	**–**	**(288)**
Written back on revaluation (note 46)	**(58)**	**–**	**–**	**–**	**(58)**
At 31 December 2008	**–**	**4,612**	**26,781**	**–**	**31,393**
Net book value at 31 December 2008	**1,965**	**41,747**	**32,692**	**1,400**	**77,804**
Cost or Valuation					
At 1 January 2007	1,989	46,544	57,767	4,905	111,205
Additions	–	–	44	1,387	1,431
Capitalisation adjustments *	–	(42)	(49)	–	(91)
Disposals / Write-offs	–	(4)	(371)	–	(375)
Surplus on revaluation (note 46)	193	–	–	–	193
Reclassification	–	(61)	61	–	–
Transfer from deferred expenditure (note 24)	–	–	59	44	103
Transfer from / (to) investment properties (note 18)	58	–	–	(4,027)	(3,969)
SkyPlaza Platform Project commissioned (note 22)	–	–	71	–	71
Other assets commissioned	–	34	1,238	(1,272)	–
At 31 December 2007	2,240	46,471	58,820	1,037	108,568
At Cost	–	46,471	58,820	1,037	106,328
At 31 December 2007 Valuation	2,240	–	–	–	2,240
Aggregate depreciation					
At 1 January 2007	–	3,864	22,937	–	26,801
Charge for the year	52	387	2,279	–	2,718
Capitalisation adjustments *	–	(1)	(3)	–	(4)
Written back on disposal	–	(2)	(337)	–	(339)
Written back on revaluation (note 46)	(52)	–	–	–	(52)
Reclassification	–	(12)	12	–	–
At 31 December 2007	–	4,236	24,888	–	29,124
Net book value at 31 December 2007	2,240	42,235	33,932	1,037	79,444

* Capitalisation adjustments relate to certain railway assets capitalised at time of commissioning based on contractors' claimed values. Such assets' final values have been adjusted following finalisation of contract claims with contractors at final contract values during the year.

Depreciation charge for the year was HK$2,615 million (2007: HK$2,714 million), comprising depreciation for the year of HK$2,621 million (2007: HK$2,718 million) less capitalisation adjustments of HK$6 million (2007: HK$4 million).

19 Other Property, Plant and Equipment *(continued)*

The Company

in HK$ million	Self–occupied land and buildings	Civil works	Plant and equipment	Assets under construction	Total
Cost or Valuation					
At 1 January 2008	**2,240**	**46,471**	**58,143**	**1,029**	**107,883**
Additions	**–**	**–**	**66**	**1,324**	**1,390**
Capitalisation adjustments *	**–**	**(96)**	**5**	**–**	**(91)**
Disposals / Write-offs	**(36)**	**(15)**	**(315)**	**(2)**	**(368)**
Deficit on revaluation (note 46)	**(285)**	**–**	**–**	**–**	**(285)**
Reclassification	**–**	**(4)**	**4**	**–**	**–**
Transfer from / (to) investment properties (note 18)	**46**	**–**	**–**	**(98)**	**(52)**
Other assets commissioned	**–**	**3**	**860**	**(863)**	**–**
At 31 December 2008	**1,965**	**46,359**	**58,763**	**1,390**	**108,477**
At Cost	**–**	**46,359**	**58,763**	**1,390**	**106,512**
At 31 December 2008 Valuation	**1,965**	**–**	**–**	**–**	**1,965**
Aggregate depreciation					
At 1 January 2008	**–**	**4,236**	**24,377**	**–**	**28,613**
Charge for the year	**58**	**389**	**2,155**	**–**	**2,602**
Capitalisation adjustments *	**–**	**(6)**	**–**	**–**	**(6)**
Written back on disposal	**–**	**(7)**	**(280)**	**–**	**(287)**
Written back on revaluation (note 46)	**(58)**	**–**	**–**	**–**	**(58)**
At 31 December 2008	**–**	**4,612**	**26,252**	**–**	**30,864**
Net book value at 31 December 2008	**1,965**	**41,747**	**32,511**	**1,390**	**77,613**
Cost or Valuation					
At 1 January 2007	1,989	46,544	57,195	4,832	110,560
Additions	–	–	39	1,346	1,385
Capitalisation adjustments *	–	(42)	(43)	–	(85)
Disposals / Write-offs	–	(4)	(371)	–	(375)
Surplus on revaluation (note 46)	193	–	–	–	193
Reclassification	–	(61)	61	–	–
Transfer from deferred expenditure (note 24)	–	–	59	44	103
Transfer from / (to) investment properties (note 18)	58	–	–	(4,027)	(3,969)
SkyPlaza Platform Project commissioned (note 22)	–	–	71	–	71
Other assets commissioned	–	34	1,132	(1,166)	–
At 31 December 2007	2,240	46,471	58,143	1,029	107,883
At Cost	–	46,471	58,143	1,029	105,643
At 31 December 2007 Valuation	2,240	–	–	–	2,240
Aggregate depreciation					
At 1 January 2007	–	3,864	22,440	–	26,304
Charge for the year	52	387	2,262	–	2,701
Capitalisation adjustments *	–	(1)	(3)	–	(4)
Written back on disposal	–	(2)	(334)	–	(336)
Written back on revaluation (note 46)	(52)	–	–	–	(52)
Reclassification	–	(12)	12	–	–
At 31 December 2007	–	4,236	24,377	–	28,613
Net book value at 31 December 2007	2,240	42,235	33,766	1,029	79,270

* Capitalisation adjustments relate to certain railway assets capitalised at time of commissioning based on contractors' claimed values. Such assets' final values have been adjusted following finalisation of contract claims with contractors at final contract values during the year.

Depreciation charge for the year was HK$2,596 million (2007: HK$2,697 million), comprising depreciation for the year of HK$2,602 million (2007: HK$2,701 million) less capitalisation adjustments of HK$6 million (2007: HK$4 million).

19 Other Property, Plant and Equipment *(continued)*

All of the Group's self-occupied land and buildings are held in Hong Kong under medium-term leases and carried at fair value.

A All self-occupied land and buildings were revalued at open market value on an existing use basis at 31 December 2008 by an independent firm of surveyors, Jones Lang LaSalle Limited, who have among their staff Members of the Hong Kong Institute of Surveyors. The valuation resulted in a revaluation loss of HK$227 million (2007: surplus of HK$245 million), which net of deferred tax credit of HK$38 million (2007: provision of HK$43 million) (note 44B), has been transferred to the fixed asset revaluation reserve account (note 46).

The carrying amount of the self-occupied land and buildings at 31 December 2008 would have been HK$949 million (2007: HK$928 million) had the land and buildings been stated at cost less accumulated depreciation.

B Assets under construction include capital works on operating railways and further renovation on a partially renovated shell of the retail shopping centre at Union Square, Kowloon Station.

C In 1986, the Company entered into a Management Agreement (the "1986 Agreement") with New Hong Kong Tunnel Company Limited ("NHKTC") to operate the Eastern Harbour Crossing ("EHC") until February 2008. Included in the assets held under the 1986 Agreement are railway and ancillary works relating to the rail tunnel.

At the expiry of the 1986 Agreement, title to the assets would, pursuant to the Eastern Harbour Crossing Ordinance, be vested in the Government which in turn entered into a Memorandum of Understanding dated 17 October 1986 with the Company to the effect that the assets would be vested in the Company on terms to be agreed between the Company and the Government. On 30 June 2000, the Company entered into a further agreement with the Government pursuant to which the relevant assets would be vested by the Government into the Company in 2008 for a nominal consideration and the Company agreed to indemnify the Government for certain amounts which were expected to be nominal. On this basis, the semi-annual payments made by the Company to NHKTC in respect of the EHC were dealt with in these accounts as payments under a finance lease.

In 2007, the Group made its final lease payment under the 1986 Agreement to NHKTC. On 5 February 2008, the Company entered into a new Operating Agreement with NHKTC whereby both companies agreed to share the future costs of maintenance, care, upkeep and repair of certain common facilities and utilities of the EHC assets; and the Company to carry out repair, maintenance and upkeep of the railway and assets solely for purpose of rail use in respect of the EHC following expiry of the 1986 Agreement.

The carrying amount of the assets in relation to the above arrangement is as follows:

The Group and The Company

	Civil works Eastern Harbour Crossing	
in HK$ million	**2008**	2007
Cost	**1,254**	1,254
Less: Aggregate depreciation	**(345)**	(326)
Net book value	**909**	928

D The Group leases out investment properties and station kiosks, including duty free shops, under operating leases. The leases typically run for an initial period of one to ten years, with an option to renew the lease after that date at which time all terms will be renegotiated. Lease payments are usually adjusted annually to reflect market rentals. Certain leases above carry additional rental based on turnover, some of which are with reference to thresholds. Lease incentives granted are amortised in the profit and loss account as an integral part of the net lease payment receivable.

The gross carrying amounts of investment properties of the Group and the Company held for use in operating leases were HK$37,737 million (2007: HK$37,723 million) and HK$36,618 million (2007: HK$36,562 million) respectively. The gross carrying amounts of station kiosks of the Group and the Company held for use in operating leases were HK$489 million (2007: HK$482 million) and the related accumulated depreciation charges were HK$143 million (2007: HK$127 million).

Total future minimum lease receipts under non-cancellable operating leases are receivable as follows:

	The Group		The Company	
in HK$ million	**2008**	2007	**2008**	2007
Within 1 year	**3,300**	3,024	**3,265**	2,960
After 1 year but within 5 years	**5,188**	6,355	**5,152**	6,338
Later than 5 years	**123**	181	**123**	181
	8,611	9,560	**8,540**	9,479

19 Other Property, Plant and Equipment *(continued)*

E In March 2003, the Group entered into a series of structured transactions with unrelated third parties to lease out and lease back certain of its passenger cars ("Lease Transaction") involving a total original cost of HK$2,562 million and a total net book value of HK$1,674 million as at 31 March 2003. Under the Lease Transaction, the Group has leased the assets to institutional investors in the United States (the "Investors"), who have prepaid all the rentals in relation to the lease agreement. Simultaneously, the Group has leased the assets back from the Investors based on terms ranging from 21 to 29 years with an obligation to pay rentals in accordance with a pre-determined payment schedule. The Group has an option to purchase the Investors' leasehold interest in the assets at the expiry of the lease term for fixed amounts. Part of the rental prepayments received from the Investors has been invested in debt securities to meet the Group's rental obligations and the amount payable for exercising the purchase option under the Lease Transaction. The Group has an obligation to replace these debt securities with other debt securities in the event those securities do not meet certain credit ratings requirements. In addition, the Group has provided standby letters of credit to the Investors to cover additional amounts payable by the Group in the event the transactions are terminated prior to the expiry of the lease terms.

The Group retains legal title to the assets and there are no restrictions on the Group's ability to utilise these assets in the operation of the railway business.

As a result of the Lease Transaction, an amount of approximately HK$3,688 million was received in an investment account and was used to purchase debt securities ("Defeasance Securities") to be used to settle the long-term lease payments with an estimated net present value in March 2003 of approximately HK$3,533 million. This resulted in the Group having received in 2003 an amount of HK$141 million net of costs. As the Group is not able to control the investment account in pursuit of its own objectives and its obligations to pay the lease payments are funded by the proceeds of the above investments, those obligations and investments in the Defeasance Securities were not recognised in March 2003 as liabilities and assets of the Group. The net amount of cash received was accounted for as deferred income by the Group.

A small portion of these Defeasance Securities was subject to replacement on credit rating downgrades. During 2008, credit ratings of some of these securities were downgraded and subsequently these securities were replaced by standby letters of credit issued to the relevant Investors to support the corresponding payment obligations. As a result, a total charge of HK$100 million was recorded as interest and finance charges for the year. There are other Defeasance Securities issued by the same issuer as the above mentioned Defeasance Securities, with accreted value of US$46.5 million as at 31 December 2008, which are not subject to replacement obligation on rating downgrades.

20 Service Concession Assets

Service concession assets are in respect of the Company's right to access, use and operate the KCRC system pursuant to the Rail Merger.

The Group and The Company

in HK$ million	Initial concession property	Additional concession property	Total
2008			
Cost			
At 1 January 2008	15,226	49	15,275
Net additions during the year	–	523	523
At 31 December 2008	15,226	572	15,798
Accumulated amortisation			
At 1 January 2008	25	–	25
Charge for the year	304	6	310
At 31 December 2008	329	6	335
Net book value at 31 December 2008	14,897	566	15,463

20 Service Concession Assets *(continued)*

The Group and The Company *(continued)*

in HK$ million	Initial concession property	Additional concession property	Total
2007			
Cost			
At 1 January 2007	–	–	–
Additions through the Rail Merger			
– Upfront payment (note 3B)	3,924	–	3,924
– Principal element of fixed annual payments (note 42)	10,687	–	10,687
– Others (note 3B)	226	31	257
Net additions during the year	–	18	18
Transfer from deferred expenditure (note 24)	389	–	389
At 31 December 2007	15,226	49	15,275
Accumulated amortisation			
At 1 January 2007	–	–	–
Charge for the year	25	–	25
At 31 December 2007	25	–	25
Net book value at 31 December 2007	15,201	49	15,250

Additional concession property represents expenditure incurred in relation to the maintenance, repair, replacement and upgrade of the KCRC system.

21 Property Management Rights

The Group and The Company

in HK$ million	**2008**	2007
Cost		
At 1 January	**40**	–
Addition through the Rail Merger	**–**	40
At 31 December	**40**	40
Accumulated amortisation		
At 1 January	**–**	–
Charge for the year	**5**	–
At 31 December	**5**	–
Net book value at 31 December	**35**	40

22 Railway Construction in Progress

The Group and The Company

in HK$ million	Balance at 1 Jan	Expenditure	Capitalised on commissioning (note 19)	Balance at 31 Dec
2008				
LOHAS Park Station Project				
Construction costs	**314**	**176**	–	**490**
Consultancy fees	**11**	**2**	–	**13**
Staff costs and other expenses	**81**	**33**	–	**114**
Finance costs	**18**	**23**	–	**41**
	424	**234**	–	**658**
Total	**424**	**234**	–	**658**
2007				
LOHAS Park Station Project				
Construction costs	117	197	–	314
Consultancy fees	10	1	–	11
Staff costs and other expenses	43	38	–	81
Finance costs	5	13	–	18
	175	249	–	424
SkyPlaza Platform Project				
Construction costs	40	10	(50)	–
Staff costs and other expenses	14	4	(18)	–
Finance costs	3	–	(3)	–
	57	14	(71)	–
Total	232	263	(71)	424

A LOHAS Park Station Project

The construction of the LOHAS Park Station is covered by the TKE Project Agreement with the Government signed on 4 November 1998.

The project's target completion is in 2009. The capital cost for the project based on the defined scope of works and programme is estimated at approximately HK$1 billion.

At 31 December 2008, the Company has incurred expenditure of HK$658 million on the project (2007: HK$424 million) and has authorised outstanding commitments on contracts totalling HK$15 million (2007: HK$147 million) related to the project.

B SkyPlaza Platform Project

The Project Agreement between Airport Authority and the Company for the design, construction, financing and operation of the SkyPlaza Platform Project was signed on 18 July 2005.

The project was completed and started to serve the public on 28 February 2007. Negotiation on the final accounts with various contractors is being performed.

22 Railway Construction in Progress *(continued)*

C Kowloon Southern Link ("KSL") Project

After the Rail Merger, the construction of KSL remains a responsibility of KCRC who continues to fund the relating construction costs. Pursuant to the KSL Project Management Agreement, the Company acts as a project management agent to KCRC in connection with the KSL under certain circumstances in return for a project management fee plus incentive payment if the construction of KSL is completed ahead of time and under budget. Expenditure incurred by the Company for the project management is charged to the profit and loss account while the project management fee is recognised as revenue in accordance with the Company's accounting policy on revenue recognition of contracts. During 2008, HK$310 million (2007: HK$24 million) of project management fee was recognised as income in the profit and loss account. KSL will form part of the service concession on opening for service which is scheduled in 2009.

D Shatin to Central Link ("SCL") Project

On 11 March 2008, the Executive Council has approved further planning and design of the SCL. On 24 November 2008, the Government and the Company entered into an Entrustment Agreement for the design of and site investigation and procurement activities in relation to the SCL. Pursuant to the Entrustment Agreement, the Company shall carry out or procure the carrying out of, and the Government shall fund, the design, site investigation and procurement activities.

E Guangzhou-Shenzhen-Hong Kong Express Rail Link ("XRL") Project

On 22 April 2008, the Executive Council decided that the Company should be asked to proceed with further planning and design of the Hong Kong section of the XRL with a view to implementing the Hong Kong section of the XRL under concession approach. On 24 November 2008, the Government and the Company entered into an Entrustment Agreement for the design of and site investigation and procurement activities in relation to the XRL. Pursuant to the Entrustment Agreement, the Company shall carry out or procure the carrying out of, and the Government shall fund, the design, site investigation and procurement activities.

23 Property Development in Progress

Under the Airport Railway Agreement related to the construction of the Airport Railway, the Government had granted to the Company development rights on the land ("Land Grant") over the five station sites along the railway at market value for property development. In preparing the sites for development, the Company incurs costs related to foundation and site enabling works and expects the costs to be reimbursed by property developers in the form of up-front cash payments when development packages are awarded. In accordance with the development agreements entered into with property developers, the developers are also responsible for the balance of the development costs.

Notwithstanding having entered into the development agreements with the developers, the Company being the grantee of the land remains primarily responsible for the fulfilment of all the conditions and obligations in the Land Grant. Such conditions and obligations include the type and quantity of the developments that must be built, public facilities to be provided, and the completion date of the project.

Costs of foundation, site enabling works and land costs incurred by the Company are capitalised as property development in progress and payments received from developers are credited to property development in progress to offset costs incurred in respect of the same development. In cases where payments received from developers exceed the related expenditure incurred by the Company, such excess is recorded as deferred income (note 23B(i)). In these cases, any subsequent expenditure incurred by the Company in respect of that development will be charged against deferred income. Deferred income is to be recognised as profits of the Company at the appropriate time after charging any remaining costs related to foundation and site enabling works, and after taking into account the outstanding risks and obligations retained by the Company relating to each development. Until such time as deferred income is recognised as profit, it is recorded as a liability of the Company in recognition of the Company's obligations under the Land Grant.

The Tseung Kwan O Extension ("TKE") Project Agreement entered into in 1998 between the then Secretary for Transport, for and on behalf of the Government, and the Company in respect of the construction of the Tseung Kwan O Extension provides the Company with the right to undertake property developments at four station and depot sites along the Tseung Kwan O Line ("Tseung Kwan O Extension Property Projects") under separate land grant agreements. The basis of accounting for development costs incurred by the Company and payment related thereto is consistent with that for the property developments along the Airport Railway.

On the Appointed Day, the Company acquired property development rights on eight development sites, comprising three awarded and five not yet awarded sites, along the East Rail Line, Kowloon Southern Link and Light Rail ("ERL/KSL/LR Property Projects"), from KCRC pursuant to the Rail Merger (note 3A). During 2008, the development site at Che Kung Temple Station of the East Rail Line was awarded.

23 Property Development in Progress *(continued)*

A Property Development in Progress

The Group and The Company

in HK$ million	Balance at 1 Jan	Expenditure	Offset against payments received from developers (note 23B(i))	Transfer out on project completion	Balance at 31 Dec
2008					
Airport Railway Property Projects	**–**	**31**	**(31)**	**–**	**–**
Tseung Kwan O Extension Property Projects	**3,307**	**382**	**(53)**	**(1,555)**	**2,081**
East Rail Line/Light Rail/Kowloon Southern Link Property Projects	**5,759**	**1,918**	**(42)**	**(1,821)**	**5,814**
	9,066	**2,331**	**(126)**	**(3,376)**	**7,895**
2007					
Airport Railway Property Projects	-	139	(139)	-	-
Tseung Kwan O Extension Property Projects	3,297	288	(278)	-	3,307
East Rail Line/Light Rail/Kowloon Southern Link Property Projects	-	5,812	(53)	-	5,759
	3,297	6,239	(470)	-	9,066

Tseung Kwan O Extension Property Projects includes capitalised interest of HK$768 million (2007: HK$768 million) in connection with the Company's interest-free loan of HK$4,000 million extended to the developer of Package 2, Tseung Kwan O Area 86 property development project in 2006 (note 35).

East Rail Line/Light Rail/Kowloon Southern Link Property Projects include the acquisition cost for the property development rights on the development sites from KCRC and mandatory payments in respect of enabling works carried out by KCRC for such sites. As at 31 December 2008, outstanding mandatory payments including interest accrued amounted to HK$818 million (2007: HK$901 million including HK$26 million of interest accrued). Expenditure during the year ended 31 December 2008 included HK$1,831 million of land premium in respect of the Che Kung Temple property development.

