Notes on the Accounts

(Expressed in United States dollars)

1. BASIS OF PRESENTATION

(a) Statement of compliance

Although not required to do so under the Bye-Laws of the Company, the accounts of the Company and the Group are prepared so as to comply with the disclosure requirements of the Hong Kong Companies Ordinance, generally accepted accounting principles in Hong Kong and all applicable Statements of Standard Accounting Practice ("SSAP") and Interpretations issued by the Hong Kong Society of Accountants. The accounts of the Company and the Group have opted to early adopt SSAP 9 (revised) "Events after the balance sheet date" ("SSAP 9"), SSAP 28 "Provisions, contingent liabilities and contingent assets", SSAP 30 "Business combinations" ("SSAP 30"), SSAP 31 "Impairment of assets" and SSAP 32 "Consolidated financial statements and accounting for investments in subsidiaries".

(b) Basis of consolidation

The consolidated accounts incorporate the accounts of the Company and all its subsidiaries made up to 30 June each year. All material intra-group accounts and transactions are eliminated upon consolidation. The Group's results include, in respect of any subsidiaries acquired during the year, their results attributable to the periods since the dates of acquisition and, in the case of subsidiaries disposed of during the year, their results attributable to the periods up to the dates of disposal.

Goodwill arising on consolidation represents the excess of the cost of investment over the fair value of the Group's share of the net assets of subsidiaries, associates and jointly controlled entities acquired. Goodwill arising on each acquisition of subsidiaries, associates and jointly controlled entities is capitalised and amortised on a straight line basis over its estimated useful life not exceeding 20 years. Any impairment loss identified will be recognised as an expense in the profit and loss account immediately.

(c) Basis of preparation of the accounts

The measurement basis used in the preparation of the accounts is historical cost modified by the revaluation of investment properties and land and buildings, and the marking to market of certain investments in securities as explained in the accounting policies set out below.

2. PRINCIPAL ACCOUNTING POLICIES

(a) Revenue recognition

Provided it is probable that the economic benefits will flow to the Group and the revenue and costs, if applicable, can be measured reliably, revenue is recognised in the profit and loss account as follows:

(i) Interest income

- interest income from loans and advances and deposits is accrued on a time-apportioned basis on the principal outstanding and at the rate applicable except where the recoverability of the principal outstanding is in doubt; and
- interest income from dated debt securities intended to be held to maturity is recognised as it accrues, as adjusted by the amortisation of the premium or discount on acquisition, so as to achieve a constant rate of return over the period from the date of purchase to the date of maturity.

2. PRINCIPAL ACCOUNTING POLICIES (CONT'D)

(a) Revenue recognition (Cont'd)

(ii) Fee income and expense from banking operations are recognised when earned or incurred except where the fee is charged to cover the costs of a continuing service to, or risk borne for, the customer, or is interest in nature. In these cases, the fee is recognised on an appropriate basis over the relevant period. Other service fee income is recognised based on the stage of completion of the service rendered.

(iii) Dividend income is recognised as follows:

– dividends from non listed investments are recognised when the right to receive payment is established; and

– dividends from listed investments are recognised when the share price of such investments goes ex-dividend.

(iv) Revenue on the disposal of development properties is recognised in the accounts using the percentage of completion method based on the stage of completion as certified by the architects or quantity surveyors. Provision for foreseeable loss is made in the year in which such loss is determined.

(v) Revenue arising from the disposal of other properties is recognised when substantially all the conditions of sales have been met and the risks and rewards of ownership have been transferred to the buyers.

(vi) Rental income from operating leases is recognised on a straight line basis over the period of the respective leases.

(vii) Commission and brokerage income in respect of securities trading is recognised on the contractual completion of trades.

(viii) Insurance premiums

Premiums are accounted for in the period in which the amount is determined, which is generally the period in which the risk commences.

Premiums, commission and claims paid or payable on inward treaty reinsurance business are accounted for on the basis of the latest advice from ceding companies or agents.

