

SECTION 1: CORPORATION AND MANAGING BOARD – ROLE OF THE CHAIRMAN, STANDING ORDERS, RULES FOR CONDUCT OF CORPORATION BUSINESS AND COMMITTEES OF THE MANAGING BOARD

THE CORPORATION

101 The Kowloon-Canton Railway Corporation (KCRC) is a public corporation established by statute and is wholly owned by the Government of the Hong Kong Special Administrative Region. It is charged with the task of operating and developing domestic, cross-boundary and intercity railway services in a prudent commercial manner. However, under the provisions of the Rail Merger Ordinance passed by Hong Kong's Legislative Council in June 2007, on 2 December 2007 the MTR Corporation assumed day-to-day responsibility for operating KCRC's railway assets by way of the grant of a service concession for an initial period of 50 years, which is extendable. KCRC retains ownership of the railway assets covered in the service concession agreement and receives annual payments from the MTR Corporation comprising a fixed sum of \$750 million and a variable sum calculated as a sliding scale proportion of annual gross revenue above \$2.5 billion generated by the MTR Corporation from the KCRC railway assets. Should the MTR Corporation fail to observe the terms of the agreement, there is provision for KCRC to take back and operate its assets.

102 KCRC retains a small management team responsible for management and financing of its debts, and for investing any available funds. KCRC is also responsible for monitoring the MTR Corporation's compliance with its various obligations under the merger-related agreements, including revenue sharing, annual payments, outsourcing to MTR Corporation of specified KCRC day-to-day activities, and for managing its remaining subsidiaries.

103 – 110 (not used)

MANAGING BOARD

111 The Kowloon-Canton Railway Ordinance (Chapter 372) sets out the powers of the Corporation.

112 The Corporation's governing body is its Managing Board. The Board may comprise a Chairman, a Chief Executive Officer and not less than four nor more than eight other Members. All are appointed by the Chief Executive of the Hong Kong Special Administrative Region with the exception of the Chief Executive Officer, who is appointed by the Corporation with the prior approval of the Chief Executive of the Hong Kong Special Administrative Region. The Chairman and the Chief Executive Officer perform the functions assigned to them by the Ordinance, the Managing Board and its Committees. Under the provisions of the Rail Merger Ordinance, the position of the Chief Executive Officer may be left vacant.

113 The Board currently comprises six Members, namely, those individuals occupying the positions in the Government of the HKSAR of Secretary for Financial Services and the Treasury (Chairman), Permanent Secretary for Transport and Housing, Deputy Secretary for Financial Services and the Treasury (Treasury) 1, Director of Accounting Services, Government Property Administrator, and Deputy Secretary for Transport and Housing (Transport) 4. The position of the Chief Executive Officer has been left vacant, with responsibility for the day-to-day management of the Corporation being taken up by the Chief Officer.

114 – 120 (not used)

ROLE OF THE CHAIRMAN

121 The Chairman is responsible for the conduct of the Business of the Managing Board.

122 The Chairman must ensure that the content and order of the Managing Board's agenda are correct, and that Members have the relevant Board papers in good time. In consultation with Members, he is required to settle the frequency, location and duration of meetings.

123 The Chairman shall preside at all meetings of the Managing Board. If he is unable to attend a meeting, and in the absence of any Member nominated and appointed to act as Chairman in his place, the relevant provisions of the Standing Orders of the Managing Board shall apply.

124 The Chairman's point of contact with Management will be through the Chief Officer for all corporate matters and the Company Secretary.

125 Other than where the matter is of a personal nature, which will be referred direct to the Chairman, correspondence addressed to the Chairman will be dealt with in the first instance by the Company Secretary, who will refer matters of a substantive nature to the Chief Officer for his decision. Where such matters might result in questions in the Legislative Council or by the media, the Chairman shall be kept informed.

126 – 130 (not used)

STANDING ORDERS OF THE MANAGING BOARD

131 The Managing Board's Standing Orders, which set out how the Board conducts its business, are reproduced as paragraphs 132 to 139 below.