B Deferred Income on Property Development

The Group and The Company

in HK$ million	**2008**	2007
Deferred income on property development comprises:		
– Upfront payments received from developers (note 23B(i))	**138**	321
– Sharing in kind (note 23B(ii))	**18**	79
	156	400

23 Property Development in Progress *(continued)*

B Deferred Income on Property Development *(continued)*

(i) Deferred Income on Upfront Payments

The Group and The Company

in HK$ million	Balance at 1 Jan	Payments received from developers	Offset against development in progress (note 23A)	Amount recognised as profit (note 8)	Balance at 31 Dec
2008					
Airport Railway Property Projects	**240**	**–**	**(31)**	**(139)**	**70**
Tseung Kwan O Extension Property Projects	**81**	**40**	**(53)**	**–**	**68**
East Rail Line/Light Rail/Kowloon Southern Link Property Projects	**–**	**42**	**(42)**	**–**	**–**
	321	**82**	**(126)**	**(139)**	**138**
2007					
Airport Railway Property Projects	1,120	120	(139)	(861)	240
Tseung Kwan O Extension Property Projects	–	359	(278)	-	81
East Rail Line/Light Rail/Kowloon Southern Link Property Projects	-	53	(53)	-	–
	1,120	532	(470)	(861)	321

(ii) Deferred Income on Sharing in Kind

Under the property development agreement in respect of an Airport Railway development package, the Company received during 2004 certain portions of the shell of a retail centre at Union Square, Kowloon Station and its car parking spaces. Part of the property development profit is deferred as the Company has an obligation under the development agreement to complete the fitting-out works. On this basis, movements of the deferred income on this sharing in kind during the year are set out below:

The Group and The Company

in HK$ million	**2008**	2007
Balance as at 1 January	**79**	442
Less: Amount recognised as profit (note 8)	**(61)**	(363)
Balance as at 31 December	**18**	79

23 Property Development in Progress *(continued)*

C Stakeholding Funds

As stakeholder under certain Airport Railway, Tseung Kwan O Extension and East Rail Line Property Projects, the Company receives and manages deposit monies and sales proceeds in respect of sales of properties under those developments. These monies are placed in separate designated bank accounts and, together with any interest earned, will be released to the developers for the reimbursement of costs of the respective developments in accordance with the terms and conditions of the Government Consent Schemes and development agreements. Any balance remaining will only be released for distribution after all obligations relating to the developments have been met. Accordingly, the balances of the stakeholding funds and the corresponding bank balances have not been included in the Group's and the Company's balance sheets. Movements in stakeholding funds during the year were as follows:

The Group and The Company

in HK$ million	**2008**	2007
Balance as at 1 January	**5,264**	6,860
Stakeholding funds received	**15,518**	19,439
Add: Interest earned thereon	**100**	260
	20,882	26,559
Disbursements during the year	**(16,307)**	(21,295)
Balance as at 31 December	**4,575**	5,264
Represented by:		
Balances in designated bank accounts as at 31 December	**4,573**	5,262
Retention receivable	**2**	2
	4,575	5,264

In addition to the above, there are certain deposit monies and sales proceeds in respect of a East Rail Line property development site, amounting to HK$1,221 million (2007: nil) at 31 December 2008, that are under the custody of the solicitors and managed by the Company on behalf of KCRC as KCRC's agent.

D West Rail Property Developments

As part of the Rail Merger, the Company was appointed to act as the agent of KCRC and certain KCRC subsidiary companies ("West Rail Subsidiaries") in the development of specified development sites along the West Rail. The Company will receive an agency fee of 0.75% of the gross sale proceeds in respect of the developments except for the Tuen Mun development on which the Company will receive 10% of the net profits accrued under the development agreement. The Company will also recover from the West Rail Subsidiaries all the costs incurred in respect of the West Rail development sites plus 16.5% on-cost, together with interest accrued thereon. During 2008, the reimbursable costs incurred by the Company including on-cost and interest accrued were HK$66 million (2007: HK$1 million).

24 Deferred Expenditure

The Group

in HK$ million	Balance at 1 Jan	Expenditure during the year	Transfer to other property, plant and equipment (note 19)	Transfer to service concession assets (note 20)	Balance at 31 Dec
2008					
Expenditure on proposed capital projects	**825**	**1,163**	**–**	**–**	**1,988**
	825	**1,163**	**–**	**–**	**1,988**
2007					
Merger expenditure	170	322	(103)	(389)	–
Expenditure on proposed capital projects	395	430	–	–	825
	565	752	(103)	(389)	825

24 Deferred Expenditure *(continued)*

The Company

in HK$ million	Balance at 1 Jan	Expenditure during the year	Transfer to other property, plant and equipment (note 19)	Transfer to service concession assets (note 20)	Balance at 31 Dec
2008					
Expenditure on proposed capital projects	**155**	**183**	**–**	**–**	**338**
	155	**183**	**–**	**–**	**338**
2007					
Merger expenditure	170	322	(103)	(389)	–
Expenditure on proposed capital projects	113	42	–	–	155
	283	364	(103)	(389)	155

The expenditure incurred on the proposed capital projects for the year mainly relates to design works for the Shenzhen Metro Line 4 Project in Mainland of China, the West Island Line, Kwun Tong Line Extension and South Island Line (East) Projects in Hong Kong.

During 2008, the Company received the first part of the Government's capital grant for the West Island Line Project of HK$400 million, of which HK$355 million has been used to offset the detailed design cost incurred up to 31 December 2008.

As at 31 December 2008, the majority of the deferred expenditure was related to the Shenzhen Metro Line 4 Project (note 52G(i)).

25 Prepaid Land Lease Payments

The Group and The Company

in HK$ million	2008	2007
Cost		
At 1 January	**732**	732
Addition	**–**	–
At 31 December	**732**	732
Accumulated amortisation		
At 1 January	**151**	138
Charge for the year	**14**	13
At 31 December	**165**	151
Net book value at 31 December	**567**	581

A The above prepaid land lease payments, all of which relate to land held for railway depots in Hong Kong, is analysed as follows:

The Group and The Company

in HK$ million	2008	2007
At net book value		
– long leases	**151**	154
– medium-term leases	**416**	427
	567	581

25 Prepaid Land Lease Payments *(continued)*

B The lease of the land on which the civil works, plant and equipment are situated for the operation of the railway was granted to the Company under a running line lease for the period up to 29 June 2050 which can be extended for further periods of 50 years at nominal payment (note 51C).

Under the terms of the lease, the Company undertakes to keep and maintain all the leased areas, including underground and overhead structures, at its own cost. With respect to parts of the railway situated in structures where access is shared with other users, such as the Lantau Fixed Crossing, the Company's obligation for maintenance is limited to the railway only. All maintenance costs incurred under the terms of the lease have been dealt with as railway operating costs in the profit and loss account.

26 Interests in Non-controlled Subsidiaries

	The Group		The Company	
in HK$ million	**2008**	2007	**2008**	2007
Unlisted shares, at cost	**–**	–	**24**	24
Share of net assets	**381**	268	**–**	–
	381	268	**24**	24

The following list contains the particulars of all major non-controlled subsidiaries of the Group:

		Proportion of ownership interest				
Name of company	Issued and paid up ordinary share capital	Group's effective interest	Held by the Company	Held by subsidiary	Place of incorporation and operation	Principal activities
Octopus Holdings Limited	HK$42,000,000	57.4%	57.4%	-	Hong Kong	Investment holding
Octopus Cards Limited	HK$42,000,000	57.4%	–	100%	Hong Kong	Operate a contactless smartcard common payment system in Hong Kong
Octopus China Investments Limited	HK$1	57.4%	–	100%	Hong Kong	Investment holding
Octopus Connect Limited	HK$2	57.4%	–	100%	Hong Kong	Customer relationship management service
Octopus International Projects Limited	HK$1	57.4%	–	100%	Hong Kong	Marketing and management of overseas automatic fare collection consultancy projects
Octopus Investments Limited	HK$2	57.4%	–	100%	Hong Kong	Investment holding
Octopus Knowledge Limited	HK$2	57.4%	–	100%	Hong Kong	Consultancy services on introducing a smartcard system in Dubai
Octopus Netherlands Limited	HK$1	57.4%	–	100%	Hong Kong	Consultancy services on introducing a smartcard system in the Netherlands
Octopus Rewards Limited	HK$1	57.4%	–	100%	Hong Kong	Develop and operate a common loyalty scheme
Octopus Solutions Limited	HK$2	57.4%	–	100%	Hong Kong	Project management
Octopus Systems Limited	HK$2	57.4%	–	100%	Hong Kong	Project management
Octopus Cards Macau Limited	MOP10,000	57.4%	–	100%	Macau	Promote the contactless smartcard common payment system in Macau
Octopus Cards (NL) B.V.	EUR18,000	57.4%	–	100%	Netherlands	Project management on introducing a smartcard system in the Netherlands

26 Interests in Non-controlled Subsidiaries *(continued)*

In June 1994, the Company entered into an agreement with four local transport companies, Kowloon-Canton Railway Corporation, The Kowloon Motor Bus Company (1933) Limited (subsequently replaced by KMB Public Bus Services Holdings Limited), Citybus Limited and The Hongkong and Yaumati Ferry Co., Limited (subsequently replaced by New World First Bus Services Limited and New World First Ferry Services Limited), to incorporate a company, Creative Star Limited, now Octopus Cards Limited ("OCL"), to undertake the development and operation of the "Octopus" contactless smart card ticketing system, which was initially used by the shareholding transport companies. Although the Company currently holds a 57.4% interest in the issued shares of OCL, its appointees to the Board of Directors of OCL are limited to 49% of the voting rights at board meetings. The shareholders have agreed to provide the necessary funding to OCL for its operations and for the development of the "Octopus" system.

On 20 April 2000, OCL received approval from The Hong Kong Monetary Authority ("HKMA") to become a deposit-taking company ("DTC") for purposes of extending the use of Octopus cards to a wider range of services, including those that are non-transport related. Prior to becoming a DTC, the Octopus card was exempted from the definition of "multi-purpose card" under the Banking Ordinance (Chapter 155 of the Laws of Hong Kong) on the basis that its use was restricted to transport related services only.

On 17 January 2001, the Company entered into a new Shareholders' Agreement with the other shareholders of OCL. Under this agreement, the Company disposed of a shareholding interest of 10.4% in OCL to certain other shareholders of OCL for a consideration of HK$16 million, together with a deferred consideration to be received in the event of OCL subsequently becoming a stock exchange listed company.

On 21 October 2005, the Company and the other shareholders of OCL entered into a number of agreements to adjust the arrangements relating to OCL, in order to make the non-payment businesses of OCL into new, separate subsidiaries independent of the payment business of OCL that is regulated by the HKMA. Accordingly, a new holding company, Octopus Holdings Limited ("OHL"), has been set up to hold the entire issued share capital of each of these new companies as well as OCL. The Company's effective interest in OHL and its subsidiaries is 57.4%.

At the same time, the shareholders of OHL made a loan in aggregate amounting to HK$150 million to OHL pursuant to a Subordinated Loan Agreement, with each shareholder lending an amount in proportion to its shareholding in OHL. The Company has therefore lent HK$86 million to OHL (or 57.4% of the total amount of the loan). The loan is for a term of five years and is unsecured, the rights of the lenders are subordinated in all respects to the rights of the other unsubordinated creditors of OHL in respect of all other unsubordinated liabilities, and interest on the loan is payable at a rate of 5.5% per annum.

During the year ended 31 December 2008, a total amount of HK$99 million (2007: HK$62 million) was paid by the Company to OCL in respect of the central clearing services provided by OCL to the Company. Load agent fees and fees for handling Octopus card issuance and refund amounting to HK$13 million (2007: HK$9 million) and HK$9 million (2007: HK$6 million) respectively were received from OCL in respect of services and facilities provided by the Company at various MTR stations. Service fees amounting to HK$3 million (2007: HK$2 million) were also received from OCL in respect of rental of computer equipment and services and warehouse storage space provided by the Company under a service agreement.

During the same period, OHL repaid the subordinated loan provided by the Company in 2005, including principal amount of HK$86 million (2007: nil) and interest of HK$1 million (2007: HK$5 million), as well as distributed dividends of HK$23 million (2007: nil) to the Company.

The condensed consolidated profit and loss account and the balance sheet for OHL are shown below:

Consolidated Profit and Loss Account

Year ended 31 December in HK$ million	**2008 (Audited)**	2007 (Audited)
Turnover	**527**	465
Other operating income	**61**	53
	588	518
Staff costs	**(133)**	(101)
Load agent fees and bank charges for add value services	**(66)**	(60)
Other expenses	**(149)**	(152)
Operating profit before depreciation	**240**	205
Depreciation	**(54)**	(63)
Operating profit before interest and finance charges	**186**	142
Net interest income	**80**	76
Profit before taxation	**266**	218
Income tax	**(28)**	(49)
Profit for the year	**238**	169
Group's share of profit before taxation (note 12)	**152**	125
Group's share of income tax (note 12)	**(16)**	(28)

26 Interests in Non-controlled Subsidiaries *(continued)*

Consolidated Balance Sheet

at 31 December in HK$ million	**2008 (Audited)**	2007 (Audited)
Assets		
Fixed assets	**164**	126
Investments	**2,142**	1,746
Other assets	**181**	170
Cash at banks and on hand	**227**	424
	2,714	2,466
Liabilities		
Card floats and card deposits due to cardholders	**(1,711)**	(1,574)
Amounts due to related parties	**(23)**	(21)
Other liabilities	**(316)**	(405)
	(2,050)	(2,000)
Net assets	**664**	466
Equity		
Share capital	**42**	42
Retained profits	**622**	424
	664	466
Group's share of net assets	**381**	268

27 Investments in Subsidiaries

The Company

in HK$ million	**2008**	2007
Unlisted shares, at cost	**1,153**	1,153
Less: Impairment losses	**(3)**	(3)
	1,150	1,150

Investments in subsidiaries include HK$24 million (2007: HK$24 million) in respect of investments in non-controlled subsidiaries, the relevant details of which are disclosed in note 26. The following list contains details of controlled subsidiaries as defined under note 2C as at 31 December 2008, which have been consolidated into the Group's accounts.

27 Investments in Subsidiaries *(continued)*

Name of company	Issued and paid up ordinary/ registered share capital	Proportion of ownership interest: Group's effective interest	Held by the Company	Held by subsidiary	Place of incorporation and operation	Principal activities
Subsidiaries held throughout 2008						
Glory Goal Limited	HK$10,000	100%	100%	–	Hong Kong	Investment holding
Hanford Garden Property Management Company Limited	HK$10,000	100%	100%	–	Hong Kong	Property management
MTR (Estates Management) Limited	HK$1,000	100%	100%	–	Hong Kong	Investment holding and property management
MTR (Shanghai Project Management) Limited	HK$1,000	100%	100%	–	Hong Kong	Railway consultancy services, property investment and development
MTR Beijing Line 4 Investment Company Limited	HK$1	100%	100%	–	Hong Kong	Investment holding
MTR China Consultancy Company Limited	HK$1,000	100%	100%	–	Hong Kong	Railway consultancy services
MTR China Property Limited	HK$1,000	100%	100%	–	Hong Kong	Property management
MTR Engineering Services Limited	HK$1,000	100%	100%	–	Hong Kong	Engineering services
MTR Hangzhou Line 1 Investment Company Limited (previously known as Hong Kong Cable Car Limited)	HK$1,000	100%	100%	–	Hong Kong	Investment holding of the proposed joint venture company for the Hangzhou Metro Line 1 project
MTR Information Solutions Company Limited (previously known as Lantau Cable Car Limited)	HK$1,000	100%	100%	–	Hong Kong	License MTR software to MTR's subsidiaries and associates
MTR Property Agency Co. Limited	HK$2	100%	100%	–	Hong Kong	Property agency
MTR Rail Transport Training (International) Company Limited	HK$2,800,000	100%	100%	–	Hong Kong	Provide rail transport training in Mainland China
MTR Shenzhen Investment Holding Limited	HK$400,000	100%	100%	–	Hong Kong	Investment holding
MTR Telecommunication Company Limited	HK$100,000,000	100%	100%	–	Hong Kong	Radio communication services
MTR Travel Limited	HK$2,500,000	100%	100%	–	Hong Kong	Travel services
Ngong Ping 360 Limited	HK$2	100%	100%	–	Hong Kong	Operate the Tung Chung to Ngong Ping cable car system and Theme Village in Ngong Ping
Pierhead Garden Management Company Limited	HK$50,000	100%	100%	–	Hong Kong	Property management
Rail Sourcing Solutions (International) Limited	HK$2	100%	100%	–	Hong Kong	Global railway supply and sourcing services
Royal Ascot Management Company Limited	HK$50,000	100%	100%	–	Hong Kong	Property management
Sun Tuen Mun Centre Management Company Limited	HK$50,000	100%	100%	–	Hong Kong	Property management
TraxComm Limited	HK$15,000,000	100%	100%	–	Hong Kong	Fixed telecommunication network services
V-Connect Limited	HK$1,000	100%	100%	–	Hong Kong	Telecommunication
MTR (Shanghai Metro Management) Limited *	HK$1,000	100%	100%	–	Hong Kong	Dormant
Fasttrack Insurance Ltd.	HK$77,500,000	100%	100%	–	Bermuda	Insurance underwriting
Candiman Limited *	US$1	100%	100%	–	British Virgin Islands	Investment holding
MTR Corporation (C.I.) Limited	US$1,000	100%	100%	–	Cayman Islands / Hong Kong	Finance
MTR Finance Lease (001) Limited *	US$1	100%	100%	–	Cayman Islands / Hong Kong	Finance
Chongqing Premier Property Management Co. Ltd. * (Incorporated)	US$150,000	70%	–	70%	The People's Republic of China	Property management

27 Investments in Subsidiaries *(continued)*

Name of company	Issued and paid up ordinary/ registered share capital	Proportion of ownership interest: Group's effective interest	Held by the Company	Held by subsidiary	Place of incorporation and operation	Principal activities
MTR (Beijing) Commercial Facilities Management Co. Ltd. (Incorporated)	HK$93,000,000	100%	–	100%	The People's Republic of China	Property management
MTR (Beijing) Property Services Co. Limited * (Incorporated)	RMB3,000,000	100%	100%	–	The People's Republic of China	Property management
MTR Consultancy (Beijing) Co. Ltd. (Incorporated)	HK$1,000,000	100%	100%	–	The People's Republic of China	Railway consultancy services, marketing and promotion
MTR Consulting (Shenzhen) Co. Ltd. (Incorporated)	HK$1,000,000	100%	100%	–	The People's Republic of China	Railway consultancy services
MTR Corporation (Shenzhen) Limited (Incorporated)	HK$250,000,000	100%	–	100%	The People's Republic of China	Conduct early-stage preparatory work for Shenzhen Metro Line 4 project
MTR Corporation (Shenzhen) Training Centre * (Incorporated)	RMB2,000,000	100%	–	100%	The People's Republic of China	Provide rail transport training
Shanghai Hong Kong Metro Construction Management Co. Ltd. (Incorporated)	HK$15,000,000	60%	–	60%	The People's Republic of China	Railway construction management and development
MTR Corporation (IKF) Limited	GBP29	100%	–	100%	United Kingdom	Investment holding
MTR Corporation (No.2) Limited	GBP1	100%	–	100%	United Kingdom	Investment holding
MTR Corporation (Silverlink) Limited	GBP1	100%	–	100%	United Kingdom	Investment holding
MTR Corporation (SWT) Limited	GBP1	100%	–	100%	United Kingdom	Investment holding
MTR Corporation (UK) Limited	GBP29	100%	100%	–	United Kingdom	Investment holding
Rail Sourcing Solutions (UK) Limited *	GBP1	100%	–	100%	United Kingdom	Railway supply and sourcing services
<u>Subsidiaries established during 2008</u>						
MTR Shenyang Holdings Limited *	HK$1,000	100%	100%	–	Hong Kong	Investment holding of the proposed joint venture company for the operation and maintenance of Shenyang Metro Line 1 and Line 2
MTR (Macau) Property Management Company Limited *	MOP25,000	100%	–	100%	Macau	Property management, consultancy and other property management related businesses

* Subsidiaries not audited by KPMG. The financial statements of the subsidiaries not audited by KPMG reflect total net assets and total turnover constituting less than 1% of the respective consolidated totals.

28 Interests in Associates

The Group

in HK$ million	**2008**	2007
Share of net assets	**743**	205

The Group and the Company had interests in the following associates as at 31 December 2008:

		Proportion of ownership interest				
Name of company	Issued and paid up ordinary / registered share capital	Group's effective interest	Held by the Company	Held by subsidiary	Place of incorporation and operation	Principal activities
Beijing MTR Corporation Limited (Incorporated)	RMB1,380,000,000	49%	–	49%	The People's Republic of China	Railway construction, management and development
London Overground Rail Operations Ltd ("LOROL") *	GBP2	50%	–	50%	United Kingdom	Railway management

* Company not audited by KPMG

During the year, South Western Railway Limited, the joint venture company established for bidding of the South West Train Operation Franchise in United Kingdom in which the Group held 50% interest, was dissolved following unsuccessful bidding of the franchise.

The registered share capital of Beijing MTR Corporation Limited is RMB1,380 million of which 49% is contributed by the Group. During the year ended 31 December 2008, the Group injected its last tranche of equity of RMB471 million (HK$515 million), making the cumulative equity contribution to RMB676 million (HK$718 million) as at 31 December 2008. During the same period, the Company provided staff secondment, information technology and other support services to Beijing MTR Corporation Limited at a total amount of HK$38 million (2007: HK$32 million).