Unearned premiums represent the estimated proportion of the net written premiums, after reinsurance and acquisition costs where applicable, which relates to periods of risk subsequent to the balance sheet date. Unearned premiums are calculated as follows:

Accident and Health, Ships, Property Damage, General Liability and Pecuniary Loss	40%
Goods in Transit	25%

2. PRINCIPAL ACCOUNTING POLICIES (CONT'D)

(b) Investments

(i) Investment in securities

Investments in debt and equity securities, except those held either solely for the purpose of recovering advances or, as investments in subsidiaries, associates or jointly controlled entities, are accounted for as follows:

Investments in securities are classified as held-to-maturity securities, investment securities and other investments in securities, and are recognised as assets from the date on which the Group is bound by the contract which gives rise to them.

Transfer of a security between categories of investments is accounted for at fair value. The profit or loss arising from transfers between categories of investments is accounted for as if the investment had been sold and repurchased at the date of transfer.

Held-to-maturity securities

Investments in dated debt securities which the Group has expressed the intention and ability to hold to maturity, are stated in the balance sheet at cost adjusted for the amortisation of premiums or discounts arising on acquisition, less any provisions for diminution in value which is other than temporary.

The carrying amounts of held-to-maturity securities are reviewed as at the balance sheet date in order to assess the credit risk and whether the carrying amounts are expected to be recovered. Provisions are made when carrying amounts are not expected to be recovered and are recognised as an expense in the profit and loss account.

Investment securities

Equity and debt securities which are intended to be held on a continuing basis for an identified long term purpose at the time of acquisition are stated in the balance sheet at cost less any provisions for diminution in value which is other than temporary.

The carrying amounts of investment securities are reviewed as at the balance sheet date in order to assess whether the fair values have declined below the carrying amounts. When such a decline has occurred, the carrying amount is reduced to the fair value unless there is evidence that the decline is temporary. The amount of the reduction is recognised as an expense in the profit and loss account.

Other investments

Other securities are stated in the balance sheet at fair value. Changes in fair value are recognised in the profit and loss account as they arise.

Fair value is the amount for which an asset can be exchanged, or a liability settled, between knowledgeable willing parties in an arm's length transaction.

Provisions against the carrying value of held-to-maturity securities and investment securities are written back when the circumstances and events that led to the write-down or write-off cease to exist and there is persuasive evidence that the new circumstances and events will persist for the foreseeable future.

Profits or losses 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.

2. PRINCIPAL ACCOUNTING POLICIES (CONT'D)

(b) Investments (Cont'd)

(ii) Interest in subsidiaries

A subsidiary 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.

Interest in subsidiaries is stated in the Company's balance sheet at cost less provision for diminution in value which is other than temporary as determined by the directors.

(iii) Interest in associates

An associate is a company in which the Group has a long term equity interest and over which the Group is in a position to exercise significant influence, but not control or joint control, in its management, including participation in financial and operating policy decisions.

The consolidated profit and loss account includes the Group's share of the post-acquisition results of its associates for the year. In the consolidated balance sheet, interest in associates is accounted under the equity method and is stated at cost, less amortised goodwill, and adjusted for the post acquisition change in the Group's share of the associates' net assets.

(iv) Interest in jointly controlled entities

A jointly controlled entity is an entity which operates under a contractual agreement whereby the Group or Company and at least one other party undertake an economic activity which is subject to control and none of the parties involved unilaterally has control over the economic activity.

The consolidated profit and loss account includes the Group's share of the post-acquisition results of its jointly controlled entities for the year. In the consolidated balance sheet, interest in jointly controlled entities is accounted for under the equity method and is stated at cost, less amortised goodwill, and adjusted for the post acquisition change in the Group's share of the jointly controlled entities' net assets.

(c) Fixed assets and depreciation

(i) In preparing these accounts, advantage has been taken of the transitional provisions set out in paragraph 72 of SSAP 17 "Property, plant and equipment" issued by the Hong Kong Society of Accountants in July 1995, with the effect that premises have not been revalued to fair value at the balance sheet date.

The Group's premises are included at directors' valuation made having regard to independent professional valuations carried out in 1993. Surplus arising on revaluation is credited to the revaluation reserve. Additions to revalued premises made subsequent to the revaluation are included at cost. Premises which have not been the subject of a revaluation are included at cost.

The carrying amount of fixed assets is reviewed periodically in order to assess whether the recoverable amount has declined below the carrying amount. When such a decline has occurred, the carrying amount is reduced to the recoverable amount. The amount of the reduction is recognised as an expense, unless it reverses a previous revaluation increase in which case it is charged directly against any related revaluation reserve to the extent that the reduction does not exceed the amount held in the revaluation reserve in respect of the same item. In determining the recoverable amount, expected future cash flows generated by the fixed assets are not discounted to their present value.

