

NOTES TO FINANCIAL STATEMENTS

31 July 2000

1. CORPORATE INFORMATION

During the period, the Group was principally involved in the marine engineering business. The Group's business segments of contracting, structural steel and electrical and mechanical engineering were discontinued during the period, as detailed in note 2(d) below.

2. CORPORATE UPDATE

(a) Restructuring agreement

During the period, the Group's operations were sustained at a significantly reduced level to preserve its resources. The focus of the Group was on concluding a viable debt restructuring arrangement with the creditors. The Group ceased to tender for public works contracts pursuant to a suspension arrangement made with the Hong Kong Government Works Bureau on 6 August 1998. As at the date of approval of these financial statements, most of the Group's construction contracts have been either terminated or completed. The Group is currently concentrating on its marine engineering business which had a profitable track record in the past. Throughout the period, the Group also held ongoing discussions with its bankers and creditors with a view to concluding a restructuring arrangement for the Group's debts.

In order to facilitate the implementation of the proposed schemes of arrangement, on 16 October 1999, the Company and certain of its subsidiaries, excluding KEL Holdings Limited ("KEL") and its subsidiaries (collectively the "KEL Group"), entered into a restructuring agreement (the "Restructuring Agreement") with, inter alia, Harbour Front Limited ("Harbour Front"), the then controlling shareholder of the Company, Mr Leung Yat Tung ("Mr Leung"), Mrs Leung Yu Oi Ling, Irene, the spouse of Mr Leung, ("Mrs Leung"), UDL Marine Assets (Hong Kong) Limited ("UMAHK") and UDL Marine Assets (Singapore) Pte Limited ("UMASPG"). Mr Leung and Mrs Leung are directors of the Company and Mrs Leung is one of the beneficiaries of a discretionary trust which beneficially owned all of the units in a unit trust, for which Harbour Front and its wholly-owned subsidiary, or their designated nominees held the controlling shares in the Company as trustee. Each of UMAHK and UMASPG currently holds a fleet of marine craft and vessels and is principally engaged in the marine engineering business. They were controlled and/or beneficially owned by Mr Leung and/or Mrs Leung as at 16 October 1999.

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2. CORPORATE UPDATE *(Continued)*

(a) Restructuring agreement *(Continued)*

The principal terms of the reorganisation proposal, which include the proposed schemes of arrangement (the "Reorganisation Proposal"), involved, inter alia, the following:

- (i) schemes of arrangement for the Company and 24 of its subsidiaries (collectively the "Scheme Participating Companies"), excluding the KEL Group, under Section 166 of the Hong Kong Companies Ordinance (individually the "Scheme" and collectively the "Schemes");
- (ii) a reduction and consolidation of the issued share capital of the Company, a reduction of its share premium account (the "UDL Capital Reorganisation"), further details of which are set out in note 28(a) to the financial statements;
- (iii) a rights issue of approximately 210 million rights shares to the then existing shareholders on the basis of five rights shares for every share held by them upon the completion of the UDL Capital Reorganisation (the "Rights Issue"), further details of which are set out in note 28(b) to the financial statements;
- (iv) a new issue of approximately 252 million new shares of \$0.10 each in the capital of the Company after the UDL Capital Reorganisation to the non-preferential scheme creditors in proportion to their non-preferential scheme debts; and
- (v) the acquisition of UMAHK and UMASPG by the Company from the proceeds of the Rights Issue.

The UDL Capital Reorganisation and the Rights Issue were approved at a special general meeting of the Company held on 24 March 2000. The UDL Capital Reorganisation became effective on 28 April 2000 and the Rights Issue became unconditional on 25 May 2000.

Further details of the Restructuring Agreement and the Reorganisation Proposal are set out in the Company's announcement dated 16 October 1999 and the Company's circular to shareholders dated 1 March 2000.