During the year ended 31 December 2008, the Company provided staff secondment and consultancy service to LOROL of HK$4 million (2007: HK$2 million). Also, the Company received HK$3 million (2007: HK$1 million) interest income in respect of the loan provided to LOROL (note 52H(i)).

The summary financial information of the Group's effective interests in associates is as follows:

in HK$ million	**2008**	2007
Non-current assets	**1,405**	692
Current assets	**208**	147
Non-current liabilities	**(36)**	(40)
Current liabilities	**(834)**	(594)
Net assets	**743**	205
Income	**1,313**	754
Expenses	**(1,281)**	(751)
Profit before taxation	**32**	3
Income tax	**(9)**	(1)
Net profit for the year	**23**	2

29 Investments in Securities

Investments in securities represent debt securities held by the overseas insurance underwriting subsidiary and the Company comprising:

The Group

in HK$ million	2008	2007
Held-to-maturity securities, at amortised cost		
– maturing within 1 year	–	–
– maturing after 1 year	90	–
	90	–
Trading securities listed overseas, at fair value		
– maturing within 1 year	100	50
– maturing after 1 year	281	283
	381	333
	471	333

The Company

in HK$ million	2008	2007
Held-to-maturity securities, at amortised cost		
– maturing within 1 year	–	–
– maturing after 1 year	90	–
	90	–

30 Staff Housing Loans

The Group and The Company

in HK$ million	2008	2007
Balance at 1 January	15	25
Redemption	(3)	(7)
Repayment	(2)	(3)
Balance at 31 December	10	15

The Group and The Company

in HK$ million	2008	2007
Amounts receivable:		
– within 1 year	2	3
– after 1 year	8	12
	10	15

The MTR Staff Housing Loan Scheme, a Company financed scheme, was introduced in 1997 to replace, on a phased basis, the previous arrangements whereby interest subsidies were paid by the Company to eligible employees. All housing loans granted to employees carry interest either at the prevailing Best Lending Rate less 1.75% per annum or at the Company's Average Cost of Borrowings plus 0.75% per annum, and are secured by mortgages over the relevant properties.

The Company considers that the nominal value of housing loans is not significantly different from their fair values.

31 Properties Held for Sale

The Group and The Company

in HK$ million	2008	2007
Properties held for sale		
– at cost	**2,092**	649
– at net realisable value	**136**	107
	2,228	756

Properties held for sale at 31 December 2008 comprised mainly residential units, retail and car parking spaces at the Olympic Station, Kowloon Station and Tung Chung Station along the Airport Railway, Hang Hau Station, Tseung Kwan O Area 55b, 57a and 86 developments along the Tseung Kwan O Line as well as Fo Tan Station along the East Rail Line. They represent either properties received by the Company as sharing in kind or as part of the profit distribution upon completion of the development and the attributable interest in unsold units of shared surplus developments for which occupation permits have been issued. The properties are stated in the balance sheet at the lower of cost, which is deemed to be their fair value upon initial recognition as determined by reference to an independent open market valuation at the date of receipt (notes 2K(vi) and (viii)), and their net realisable value at the balance sheet date. Net realisable value represents the estimated selling price less costs to be incurred in selling the properties. The net realisable values as at 31 December 2008 and 2007 are determined by reference to an open market valuation of the properties as at those dates, undertaken by an independent firm of surveyors, Jones Lang LaSalle Limited, who have among their staff Members of the Hong Kong Institute of Surveyors.

Properties held for sale at net realisable value are stated net of provision of HK$13 million (2007: HK$12 million), made in order to state these properties at the lower of their cost and estimated net realisable value.

32 Derivative Financial Assets and Liabilities

A Fair Value

The contracted notional amounts, fair values and maturities based on contractual undiscounted cash flows of derivative financial instruments outstanding are as follows:

The Group and The Company

in HK$ million	Notional amount	Fair value	Contractual undiscounted cash flow maturing in Less than 1 year	1-2 years	2-5 years	Over 5 years	Total
2008							
Derivative Financial Assets							
Gross settled:							
Foreign exchange forwards							
– fair value hedges:	387	–					
– inflow			387	–	–	–	387
– outflow			(387)	–	–	–	(387)
– cash flow hedges:	961	14					
– inflow			441	535	–	–	976
– outflow			(432)	(528)	–	–	(960)
– not qualified for hedge accounting:	3	–					
– inflow			3	–	–	–	3
– outflow			(3)	–	–	–	(3)
Cross currency swaps							
– fair value hedges:	2,537	83					
– inflow			1,810	60	886	–	2,756
– outflow			(1,757)	(34)	(848)	–	(2,639)
Net settled:							
Interest rate swaps							
– fair value hedges	4,854	427	88	112	195	90	485
Others	300	4	–	–	–	–	–
	9,042	528	150	145	233	90	618
Derivative Financial Liabilities							
Gross settled:							
Foreign exchange forwards							
– cash flow hedges:	396	13					
– inflow			339	37	7	–	383
– outflow			(348)	(40)	(8)	–	(396)
– not qualified for hedge accounting:	131	4					
– inflow			127	–	–	–	127
– outflow			(131)	–	–	–	(131)
Cross currency swaps							
– fair value hedges:	13,547	100					
– inflow			3,798	4,666	47	5,038	13,549
– outflow			(3,787)	(4,700)	(48)	(5,133)	(13,668)
Net settled:							
Interest rate swaps							
– cash flow hedges	2,592	187	(48)	(62)	(67)	(16)	(193)
Others	300	1	–	–	–	–	–
	16,966	305	(50)	(99)	(69)	(111)	(329)
Total	26,008						

32 Derivative Financial Assets and Liabilities *(continued)*

A Fair Value *(continued)*

The Group and The Company *(continued)*

in HK$ million	Notional amount	Fair value	Contractual undiscounted cash flow maturing in: Less than 1 year	1-2 years	2-5 years	Over 5 years	Total
2007							
Derivative Financial Assets							
Gross settled:							
Foreign exchange forwards							
– fair value hedges:	7	–					
– inflow			7	–	–	–	7
– outflow			(7)	–	–	–	(7)
– cash flow hedges:	777	15					
– inflow			684	7	103	–	794
– outflow			(669)	(6)	(102)	–	(777)
– not qualified for hedge accounting:	265	3					
– inflow			266	3	–	–	269
– outflow			(262)	(3)	–	–	(265)
Cross currency swaps							
– fair value hedges:	2,012	70					
– inflow			175	2,034	40	–	2,249
– outflow			(120)	(1,985)	(31)	–	(2,136)
Net settled:							
Interest rate swaps							
– fair value hedges	4,698	184	34	59	93	43	229
– cash flow hedges	300	1	1	–	–	–	1
	8,059	273	109	109	103	43	364
Derivative Financial Liabilities							
Gross settled:							
Foreign exchange forwards							
– cash flow hedges:	593	1					
– inflow			–	591	–	–	591
– outflow			–	(593)	–	–	(593)
Cross currency swaps							
– fair value hedges:	14,480	142					
– inflow			182	3,982	4,822	5,789	14,775
– outflow			(145)	(3,983)	(4,884)	(5,969)	(14,981)
Net settled:							
Interest rate swaps							
– cash flow hedges	2,242	49	(15)	(18)	(16)	(2)	(51)
– not qualified for hedge accounting	100	–	–	–	–	–	–
	17,415	192	22	(21)	(78)	(182)	(259)
Total	25,474						

32 Derivative Financial Assets and Liabilities *(continued)*

A Fair Value *(continued)*

The discounted cash flow method, which discounts the future contractual cash flows at the current market interest and foreign exchange rates that are available to the Group for similar financial instruments, is the main valuation technique used to determine the fair value of the Group's borrowings and derivative financial instruments such as interest rate swaps and cross currency swaps. The fair value of forward foreign exchange contracts is determined using forward exchange market rates at the balance sheet date.

The Group's derivative financial instruments consist predominantly of interest rate and cross currency swaps, and the relevant interest rate swap curves as of 31 December 2008 and 2007 were used to discount the cash flows of financial instruments. For Hong Kong dollars, interest rates used ranged from 0.299% to 2.042% (2007: 2.945% to 4.122%), U.S dollars from 0.263% to 2.875% (2007: 3.832% to 5.161%) and Euro from 2.271% to 3.982% (2007: 4.097% to 4.982%).

The table above details the remaining contractual maturities at the balance sheet date of the Group's and the Company's derivative financial liabilities and assets, 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.

B Financial Risks

The Group's operating activities and financing activities expose it to four main types of financial risks, namely liquidity risk, interest rate risk, foreign exchange risk and credit risk. The Group's overall risk management policy focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects of these financial risks on the Group's financial performance.

The Board of Directors provides principles for overall risk management and approves policies covering specific areas, such as liquidity risk, interest rate risk, foreign exchange risk, credit risk, concentration risk, use of derivative financial instruments and non-derivative financial instruments, and investing excess liquidity. The Group's Preferred Financing Model (the "Model") is an integral part of its risk management policies. The Model specifies amongst other things, the preferred mix of fixed and floating rate debts, the permitted level of foreign currency debts and an adequate length of financing horizon for coverage of forward funding requirements, against which the Group's financing related liquidity, interest rate and currency risk exposures are measured, monitored and controlled. The Board regularly reviews its risk management polices and authorises changes if necessary based on operating and market conditions and other relevant factors. The Board also reviews on an annual basis as part of the budgeting process and authorises changes if necessary to the Model in accordance with changes in market conditions and practical requirements.

The use of derivative financial instruments to control and hedge against interest rate and foreign exchange risk exposures is an integral part of the Group's risk management strategy. In accordance with Board policy, these instruments shall only be used for controlling or hedging risk exposures, and cannot be used for speculation purposes. All of the derivative instruments used by the Group are over-the-counter derivatives comprising principally interest rate swaps, cross currency swaps and foreign exchange forward contracts.

(i) Liquidity Risk

Liquidity risk refers to the risk that funds are not be available to meet liabilities as they fall due, and it may result from timing and amount mismatches of cash inflow and outflow. As a net borrower of funds, the Group does not maintain any sizeable cash surplus or short-term investment portfolio as it will usually use excess cash to pay down debt outstanding to reduce borrowing costs.

The Group employs projected cash flow analysis to manage liquidity risk by forecasting the amount of cash required, including working capital, debt repayments, dividend payments, capital expenditures and new investments, and by maintaining sufficient undrawn committed banking facilities to ensure these requirements are met. It adopts a prudent approach and will maintain sufficient committed banking facilities to provide forward coverage of at least 6 to 15 months of projected cash requirements as specified in the Model. The Group also conducts stress testing of its projected cash flow to analyse liquidity risk, and would arrange additional banking facilities or debt issuance or otherwise take appropriate actions if necessary should such stress test reveal significant risk of material cash flow shortfall.

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, 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:

The Group

	2008				2007			
in HK$ million	Capital market instruments	Bank loans and overdrafts	Others	Total	Capital market instruments	Bank loans and overdrafts	Others	Total
Loans and other obligations								
Amounts repayable beyond 5 years	**8,705**	**–**	**536**	**9,241**	11,221	–	–	11,221
Amounts repayable within a period of between 2 and 5 years	**4,199**	**2,519**	**–**	**6,718**	6,676	11,563	–	18,239
Amounts repayable within a period of between 1 and 2 years	**6,919**	**3,126**	**–**	**10,045**	7,903	542	–	8,445
Amounts repayable within 1 year	**7,960**	**1,840**	**–**	**9,800**	2,339	1,042	–	3,381
	27,783	**7,485**	**536**	**35,804**	28,139	13,147	–	41,286

32 Derivative Financial Assets and Liabilities *(continued)*

B Financial Risks *(continued)*

The Company

in HK$ million	2008 Capital market instruments	2008 Bank loans and overdrafts	2008 Others	2008 Total	2007 Capital market instruments	2007 Bank loans and overdrafts	2007 Others	2007 Total
Loans and other obligations								
Amounts repayable beyond 5 years	**604**	**–**	**536**	**1,140**	657	–	–	657
Amounts repayable within a period of between 2 and 5 years	**116**	**2,519**	**–**	**2,635**	5,071	11,563	–	16,634
Amounts repayable within a period of between 1 and 2 years	**5,035**	**3,126**	**–**	**8,161**	6,404	542	–	6,946
Amounts repayable within 1 year	**6,418**	**812**	**–**	**7,230**	825	721	–	1,546
	12,173	**6,457**	**536**	**19,166**	12,957	12,826	–	25,783

Others represent obligations under lease out/lease back transaction (note 19E).

(ii) Interest Rate Risk

The Group's interest rate risk arises principally from its borrowing activities. Borrowings issued at fixed rates expose the Group to fair value interest rate risk whilst borrowings based on floating rates expose the Group to cash flow interest rate risk both because of changes in market interest rates. The Group manages and controls its interest rate risk exposure by maintaining a minimum level of fixed rate debt of 40% to 60% of total debt outstanding as specified by the Model. Should the actual fixed rate debt level deviate substantially from the Model, derivative financial instruments in the form of interest rate swaps would be procured to change the fixed and floating mix to align with the Model. As at 31 December 2008, 62% of the Group's total debt outstanding was denominated either in or converted to fixed interest rate after taking into account outstanding cross currency and interest rate swaps.

As at 31 December 2008, it is estimated that a 200 basis points increase / 50 basis points decrease in interest rates, with all other variables held constant, would decrease/increase the Group's profit after tax and retained profits by approximately HK$142/37 million. Other components of consolidated equity would increase/decrease by approximately HK$173/47 million.

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 interest rate assumptions represent management's assessment of a reasonable possible change in interest rates over the period until the next annual balance sheet date in the light of the current low absolute levels of interest rates and the greater scope for rate increase than decrease in the future.

In 2007, a similar analysis was performed based on the assumption of a general increase/decrease of 200 basis points in interest rates, which would decrease/increase the Group's profit after tax and retained profits by approximately HK$232/233 million. Other components of consolidated equity would increase/decrease by approximately HK$133/147 million.

(iii) Foreign Exchange Risk

Foreign exchange risk arises when recognised assets and liabilities are denominated in a currency that is not the Group's functional currency. For the Group, it arises principally from its borrowing and overseas procurement activities.

The Group manages and controls its exposure to the foreign exchange risk exposure by maintaining a modest level of unhedged non-Hong Kong dollar debt as specified by the Model, and minimal foreign exchange open positions created by its procurements overseas. This is usually achieved by converting non-Hong Kong dollar debt upon its inception to Hong Kong dollar through cross currency swaps and by entering into foreign exchange forward contracts to provide the necessary foreign currencies for settlement soon after the commitment to procure overseas.

As most of the company's receivables and payables are denominated in local currencies (Hong Kong dollars or Renminbi) or United States dollars (with which Hong Kong dollars are pegged) and most of its payment commitments denominated in foreign currencies are covered by foreign exchange forward contracts, management does not expect that there will be any significant currency risk associated with them.

(iv) Credit Risk

Credit risk refers to the risk that a counterparty will be unable to pay amounts in full when due. For the Group, this arises mainly from the deposits it maintains and the derivative financial instruments that it has entered into with various banks and counterparties as well as from the Defeasance Securities it procured under the lease out/lease back transaction (note 19E). The Group limits its exposure to credit risk by placing deposits and transacting derivative financial instruments only with financial institutions with acceptable investment grade credit ratings, and diversifying its exposure to various counterparties.

32 Derivative Financial Assets and Liabilities *(continued)*

B Financial Risks *(continued)*

(iv) Credit Risk *(continued)*

All derivative financial instruments are subject to a maximum counterparty limit based on the respective counterparty's credit ratings in accordance with policy approved by the Board. Credit exposure in terms of estimated fair market value of and largest potential loss arising from these instruments based on the "value-at-risk" concept is measured, monitored and controlled against their respective counterparty limits. To further reduce counterparty risk exposure, the Group also applies set-off and netting arrangements across all derivative financial instruments and other financial transactions with the same counterparty.

All deposits are similarly subject to a separate maximum counterparty limit based on the respective counterparty's credit ratings and/or status as Hong Kong's note-issuing banks. There is also a limit on the length of time that the Group can maintain a deposit with a counterparty based upon the latter's credit ratings. Deposit outstanding and maturity profile are monitored on a frequent basis to ensure they are within the limits established for the counterparties. In addition, the Group actively monitors the credit default swap levels of counterparties and their daily change levels, and may on the basis of the observed levels and other considerations adjust its exposure and/or maximum counterparty limit to the relevant counterparty.

As at balance sheet date, the maximum exposure to credit risk of the Group with respect to derivative financial assets and bank deposits is represented respectively by carrying amount of the derivative financial assets and aggregate amount of deposit on its balance sheet. As at balance sheet date, there was no significant concentration risk to a single counterparty.

In addition, the Company also manages and controls its exposure to credit risks in respect of receivables and loan to a property developer as stated in notes 34 and 35 respectively.

33 Stores and Spares

	The Group		The Company	
in HK$ million	**2008**	2007	**2008**	2007
Stores and spares expected to be consumed:				
– within 1 year	**490**	347	**477**	345
– after 1 year	**206**	315	**196**	315
	696	662	**673**	660
Less: Provision for obsolete stock	**(6)**	(20)	**(6)**	(20)
	690	642	**667**	640

Stores and spares expected to be consumed after 1 year comprise mainly contingency spares and stocks kept to meet cyclical maintenance requirements.

34 Debtors, Deposits and Payments in Advance

	The Group		The Company	
in HK$ million	**2008**	2007	**2008**	2007
Debtors, deposits and payments in advance relate to:				
– Property development projects	**5,818**	3,774	**5,818**	3,774
– Railway operations and others	**1,372**	1,393	**1,182**	1,283
	7,190	5,167	**7,000**	5,057

The Group's credit policies in respect of receivables arising from its principal activities are as follows:

(i) The majority of fare revenue is collected either through Octopus Cards with daily settlement or in cash for other ticket types. A small portion of fare revenue collected through pre-sale agents is due within 21 days.

(ii) Rentals, advertising and telecommunications service fees are billed monthly with due dates ranging from immediately due to 50 days. Tenants of the Group's investment properties and station kiosks are required to pay three months' rental deposit upon the signing of lease agreements.

(iii) Amounts receivable under interest rate and currency swap agreements with financial institutions are due in accordance with the respective terms of the agreements.

(iv) Consultancy service incomes are billed monthly and are due within 30 days.

(v) Debtors in relation to contracts and capital works entrusted to the Group, subject to any agreed retentions, are due within 21 days upon the certification of work in progress.

34 Debtors, Deposits and Payments in Advance *(continued)*

The ageing analysis of debtors included above is as follows:

	The Group		The Company	
in HK$ million	**2008**	2007	**2008**	2007
Amounts not yet due	**6,219**	4,201	**6,188**	4,211
Overdue by 30 days	**148**	172	**139**	145
Overdue by 60 days	**30**	19	**26**	13
Overdue by 90 days	**3**	14	**3**	9
Overdue by more than 90 days	**16**	55	**14**	48
Total debtors	**6,416**	4,461	**6,370**	4,426
Deposits and payments in advance	**558**	552	**414**	477
Prepaid pension costs	**216**	154	**216**	154
	7,190	5,167	**7,000**	5,057

Amounts not yet due includes HK$5,801 million (2007: HK$3,731 million) in respect of property development which are due according to the terms of relevant development agreements or sale and purchase agreements as well as receivable from certain stakeholding funds (note 23C) awaiting finalisation of the respective development accounts.

As at 31 December 2008, all debtors, deposits and payments in advance were expected to be recovered within one year except for HK$161 million (2007: HK$139 million) included in the amounts relating to deposits and receivables in respect of railway operations and others, which were expected to be recovered between one to three years. The nominal values less impairment losses for bad and doubtful debts are not discounted as it is considered that the effect of discounting would not be significant.

Included in debtors, deposits and payments in advance are the following amounts denominated in a currency other than the functional currency of the entity to which they relate:

	The Group		The Company	
	2008	2007	**2008**	2007
Dirhams (in million)	**6**	–	**6**	–
Euros (in thousand)	**206**	579	**206**	579
New Taiwan dollars (in million)	**8**	20	**8**	20
Pound sterling (in million)	**1**	1	**1**	1
Renminbi (in million)	**79**	41	**–**	–
United States dollars (in million)	**21**	24	**21**	24

35 Loan to a Property Developer

The Group and The Company

	2008		2007	
in HK$ million	Nominal amount	Carrying amount	Nominal amount	Carrying amount
Interest-free loan to a property developer	**4,000**	**3,720**	4,000	3,532

The loan was provided to the developer of Package 2, Tseung Kwan O Area 86 property development project under the terms of the development agreement. The loan is interest-free and guaranteed by the developer's ultimate holding company (the "Guarantor") and is repayable on completion of the respective phases of the project. The Company monitors the exposure to credit risk in respect of the loan by regularly assessing the credit quality of the Guarantor, taking into account the Guarantor's current financial position, the Company's past experience on transactions with the Guarantor and other relevant factors.