132 The Board may appoint a Secretary and shall cause minutes to be kept of all resolutions and proceedings of the Board at each meeting. The minutes of each meeting shall include a record of the Members, Corporate staff and any other parties who are present.

133 The Chairman, in consultation with Members, will decide the date, location and duration of meetings. When possible, formal notice will be given at the end of the minutes of each meeting of the intended date, time and venue for the next meeting.

134 Any paper for consideration of the Board should be forwarded to reach Members at least 7 days prior to the relevant Board meeting. With the Chairman's approval, urgent or sensitive papers may be distributed at any time prior to the meeting, or tabled at the meeting.

135 In addition, the Chairman is empowered to call extraordinary meetings of the Board at any time, and any 2 Members of the Board may together call a meeting by requisition to the Secretary in writing specifying the business of the meeting.

136 At least 48 hours' notice of any extraordinary meeting shall be given in writing to each Member. The notice shall specify the place, date and time of the meeting and the business to be conducted.

137 The Chairman may also, without calling a meeting, circulate in writing any resolution to all Members of the Board, and such resolution shall be duly passed if signed by not less than a simple majority of the Members of the Corporation for the time being.

138 In the absence of the Chairman of the Board and of any Member nominated and appointed to act as Chairman in his place, the Board may appoint a Member to chair the meeting or to respond to problems on behalf of the Board.

139 In the event of any inconclusive ballot of Members on any issue, the Chairman, in addition to his personal vote, shall exercise a casting vote.

140 – 150 (not used)

RULES FOR CONDUCT OF CORPORATION BUSINESS

151 The following matters will in all cases be referred to the Managing Board for its consideration and approval, together with any further items which the Board may from time to time decide –

- (a) Board General Standing Orders.
- (b) Rules for Conduct of Corporation Business.
- (c) By-laws (unless suspended under the Service Concession)
- (d) 3 Year Business Plans, including revenue, expenses and capital budgets for the ensuing year, annual manpower plan and pay review.
- (e) Annual Budget.
- (f) Annual Report and Audited Accounts.
- (g) Recommendations with respect to Dividend Payments.
- (h) Major Business Strategies.
- (i) Any proposed amendment to the merger transaction documents, and any interpretation arising from those documents that has the potential to carry significant adverse financial or legal implications for the Corporation.
- (j) Capital projects of any nature.
- (k) All contracts in excess of HK\$50 million, and variations to any contract with a cumulative value of \$50 million over the life of the contract. This rule does not apply to Treasury investment activities, which are subject to separate guidelines and policies.
- (l) All non-lowest conforming expenditure and all non-highest conforming revenue contracts in excess of HK\$20 million, and variations to any such contract with a cumulative value of \$20 million over the life of the contract.
- (m) All consultancy contracts in excess of HK\$10 million, and variations to any consultancy contract with a cumulative value of \$10 million over the life of the contract.
- (n) Appointment of the Chief Officer, including prior clearance with the Board of any terms and conditions providing for pension, gratuities, settlement and other financial benefits.
- (o) Borrowings other than those involving uncommitted facilities with maturities of one year or shorter.
- (p) Purchase and sale of all real property.
- (q) Formation, acquisition and disposal of companies.
- (r) Write off of fixed assets, the original cost of each of which exceeded \$50 million, and write off of items of capitalized expenses exceeding \$10 million each. This rule does not apply to Initial and Additional Concession Assets used or operated by MTRC under the Service Concession Agreement.
- (s) Any proposals for leasing or generating additional revenue in excess of \$50 million from the land or property held by the Corporation.

152 In addition, Management must report to the Board each month on significant developments, together with the operating and financial results, information on use of the Corporate Seal, letting of

major contracts, public complaints and any other matters which may be required by the Board from time to time.

153 All other authorities to carry out Corporation activities are delegated to the Chief Officer, who may delegate his authority further.