2. PRINCIPAL ACCOUNTING POLICIES (CONT'D)

(c) Fixed assets and depreciation (Cont'd)

A subsequent increase in the recoverable amount of an asset carried at depreciated cost is written back to the profit and loss account when the circumstances and events that led to the write-down or write-off cease to exist. Any subsequent increase in the recoverable amount of an asset carried at valuation is credited firstly to the profit and loss account to the extent of any deficit previously charged to the profit and loss account in respect of that same asset, and is thereafter taken to the revaluation reserve.

(ii) Premises are stated at cost or valuation less depreciation calculated to write off the assets over their estimated useful lives as follows:

- freehold land is not depreciated.
- land held on lease is depreciated over the unexpired terms of the leases on a straight line basis.
- buildings and improvements thereto are depreciated at the higher of 2% per annum or over the unexpired terms of the leases on a straight line basis.

Furniture, fixtures and equipment are stated at cost less depreciation calculated on a straight line basis to write off the assets over their estimated useful lives, taken as being between 3 to 10 years.

(iii) On disposal of fixed assets, the profit or loss is determined as the difference between the net sale proceeds and the carrying amount. Any related revaluation surplus is transferred from the revaluation reserve to retained profits.

(d) Investment properties

Investment properties with an unexpired lease terms of more than 20 years are stated in the balance sheet at their open market value. An internal valuation is done annually and an independent professional valuation is made at least once every three years. The net surplus or deficit on revaluation is taken to the investment property revaluation reserve except when the total of the reserve is not sufficient to cover a deficit on an aggregate basis, in which case the amount by which the deficit exceeds the amount in the investment property revaluation reserve is charged to the profit and loss account.

No depreciation is provided in respect of investment properties with an unexpired lease term of over 20 years since the valuation takes into account the state of each property at the date of valuation.

On disposal of an investment property, the related portion of surpluses or deficits previously taken to the investment property revaluation reserve is transferred to the profit and loss account for the year.

(e) Properties held for resale

Properties held for resale are included in the balance sheet as current assets and are stated at the lower of cost and net realisable value. Cost includes land and building cost and other expenses incurred incidental to the acquisition of these properties. Net realisable value represents the estimated selling price less costs to be incurred in selling the properties.

(f) Development properties

Development properties are stated at cost less any provisions for diminution in value which is other than temporary as determined by the directors, plus, where appropriate, a portion of attributable profit less progress billings. Land, related acquisition expenses, development expenditure, interest and other related expenditure are capitalised as part of the cost of development properties.

2. PRINCIPAL ACCOUNTING POLICIES (CONT'D)

(g) Impairment of assets

Internal and external sources of information are reviewed at each balance sheet date to identify indications that the following assets may be impaired:

– furniture, fixtures and equipment;

– properties (other than investment properties);

– investments in subsidiaries, associates and joint ventures; and

– goodwill.

If any such indication exists, the asset's recoverable amount is estimated. An impairment loss is recognised whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount.

(i) Calculation of recoverable amount

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 there are assets that do not generate cash flows largely independent of those from other assets, recoverable amounts are determined for the smallest group of assets that generates cash inflows independently.

(ii) Reversals of impairment losses

In respect of assets other than goodwill, an impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. Impairment loss in respect of goodwill is reversed only if the loss was caused by a specific external event of an exceptional nature that is not expected to recur, and the increase in recoverable amount relates clearly to the reversal of the effect of that specific event.

A reversal of impairment loss 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, except where the assets are carried at revalued amounts, in which case the reversal of impairment loss is treated as a revaluation movement.

(h) Borrowing costs

Borrowing costs are expensed in the profit and loss account in the period in which they are incurred, except to the extent that they are capitalised as being directly attributable to the acquisition, construction or production of an asset which necessarily takes a substantial period of time to get ready for its intended use or sale.

(i) Finance leases and hire purchase transactions

Leases under which substantially all the risks and benefits of ownership are transferred to lessees are classified as finance lease. Where leases are leased out under finance lease, an amount representing the net investment in the lease is included in the balance sheet as advances to customers. Finance income implicit in the lease payments is credited to the profit and loss account over the period of the leases so to produce a constant periodic rate of return on the outstanding net investment in the leases for each accounting period. Contingent rentals are recognised as income in the accounting period in which they are receivable.