36 Amounts Due from the Government and Other Related Parties

	The Group		The Company	
in HK$ million	**2008**	2007	**2008**	2007
Amounts due from:				
– the Government	**187**	34	**187**	34
– the Housing Authority	**24**	22	**24**	22
– KCRC	**127**	261	**127**	261
– non-controlled subsidiaries	**16**	96	**16**	96
– associates	**72**	131	**82**	138
– other subsidiaries of the Company (net of impairment losses)	**–**	–	**1,692**	764
	426	544	**2,128**	1,315

The amount due from the Government is related to outstanding receivables and retention, as well as provision for contract claims recoverable from the Government, in connection with infrastructure works entrusted to the Company, reimbursable costs incurred by the Company for West Rail property developments (note 23D) and outstanding receivables in respect of the costs recoverable from the Government for the Shatin to Central Link and Express Rail Link Projects (notes 22D and 22E).

The amount due from the Housing Authority is related to infrastructure works entrusted to the Company in respect of the Tseung Kwan O Extension Project.

The amount due from KCRC is related to KCRC's cost sharing of the Rail Merger integration works, payments to the Company in respect of the Outsourcing Agreement and KSL Project Management Agreement, costs on certain capital works recoverable from KCRC in accordance with the Merger Framework Agreement as well as certain reimbursable expenditures of KCRC settled by the Company on KCRC's behalf.

The amount due from non-controlled subsidiaries is related to receivables from Octopus Holdings Limited, including the outstanding balance of a loan and the related interest which were fully settled in 2008 (note 26).

The amount due from associates as at 31 December 2008 includes the outstanding balance of loans, amounting to HK$28 million (GBP2.5 million) (2007: HK$62 million or GBP 4 million), to London Overground Rail Operations Ltd (note 52H(i)).

All contract retentions on the above entrusted works were due for release within one year. All other amounts due from the Government and other related parties were expected to be received within 12 months.

The nominal values of amounts due from the Government and other related parties are considered not significantly different from their fair values as the amounts due are expected to be substantially settled within 24 months.

37 Cash and Cash Equivalents

	The Group		The Company	
in HK$ million	**2008**	2007	**2008**	2007
Deposits with banks and other financial institutions	**104**	46	**104**	42
Cash at banks and on hand	**689**	530	**158**	142
Cash and cash equivalents in the balance sheet	**793**	576	**262**	184
Bank overdrafts (note 38A)	**(59)**	(2)	**(59)**	(2)
Cash and cash equivalents in the cash flow statement	**734**	574	**203**	182

During the year, the Group recognised deferred income and received properties in kind in respect of property development of HK$200 million (2007: HK$1,245 million), which did not involve movements of cash or cash equivalents.

37 Cash and Cash Equivalents *(continued)*

Included in cash and cash equivalents in the balance sheet are the following amounts denominated in a currency other than the functional currency of the entity to which they relate:

	The Group		The Company	
	2008	2007	**2008**	2007
Australian dollars (in thousand)	**974**	–	**501**	–
Euros (in million)	**4**	3	**4**	3
Japanese Yen (in million)	**221**	–	**221**	–
Pound sterling (in million)	**3**	1	**3**	1
New Taiwan dollars (in million)	**31**	38	**31**	38
Renminbi (in million)	**95**	197	**–**	–
United States dollars (in million)	**9**	7	**–**	–

38 Loans and Other Obligations

A By Type

The Group

	2008			2007		
in HK$ million	Carrying amount	Fair value	Repayable amount	Carrying amount	Fair value	Repayable amount
Capital market instruments						
Listed or publicly traded:						
US dollar Global notes due 2009	**5,730**	**5,851**	**5,834**	5,746	6,060	5,834
US dollar Global notes due 2010	**4,670**	**5,165**	**4,679**	4,649	5,126	4,679
Debt issuance programme (Eurobond due 2014)	**4,744**	**5,232**	**4,663**	4,580	4,790	4,663
	15,144	**16,248**	**15,176**	14,975	15,976	15,176
Unlisted:						
Debt issuance programme notes due 2008 to 2020	**8,647**	**9,563**	**8,347**	7,121	7,493	7,097
HK dollar notes due 2008	**–**	**–**	**–**	506	502	500
	8,647	**9,563**	**8,347**	7,627	7,995	7,597
Total capital market instruments	**23,791**	**25,811**	**23,523**	22,602	23,971	22,773
Bank loans	**5,496**	**5,500**	**5,487**	10,939	10,944	10,921
Others	**297**	**337**	**297**	–	–	–
Loans and others	**29,584**	**31,648**	**29,307**	33,541	34,915	33,694
Bank overdrafts	**59**	**59**	**59**	2	2	2
Short-term loans	**1,646**	**1,646**	**1,646**	507	507	507
Total	**31,289**	**33,353**	**31,012**	34,050	35,424	34,203

38 Loans and Other Obligations *(continued)*

A By Type *(continued)*

The Company

in HK$ million	2008 Carrying amount	2008 Fair value	2008 Repayable amount	2007 Carrying amount	2007 Fair value	2007 Repayable amount
Capital market instruments						
Listed or publicly traded:						
US dollar Global notes due 2009	**5,730**	**5,851**	**5,834**	5,746	6,060	5,834
US dollar Global notes due 2010	**4,670**	**5,165**	**4,679**	4,649	5,126	4,679
	10,400	**11,016**	**10,513**	10,395	11,186	10,513
Unlisted:						
Debt issuance programme notes due 2018	**435**	**703**	**482**	437	615	448
	435	**703**	**482**	437	615	448
Total capital market instruments	**10,835**	**11,719**	**10,995**	10,832	11,801	10,961
Bank loans	**5,496**	**5,500**	**5,487**	10,939	10,944	10,921
Others	**297**	**337**	**297**	–	–	–
Loans and others	**16,628**	**17,556**	**16,779**	21,771	22,745	21,882
Bank overdrafts	**59**	**59**	**59**	2	2	2
Short-term loans	**624**	**624**	**624**	186	186	186
Total	**17,311**	**18,239**	**17,462**	21,959	22,933	22,070

Others represent non-defeased obligations under lease out/lease back transaction (note 19E).

As at 31 December 2008, the Group had available undrawn committed bank loan facilities amounting to HK$10,400 million (2007: HK$6,300 million). In addition, the Group had a number of uncommitted facilities with undrawn amounts totalling HK$12,463 million (2007: HK$15,464 million), comprising a debt issuance programme and short-term bank loan facilities.

The fair values are based on the discounted cash flows method which discounts the future contractual cash flows at the current market interest and foreign exchange rates that is available to the Group for similar financial instruments.

The carrying amounts of short-term loans and overdrafts approximated their fair values.

The amounts of borrowings, denominated in a currency other than the functional currency of the entity to which they relate, before and after currency hedging activities are as follows:

The Group

	Before hedging activities 2008	Before hedging activities 2007	After hedging activities 2008	After hedging activities 2007
Euros (in million)	**6**	8	**–**	–
Pound sterling (in million)	**3**	4	**3**	4
Renminbi (in million)	**900**	300	**900**	300
United States dollars (in million)	**2,115**	2,117	**5**	6

The Company

	Before hedging activities 2008	Before hedging activities 2007	After hedging activities 2008	After hedging activities 2007
Euros (in million)	**6**	8	**6**	–
Pound sterling (in million)	**3**	4	**3**	4
United States dollars (in million)	**2,115**	1,417	**5**	6

38 Loans and Other Obligations *(continued)*

B. By Repayment Terms

The Group

in HK$ million	2008 Capital market instruments	2008 Bank loans and overdrafts	2008 Others	2008 Total	2007 Capital market instruments	2007 Bank loans and overdrafts	2007 Others	2007 Total
Long-term loans and others								
Amounts repayable beyond 5 years	7,878	–	297	8,175	10,008	–	–	10,008
Amounts repayable within a period of between 2 and 5 years	2,732	2,417	–	5,149	4,931	10,611	–	15,542
Amounts repayable within a period of between 1 and 2 years	6,079	3,035	–	9,114	6,834	155	–	6,989
Amounts repayable within 1 year	6,834	35	–	6,869	1,000	155	–	1,155
	23,523	5,487	297	29,307	22,773	10,921	–	33,694
Bank overdrafts	–	59	–	59	–	2	–	2
Short-term loans	–	1,646	–	1,646	–	507	–	507
	23,523	7,192	297	31,012	22,773	11,430	–	34,203
Less: Unamortised discount / premium / finance charges outstanding	(38)	(14)	–	(52)	(101)	(19)	–	(120)
Adjustment due to fair value change of financial instruments	306	23	–	329	(70)	37	–	(33)
Total carrying amount of debt	23,791	7,201	297	31,289	22,602	11,448	–	34,050

The Company

in HK$ million	2008 Capital market instruments	2008 Bank loans and overdrafts	2008 Others	2008 Total	2007 Capital market instruments	2007 Bank loans and overdrafts	2007 Others	2007 Total
Long-term loans and others								
Amounts repayable beyond 5 years	477	–	297	774	448	–	–	448
Amounts repayable within a period of between 2 and 5 years	5	2,417	–	2,422	4,679	10,611	–	15,290
Amounts repayable within a period of between 1 and 2 years	4,679	3,035	–	7,714	5,834	155	–	5,989
Amounts repayable within 1 year	5,834	35	–	5,869	–	155	–	155
	10,995	5,487	297	16,779	10,961	10,921	–	21,882
Bank overdrafts	–	59	–	59	–	2	–	2
Short-term loans	–	624	–	624	–	186	–	186
	10,995	6,170	297	17,462	10,961	11,109	–	22,070
Less: Unamortised discount / premium / finance charges outstanding	(19)	(14)	–	(33)	(37)	(19)	–	(56)
Adjustment due to fair value change of financial instruments	(141)	23	–	(118)	(92)	37	–	(55)
Total carrying amount of debt	10,835	6,179	297	17,311	10,832	11,127	–	21,959

The amounts repayable within 1 year in respect of capital market instruments and bank loans are included in long-term loans as these amounts are intended to be refinanced on a long-term basis.

38 Loans and Other Obligations *(continued)*

C Bonds and Notes Issued and Redeemed

Bonds and notes issued during the year ended 31 December 2008 and 2007 comprise:

The Group

in HK$ million	2008 Principal amount	2008 Net consideration received	2007 Principal amount	2007 Net consideration received
Debt issuance programme notes	**1,750**	**1,750**	–	–

The above notes were issued by a subsidiary, MTR Corporation (C.I.) Limited. The notes issued are unconditionally and irrevocably guaranteed by the Company; and are direct, unsecured, unconditional and unsubordinated to other unsecured and unsubordinated obligations of MTR Corporation (C.I.) Limited. The obligations of the Company under the guarantee are direct, unsecured, unconditional, and unsubordinated to other unsecured and unsubordinated obligations of the Company. The net proceeds received from the issues were on lent to the Company for general working capital, refinancing or other corporate purposes.

During the year ended 31 December 2008, the Group redeemed HK$1,000 million (2007: nil) of its unlisted debt securities.

None of the Group's listed debt securities was redeemed during the years ended 31 December 2008 and 2007.

D Guarantees and Pledges

(i) There were no guarantees given by the Government in respect of loan facilities as at 31 December 2008 and 2007.

(ii) As at 31 December 2008, certain assets held by MTR Corporation (Shenzhen) Limited, an indirect wholly owned subsidiary of the Company in the Mainland of China, were pledged as security for a RMB900 million short-term bank loan facility granted to it.

Apart from the above, none of the other Group's assets was charged or subject to any encumbrance as at 31 December 2008.

39 Creditors, Accrued Charges and Provisions

in HK$ million	The Group 2008	The Group 2007	The Company 2008	The Company 2007
Creditors, accrued charges and provisions				
– Airport Railway Project	**68**	70	**68**	70
– Tseung Kwan O Extension Project	**16**	120	**16**	120
– LOHAS Park Station Project	**31**	58	**31**	58
– West Island Line Project	**89**	2	**89**	2
– Property projects and management	**1,728**	1,776	**1,631**	1,675
– Railway operations and others	**3,346**	3,330	**2,775**	2,875
Gross amount due to customers for contract work	**56**	56	**56**	56
	5,334	5,412	**4,666**	4,856

The above amounts are mainly related to capital projects to be settled upon certification of work in progress and swap interest payable. The Group has no significant balances of trade creditors resulting from its provision of transportation services.

At 31 December 2008, the aggregate amount of costs incurred plus recognised profits less recognised losses included in the gross amount due to customers for contract works was HK$273 million (2007: HK$244 million).

The gross amount due to customers for contract work at 31 December 2008 that is expected to be settled after more than one year is HK$56 million (2007: HK$56 million).

39 Creditors, Accrued Charges and Provisions *(continued)*

The analysis of creditors included above by due dates is as follows:

in HK$ million	The Group 2008	The Group 2007	The Company 2008	The Company 2007
Due within 30 days or on demand	**1,188**	1,354	**800**	1,128
Due after 30 days but within 60 days	**927**	652	**864**	573
Due after 60 days but within 90 days	**234**	218	**224**	204
Due after 90 days	**1,392**	1,563	**1,249**	1,359
	3,741	3,787	**3,137**	3,264
Rental and other refundable deposits	**1,353**	1,462	**1,291**	1,429
Accrued employee benefits	**240**	163	**238**	163
Total	**5,334**	5,412	**4,666**	4,856

Creditors, accrued charges and provisions in respect of the capital projects and other construction works include provisions for claims on completed contracts, which were capitalised as part of the related assets. Most of these claims have been resolved and it is anticipated that, subject to unforeseen circumstances, the remaining amount required to be paid will be sufficiently covered by the above mentioned provisions of the respective projects. The carrying amounts of such claim provisions and their movements are not separately disclosed in view of their commercial sensitivity.

As at 31 December 2008, all creditors, accrued charges and provisions were expected to be settled within one year except for HK$852 million (2007: HK$920 million) included in the amounts relating to railway operations and others, which were expected to be settled after one year. The amounts due after one year are mainly rental deposits received from shop and station kiosk tenants and advance income received from telecommunication services operators, majority of which are due to be repaid within three years. The Group considers the effect of discounting these deposits would be immaterial.

The nominal values of creditors, accrued charges and provisions are not significantly different from their fair values.

Included in creditors, accrued charges and provisions are the following amounts denominated in a currency other than the functional currency of the entity to which they relate:

	The Group 2008	The Group 2007	The Company 2008	The Company 2007
Australian dollars (in thousand)	**1,660**	429	**1,660**	429
Euros (in million)	**5**	4	**5**	4
Japanese Yen (in million)	**100**	39	**100**	39
Pound sterling (in million)	**2**	1	**2**	1
Renminbi (in million)	**305**	202	**–**	–
Swedish krona (in thousand)	**933**	421	**933**	421
Swiss franc (in thousand)	**368**	216	**368**	216
United States dollars (in million)	**65**	53	**51**	38

40 Contract Retentions

The Group

in HK$ million	Due for release within 12 months	Due for release after 12 months	Total
2008			
Railway extension projects	**29**	**80**	**109**
Railway operations	**100**	**15**	**115**
	129	**95**	**224**
2007			
Railway extension projects	52	34	86
Railway operations	98	41	139
	150	75	225

The Company

in HK$ million	Due for release within 12 months	Due for release after 12 months	Total
2008			
Railway extension projects	**24**	**27**	**51**
Railway operations	**100**	**15**	**115**
	124	**42**	**166**
2007			
Railway extension projects	24	34	58
Railway operations	98	41	139
	122	75	197

The effect of discounting these contract retentions is considered immaterial as these amounts are substantially due to be released within 24 months.

Included in contract retentions are the following amounts denominated in a currency other than the functional currency of the entity to which they relate:

	The Group		The Company	
	2008	2007	**2008**	2007
Euros (in thousand)	**484**	337	**484**	337
Pound sterling (in thousand)	**39**	37	**39**	37
Renminbi (in million)	**52**	26	**–**	–
United States dollars (in million)	**2**	–	**2**	–

41 Amounts Due to Related Parties

	The Group		The Company	
in HK$ million	**2008**	2007	**2008**	2007
Amounts due to:				
– KCRC	**882**	975	**882**	975
– subsidiaries	**–**	–	**13,239**	11,987
	882	975	**14,121**	12,962

The amounts due to KCRC are related to mandatory payments and interest payable to KCRC in respect of the East Rail Line / Light Rail / Kowloon Southern Link property development sites as well as the accrued portion of the fixed annual payment for the service concession.

The amounts due to the subsidiaries as at 31 December 2008 of HK$11,956 million (2007: HK$10,763 million) are expected to be settled after one year.

The amounts due to the Company's subsidiaries include HK$13,156 million (2007: HK$11,960 million) due to MTR Corporation (C.I.) Limited in respect of proceeds from bonds and notes issued by the subsidiary, which were on-lent to the Company for its general corporate purposes with specified repayment dates and interest rates (note 38C), and accrued interest. These amounts are stated at their fair values. The remaining balances due to subsidiaries are non-interest bearing and have not been discounted as they do not have any fixed repayment terms and the amount is not material.

42 Obligations under Service Concession

As at 31 December 2008 and 2007, the Group and the Company had the following obligations under service concession in respect of the fixed annual payments for the Rail Merger (note 3):

in HK$ million	**2008**	2007
Balance as at 1 January	**10,685**	–
Total fixed annual payments capitalised at inception	**–**	10,687
Less: Amount repaid/payable during the year	**(29)**	(2)
Balance as at 31 December	**10,656**	10,685

The outstanding balances as at 31 December 2008 and 2007 are repayable as follows:

	2008			2007		
in HK$ million	Present value of fixed annual payments	Interest expense relating to future periods	Total fixed annual payments	Present value of fixed annual payments	Interest expense relating to future periods	Total fixed annual payments
Amounts repayable beyond 5 years	**10,480**	**22,457**	**32,937**	10,520	23,168	33,688
Amounts repayable within a period of between 2 and 5 years	**112**	**2,138**	**2,250**	105	2,145	2,250
Amounts repayable within a period of between 1 and 2 years	**33**	**717**	**750**	31	719	750
Amounts repayable within 1 year	**31**	**719**	**750**	29	721	750
	10,656	**26,031**	**36,687**	10,685	26,753	37,438

43 Deferred Income

The Group and The Company

in HK$ million	2008	2007
Deferred income on property development (note 23B)	**156**	400
Other deferred income (note 19E)	**–**	115
	156	515

44 Income Tax in the Balance Sheet

A Current taxation in the consolidated balance sheet comprised provision for Hong Kong Profits Tax for the Company and certain subsidiaries for the year ended 31 December 2008, chargeable at Hong Kong Profits Tax Rate at 16.5% (2007: 17.5%) and after netting off provisional tax paid, and overseas tax chargeable at the appropriate current tax rates of taxation ruling in the relevant countries.

	The Group		The Company	
in HK$ million	2008	2007	2008	2007
Provision for Hong Kong Profits Tax for the year (note 13)	**1,021**	1	**1,014**	–
Overseas tax for the year (note 13)	**3**	2	**1**	1
Hong Kong Provisional Profits Tax paid	**(575)**	–	**(574)**	–
	449	3	**441**	1
Balance of Profits Tax provision relating to prior years	**1**	–	**–**	–
	450	3	**441**	1

B Deferred tax assets and liabilities recognised

The components of deferred tax assets and liabilities recognised in the balance sheet and the movements during the year are as follows:

The Group

	Deferred tax arising from					
in HK$ million	Depreciation allowances in excess of related depreciation	Revaluation of properties	Provision and other temporary differences	Cash flow hedges	Tax losses	Total
2008						
At 1 January 2008	**8,809**	**4,126**	**215**	**(5)**	**(575)**	**12,570**
Effect on deferred tax balances resulting from a change in tax rate	**(503)**	**(235)**	**(12)**	**–**	**32**	**(718)**
Charged/(credited) to consolidated profit and loss account	**17**	**(24)**	**(98)**	**–**	**532**	**427**
Credited to reserves (note 46)	**–**	**(45)**	**–**	**(25)**	**–**	**(70)**
At 31 December 2008	**8,323**	**3,822**	**105**	**(30)**	**(11)**	**12,209**
2007						
At 1 January 2007	8,749	2,681	205	(2)	(2,181)	9,452
Addition through subsidiary acquisition	–	–	–	–	(2)	(2)
Charged to consolidated profit and loss account	60	1,402	10	–	1,608	3,080
Charged/(credited) to reserves (note 46)	–	43	–	(3)	–	40
At 31 December 2007	8,809	4,126	215	(5)	(575)	12,570

44 Income Tax in the Balance Sheet *(continued)*

The Company

in HK$ million	Deferred tax arising from: Depreciation allowances in excess of related depreciation	Revaluation of properties	Provision and other temporary differences	Cash flow hedges	Tax losses	Total
2008						
At 1 January 2008	**8,802**	**4,126**	**215**	**(5)**	**(564)**	**12,574**
Effect on deferred tax balances resulting from a change in tax rate	**(503)**	**(235)**	**(12)**	**–**	**32**	**(718)**
Charged/(credited) to profit and loss account	**16**	**(17)**	**(98)**	**–**	**532**	**433**
Credited to reserves (note 46)	**–**	**(45)**	**–**	**(25)**	**–**	**(70)**
At 31 December 2008	**8,315**	**3,829**	**105**	**(30)**	**–**	**12,219**
2007						
At 1 January 2007	8,743	2,681	205	(2)	(2,174)	9,453
Charged to profit and loss account	59	1,402	10	–	1,610	3,081
Charged/(credited) to reserves (note 46)	–	43	–	(3)	–	40
At 31 December 2007	8,802	4,126	215	(5)	(564)	12,574

	The Group		The Company	
in HK$ million	**2008**	2007	**2008**	2007
Net deferred tax asset recognised in the balance sheet	**(11)**	(4)	**–**	–
Net deferred tax liability recognised in the balance sheet	**12,220**	12,574	**12,219**	12,574
	12,209	12,570	**12,219**	12,574

C The Group has not recognised deferred tax assets in respect of some of its subsidiaries' cumulative tax losses of HK$227 million (2007: HK$217 million) as it is not probable that future taxable profits against which the losses can be utilised will be available in the relevant tax jurisdictions and entities.