154 – 160 (not used)

COMMITTEES OF THE MANAGING BOARD

161 Where a Committee of the Board is formed to handle a particular subject, a Chairman and a Secretary shall be appointed by the Board and minutes shall be kept in the same manner as for the Board itself. Furthermore, the decisions arising from the deliberations of any such Committee shall be referred to the full Board for ratification.

The Audit Committee

162 The Managing Board has established an Audit Committee, with membership and terms of reference as set out below.

1. Membership

1.1 The Committee shall consist of three Members appointed by the Board from amongst the Board Members, other than the Board Chairman, none of whom may be a consultant to the Corporation.

1.2 The Chairman of the Committee shall be appointed by the Board. The Chairman of the Committee may appoint one of the Members of the Committee to act as the Chairman in his absence.

1.3 A quorum shall be two Members.

1.4 The Chairman of the Committee should have appropriate accounting and financial experience.

2. Attendance at meetings

2.1 The Chief Officer, the internal auditor and the external auditor shall normally attend meetings of the Committee, except in the case of 3.2

2.2 The Committee may invite any other officer or employee to attend as and when appropriate.

2.3 The Company Secretary or his nominee shall be the Secretary to the Committee.

3. Frequency of meetings and reporting

3.1 The Committee shall meet at least three times a year, and otherwise as required. The Chairman of the Committee shall decide the frequency and timing of meetings.

3.2 At least once a year the Committee shall hold an “in camera” session with each of the external auditor and internal auditor separately without management being present. The Committee at its own consideration, or at the request of the external auditor or internal auditor, may also hold additional “in camera” sessions at any time throughout the year as the Committee so decides.

3.3 The Committee shall be accountable to the Board and shall report on its business to the Board.

- 3.4 Minutes of Committee meetings shall be circulated promptly to all Members of the Committee and, once agreed, to all Members of the Board.
- 3.5 Notice of each meeting confirming the venue, time and date together with an agenda of items to be discussed shall be forwarded to each member of the Committee prior to the date of the meeting in a timely manner.

4. Authority and duties

Authority

- 4.1 The Committee is authorised by the Board to –
- (a) investigate any activity within its terms of reference and shall have unrestricted access to books and records for this purpose;
 - (b) seek any information that it requires from any employee and all employees shall be directed to cooperate with any request made by the Committee; and
 - (c) obtain outside legal, accounting or other independent professional advice at the Corporation's expense and to secure the attendance of outsiders with relevant experience and expertise if it considers this necessary.

Duties and responsibilities

- 4.2 The duties and responsibilities of the Committee shall be to -
- (a) give to the Board such assurance as it may reasonably require regarding the reliability of financial information submitted to it and of financial statements issued by the Corporation;
 - (b) make recommendations to the Board on the appointment, removal and remuneration of the external auditor;
 - (c) oversee the process for selecting the external auditor and make appropriate recommendations through the Board to the Chief Executive of the HKSAR;
 - (d) assess the independence and objectivity of the external auditor having regard to HK professional and regulatory requirements, including ensuring the rotation of key partners at appropriate intervals;
 - (e) pre-approve/monitor (whichever is appropriate) the appointment of the external auditor to any of the Corporation's subsidiary companies and any additional services to be undertaken by the external auditor of such companies;
 - (f) pre-approve all additional audit or non audit services to be undertaken by the external auditor, including associated fees;
 - (g) ensure that the provision of additional audit or non-audit services does not impair the external auditor's independence or objectivity;
 - (h) review, and challenge, where necessary, the actions and judgements of management in relation to the Annual Report and Accounts before submission to the Board, paying particular attention to -
 - critical accounting policies and practices, and any changes in them
 - decisions requiring a major element of judgement
 - the extent to which the financial statements are affected by any unusual transactions in the year and how they are disclosed