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2. CORPORATE UPDATE *(Continued)*

(b) The Schemes

The implementation of the Schemes involve, inter alia, the following principal steps:

- (i) the transfer of the unencumbered assets of the Scheme Participating Companies (the "Unencumbered Assets") and the net proceeds from the recovery of their accounts receivable (the "Accounts Receivable"), other than those receivables which are intercompany debts and those charged to financial creditors as security, for no consideration to a company newly incorporated in Hong Kong with limited liability (the "Newco"), the shares of which are held by the administrator of the Schemes (the "Scheme Administrator") on trust for the scheme creditors;
- (ii) the distribution of the proceeds from the sale of the Unencumbered Assets and the recovery of the Accounts Receivable, after settlement of post-scheme costs and the preferential claims of the scheme creditors, to the scheme creditors in proportion to their scheme debts as cash dividends;
- (iii) the issue of 252,306,195 new shares of HK\$0.10 each to the scheme creditors in proportion to their non-preferential scheme debts, representing 50% of the enlarged issued share capital of the Company; and
- (iv) the acceptance by each non-preferential scheme creditor of (i) the payment of cash dividends and (ii) the issue and allotment of new shares of the Company to him, in each case in accordance with the provisions of the Scheme, in full satisfaction and discharge of his non-preferential scheme debt.

The Company has undertaken to the trustee, being the Scheme Administrator for the time being, by a trust deed dated 11 February 2000 made between the Company and the trustee for the benefit of the scheme creditors, that the aggregate disposal proceeds of the Unencumbered Assets and the Accounts Receivable realised under the Schemes shall not be less than HK\$176 million. In the event of a shortfall (the "Shortfall"), the Company is required to make up the Shortfall beginning in the fourth financial year after the financial year in which the Schemes became effective. The amount of payment for the Shortfall by the Company in every financial year is limited to a maximum of 60% of the consolidated net profit of the Company and its subsidiaries for that financial year. There are no payment obligations on the Company in respect of the Shortfall in respect of any financial year in which the Company does not make an audited consolidated net profit. The Company's obligation to make up the Shortfall shall not be discharged unless and until the Company has paid the Shortfall in full.

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2. CORPORATE UPDATE *(Continued)*

(b) The Schemes *(Continued)*

On 14 March 2000, the Schemes were approved with the requisite majority of creditors at the respective creditors' meetings of the Scheme Participating Companies and were conditionally sanctioned by the Hong Kong Court of First Instance (the "Court") on 18 April 2000. On 28 April 2000 (the "Effective Date"), all conditions precedent were fulfilled and the Court sanctioning of the Schemes became unconditional and the Schemes became effective upon the registration of the court order sanctioning the Schemes with the Registrar of Companies in Hong Kong. On 26 May 2000, the Rights Issue and the acquisition of the shares of UMAHK and UMASPG by the Company under the Restructuring Agreement were completed, the implementation of the Schemes became unconditional and the Company issued approximately 252 million new shares of HK\$0.10 each to the Scheme Administrator pending distribution to the non-preferential scheme creditors upon the implementation of the Schemes.

Since 21 August 1998, 10 winding-up petitions have been presented by certain creditors against nine of the Scheme Participating Companies, excluding the KEL Group. The winding-up petition presented against the Company was dismissed pursuant to a court order dated 29 May 2000 and all other winding-up petitions were dismissed pursuant to court orders dated on 26 June 2000. On 20 July 2000, appeals were made against dismissal of 5 of the winding-up petitions which were presented by ex-employees of certain of the Scheme Participating Companies. Those appeals were heard on 7 and 8 November 2000 and the Court of Appeal will hand down its written judgement in due course. The directors, having consulted their legal advisers, are of the opinion that the likelihood of success of the appeals is remote.

During the period, KEL and certain of its subsidiaries have also undertaken schemes of arrangement under Section 166 of the Hong Kong Companies Ordinance, not connected with the Schemes, for the restructuring of the KEL Group's debts. The two winding-up petitions against UDL Kenworth Engineering Limited, which were presented by certain creditors of the KEL Group prior to the current period, were dismissed pursuant to court orders on 19 July 1999 and 21 August 2000, respectively.