45 Share Capital and Capital Management

A Share Capital, Share Premium and Capital Reserve

in HK$ million	**2008**	2007
Authorised:		
6,500,000,000 shares of HK$1.00 each	**6,500**	6,500
Issued and fully paid:		
5,661,143,113 shares (2007: 5,611,057,035 shares) of HK$1.00 each	**5,661**	5,611
Share premium	**8,270**	7,029
Capital reserve	**27,188**	27,188
	41,119	39,828

Pursuant to the Articles of Association of the Company, the capital reserve can only be applied in paying up in full unissued shares to be allotted and distributed as fully paid bonus shares to the shareholders of the Company.

Share premium represents the amount by which the issue price of shares exceeds the par value of those shares. The application of the share premium account is governed by section 48B of the Hong Kong Companies Ordinance.

45 Share Capital and Capital Management *(continued)*

A Share Capital, Share Premium and Capital Reserve *(continued)*

New shares issued and fully paid up during the year comprise:

	Number of shares	Option/ scrip price	Proceeds received / Transfer from employee share-based capital reserve: Share capital account	Share premium account	Total
		HK$	HK$ million	HK$ million	HK$ million
Employee share options exercised					
– Pre-Global Offering Share Option Scheme	**1,644,500**	**8.440**	**2**	**12**	**14**
– New Joiners Share Option Scheme	**31,500**	**15.450**	**–**	**1**	**1**
	45,000	**15.970**	**–**	**1**	**1**
	31,500	**18.300**	**–**	**1**	**1**
	355,500	**19.404**	**–**	**8**	**8**
	30,000	**20.660**	**–**	**1**	**1**
	142,000	**21.000**	**–**	**3**	**3**
Issued as 2007 final scrip dividends	**32,071,954**	**27.070**	**32**	**836**	**868**
Issued as 2008 interim scrip dividends	**15,734,124**	**25.020**	**16**	**378**	**394**
	50,086,078		**50**	**1,241**	**1,291**

An analysis of the Company's outstanding share options as at 31 December 2008 are disclosed in note 47.

B Capital Management

The Group's primary objectives in managing capital are to safeguard its ability to continue as a going concern, and to generate sufficient profit to maintain growth and provide an adequate return to its shareholders.

The Group manages the amount of capital in proportion to risk, and makes adjustments to its capital structure through the amount of dividend payment to shareholders, issuance of scrip and new shares, and managing its debt portfolio in conjunction with projected financing requirement. The Financial Secretary Incorporated of the Government of the Hong Kong SAR is the majority shareholder of the Company holding 4,344,710,490 shares as of 31 December 2008, representing 76.7% of total equity interest in the Company.

The Group monitors capital on the basis of the net debt-to-equity ratio, which is calculated on net borrowings as a percentage of the total equity attributable to shareholders of the Company where net borrowings are represented by the aggregate of loans, obligations under finance leases, bank overdrafts and obligations under service concession net of cash and cash equivalents. The Group's net debt-to-equity ratios over the past years have been trending downward in general, from approximately 60% at 31 December 2002 to 36% at 31 December 2006. Owing to the increase in borrowings to finance payments for the Rail Merger and the incorporation of the obligations under service concession as a component of debt, the ratio rose to 49% at 31 December 2007 and reverted to a downward trend to 42% at 31 December 2008.

Neither the Company nor any of its subsidiaries are subject to externally imposed capital requirements.

46 Other Reserves

The Group

in HK$ million	Fixed asset revaluation reserve	Hedging reserve	Employee share-based capital reserve	Exchange reserve	Retained profits	Total
	Attributable to equity shareholders of the Company					
2008						
Balance as at 1 January 2008	**1,170**	**(25)**	**7**	**42**	**49,992**	**51,186**
Cash flow hedges:						
Effective portion of changes in fair value, net of deferred tax	**–**	**(151)**	**–**	**–**	**–**	**(151)**
Transfer from equity						
– to consolidated profit and loss account	**–**	**41**	**–**	**–**	**–**	**41**
– to initial carrying amount of non-financial hedged items	**–**	**(14)**	**–**	**–**	**–**	**(14)**
– to deferred tax	**–**	**(5)**	**–**	**–**	**–**	**(5)**
2007 final dividend	**–**	**–**	**–**	**–**	**(1,740)**	**(1,740)**
2008 interim dividend	**–**	**–**	**–**	**–**	**(790)**	**(790)**
Deficit on revaluation, net of deferred tax (notes 19 and 44)	**(189)**	**–**	**–**	**–**	**–**	**(189)**
Release of revaluation reserve on disposal, net of deferred tax (note 44)	**(35)**	**–**	**–**	**–**	**42**	**7**
Effect on deferred tax balances resulting from a change in tax rate	**14**	**–**	**–**	**–**	**–**	**14**
Employee share-based payments	**–**	**–**	**20**	**–**	**–**	**20**
Release to share premium upon share options exercised	**–**	**–**	**(2)**	**–**	**–**	**(2)**
Exchange difference on translation of accounts of overseas subsidiaries	**–**	**–**	**–**	**21**	**–**	**21**
Profit for the year	**–**	**–**	**–**	**–**	**8,284**	**8,284**
Balance as at 31 December 2008	**960**	**(154)**	**25**	**63**	**55,788**	**56,682**
2007						
Balance as at 1 January 2007	968	(10)	5	17	37,148	38,128
Cash flow hedges:						
Effective portion of changes in fair value, net of deferred tax	–	(13)	–	–	–	(13)
Transfer from equity						
– to consolidated profit and loss account	–	–	–	–	–	–
– to initial carrying amount of non-financial hedged items	–	(2)	–	–	–	(2)
– to deferred tax	–	–	–	–	–	–
2006 final dividend	–	–	–	–	(1,554)	(1,554)
2007 interim dividend	–	–	–	–	(782)	(782)
Surplus on revaluation, net of deferred tax (notes 19 and 44)	202	–	–	–	–	202
Employee share-based payments	–	–	2	–	–	2
Exchange difference on translation of accounts of overseas subsidiaries	–	–	–	25	–	25
Profit for the year	–	–	–	–	15,180	15,180
Balance as at 31 December 2007	1,170	(25)	7	42	49,992	51,186

46 Other Reserves *(continued)*

The Company

in HK$ million	Fixed asset revaluation reserve	Hedging reserve	Employee share-based capital reserve	Retained profits	Total
2008					
Balance as at 1 January 2008	**1,170**	**(25)**	**7**	**49,349**	**50,501**
Cash flow hedges:					
Effective portion of changes in fair value, net of deferred tax	**–**	**(151)**	**–**	**–**	**(151)**
Transfer from equity					
– to profit and loss account	**–**	**41**	**–**	**–**	**41**
– to initial carrying amount of non-financial hedged items	**–**	**(14)**	**–**	**–**	**(14)**
– to deferred tax	**–**	**(5)**	**–**	**–**	**(5)**
2007 final dividend	**–**	**–**	**–**	**(1,740)**	**(1,740)**
2008 interim dividend	**–**	**–**	**–**	**(790)**	**(790)**
Deficit on revaluation, net of deferred tax (notes 19 and 44)	**(189)**	**–**	**–**	**–**	**(189)**
Release of revaluation reserve on disposal, net of deferred tax (note 44)	**(35)**	**–**	**–**	**42**	**7**
Effect on deferred tax balances resulting from a change in tax rate	**14**	**–**	**–**	**–**	**14**
Employee share-based payments	**–**	**–**	**20**	**–**	**20**
Release to share premium upon share options exercised	**–**	**–**	**(2)**	**–**	**(2)**
Profit for the year	**–**	**–**	**–**	**8,118**	**8,118**
Balance as at 31 December 2008	**960**	**(154)**	**25**	**54,979**	**55,810**
2007					
Balance as at 1 January 2007	968	(10)	5	36,802	37,765
Cash flow hedges:					
Effective portion of changes in fair value, net of deferred tax	–	(13)	–	–	(13)
Transfer from equity					
– to profit and loss account	–	–	–	–	–
– to initial carrying amount of non-financial hedged items	–	(2)	–	–	(2)
– to deferred tax	–	–	–	–	–
2006 final dividend	–	–	–	(1,554)	(1,554)
2007 interim dividend	–	–	–	(782)	(782)
Surplus on revaluation, net of deferred tax (notes 19 and 44)	202	–	–	–	202
Employee share-based payments	–	–	2	–	2
Profit for the year	–	–	–	14,883	14,883
Balance as at 31 December 2007	1,170	(25)	7	49,349	50,501

The fixed asset revaluation reserve was set up to deal with the surpluses or deficits arising from the revaluation of self-occupied land and buildings (note 2F(ii)).

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

The employee share-based capital reserve comprises the fair value of share options granted which are yet to be exercised, as explained in accounting policy under note 2V(iv). The amount will either be transferred to the share premium account when the option is exercised, or be released directly to retained profits if the option is expired or forfeited.

46 Other Reserves *(continued)*

The exchange reserve comprises all foreign exchange differences arising from the translation of the accounts of foreign enterprises. The reserve is dealt with in accordance with the accounting policy set out in note 2DD.

Apart from retained profits, the other reserves are not available for distribution to shareholders because they do not constitute realised profits. In addition, the Company considers the cumulative surpluses on revaluation of investment properties, net of tax of HK$18,417 million (2007: HK$18,280 million) included in retained profits are non-distributable as they also do not constitute realised profits. As at 31 December 2008, the Company considers that the total amount of reserves available for distribution to equity shareholders amounted to HK$36,562 million (2007: HK$31,069 million).

Included in the Group's retained profits as at 31 December 2008 is an amount of HK$328 million (2007: HK$192 million), being the retained profits attributable to the non-controlled subsidiaries and associates.

47 Share-based Payments

A Equity-settled Share-based Payments

The Group granted equity-settled share options to its Members of the Executive Directorate and certain employees under three share option schemes namely, the Pre-Global Offering Share Option Scheme, the New Joiners Share Option Scheme and the 2007 Share Option Scheme. Details of the schemes are as follows:

(i) Pre-Global Offering Share Option Scheme

In connection with the Initial Public Offering ("IPO") and Stock Exchange listing of the Company's shares in October 2000, a Pre-Global Offering Share Option Scheme ("Pre-IPO Option Scheme") was established. Under the Pre-IPO Option Scheme, a total of 769 employees including all the Members of the Executive Directorate, except C K Chow, Lincoln K K Leong and Francois K K Lung who were appointed on 1 December 2003, 1 February 2002 and 26 September 2005 respectively, were granted on 20 September 2000 options to purchase an aggregate of 48,338,000 shares, representing 0.9% of the issued share capital of the Company as at 31 December 2008. The options carry an exercise price of HK$8.44 per share, which was equivalent to 90% of the IPO offer price of HK$9.38 per share. The options may be exercised prior to 11 September 2010, subject to the vesting provisions under the Scheme. As of 31 December 2008, all options granted under the Pre-IPO Option Scheme have vested.

In 2008, a total of 1,644,500 previously vested share options have been exercised. The weighted average closing price in respect of the share options exercised during the year was HK$25.159 per share. In addition, 17,000 share options lapsed as a result of resignation of option holders during the year. As at 31 December 2008, total options to subscribe for 3,605,500 (2007: 5,267,000) shares remained outstanding.

(ii) New Joiners Share Option Scheme

In May 2002, the New Joiners Share Option Scheme (the "New Option Scheme") was adopted at the 2002 Annual General Meeting to provide share options to new members of the top and senior management of the Company who did not participate in the Pre-IPO Option Scheme. Under the Rules of the New Option Scheme, a maximum of 5,056,431 shares, which represent 0.1% of the issued share capital of the Company as at 31 December 2008, may be issued pursuant to the exercise of options granted under the New Option Scheme. Options granted will be evenly vested in respect of their underlying shares over a period of three years from the date on which the relevant option is offered. The exercise price of any option granted under the New Option Scheme is to be determined by the Company upon the offer of grant of the option and which should not be less than the greatest of (i) the average closing price of an MTR share for the five business days immediately preceding the day of offer of such option; (ii) the closing price of an MTR share on the day of offer of such option, which must be a business day; and (iii) the nominal value of an MTR share. The New Option Scheme expired on 16 May 2007 and no options can be granted under this Scheme on or after that date.

The following table summarises the outstanding share options granted under the New Option Scheme since inception:

Date of grant	Number of share options	Exercise price HK$	Exercisable period
1 August 2003	1,245,200	9.75	on or prior to 14 July 2013
13 September 2005	49,000	15.97	on or prior to 9 September 2015
23 September 2005	213,000	15.97	on or prior to 9 September 2015
31 March 2006	94,000	18.05	on or prior to 20 March 2016
12 May 2006	266,500	20.66	on or prior to 25 April 2016
15 May 2006	183,000	20.66	on or prior to 25 April 2016
5 October 2006	94,000	19.732	on or prior to 29 September 2016
22 March 2007	355,500	19.404	on or prior to 19 March 2017

47 Share-based Payments *(continued)*

A Equity-settled Share-based Payments *(continued)*

Movements in the number of share options outstanding and their related weighted average exercise prices were as follows:

	2008		2007	
	Number of options	Weighted average exercise price HK$	Number of options	Weighted average exercise price HK$
Outstanding at 1 January	**3,717,700**	**16.017**	2,780,700	14.598
Granted during the year	**–**	**–**	1,066,000	19.404
Exercised during the year	**(635,500)**	**19.326**	(129,000)	13.426
Lapsed during the year	**(582,000)**	**19.237**	–	–
Outstanding at 31 December	**2,500,200**	**14.426**	3,717,700	16.017
Exercisable at 31 December	**2,278,700**	**13.865**	1,775,700	12.377

The weighted average closing price in respect of the share options exercised during the year was HK$27.985 (2007: HK$22.80).

Share options outstanding at 31 December 2008 had the following exercise prices and remaining contractual lives:

	2008		2007	
Exercise price	Number of options	Remaining contractual life years	Number of options	Remaining contractual life years
HK$9.75	**1,245,200**	**4.54**	1,245,200	5.54
HK$15.97	**262,000**	**6.69**	307,000	7.69
HK$15.45	**–**	**–**	62,500	8.02
HK$18.05	**94,000**	**7.22**	94,000	8.22
HK$20.66	**449,500**	**7.32**	479,500	8.32
HK$21.00	**–**	**–**	213,000	8.34
HK$18.30	**–**	**–**	94,000	8.47
HK$19.732	**94,000**	**7.75**	94,000	8.75
HK$19.104	**–**	**–**	62,500	8.87
HK$19.404	**355,500**	**8.22**	1,066,000	9.22
	2,500,200		3,717,700	

(iii) 2007 Share Option Scheme

Following the expiry of the New Option Scheme in May 2007, the 2007 Share Option Scheme (the "2007 Option Scheme") was submitted and approved at the 2007 Annual General Meeting to enhance the Company's ability to attract the best available personnel, to retain and motivate critical and key employees, to align their interest to the long-term success of the Company and to provide them with fair and market competitive remuneration. Under the Rules of the 2007 Option Scheme, a maximum of 277,461,072 shares, which represent 4.9% of the issued share capital of the Company as at 31 December 2008, may be issued pursuant to the exercise of options granted after 7 June 2007 under all share option schemes of the Company including the 2007 Option Scheme. Options granted will be vested in respect of their underlying shares not less than 1 year from the date on which the relevant option is offered. The exercise price of any option granted under the 2007 Option Scheme is to be determined by the Company upon the offer of grant of the option and which should not be less than the greatest of (i) the average closing price of an MTR share for the five business days immediately preceding the day of offer of such option; (ii) the closing price of an MTR share on the day of offer of such option, which must be a business day; and (iii) the nominal value of an MTR share.

Subject to the rules of the 2007 Option Scheme, the Company may from time to time during the scheme period, at its absolute discretion, offer to grant share options to any eligible employees. Under the 2007 Option Scheme, the date of grant is defined as the date of acceptance of the offer to grant the option. On 10 December 2007, share options in respect of 8,273,000 shares were offered to Members of the Executive Directorate and selected employees of the Company as the first tranche of the share option awards for 2008 (the "First 2008 Award"). For the First 2008 Award, share options in respect of 7,968,000 shares were accepted by the grantees during the period from 11 December 2007 to 31 December 2007 and share options in respect of 305,000 shares were accepted by the grantees during the period from 2 January 2008 to 7 January 2008. On 26 March 2008, share options in respect of 2,749,000 shares were offered to selected employees of the Company and were accepted by the grantees during the period from 28 March 2008 to 23 April 2008, as the second tranche of the share option awards for 2008. This award, together with the First 2008 Award, forms the "2008 Award". On 8 December 2008, share options in respect of 12,712,000 shares were offered to Members of the Executive Directorate and other selected employees of the Company and were accepted by the grantees during the period from 8 December 2008 to 30 December 2008, as share option awards for 2009 (the "2009 Award").

47 Share-based Payments *(continued)*

A Equity-settled Share-based Payments *(continued)*

The following table summarises the outstanding share options granted under the 2007 Option Scheme since inception.

Date of grant	Number of share options	Exercise price HK$	Exercisable period
2008 Award			
11 December 2007	45,000	27.60	on or prior to 10 December 2014
12 December 2007	2,642,000	27.60	on or prior to 10 December 2014
13 December 2007	1,805,000	27.60	on or prior to 10 December 2014
14 December 2007	1,005,000	27.60	on or prior to 10 December 2014
15 December 2007	370,000	27.60	on or prior to 10 December 2014
17 December 2007	835,000	27.60	on or prior to 10 December 2014
18 December 2007	380,000	27.60	on or prior to 10 December 2014
19 December 2007	115,000	27.60	on or prior to 10 December 2014
20 December 2007	190,000	27.60	on or prior to 10 December 2014
21 December 2007	45,000	27.60	on or prior to 10 December 2014
22 December 2007	35,000	27.60	on or prior to 10 December 2014
24 December 2007	118,000	27.60	on or prior to 10 December 2014
28 December 2007	35,000	27.60	on or prior to 10 December 2014
31 December 2007	130,000	27.60	on or prior to 10 December 2014
2 January 2008	75,000	27.60	on or prior to 10 December 2014
3 January 2008	40,000	27.60	on or prior to 10 December 2014
4 January 2008	65,000	27.60	on or prior to 10 December 2014
7 January 2008	125,000	27.60	on or prior to 10 December 2014
28 March 2008	255,000	26.52	on or prior to 26 March 2015
31 March 2008	379,000	26.52	on or prior to 26 March 2015
1 April 2008	261,000	26.52	on or prior to 26 March 2015
2 April 2008	296,000	26.52	on or prior to 26 March 2015
3 April 2008	171,000	26.52	on or prior to 26 March 2015
4 April 2008	23,000	26.52	on or prior to 26 March 2015
5 April 2008	17,000	26.52	on or prior to 26 March 2015
7 April 2008	358,000	26.52	on or prior to 26 March 2015
8 April 2008	155,000	26.52	on or prior to 26 March 2015
9 April 2008	85,000	26.52	on or prior to 26 March 2015
10 April 2008	58,000	26.52	on or prior to 26 March 2015
11 April 2008	117,000	26.52	on or prior to 26 March 2015
12 April 2008	48,000	26.52	on or prior to 26 March 2015
14 April 2008	40,000	26.52	on or prior to 26 March 2015
15 April 2008	34,000	26.52	on or prior to 26 March 2015
16 April 2008	40,000	26.52	on or prior to 26 March 2015
17 April 2008	124,000	26.52	on or prior to 26 March 2015
18 April 2008	32,000	26.52	on or prior to 26 March 2015
19 April 2008	25,000	26.52	on or prior to 26 March 2015
20 April 2008	23,000	26.52	on or prior to 26 March 2015
21 April 2008	66,000	26.52	on or prior to 26 March 2015
23 April 2008	19,000	26.52	on or prior to 26 March 2015
2009 Award			
8 December 2008	155,000	18.30	on or prior to 8 December 2015
9 December 2008	1,463,000	18.30	on or prior to 8 December 2015
10 December 2008	2,176,400	18.30	on or prior to 8 December 2015
11 December 2008	2,464,200	18.30	on or prior to 8 December 2015
12 December 2008	1,481,500	18.30	on or prior to 8 December 2015
13 December 2008	84,500	18.30	on or prior to 8 December 2015
14 December 2008	88,200	18.30	on or prior to 8 December 2015
15 December 2008	1,084,700	18.30	on or prior to 8 December 2015
16 December 2008	581,500	18.30	on or prior to 8 December 2015
17 December 2008	513,500	18.30	on or prior to 8 December 2015
18 December 2008	611,500	18.30	on or prior to 8 December 2015
19 December 2008	198,000	18.30	on or prior to 8 December 2015
20 December 2008	19,000	18.30	on or prior to 8 December 2015
22 December 2008	772,500	18.30	on or prior to 8 December 2015
23 December 2008	306,000	18.30	on or prior to 8 December 2015
24 December 2008	500,500	18.30	on or prior to 8 December 2015
25 December 2008	45,000	18.30	on or prior to 8 December 2015
29 December 2008	148,000	18.30	on or prior to 8 December 2015
30 December 2008	19,000	18.30	on or prior to 8 December 2015