- the clarity of disclosures
 - significant adjustments resulting from the audit
 - the going concern assumption
 - compliance with accounting standards
 - compliance with stock exchange, and other regulatory and legal, requirements to the extent that they are applicable to the Corporation
- (i) discuss with the external auditor, at an early stage, the nature and scope of the audit, including, in particular, the nature of any significant unresolved accounting and auditing problems; the nature of any significant adjustments, reclassification or additional disclosures proposed by the external auditor which are significant or which may in the future become material; and the nature and impact of any material changes in accounting policies;
 - (j) review subsequently whether the external auditor has met the Audit Committee's expectations as regards the agreed plan, their handling of key accounting and audit judgements, and in responding to questions from the Audit Committee;
 - (k) review the external auditor's management letter and management's response, and approve the same;
 - (l) keep under general review the system of internal audit in operation within the Corporation and to receive periodically reports from the internal auditor;
 - (m) recommend to the Managing Board the appointment or dismissal of the internal auditor;
 - (n) approve the annual internal audit plan and ensure that the internal audit function is adequately resourced and has appropriate standing within the Corporation, and make recommendations to the Managing Board where necessary;
 - (o) review management's and the internal auditor's reports on the adequacy and effectiveness of systems of internal control, financial reporting and risk management, and make recommendations to the Managing Board where necessary;
 - (p) review the Corporation's statement on internal control systems prior to endorsement by the Board and to review the policies and processes for identifying and assessing business risks and the management of these risks by the Corporation, and make recommendations to the Managing Board where necessary; and
 - (q) give to the Board such other assurance as it may reasonably require regarding compliance by the Corporation, its subsidiaries and those of its associates for which it provides management services with all legal and other regulations to which they are subject.

5. Whistle blowing

5.1 Establish and keep under review arrangements whereby employees of the Corporation can, in confidence, raise concerns about possible improprieties in financial reporting, internal control or other matters. The Committee should ensure that proper arrangements are in place for fair and independent investigation of these matters and for appropriate follow-up action.

6. Other Matters

6.1 The Committee shall -

- (a) review its TOR periodically and not less than once every three years, and make recommendations to the Board for changes where necessary;

- (b) ensure that the Committee's duties and activities during the year are adequately disclosed in the Annual Report; and
- (c) undertake on behalf of the Chairman or the Board such other related tasks as the Chairman or the Board may from time to time entrust to it.

163 – 170 (not used)

SUBMISSIONS TO THE MANAGING BOARD AND ITS COMMITTEES

171 The Managing Board has consciously decided to limit its consideration to those key matters specified in the Rules for Conduct of Corporation Business. The Chief Officer is responsible for deciding what other matters should be submitted to the Managing Board or one of its Committees. Advice may be sought from the Company Secretary.

172 The Chief Officer has a duty to ensure that all submissions to the Managing Board and its Committees (except the Audit Committee) state the relevant issues and proposals succinctly and definitively. In the case of the Audit Committee, the Chief Officer will only be concerned with those parts of papers which reflect Management's responses to audit findings and recommendations, and not with the findings and recommendations of either the Internal Auditor or the External Auditor, which will not be subject to amendment or softening.

173 The Chief Officer is responsible for deciding the content of papers to be submitted to the Board. In addition, the Chief Officer will ensure that the Chairman is appropriately briefed on the content of papers. The Chairman has the responsibility to ensure that the content of papers submitted to the Managing Board accord with the policy previously laid down by the Managing Board, and where they do not, to bring this to the attention of the Chief Officer. In consultation with the Chairman, the Chief Officer will then be responsible for deciding whether any paper should be withdrawn from the agenda, whether the content of any paper should be amended to accord with the approved policy or whether the Managing Board's approval should be sought to amend the prevailing policy. Where the Chairman holds a different view from those expressed in a paper, Management will ensure that the Chairman's views and arguments are incorporated in the paper.

174 All papers relating to matters falling within the terms of reference of a Board Committee must be considered by that Committee before being submitted to the Board unless the Board or the Chairman declares otherwise.

175 The Chairman, and Members having cleared any board paper initiated by them with the Chairman, may submit papers to the Managing Board in accordance with paragraph 134.

176 - 200 (not used)