2. PRINCIPAL ACCOUNTING POLICIES (CONT'D)

(j) Operating leases

Payments under operating leases are charged to the profit and loss account on a straight line basis over the periods of the respective leases.

(k) Provisions for bad and doubtful loans and advances

Specific provisions are made for bad and doubtful loans and advances as and when they are so considered by the directors. In addition, amounts have been set aside as general provisions for doubtful loans and advances. The specific element relates to individual accounts; the general element relates to other exposures not separately identified but known from experience to exist in any portfolio of banking facilities. When there is no longer any realistic prospect of recovery, the outstanding loan is written off.

Interest on bad and doubtful loans and advances is credited to a suspense account which is netted in the balance sheet against the relevant balances.

(l) Long term notes and bonds issued

Long term notes and bonds are stated at their principal amounts plus unamortised premium. The premium arising from the issue of the notes and bonds is deferred and amortised on a straight line basis over the repayment period of the notes and bonds.

(m) Deferred taxation

Deferred taxation is provided using the liability method in respect of the taxation effect arising from all material timing differences between the accounting and tax treatments of income and expenditure, which are expected with reasonable probability to crystallise in the foreseeable future.

Future deferred tax benefits are not recognised unless their realisation is assured beyond reasonable doubt.

(n) Translation of foreign currencies

Foreign currency transactions during the year are translated into United States dollars at the rates of exchange ruling at the transaction dates. Monetary assets and liabilities in foreign currencies and the accounts of overseas subsidiaries, associates and jointly controlled entities are translated into United States dollars at the rates of exchange ruling at the balance sheet date. Differences on foreign currency translation are dealt with in the profit and loss account with the exception of those arising on the translation of foreign currency accounts of subsidiaries, associates and jointly controlled entities which are dealt with in reserves.

(o) Insurance operations

The insurance results are determined after making provision for unexpired risks and outstanding claims, whether or not reported at the balance sheet date.

2. PRINCIPAL ACCOUNTING POLICIES (CONT'D)

(p) Staff retirement scheme

The Group operates a defined contribution provident fund scheme (the "Scheme") for its wholly own subsidiaries incorporated in Hong Kong, and the contributions thereto are charged to the profit and loss account for the year. With the introduction of Mandatory Provident Fund ("MPF"), the Group has wound up the Scheme with effect from 1 December 2000. The Group has set up a MPF scheme by participating in a master trust scheme provided by a subsidiary of the Company to comply with the requirements under the MPF legislation. Contributions and accrued benefits under the Scheme as at 30 November 2000 were transferred to the Employer's Voluntary Contribution Account of the Dao Heng MPF Master Trust Plan.

The Group also contributed to retirement schemes of its overseas subsidiaries in accordance with their respective requirements and the contributions thereto are charged to the profit and loss account for the year.

(q) Off-balance sheet financial instruments

Off-balance sheet financial instruments arise from futures, forward, swap and option transactions undertaken by the Group in the foreign exchange, interest rate and equity markets. The accounting for these instruments is dependent upon whether the transactions are undertaken for dealing purposes, to hedge risk, or as part of the management of asset and liability portfolios.

Transactions undertaken for dealing purposes are marked to market and the net present value of the gain or loss arising is recognised in the profit and loss account as dealing profits/losses, after appropriate deferrals for unearned credit margin and future servicing costs.

Transactions designated as hedges are valued on an equivalent basis to the assets, liabilities or net positions which they are hedging. Any profit or loss is recognised on the same basis as that arising from the related assets, liabilities or net positions.

Interest rate swap transactions undertaken as part of the management of asset and liability portfolios are separately identified and interest income or expenses arising therefrom is netted off against the related interest income or expenses on the on-balance sheet items these transactions are hedged against.

Unrealised gains on transactions which are marked to market are included in "Other assets" in the balance sheet. Unrealised losses on transactions which are marked to market are included in "Other payables and provision".

(r) 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 or entities.

(s) Cash equivalents

For the purpose of the consolidated cash flow statement, cash equivalents include short-term, highly liquid investments which are readily convertible into known amounts of cash without notice and which were within three months of maturity when acquired net off advances from banks repayable within three months from the date of the advance.