47 Share-based Payments *(continued)*

A Equity-settled Share-based Payments *(continued)*

Movements in the number of share options outstanding and their related weighted average exercise prices were as follows:

	2008		2007	
	Number of options	Weighted average exercise price HK$	Number of options	Weighted average exercise price HK$
Outstanding at 1 January	**7,968,000**	**27.600**	–	–
Granted during the year	**15,766,000**	**19.913**	7,968,000	27.600
Exercised during the year	**–**	**–**	–	–
Lapsed during the year	**(341,000)**	**27.210**	–	–
Outstanding at 31 December	**23,393,000**	**22.425**	7,968,000	27.600
Exercisable at 31 December	**2,811,000**	**27.600**	–	–

Share options outstanding at 31 December 2008 had the following exercise prices and remaining contractual lives:

	2008		2007	
Exercise price	Number of options	Remaining contractual life years	Number of options	Remaining contractual life years
HK$27.60	**8,055,000**	**6**	7,968,000	7
HK$26.52	**2,626,000**	**6**	–	–
HK$18.30	**12,712,000**	**7**	–	–
	23,393,000		7,968,000	

47 Share-based Payments *(continued)*

A Equity-settled Share-based Payments *(continued)*

According to the Black-Scholes pricing model, the fair values of options granted during the year ended 31 December 2008 were as follows:

		Inputs into the Black-Scholes pricing model					
Date of grant	Fair value of options granted	Share price immediately before grant date	Exercise price	Expected volatility	Expected life	Risk-free interest rate	Expected dividend per share
	HK$	HK$	HK$		years	%	HK$
2 January 2008	5.49	28.70	27.60	0.22	3.5	2.82	0.45
3 January 2008	6.88	30.80	27.60	0.22	3.5	2.71	0.45
4 January 2008	7.65	31.80	27.60	0.22	3.5	2.77	0.45
7 January 2008	7.79	32.00	27.60	0.22	3.5	2.77	0.45
28 March 2008	3.80	25.90	26.52	0.22	3.5	1.69	0.45
31 March 2008	3.90	26.10	26.52	0.22	3.5	1.68	0.45
1 April 2008	4.39	26.70	26.52	0.23	3.5	1.66	0.45
2 April 2008	4.42	26.70	26.52	0.23	3.5	1.75	0.45
3 April 2008	4.84	27.35	26.52	0.23	3.5	1.83	0.45
4 April 2008	4.78	27.25	26.52	0.23	3.5	1.83	0.45
5 April 2008	4.78	27.25	26.52	0.23	3.5	1.83	0.45
7 April 2008	4.76	27.25	26.52	0.23	3.5	1.79	0.45
8 April 2008	4.69	27.10	26.52	0.23	3.5	1.84	0.45
9 April 2008	4.72	27.20	26.52	0.23	3.5	1.76	0.45
10 April 2008	4.49	26.90	26.52	0.23	3.5	1.65	0.45
11 April 2008	4.52	26.90	26.52	0.23	3.5	1.72	0.45
12 April 2008	4.63	27.10	26.52	0.23	3.5	1.72	0.45
14 April 2008	4.60	27.10	26.52	0.23	3.5	1.65	0.45
15 April 2008	4.37	26.65	26.52	0.23	3.5	1.74	0.45
16 April 2008	4.63	27.05	26.52	0.23	3.5	1.81	0.45
17 April 2008	4.42	26.65	26.52	0.23	3.5	1.88	0.45
18 April 2008	4.52	26.80	26.52	0.23	3.5	1.91	0.45
19 April 2008	4.54	26.85	26.52	0.23	3.5	1.91	0.45
20 April 2008	4.54	26.85	26.52	0.23	3.5	1.91	0.45
21 April 2008	4.54	26.85	26.52	0.23	3.5	1.91	0.45
23 April 2008	4.88	27.35	26.52	0.23	3.5	1.99	0.45
8 December 2008	2.31	16.90	18.30	0.27	3.5	1.35	0.45
9 December 2008	3.03	18.30	18.30	0.27	3.5	1.28	0.45
10 December 2008	2.87	18.02	18.30	0.27	3.5	1.26	0.45
11 December 2008	3.41	18.98	18.30	0.27	3.5	1.22	0.45
12 December 2008	3.22	18.68	18.30	0.27	3.5	1.17	0.45
13 December 2008	2.84	18.00	18.30	0.27	3.5	1.17	0.45
14 December 2008	2.84	18.00	18.30	0.27	3.5	1.17	0.45
15 December 2008	2.84	18.00	18.30	0.27	3.5	1.20	0.45
16 December 2008	3.12	18.50	18.30	0.27	3.5	1.21	0.45
17 December 2008	3.07	18.48	18.30	0.27	3.5	1.04	0.45
18 December 2008	3.32	18.90	18.30	0.27	3.5	1.05	0.45
19 December 2008	3.40	19.06	18.30	0.27	3.5	1.01	0.45
20 December 2008	3.00	18.36	18.30	0.27	3.5	1.01	0.45
22 December 2008	2.99	18.36	18.30	0.27	3.5	0.99	0.45
23 December 2008	2.72	17.86	18.30	0.27	3.5	1.01	0.45
24 December 2008	2.60	17.64	18.30	0.27	3.5	0.98	0.45
25 December 2008	2.77	17.96	18.30	0.27	3.5	0.98	0.45
29 December 2008	2.76	17.96	18.30	0.27	3.5	0.97	0.45
30 December 2008	2.86	18.16	18.30	0.27	3.5	0.92	0.45

When computing fair values of the options granted, expected volatility was determined by calculating the historical volatility of the Group's share price over the previous 3.5 years and the expected life adopted was assumed to be 3.5 years after granting of the options, with expected dividends based on historical dividends. In addition, vesting terms under the grants have been taken into account whilst no market conditions associated with the share option grants have been considered. Changes in the subjective input assumptions could materially affect the fair value estimate.

47 Share-based Payments *(continued)*

A Equity-settled Share-based Payments *(continued)*

(iv) During the year, the equity-settled share-based payments recognised in respect of the above share option schemes were as follows:

in HK$ million	2008	2007
Equity-settled share-based payments in respect of:		
– New Option Scheme	**3**	1
– 2007 Option Scheme	**17**	1
	20	2

B Cash-settled Share-based Payments

(i) C K Chow did not participate in the Company's Pre-Global Offering Share Option Scheme and New Joiners Share Option Scheme. Pursuant to his three-year contract expiring on 30 November 2009, he is entitled to receive an equivalent value in cash of 418,017 shares in the Company on completion of this contract. As at 31 December 2008, an amount of HK$0.9 million (2007: HK$4.1 million) has been recorded as share-based payment expense for the year. Fair value of the outstanding entitlement is calculated based on the closing price of the Company's shares at year-end date. As at 31 December 2008, the fair value of these shares was HK$17.96 per share (2007: HK$28.70).

(ii) Lincoln K K Leong has a derivative interest in the Company's shares, which entitled him to receive an equivalent value in cash of 160,000 shares in the Company on 9 April 2010. As at 31 December 2008, an amount of HK$0.5 million (2007: HK$1.1 million) has been recorded as share-based payment expense for the year, measured at the same basis as described in note 47B(i) above.

48 Retirement Schemes

The Company operates two occupational retirement schemes, the MTR Corporation Limited Retirement Scheme (the "Retirement Scheme") and a top-up scheme, the MTR Corporation Limited Retention Bonus Scheme (the "RBS"). In addition, in accordance with the Mandatory Provident Fund ("MPF") Schemes Ordinance, the Company has set up an MPF scheme (the "MTR MPF Scheme") on 1 December 2000 by participating in a master trust scheme provided by an independent MPF service provider. Eligible employees could choose between the Retirement Scheme and the MTR MPF Scheme while temporary employees are required to join the MTR MPF Scheme.

Following the Rail Merger on 2 December 2007, the Company has assumed the operations of KCRC's two retirement schemes. One was a defined contribution scheme namely the Kowloon-Canton Railway Corporation Retirement Benefit Scheme (the "KCR Scheme"), which was renamed as the MTR Corporation Limited Provident Fund Scheme (the "Provident Fund Scheme") on 1 March 2008. The other was a MPF scheme ("KCR MPF Scheme") for employees who did not opt for or who were not eligible for the KCR Scheme.

Currently, new eligible employees can choose between the Provident Fund Scheme and the MTR MPF Scheme while temporary employees are required to join the MTR MPF Scheme.

The assets of these schemes are held under the terms of separate trust arrangements so that the assets are kept separate from those of the Company.

A The Retirement Scheme

The Retirement Scheme was established under trust at the beginning of 1977 containing both defined benefit and defined contribution elements. The Retirement Scheme was registered under the Occupational Retirement Schemes Ordinance (Chapter 426 of the Laws of Hong Kong) ("ORSO") with effect from 31 October 1994. On 3 July 2000, exemption was granted by the MPF Authority to maintain the Retirement Scheme and offer it as an alternative to the MPF Scheme.

The Retirement Scheme offers benefits on retirement, permanent disability, death and leaving service to its members. The hybrid benefit section of the Retirement Scheme provides benefits based on the greater of a multiple of final salary and accumulated contributions with investment returns. This section has been closed to new entrants since 31 March 1999. Before 1 March 2008, the Retirement Scheme used to contain a defined contribution section, a member choice plan provided to non-temporary employees who were hired on or after 1 April 1999 with benefits based on accumulated contributions and investment returns only. On 1 March 2008, the members and assets of the defined contribution section were transferred to the Provident Fund Scheme and the defined contribution section ceased to exist.

Given that the defined contribution benefit section was transferred to the Provident Fund Scheme, commencing 1 March 2008 (note 48E), promotees and new entrants can choose to join either the Provident Fund Scheme or the MTR MPF Scheme.

Members' contributions to the hybrid benefit section are based on a fixed percentage of basic salary. The Company's contributions are determined by the Executive Directorate with reference to an actuarial valuation. As at 31 December 2008, the total membership was 5,406 (2007: 5,655). In 2008, members contributed HK$68 million (2007: HK$66 million) and the Company contributed HK$152 million (2007: HK$152 million) to the hybrid benefit section. The net asset value of the hybrid benefit section as at 31 December 2008 was HK$6,162 million (2007: HK$7,929 million).

48 Retirement Schemes *(continued)*

A The Retirement Scheme *(continued)*

According to the terms of the trust deed, forfeitures were transferred to the reserve account to be utilised at the discretion of the Company.

Actuarial valuations are carried out annually in accordance with the ORSO. A full actuarial valuation of the Retirement Scheme was carried out as at 31 December 2008 by Towers, Perrin, Forster & Crosby, Inc., an independent firm of consulting actuaries, using the Attained Age Method. The principal actuarial assumptions used included a long-term rate of investment return net of salary increases of 2.5% (2007: 2.0%) per annum, together with appropriate allowances for expected rates of mortality, turnover, redundancy and retirement and an adjustment for salary increases expected over the short term. The actuary confirmed that, as at the valuation date:

(a) the Retirement Scheme was solvent, with assets more than adequate to cover the aggregate value of members' vested benefits had all members left the Retirement Scheme; and

(b) on the assumption that the Retirement Scheme continued in force, the aggregate past service liability was almost fully funded at 99.9% by the value of the assets.

B RBS

The RBS was established under trust as of 1 January 1995. It is a defined benefit scheme and applies to all employees classified by the Company as staff working on designated projects and who are not on gratuity terms. The RBS provides for benefits to be payable only in the event of redundancy for accrued service accrued up to 31 December 2002. The RBS was registered under the ORSO with effect from 1 December 1995. As at 31 December 2008, there were 327 members (2007: 346).

The RBS is non-contributory for members. The Company's contributions are determined by the Executive Directorate with reference to an actuarial valuation and are charged as part of the staff costs to various projects on the basis of the amount contributed. During 2007 and 2008, the Company was not required to make any contribution to the RBS. The net asset value of the RBS as at 31 December 2008 was HK$12 million (2007: HK$12 million).

Actuarial valuations are carried out annually. A full actuarial valuation of the RBS was carried out as at 31 December 2008 by Towers, Perrin, Forster & Crosby, Inc. using the Attained Age Method. The principal actuarial assumptions used included an expected weighted rate of investment return net of salary increases, of approximately -1.7% (2007: -2.0%) per annum, together with appropriate allowance for expected rates of redundancy. The actuary confirmed that, as at the valuation date:

(a) due to the nature of the RBS which provides for benefits only on redundancy, there was no aggregate vested liability, and thus the RBS was technically solvent; and

(b) on the assumption that the RBS continued in force, the value of assets was more than sufficient to cover the aggregate past service liability.

C MTR MPF Scheme

Effective from the MPF commencement date of 1 December 2000, the Company joined The Bank Consortium MPF Plan which has been registered with the Mandatory Provident Fund Schemes Authority and authorised by the Securities and Futures Commission. As at 31 December 2008, the total number of employees of the Company participating in the MTR MPF Scheme was 1,337 (2007: 885). In 2008, total members' contributions were HK$5.3 million (2007: HK$3.9 million) and total contribution from the Company was HK$6.3 million (2007: HK$4.5 million).

D KCR MPF Scheme

The KCR MPF Scheme is operated under the Hong Kong Mandatory Provident Fund Schemes Ordinance. It is a defined contribution retirement plan administered by independent trustees. The KCR MPF Scheme was introduced on 1 April 2000 to employees who did not opt for or who were not eligible for the KCR Scheme. On the Appointed Day, the KCR MPF Scheme was closed to new entrants.

As at 31 December 2008, the total number of employees of the Company participating in the KCR MPF Scheme was 1,029 (2007: 2,578). In 2008, total members' contributions were HK$10 million (2007: HK$1.9 million since the Appointed Day) and total contribution from the Company was HK$10.7 million (2007: HK$1.9 million since the Appointed Day).

E The Provident Fund Scheme

The Provident Fund Scheme (previously the KCR Scheme) is a defined contribution scheme which was established on 1 February 1983 under trust. The Provident Fund Scheme was registered under the ORSO with effect from 16 November 1994.

All benefits payable under the Provident Fund Scheme are calculated by reference to the employer's contributions and members' own contributions, based on fixed percentages of members' basic salaries, together with investment returns on these contributions.

On 1 March 2008, the defined contribution section of the Retirement Scheme was transferred to the KCR Scheme, which was subsequently renamed as the MTR Corporation Limited Provident Fund Scheme. As at 31 December 2008, the total number of employees participating in the Provident Fund Scheme was 5,575 (2007: 4,540). In 2008, total members' contribution was HK$42.4 million (2007: HK$10.8 million for the defined contribution section of the Retirement Scheme and HK$4.5 million for the KCR Scheme since the Appointed Day) and total contribution from the Company was HK$139.4 million (2007: HK$22 million for the defined contribution section of the Retirement Scheme and HK$9.5 million for the KCR Scheme since the Appointed Day). The net asset value as at 31 December 2008 was HK$2,522 million (2007: HK$3,577 million).

49 Defined Benefit Retirement Plan Obligations

The Company makes contributions to two defined benefit plans that provide benefits for employees upon retirement or termination of services for other reasons (note 48). The movements in respect of these defined benefit plans during the year are summarised as follows.

A The amounts recognised in the balance sheets are as follows:

The Group and The Company

	2008			2007		
in HK$ million	Retirement Scheme	RBS	Total	Retirement Scheme	RBS	Total
Present value of funded obligations	**(9,064)**	**(1)**	**(9,065)**	(8,577)	(1)	(8,578)
Fair value of plan assets	**6,162**	**12**	**6,174**	7,929	12	7,941
Net unrecognised actuarial (gains)/losses	**3,112**	**(4)**	**3,108**	796	(5)	791
Net asset	**210**	**7**	**217**	148	6	154

A portion of the above asset is expected to be recovered after more than one year. However, it is not practicable to segregate this amount from the amounts receivable in the next twelve months, as future contributions will also relate to future services rendered and future changes in actuarial assumptions and market conditions. The Company expects to pay HK$199 million in contribution to the Retirement Scheme in 2009.

B Plan assets consist of the following:

The Group and The Company

	2008			2007		
in HK$ million	Retirement Scheme	RBS	Total	Retirement Scheme	RBS	Total
Equity securities	**2,675**	**–**	**2,675**	3,696	–	3,696
Bonds	**3,364**	**–**	**3,364**	3,976	–	3,976
Cash	**168**	**12**	**180**	311	12	323
	6,207	**12**	**6,219**	7,983	12	7,995
Voluntary units	**(45)**	**–**	**(45)**	(54)	–	(54)
	6,162	**12**	**6,174**	7,929	12	7,941

Included in the plan assets are investments in the Company's ordinary shares and debt securities of nil (2007: nil) and HK$16 million (2007: HK$13 million) respectively.

C Movements in the present value of the defined benefit obligations

The Group and The Company

	2008			2007		
in HK$ million	Retirement Scheme	RBS	Total	Retirement Scheme	RBS	Total
At 1 January	**8,577**	**1**	**8,578**	7,311	3	7,314
Members' contributions paid to the Schemes	**68**	**–**	**68**	66	–	66
Benefits paid by the Schemes	**(468)**	**–**	**(468)**	(125)	–	(125)
Current service cost	**273**	**–**	**273**	264	–	264
Interest cost	**297**	**–**	**297**	271	–	271
Actuarial losses/(gains)	**317**	**–**	**317**	790	(2)	788
At 31 December	**9,064**	**1**	**9,065**	8,577	1	8,578

49 Defined Benefit Retirement Plan Obligations *(continued)*

D Movements in plan assets

The Group and The Company

in HK$ million	2008 Retirement Scheme	2008 RBS	2008 Total	2007 Retirement Scheme	2007 RBS	2007 Total
At 1 January	**7,929**	**12**	**7,941**	6,906	12	6,918
Group's contributions paid to the Schemes	**152**	**–**	**152**	152	–	152
Members' contributions paid to the Schemes	**68**	**–**	**68**	66	–	66
Benefits paid by the Schemes	**(468)**	**–**	**(468)**	(125)	–	(125)
Expected return on plan assets	**477**	**–**	**477**	416	–	416
Actuarial (losses)/gains	**(1,996)**	**–**	**(1,996)**	514	–	514
At 31 December	**6,162**	**12**	**6,174**	7,929	12	7,941

E Expense recognised in the consolidated profit and loss account is as follows:

in HK$ million	2008 Retirement Scheme	2008 RBS	2008 Total	2007 Retirement Scheme	2007 RBS	2007 Total
Current service cost	**273**	**–**	**273**	264	–	264
Interest cost	**297**	**–**	**297**	271	–	271
Expected return on plan assets	**(477)**	**–**	**(477)**	(416)	–	(416)
Net actuarial gains recognised	**–**	**(1)**	**(1)**	–	(1)	(1)
Expense recognised	**93**	**(1)**	**92**	119	(1)	118
Less: Amount capitalised	**(12)**	**–**	**(12)**	(20)	–	(20)
	81	**(1)**	**80**	99	(1)	98

The retirement expense is recognised under staff costs and related expenses in the consolidated profit and loss account.

F Actual return on plan assets

in HK$ million	2008	2007
MTR Corporation Limited Retirement Scheme	**(1,519)**	930
MTR Corporation Limited Retention Bonus Scheme	**–**	–

G The principal actuarial assumptions used as at 31 December 2008 (expressed as weighted average) are as follows:

	2008 Retirement Scheme	2008 RBS	2007 Retirement Scheme	2007 RBS
Discount rate at 31 December	**1.2%**	**0.8%**	3.5%	3.0%
Expected rate of return on plan assets	**6.0%**	**1.5%**	6.0%	2.5%
Future salary increases	**3.5%**	**3.2%**	4.0%	4.5%

The expected long-term rate of return on plan assets have been determined after taking into account actual experience, expected investment volatility and inflation in the long-term. Furthermore, it is based on the portfolio as a whole and not on the sum of the returns on individual asset categories. The amount is based exclusively on historical returns, without adjustments.

49 Defined Benefit Retirement Plan Obligations *(continued)*

H Historical information

The Group and The Company

	Retirement Scheme				
in HK$ million	**2008**	2007	2006	2005	2004
Present value of funded obligations	**(9,064)**	(8,577)	(7,311)	(5,974)	(5,456)
Fair value of plan assets	**6,162**	7,929	6,906	5,899	5,365
Deficit in the Scheme	**(2,902)**	(648)	(405)	(75)	(91)
Experience adjustments arising on plan liabilities – gain/(loss)	**1,391**	(556)	(464)	(98)	(154)
Experience adjustments arising on plan assets – gain/(loss)	**(1,997)**	514	510	119	243

	RBS				
in HK$ million	**2008**	2007	2006	2005	2004
Present value of funded obligations	**(1)**	(1)	(3)	(7)	(7)
Fair value of plan assets	**12**	12	12	13	14
Surplus in the Scheme	**11**	11	9	6	7
Experience adjustments arising on plan liabilities – gain / (loss)	**–**	1	3	(2)	5
Experience adjustments arising on plan assets – gain / (loss)	**–**	–	–	–	–

50 Interests in Jointly Controlled Operations

The Group has the following jointly controlled operations in respect of its awarded property development projects as at 31 December 2008:

Location / Development Package	Land Use	Total Gross Floor Area (sq.m.)	Actual or Expected Date of Completion of Construction Works *
Hong Kong Station	Office/Retail/Hotel	415,894	Completed by phases from 1998–2005
Kowloon Station			
Package One	Residential	147,547	Completed in 2000
Package Two	Residential	210,319	Completed by phases from 2002–2003
Package Three	Residential/Cross Border Bus Terminus	105,113	Completed in 2005
Package Four	Residential	128,845	Completed in 2003
Package Five, Six and Seven	Residential/Office/Retail/Hotel/ Serviced Apartment/ Kindergarten	504,350	By phases from 2006–2010
Olympic Station			
Package One	Residential/Office/Retail/Indoor Sports Hall	309,069	Completed in 2000
Package Two	Residential/Retail/Market	268,650	Completed in 2001
Package Three	Residential/Kindergarten	104,452	Completed in 2006
Tsing Yi Station	Residential/Retail/Kindergarten	292,795	Completed in 1999
Tung Chung Station			
Package One	Residential/Office/Retail/Hotel/ Kindergarten	361,531	Completed by phases from 1999–2005
Package Two	Residential/Retail/Kindergarten	255,949	Completed by phases from 2002–2008
Package Three	Residential/Retail/Wet Market/ Kindergarten	413,154	Completed by phases from 2002–2008
Hang Hau Station	Residential/Retail	142,152	Completed in 2004
Tiu Keng Leng Station	Residential/Retail	253,765	Completed by phases from 2006–2007
Tseung Kwan O Station			
Area 55b	Residential/Retail	96,797	Completed in 2006
Area 57a	Residential/Retail	29,642	Completed in 2005
Area 56	Residential/Hotel/Retail/Office	163,130	2011
Tseung Kwan O Area 86			
Package One	Residential/Retail/Residential Care Home for the Elderly	139,840	Completed in 2008
Package Two	Residential/Kindergarten	310,496	By phases from 2009–2010
Package Three	Residential/Kindergarten	129,544	2012
Choi Hung Park-and-Ride	Residential/Retail	21,538	Completed in 2005
Che Kung Temple Station	Residential/Retail/Kindergarten	90,655	2012

* Completion based on issuance of occupation permit

The Group's assets held in relation to these joint venture operations include various site foundation works and related staff and overhead costs, land costs, acquisition cost of development rights and interest expense. These are set off against any up-front payments received from developers in relation to that development package, and the balance is shown on the balance sheet either as property development in progress or deferred income (note 23) as the case may be. As at 31 December 2008, total property development in progress in respect of these jointly controlled operations was HK$3,036 million (2007: HK$1,961 million) and total deferred income was HK$156 million (2007: HK$400 million).

During the year ended 31 December 2008, profits of HK$4,670 million (2007: HK$8,304 million) were recognised (note 8).

50 Interests in Jointly Controlled Operations *(continued)*

In connection with the Rail Merger, the Company entered into agreements with KCRC relating to the property development projects on the following three awarded sites:

Location / Development Package	Land Use	Total Gross Floor Area (sq.m.)	Actual or Expected Date of Completion of Construction Works *
Fo Tan Station Ho Tung Lau	Residential/Retail	122,900	Completed in 2008
Wu Kai Sha Station	Residential/Retail/Kindergarten	172,650	2009
Tai Wai Maintenance Centre	Residential	313,955	By phases from 2009–2011

Under these agreements, the Company was appointed as KCRC's agent to exercise the rights and to perform the obligations of KCRC as stipulated in the agreements. The Company received a right to share the net surplus from the sale of these property development projects.

51 Material Related Party Transactions

The Financial Secretary Incorporated, which holds approximately 77% of the Company's issued share capital on trust for the Government of the Hong Kong SAR, is the majority shareholder of the Company. Transactions between the Group and Government departments, agencies or Government controlled entities, other than those transactions such as the payment of fees, taxes, leases and rates, etc. that arise in the normal dealings between the Government and the Group, are considered to be related party transactions pursuant to HKAS 24 "Related party disclosures" and are identified separately in these accounts.

Members of the Board and Members of the Executive Directorate, and parties related to them including their close family members, are also considered to be related parties of the Group. Transactions with these parties, except for those involving a Member of the Board or his related parties where the relevant Member abstains from voting, are separately disclosed in the accounts.

Major related party transactions entered into by the Group in prior years which are still relevant for the current year include:

A The Company entered into the Airport Railway Agreement with the Government on 5 July 1995 for the construction of the Airport Railway. In addition to specifying the parameters for the design, construction and operation of the Tung Chung and Airport Express Lines, the Agreement also included provisions for the granting of land to the Company for property development (note 23).

B The Company entered into the TKE Project Agreement with the Government on 4 November 1998 for the design, construction, financing and operation of the Tseung Kwan O Extension and the granting of land for commercial and residential property developments along the railway extension.

C On 30 June 2000, the Appointed Day for the purposes of the Mass Transit Railway Ordinance, the Company was granted a franchise, for an initial period of 50 years, to operate the existing mass transit railway, and to operate and construct any extension to the railway. On the same day, the Company entered into an Operating Agreement ("OA") with the Government which detailed provisions for the design, construction, maintenance and operation of the railway under the franchise. Pursuant to the terms of the OA, the Company's franchise will be extended for further periods of 50 years upon satisfying certain capital expenditure requirements at no payment and without any change in the terms of the franchise. The OA also provides that upon extension of the franchise and subject to the Government's prevailing land policy on the date on which the franchise is extended, certain consequential amendments will be made to agreements between the Government and the Company in relation to the mass transit railway, including the renewal of various railway running line leases and land leases at nominal cost. With effect from 2 December 2007, the OA was replaced by a new operating agreement, details of which are set out in note 51I below.

D On 14 July 2000, the Company received a comfort letter from the Government pursuant to which the Government agreed to extend the period of certain of the Company's land interests so that they are coterminous with the Company's franchise period. In addition, on 3 August 2007, the Government wrote to KCRC confirming that, subject to all necessary approvals being obtained, the period of certain of KCRC's land interests (which are the subject of the service concession) will be extended so that they are coterminous with the Concession Period.

E On 24 July 2002, the Company entered into an agreement with the Government specifying the parameters for the design, construction, financing and operation of the Disneyland Resort Line ("DRL"). In connection with the financing of the DRL Project, the Government agreed to provide financial support through the Government waivers of its entitlement to cash dividends in respect of its shareholding. Such committed financial support has been met in 2004. The DRL was completed in June 2005 and commenced operation on 1 August 2005.

F On 19 November 2003, the Company entered into a formal project agreement with the Government to develop, on a build, operate and transfer basis, the Tung Chung Cable Car System together with a Theme Village at Ngong Ping on the Lantau Island under a franchise granted by the Government for a period of 30 years commencing on 24 December 2003. The project was completed with operation commenced on 18 September 2006.

G On 24 January 2005, the Company accepted an offer from the Government to allow the Company to proceed with the proposed development on Site F of Tseung Kwan O Town Lot No. 70, Area 86, at an assessed land premium of HK$2,319 million together with other ancillary terms and conditions as specified in the modification letter to be entered into between the Company and the Government. Upon award of the development package on 8 February 2005, the agreed land premium, of which one-half or HK$1,160 million was paid by the Company, was settled.

51 Material Related Party Transactions *(continued)*

H On 18 July 2005, the Company entered into a project agreement with the Airport Authority for the procurement of MTR station extension works and related railway facilities to serve the SkyPlaza at the Hong Kong International Airport. The project was completed with the facilities opened on 28 February 2007.

I On 8 June 2007, the Legislative Council approved the Rail Merger Ordinance which came into effect on the Appointed Day. Amongst other things, the Rail Merger Ordinance amends the KCRC Ordinance and the MTR Ordinance to provide the necessary legislative framework for the Rail Merger and the operation by the Company of the MTRC railway, KCRC railway and certain other railways under one franchise, and enables KCRC to enter into the Service Concession Agreement referred to in note 51K(ii) below with the Company.

J In connection with the Rail Merger, on 9 August 2007, the Company entered into a new operating agreement with the Government ("new OA"), which is based on the existing OA referred to in note 51C above. On the Appointed Day, the Company's existing franchise under the Mass Transit Railway Ordinance was expanded to cover railways other than the existing MTR railway for an initial period of 50 years from the Appointed Day ("expanded franchise"). The new OA detailed the design, construction, maintenance and operation of the railways under the expanded franchise. Pursuant to the terms of the new OA (and the MTR Ordinance), the Company's franchise may be extended for further periods of 50 years (from the date of the extension) upon satisfying certain capital expenditure requirements at no payment and without any change in the terms of the franchise. The new OA includes terms relating to the Company's obligations in relation to electrical power supply, control centres, the monitoring of environmental conditions, the provision of accommodation for the Hong Kong Police Force, the notification of certain events to the Commissioner for Transport, hours of operation and service capacity, performance requirements, customer service pledges and safety management. The new OA also sets out a framework for the award of new railway projects in Hong Kong and introduces a fare adjustment mechanism. A detailed description of the new OA is contained in the circular to shareholders in respect of the Extraordinary General Meeting convened to approve the Rail Merger.

K Other than the new OA described in note 51J above, the Company also entered into the following principal agreements with KCRC and the Government in connection with the Rail Merger on 9 August 2007:

(i) Merger Framework Agreement, which contains provisions for the overall structure and certain specific aspects of the rail merger, including the seamless interchange programme, corporate governance, certain employee arrangements, implementation of certain fare reductions, the payments for property package, arrangements relating to flat production and land premium, the treatment of KCRC's cross border leases, Shatin to Central Link arrangements and the allocation of liabilities for certain pre and post merger claims by third parties;

(ii) Service Concession Agreement, which contains provisions in relation to the grant of the right to access, use and operate the concession property and a licence to access and use certain KCRC land; the term of the service concession; the arrangements for the redelivery of the KCRC system upon concession expiry; the provision of ex-KCRC services by the Company to specified standards; the obligation to pay upfront and annual payments; the legal and beneficial ownership of future concession property (Additional Concession Property); and the regime for compensation payable by KCRC upon return of the Additional Concession Property;

(iii) Sale and Purchase Agreement, which sets out the terms pursuant to which the Company acquired certain assets and contracts from KCRC;

(iv) Kowloon Southern Link ("KSL") Project Management Agreement, which sets out the terms on which the Company was appointed by KCRC to project manage the design and construction of the KSL in return for a management fee of approximately HK$710.8 million and an incentive payment of up to HK$110 million if the construction of the KSL is completed ahead of time and under budget. The Company itself will not construct, nor be responsible for the costs of the KSL works. On opening of service, the KSL will form part of the service concession;

(v) West Rail Agency Agreement, which sets out the terms on which the Company was appointed to act as KCRC's agent and to exercise certain rights and perform certain obligations relating to specified development sites along the West Rail;

(vi) Outsourcing Agreement, which sets out the terms on which the Company is to provide certain financial and administrative services to KCRC after the Rail Merger, in return for an annual fee of HK$19.8 million; and

(vii) Property Package Agreements, which set out the arrangements in respect of the acquisition of the property package. These arrangements include the assignment of certain properties by KCRC to the Company, the acquisition of certain properties by the Company through its acquisition of certain KCRC subsidiaries under the Sale and Purchase Agreement, the granting of leases on certain properties by the Government to the Company and the relating interim arrangements before such granting is effective, the management of certain development sites by the Company in return for a fee substantially equal to the profits from the developments, and the granting of certain potential development sites to the Company.

A detailed description of each of these documents is contained under the paragraph "Connected Transactions" of the Report of the Members of the Board.

L Also in connection with the Rail Merger, the Company entered into US Cross Border Lease ("CBL") Assumption Agreements with KCRC on 30 November 2007 and US CBL Allocation Agreement with KCRC and KCRC's subsidiaries on 2 December 2007. The agreements set out the terms on which the Company has undertaken to perform, on a joint and several basis with KCRC, the obligations of KCRC under the respective CBLs, and delineate and allocate the obligations and responsibility for risks relating to the CBLs. Details of the commitment of the Company in connection with these agreements are specified in note 52E and a detailed description of these agreements are contained under the paragraph "Connected Transactions" of the Report of the Members of the Board.

51 Material Related Party Transactions *(continued)*

During the year, the Group has had the following material related party transactions:

M On 6 February 2008, the Company entered into a preliminary project agreement with the Government for the undertaking of the pre-authorisation activities of the West Island Line. Pursuant to the agreement, the Company has received HK$400 million from the Government to undertake the detailed design of the railway works, carry out all necessary ground investigations, invite and assess tenders for the railway works construction contracts, and carry out ancillary and other support services.

N On 22 July 2008, the Government granted Sha Tin Town Lot No. 519 to the Company for the development at Che Kung Temple Station with a total consideration of HK$3,662 million.

O On 21 August 2008, the Company entered into a maintenance agreement with the Hong Kong Airport Authority for the renewal of an expired maintenance agreement for the automatic people mover system serving the Hong Kong International Airport including the SkyPlaza and SkyPier terminal buildings. The renewed agreement has a duration of five years effective from 6 July 2008 and widens the scope to cover the operation and maintenance of eight new vehicles and one new line, both of which will be ready for passenger service starting from the fourth quarter of 2009. During 2008, HK$32 million (2007: HK$23 million) was recognised as consultancy income in respect of the maintenance agreements.

P On 30 September 2008, the Company entered into a management agency agreement with KCRC in relation to 7th, 8th, 9th and 10th floors of Citylink Plaza, No. 1 Sha Tin Station Circuit, Shatin, New Territories. Pursuant to the agreement, the Company acts as KCRC's agent in the management and lease administration of the relating premises with effect from the Appointed Day to the end of the Concession Period. During 2008, HK$1 million (2007: nil) was recognised as property management income in respect of the property agency agreement.

Q On 24 November 2008, the Company entered into an entrustment agreement with the Government to provide for the design of and site investigation and procurement activities in relation to the Shatin to Central Link.

R On 24 November 2008, the Company entered into an entrustment agreement with the Government to provide for the design of and site investigation and procurement activities in relation to the Express Rail Link.

S In connection with the construction of various railway projects, certain essential project works are embedded within the infrastructure works to be undertaken by the Government or certain of its related parties. These works have been entrusted to the Government and its related parties and are payable on an actual cost basis according to architectural certifications. The Government and certain of its related parties, on the other hand, have entered into entrustment agreements with the Company for the construction of various other infrastructure works that are also reimbursable according to actual costs certified. Details of the amounts paid and the amounts receivable and payable as at 31 December 2008 are provided in notes 22, 36 and 41 respectively.

T The Company has business transactions with its non-controlled subsidiaries in the normal course of operations, details of which are disclosed in note 26.

U The Group has paid remuneration to the Members of the Board and Members of the Executive Directorate. Details of these transactions are described in note 7A. In addition, the Members of the Executive Directorate were granted share options under the Company's Pre-Global Offering Share Option Scheme, New Joiners Share Option Scheme and 2007 Share Option Scheme. Details of the terms of these directors' options are disclosed in note 7B and under the paragraph "Board Members' and Executive Directorate's Interests in Shares" of the Report of the Members of the Board. Their gross remuneration charged to the profit and loss account is summarised as follows:

in HK$ million	2008	2007
Short-term employee benefits	**67.0**	50.6
Post-employment benefits	**2.2**	1.5
Equity compensation benefits	**6.4**	6.5
	75.6	58.6

The above remuneration is included in staff costs and related expenses.

V During the year, the following dividends were paid to the Government:

in HK$ million	2008	2007
Cash dividends paid	**806**	765
Shares allotted in respect of scrip dividends	**1,134**	1,025
	1,940	1,790

52 Commitments

A Capital Commitments

(i) Outstanding capital commitments as at 31 December 2008 not provided for in the accounts were as follows:

The Group

in HK$ million	Railway operations	Railway extension projects	Property projects and management	Mainland of China and Overseas projects	Total
2008					
Authorised but not yet contracted for	**846**	**–**	**57**	**–**	**903**
Authorised and contracted for	**1,832**	**180**	**264**	**859**	**3,135**
	2,678	**180**	**321**	**859**	**4,038**
2007					
Authorised but not yet contracted for	916	–	68	–	984
Authorised and contracted for	547	152	377	633	1,709
	1,463	152	445	633	2,693

The Company

in HK$ million	Railway operations	Railway extension projects	Property projects and management	Total
2008				
Authorised but not yet contracted for	**841**	**–**	**57**	**898**
Authorised and contracted for	**1,832**	**180**	**260**	**2,272**
	2,673	**180**	**317**	**3,170**
2007				
Authorised but not yet contracted for	889	–	68	957
Authorised and contracted for	547	152	377	1,076
	1,436	152	445	2,033

Included in the amounts authorised but not yet contracted for are costs that will not be subject to capital contracts such as staff costs, overhead expenses and capitalised interest.

(ii) The commitments under railway operations comprise the following:

The Group and The Company

in HK$ million	Improvement and enhancement works	Acquisition of property, plant and equipment	Additional concession property	Total
2008				
Authorised but not yet contracted for	**661**	**12**	**173**	**846**
Authorised and contracted for	**491**	**1,105**	**236**	**1,832**
	1,152	**1,117**	**409**	**2,678**
2007				
Authorised but not yet contracted for	854	11	51	916
Authorised and contracted for	342	9	196	547
	1,196	20	247	1,463

52 Commitments *(continued)*

B Operating Lease Commitments

The Group had operating leases on office buildings, staff quarters, bus depot and a shopping centre in Beijing as at 31 December 2008. The total future minimum lease payments under non-cancellable operating leases are payable as follows:

	The Group		The Company	
in HK$ million	**2008**	2007	**2008**	2007
Payable within one year	**73**	67	**21**	17
Payable after one but within five years	**187**	228	**9**	13
	260	295	**30**	30

The above includes HK$21 million (2007: HK$24 million) in respect of the office accommodation and quarters for construction project staff, majority of which are subject to rent reviews.

In respect of the operating lease on the shopping centre in Beijing, the Group has the right to acquire the shopping centre in Beijing at a pre-determined price during the first five years of the lease term, which commenced from April 2006, or release its obligation as a tenant by making a compensation to the landlord upon expiry of the fifth year. The Group obtained a bank guarantee of RMB12.5 million in respect of the quarterly rental payment arrangement with the landlord. In addition, the Company provides guarantees amounting to RMB102.5 million to the landlord for the rental payments for the first five years of the lease, which was entered into by the Company's subsidiary, MTR (Beijing) Commercial Facilities Management Co. Ltd..

C Liabilities and Commitments in Respect of Property Management Contracts

The Group has, over the years, jointly developed with outside property developers certain properties above or adjacent to railway depots and stations. Under most of the development agreements, the Group retained the right to manage these properties after their completion. The Group, as manager of these properties, enters into services contracts with outside contractors for the provision of security, cleaning, maintenance and other services on behalf of the managed properties. The Group is primarily responsible for these contracts, but any contract costs incurred will be reimbursed by the owners and tenants of the managed properties from the management funds as soon as they are paid.

As at 31 December 2008, the Group had total outstanding liabilities and contractual commitments of HK$875 million (2007: HK$969 million) in respect of these works and services. Cash funds totalling HK$1,072 million (2007: HK$989 million) obtained through monthly payments of management service charges from the managed properties are held by the Group on behalf of those properties for settlement of works and services provided.

D Material Financial Guarantee Contracts

The Company provides guarantees to investors of debt securities issued by one of its subsidiaries, MTR Corporation (C.I.) Limited (note 38C), which amounted to approximately HK$12,528 million (in notional amount) as at 31 December 2008. Proceeds from such debts issued have been on lent to the Company. As such, the primary liabilities have already been recorded in the Company's balance sheet.

The Group provides standby letters of credit ("standby LC's") to the Investors to the lease out/lease back transaction ("Lease Transaction") (note 19E) to cover additional amounts payable by the Group in the event the transactions are terminated prior to the expiry of the lease terms, and such standby LC's amounted to US$113 million (HK$872 million) as at 31 December 2008. The Group also provides standby LC's to certain of the Investors under the Lease Transaction (note 19E) to replace some of the Defeasance Securities previously used to support the corresponding long-term lease payments as a result of credit rating downgrades of these securities, and such standby LC's amounted to US$33 million (HK$255 million) as at 31 December 2008.

E US Cross Border Lease ("CBL") Agreements

In connection with the Rail Merger in December 2007, the Company entered into a number of agreements ("US CBL Assumption Agreements") with respect to the CBLs that KCRC had entered into with its CBL counterparties in relation to certain of its property and equipment ("CBL Property") between 1998 and 2003. Pursuant to the US CBL Assumption Agreements, the Company has undertaken to perform, on a joint and several basis with KCRC, the obligations of KCRC under the respective CBLs.

In addition, the Company has entered into a US CBL Allocation Agreement with KCRC, whereby the rights, obligations and responsibility for risks relating to the CBLs are delineated and allocated between the Company and KCRC. Generally, the Company is responsible for operational matters, such as repair, maintenance and insurance of the CBL Property, and KCRC is responsible for all other obligations, including payment of periodic rents and collateral related obligations. Despite this allocation of obligations, the Company is prima facie jointly and severally liable to the CBL counterparties for any failure of KCRC to perform its obligations under the CBLs.

KCRC and the Government of Hong Kong have agreed to indemnify the Company for its reasonable costs incurred as a result of the due and proper performance by the Company of its obligations under the CBLs (unless such costs would have been incurred in any event). In addition, KCRC has agreed to indemnify the Company for losses and reasonable costs incurred arising from KCRC not complying with its obligations under the CBLs or from any breach of KCRC's representations, covenants and agreements provided for in relation to the CBLs.

The Company has agreed to indemnify each of the Government of Hong Kong and KCRC for losses and reasonable costs incurred arising from any breach of the Company's representations, covenants and agreements provided for in relation to the CBLs.

52 Commitments *(continued)*

F Service Concession

Pursuant to the Rail Merger, the Company is obliged under the Service Concession Agreement ("SCA") to pay an annual fixed payment of HK$750 million to KCRC over the period of the service concession. Additionally, commencing after three years from the Appointed Day, the Company is obliged to pay an annual variable fee to KCRC based on the revenue generated from the KCRC system above certain thresholds. Furthermore, under the SCA, the Company is obliged to maintain, repair, replace and/or upgrade the KCRC system over the period of the service concession which is to be returned at the expiry of the service concession.

G Investments in Mainland of China

(i) Investment in Line 4 of Shenzhen Metro System ("Shenzhen Line 4")

In January 2004, the Group entered into an Agreement in Principle for a Build-Operate-Transfer ("BOT") project with the Shenzhen Municipal People's Government ("Shenzhen Government") in respect of the construction of Phase 2 of Shenzhen Line 4 of the proposed Shenzhen Metro System and the operation of the entire line for a term of 30 years. In May 2005, the Group and the Shenzhen Government initialled the project Concession Agreement. Approval of the project has been obtained from the National Development and Reform Commission in Beijing in January 2009.

Shenzhen Line 4 is a 21-kilometre urban railway running from Huanggang to Longhua New Town in Shenzhen, forming the major north-south railway corridor of the Shenzhen Special Economic Zone. Upon completion of Phase 2 of Shenzhen Line 4, both Phases 1 and 2 will be operated by the Company's subsidiary established in Shenzhen. Total investment of the project is estimated at RMB6 billion (HK$6.8 billion), which will be financed by equity capital contributed by the Group of RMB2.4 billion (HK$2.7 billion) and the balance by bank loans in Renminbi.

Preparatory work including design and tendering and expanded trial section is in progress. As of 31 December 2008, costs of HK$1,650 million (2007: HK$670 million) incurred for the project have been included in deferred expenditure and the Group had other contract commitments totalling HK$859 million (2007: HK$633 million) in relation to this project.

(ii) Investment in Beijing Metro Line 4 Project ("Beijing Line 4")

In December 2004, an Agreement in Principle was entered into between the Group, Beijing Infrastructure Investment Co. Ltd ("BIIC") and Beijing Capital Group ("BCG"), both are subsidiaries of the Beijing Municipal People's Government, to form a public-private partnership company ("PPP") for the investment in the Beijing Line 4 project, which involves the investment, construction and operation of the line for a term of 30 years. In September 2005, approval from the Central Government for the project was obtained. The PPP, Beijing MTR Corporation Limited, completed all registration requirements and obtained its business license in January 2006. In April 2006, Concession Agreement with the Beijing Municipal People's Government was signed.

Beijing Line 4 is a 29-kilometre underground metro line running from Majialou Station to Longbeicun Station, forming a main north-south traffic artery of Beijing. The total investment for the Beijing Line 4 project is estimated at RMB15.3 billion (HK$17.4 billion), of which 70% will be borne by the Beijing Municipal People's Government to finance mainly land acquisition and civil construction. Total investment by the PPP is RMB4.6 billion (HK$5.2 billion), contributing to 30% of the total investment in the project to finance mainly the electrical and mechanical systems and rolling stock. The Group and BCG each owns 49% interests of the PPP whilst BIIC owns the remaining 2% interest. The PPP is to operate and be responsible for the maintenance of Beijing Line 4 for a term of 30 years. The PPP has a registered capital of approximately RMB1.4 billion (HK$1.6 billion) with the Company's contribution amounting to RMB676 million. During 2008, the Group injected its last tranche of equity of RMB471 million (HK$515 million), making the total equity contribution as at 31 December 2008 at HK$718 million (2007: HK$203 million), which represents 100% of the Group's committed share. Apart from equity, the PPP's investment is financed by non-recourse bank loans provided by Industrial and Commercial Bank of China and China Development Bank.

Equipment production and site installation were in progress as scheduled. As of 31 December 2008, the PPP has outstanding contract commitments totalling at approximately RMB1.3 billion (HK$1.4 billion) (2007: HK$2.5 billion).

(iii) Investment in Shenyang Metro Lines Project

On 26 November 2008, the Company entered into an Agreement in Principle with Shenyang Municipal Government and its wholly-owned subsidiary, Shenyang Metro Group Limited, for the operation and maintenance of Shenyang Metro Lines 1 and 2 for a term of 30 years, with the Company owning 49% of the joint venture company to be set up for the operation and maintenance franchise. Shenyang Metro Lines 1 and 2, with a total route length of 50 kilometres, are the first two metro lines among the eleven planned lines of Shenyang city. Civil construction works for the two lines commenced in 2005 and the two lines are expected to commence service by 2010 and 2012 respectively. Under a separate Principle Agreement, the Company and Shenyang Municipal Government will form Joint Working Groups to conduct planning studies for future Shenyang Metro Lines 4, 9 and 10 as well as the extension of Shenyang Metro Lines 1 and 2. Under another Principle Agreement, the Company will join the Shenyang Municipal Government for a study on town planning and to explore property development opportunities along Shenyang Metro Lines 1 and 2 corridors.

(iv) Investment in Beijing Daxing Line Project

On 27 November 2008, the Company, together with its joint venture partners of Beijing MTR Corporation Limited, Beijing Infrastructure Investment Company Limited ("BIIC") and Beijing Capital Group Company Limited ("BCG"), signed a Memorandum of Understanding (MOU) with Beijing Metro Daxing Line Investment Company Limited, the wholly owned subsidiary of Beijing Municipal Government for the operations and maintenance of Daxing Line of the Beijing Metro Network. Daxing Line is a 22-kilometre extension of the Beijing Metro Line 4 from Gongyixiqiao Station extending southward to Nanzhaolu Station and is expected to commence service in 2010.

52 Commitments *(continued)*

G Investments in Mainland of China *(continued)*

(v) Investment in Hangzhou Metro Line 1 Project

On 16 January 2009, the Company entered into a Principle Agreement for a public-private partnership project with Hangzhou Municipal Government and Hangzhou Metro Group Company Limited for the investment, construction and operation of Hangzhou Metro Line 1.

The Principle Agreement sets out the framework for the Company to further discuss with Hangzhou Municipal Government for the concession agreement for the investment in Hangzhou Metro Line 1 and for the operational right of Hangzhou Metro Line 1 Phase 1 for a period of 25 years. The 48-kilometre Hangzhou Metro Line 1 consists of 41 kilometres of underground section and 7 kilometres of at-grade and elevated sections. Hangzhou Metro Line 1 has a total of 30 stations running from south to north of Hangzhou city to other cities, namely Xiasha, Linping and Jiangnan. This line is expected to commence service in 2012.

The project will be divided into Part A and Part B, representing approximately 63% and 37% respectively of the total investment of RMB22 billion. Part A, which covers civil construction of the metro system, is being undertaken by Hangzhou Metro Group Company Limited. Part B, which mainly covers the electrical and mechanical system and operation of the metro system, will be undertaken by a cooperative joint venture owned by the Company and Hangzhou Metro Group Company Limited with equity interest of 49% and 51% respectively.

At the same time, the Company also entered into a Strategic Agreement with the same parties to explore property development opportunities along the Hangzhou Metro lines.

H Investments in Europe

(i) Investment in London Overground Franchise

On 2 July 2007, London Overground Rail Operations Ltd ("LOROL"), the 50/50 partnership between the Group and DB Reggio (UK) Limited (formerly Laing Rail Limited), was awarded the concession to operate the new London Overground service in Greater London for seven years from 11 November 2007 with an option for a two year extension. London Overground is a semi-orbital route of five rail lines serving West, North and East London and will act as a crucial link for the 2012 Olympic Games. The total London Overground route network measures 107.2 kilometres.

Under the terms of the concession agreement between LOROL and Transport for London ("TfL"), LOROL has provided a performance bond of GBP15 million to TfL, which is jointly and severally indemnified by the parent companies, that is the Company and DB Reggio (UK) Limited, through parent company guarantees. The bond may be called by TfL if the concession is terminated early as a result of default.

As at 31 December 2008, an unsecured debt of GBP5 million with interest rate at 2.5% per annum above the published Bank of England base rate from time to time was provided by the Group and DB Reggio (UK) Limited to LOROL. The final repayment date of this debt is on the date of expiry or the earlier termination of the term of the London Rail Concession under the concession agreement. Each lender shares 50% of the debt.

(ii) Investment in Stockholm Metro Franchise

On 20 January 2009, the board of the Stockholm transport authority ("SL") announced the Company as the winner of the tender for the Stockholm Metro operations concession in Sweden for a period of eight years, starting from 2 November 2009, with a possible extension for an additional period of six years.

The concession includes train and station operations as well as rolling stock maintenance. For servicing, maintenance and cleaning of trains, the Company will team up with Mantena AS, a leading maintainer of rolling stock in Norway.

The Stockholm Metro consists of three dedicated lines with 108 kilometres in total track length and 100 surface and underground stations.

The Company is in the process of mobilising resources for the contract and will invest a total of SEK175 million (approximately HK$175 million) in a mixture of equity and shareholder loans or deeply discounted securities.

Under the agreement, the Company will provide to SL a guarantee of SEK1,000 million (approximately HK$1,000 million), which can be called if the concession is early terminated as a result of default.

53 Accounting Estimates and Judgements

A Key sources of accounting estimates and estimation uncertainty include the following:

(i) Estimated Useful Life and Depreciation of Property, Plant and Equipment

The Group estimates the useful lives of the various categories of property, plant and equipment on the basis of their design lives, planned asset maintenance programme and actual usage experience. Depreciation is calculated using the straight-line method at rates sufficient to write off their cost or valuation over their estimated useful lives (note 2I).

(ii) Impairment of Long-lived Assets

The Group reviews its long-lived assets for indications of impairment at each balance sheet date according to accounting polices set out in note 2H(ii). In analysing potential impairments identified, the Group uses projections of future cash flows from the assets based on management's assignment of a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

(iii) Pension Costs

The Group employs independent valuation professionals to conduct annual assessment of the actuarial position of the Group's retirement plans. The determination of the Group's obligation and expense for the defined benefit element of these plans is dependent on certain assumptions and factors provided by the Company, which are disclosed in notes 48A and 48B.

(iv) Revenue Recognition on Property Development

Recognition of property development profits requires management's estimation of the final project costs upon completion, assessment of outstanding transactions and market values of unsold units and, in the case of property distribution-in-kind, the properties' fair value upon recognition. The Company takes into account independent qualified surveyors report, past experience on sales and marketing costs when estimating final project costs on completion; and makes reference to professionally qualified valuers' reports in determining the estimated fair value of property distribution-in-kind.

(v) Properties Held for Sale

The Group values unsold properties at the lower of their costs or net realisable values (note 31) at the balance sheet date. In ascertaining the properties' net realisable values, which are represented by the estimated selling prices less costs to be incurred in relation to the sales, the Group employs independent valuation professionals to assess the properties' estimated selling prices, and makes estimations on further selling and property holding costs to be incurred based on past experience and with reference to general market practice.

(vi) Interest-free Loan to a Property Developer

The Group estimated the fair value of the interest-free loan to a developer at its present value discounted at the prevailing market rates of interest at inception.

(vii) Valuation of Investment Properties

The valuation of investment properties requires management's input of various assumptions and factors relevant to the valuation. The Group conducts annual revaluation of its investment properties by independent professionally qualified valuers based on these assumptions agreed with the valuers prior to adoption.

(viii) Franchise

The current franchise under which the Group is operating allows it to run the mass transit railway system until 1 December 2057. Pursuant to the terms stipulated in the new Operating Agreement with the Government, the Company considers that it has the legal right to extend the franchise for further periods of 50 years upon expiry of each franchise term (note 51J). The Group's depreciation policies (note 2I) in respect of certain assets' lives which extend beyond 2057 are on this basis.

(ix) Income Tax

Certain treatments adopted by the Company in its tax returns in the past years are yet to be finalised with the Hong Kong Inland Revenue Department. In assessing the Company's income tax and deferred taxation in the 2008 accounts, the Company has followed the tax treatments it has adopted in those tax returns, which may be different from the final outcome in due course.

(x) Project Provisions

The Group establishes project provisions for the settlement of estimated claims that may arise due to time delays, additional costs or other unforeseen circumstances common to major construction contracts. The claims provisions are estimated based on an assessment of the Group's liabilities under each contract by professionally qualified personnel, which may differ from the actual claims settlement.

(xi) Deferred Expenditure

As disclosed in note 2J(i), the Group capitalises proposed railway project costs in deferred expenditure when the projects are at a detailed study stage and having been approved in principle by the Members of the Board. Such decision involves the Board's judgement on the outcome of the proposed project.

53 Accounting Estimates and Judgements *(continued)*

A Key sources of accounting estimates and estimation uncertainty include the following: *(continued)*

(xii) Fair Value of Derivatives and Other Financial Instruments

In determining the fair value of financial instruments, the Group uses its judgement to select a variety of methods and make assumptions that are mainly based on market conditions existing at each balance sheet date. For financial instruments that are not traded in active markets, the fair values were based on the discounted cash flows method which discounts the future contractual cash flows at the current market interest or foreign exchange rates, as applicable, for similar financial instruments that were available to the Group at the time.

(xiii) Obligations under Service Concession

In determining the present value of the obligations under service concession, the discount rate adopted was the Company's estimated long-term incremental cost of borrowing at inception after due consideration of the Company's existing fixed rate borrowing cost, future interest rate and inflation trends.

B Critical accounting judgements in applying the group's accounting policies:

(i) Provisions and Contingent Liabilities

The Group recognises provisions for liabilities of uncertain timing or amount when the Group has a legal or constructive obligation arising as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made. 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 contingent liability. As at 31 December 2008, the Group considered that it had no disclosable contingent liabilities as there were neither pending litigations nor events with potential obligation which were probable to result in material outflow of economic benefits to the Group.

(ii) Non-controlled Subsidiaries

The Company regards Octopus Holdings Limited and its subsidiaries (the "OHL Group") as non-controlled subsidiaries. In determining whether the Group has control over these subsidiaries, the Company has taken into account its voting right conferred to it under the Shareholder's Agreement of OHL and the effective influence it may exercise over the decision of OHL's Board. Throughout the year ended 31 December 2008, the Group considered that its voting right in the OHL Group has been maintained at 49% despite an equity interest of 57.4%. As such, the OHL Group of companies were accounted for as non-controlled subsidiaries in the Group's accounts.

54 Possible Impact of Amendments, New Standards and Interpretations Issued but Not Yet Effective for the Annual Accounting Period ended 31 December 2008

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

The Company 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 following developments are relevant to the Group's accounts:

	Effective for accounting periods beginning on or after
HK(IFRIC) Interpretation 13, *Customer Loyalty Programme*	1 July 2008
Amendment to HKAS 40, *Investment Property*, under Improvements to HKFRs 2008	1 January 2009

However, the adoption of the above developments is unlikely to result in a significant restatement of the Group's results of operations and financial position.

In addition, the following developments are expected to result in amended disclosures in the financial statements, including restatement of comparative amounts in the first period of adoption:

	Effective for accounting periods beginning on or after
HKFRS 8, *Operating segments*	1 January 2009
HKAS 1 (revised 2007), *Presentation of financial statements*	1 January 2009

55 Approval of Accounts

The accounts were approved by the Board on 10 March 2009.

Glossary

Airport Express	Train Service provided between AsiaWorld-Expo Station and Hong Kong Station
Appointed Day or Day One or Merger Date	2 December 2007 when the Rail Merger was completed
Articles of Association	The articles of association of the Company
Board	The board of directors of the Company
Bus	Feeder bus services operated in support of West Rail Line, East Rail Line and Light Rail
Company or MTR Corporation	MTR Corporation Limited 香港鐵路有限公司, a company which was incorporated under the Companies Ordinance (Chapter 32 of the Laws of Hong Kong) on 26 April 2000
Computershare	Computershare Hong Kong Investor Services Limited
Cross-boundary Service or Cross-boundary	Journeys with the destination to / commencing from Lo Wu and Lok Ma Chau stations
Customer Service Pledge	Annually published performance targets in accordance with the Operating Agreement
Director and Member of the Board	A member of the Board
Domestic Service	Collective name for MTR Lines and KCR Lines
FSI	The Financial Secretary Incorporated, a corporation solely established under the Financial Secretary Incorporation Ordinance (Chapter 1015 of the Laws of Hong Kong)
Government	The Government of the Hong Kong SAR
Group	The Company and its subsidiaries
HKSE or Stock Exchange	The Stock Exchange of Hong Kong Limited
Hong Kong or Hong Kong SAR or HKSAR	The Hong Kong Special Administrative Region of the People's Republic of China
Integrated MTR System	Collective name for MTR System and KCR System
Intercity	Intercity passenger services operated between Hong Kong and certain major cities in the Mainland of China such as Guangzhou, Beijing and Shanghai
Interest Cover	Operating profit before depreciation and amortisation divided by gross interest and finance charges before capitalisation and accreted interest on loan to a property developer
KCRC	Kowloon-Canton Railway Corporation
KCR Lines	Collective name for East Rail Line (excluding Cross-boundary Service), West Rail Line and Ma On Shan Line
KCR System	Collective name for KCR Lines, Cross-boundary Service, Light Rail, Bus and Intercity services
Light Rail	Light rail system serving North West New Territories
Listing Rules	The Rules Governing the Listing of Securities on the Stock Exchange
Mainland or Mainland China or Mainland of China	The People's Republic of China
MTR Lines	Collective name for the Kwun Tong Line, Tsuen Wan Line, Island Line, Tung Chung Line, Tseung Kwan O Line and Disneyland Resort Line
MTR Ordinance	The Mass Transit Railway Ordinance (Chapter 556 of the Laws of Hong Kong)
MTR System	Collective name for MTR Lines and Airport Express
Net Debt-to-equity Ratio	Loans, obligations under finance leases, bank overdrafts and obligations under service concession net of cash and cash equivalents in the balance sheet as a percentage of the total equity attributable to equity shareholders of the Company
Operating Agreement	The agreement entered into by the Company and the Government on 30 June, 2000 for the operation of the MTR System in the pre-Merger period and a new agreement entered on 9 August 2007 for the operation of the Integrated MTR System after the Rail Merger
Operating Margin	Operating profit from railway and related businesses before depreciation and amortisation as a percentage of turnover
Ordinary Shares	Ordinary shares of HK$1.00 each in the capital of the Company
Rail Merger or Merger	The merger of the rail operations of MTR Corporation and KCRC and the acquisition of certain property interests by MTR Corporation from KCRC, full details of which are set out in the Rail Merger Circular. The Rail Merger was completed on 2 December 2007
Rail Merger Bill or Rail Merger Ordinance	The Rail Merger Bill refers to the draft legislation on the Rail Merger which was passed by the Legislative Council of Hong Kong on 8 June 2007 and became the Rail Merger Ordinance (Ordinance No.11 of 2007)
Rail Merger Circular	Refers to the circular dated 3 September 2007 despatched to the Company's shareholders in connection with the Rail Merger
Return on Average Equity Attributable to Equity Shareholders	Profit attributable to equity shareholders of the Company as a percentage of the average of the beginning and closing total equity attributable to equity shareholders of the Company of the period
SEC	The U.S. Securities and Exchange Commission
Service Concession	The service concession and licence granted by KCRC to the Company under the Service Concession Agreement, full details of which are set out in the Rail Merger Circular
Service Quality Index	A measure of customer satisfaction for the services provided by Domestic / Cross-boundary services and Airport Express based on the service attributes (excluding fares) weighted by the corresponding importance from the customer research

Shareholder Services

Any matters relating to your shareholding, such as transfer of shares, change of name or address, and loss of share certificates should be addressed in writing to the Registrar:

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Concept & Design: YELLOW CREATIVE (HK) LIMITED   Printed by C & C SECURITY PRINTING Co., LTD

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