

The Company's financial statements are prepared in accordance with the accounting principles generally accepted applicable in Hong Kong ("HK GAAP"), which differ in certain significant respects from those applicable in the United States ("US GAAP"). The significant differences relate principally to the following items, and the adjustments considered necessary to restate profit ("net income") and shareholders' funds ("shareholders' equity") in accordance with US GAAP are shown in the tables set out below.

A Revenue recognition on property developments

Under HK GAAP, where the Company 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 Company in connection with the development. Also under HK GAAP, where the Company receives a distribution of the assets of the development upon completion of construction, profit is recognised based on the fair value of such assets at the time of receipt. Under US GAAP, such profits would be recognised during construction of the property on a percentage-of-completion basis.

B Telford headquarters redevelopment

Under HK GAAP, the redeveloped headquarters building retained by the Company was recorded as an addition of land and buildings at open market value. The shopping centre and cash received from the developer, net of related costs, were recognised as property development profits. Under US GAAP, the redevelopment would be accounted for as a non-monetary transaction and such redevelopment would be recorded at historical cost with no profit recognition thereon.

C Asset revaluations and depreciation

Under HK GAAP, investment properties are stated on the basis of appraised value, and depreciation expense is not provided on such properties. Also under HK GAAP, office land and buildings are stated at their open market values on the basis of their existing use at the date of revaluation less any subsequent accumulated depreciation. Under US GAAP, such revaluations are not permitted. Accordingly, the properties of the Company, which are stated at appraised or open

market value, have been restated at historical cost less accumulated depreciation. Depreciation has been based on the historical cost of the properties and a useful life of 50 years. The approximate gross historical cost of investment properties subject to depreciation under US GAAP which are not depreciated under HK GAAP amounted to HK\$2,978 million and HK\$3,039 million at 31 December 1999 and 2000, respectively.

D Depreciation of certain fixed assets

Prior to 1995, under HK GAAP, the historical cost of the Company's tunnel lining and underground civil structures was not depreciated. Under established industry practice in the United States for similar costs, depreciation is provided for financial accounting purposes over extended periods. For US GAAP purposes, the Company has depreciated such costs over a 100-year period.

With effect from 1 January 1995, under HK GAAP, the Company re-appraised the estimated useful life of the tunnel lining and underground civil structures. In accordance with such re-appraisal, such costs are being depreciated over the number of years remaining using an original life of 100 years. Such change in life was accounted for prospectively, with no cumulative adjustment recognised in 1995.

Additionally, prior to 1995 under HK GAAP, the cost of leasehold land was not amortised, based on assumed extensions of the leases. Under US GAAP, the amortisation of the historical cost of leasehold land is provided over the life of the leases, without any consideration of renewals.

With effect from 1 January 1995, under HK GAAP, all leasehold land is amortised over the unexpired terms of the leases. This change in accounting policy under HK GAAP was applied prospectively, with no cumulative adjustment recognised in 1995.

E Pension costs

Under HK GAAP, the provision for the defined benefit element of the MTR Corporation Limited Retirement Scheme is generally based on the contributions made to the Scheme. Such contributions are determined by the Board with reference to an actuarial valuation. Under US GAAP, the defined benefit element of the Scheme is recognised as a charge to income over the employees' approximate service period, in accordance with United States Statement of Financial Accounting

Standards ("SFAS") No. 87, "Employers' Accounting for Pensions". SFAS No. 87 focuses on the Scheme's benefit formula as the basis for determining the benefit earned, and therefore the cost incurred, in each year. The determination of the benefit earned is actuarially determined and includes components for service cost, time value of money, return on plan assets and gains or losses from changes in previous assumptions.

F Income taxes

The Company's deferred taxation is provided using the liability method in respect of the taxation effect arising from all material timing differences which are expected with reasonable probability to become payable in the foreseeable future. With respect to deferred tax assets (a net deferred tax debit), HK GAAP includes recognition criteria providing for net deferred tax assets which are probable of recovery in the foreseeable future, with assurance beyond a reasonable doubt that taxable income will be generated in the future. Based on these recognition criteria, as disclosed in Note 12, the Company had an unrecognised net deferred tax liability at 31 December 2000, which is not expected with reasonable probability to become payable.

US GAAP requires that full provision be made for all deferred taxes as they arise, except that a valuation allowance is provided on deferred tax assets to the extent that it is not "more likely than not" that such deferred tax assets will be realised. Under US GAAP, "more likely than not" is defined as a likelihood of more than 50 percent.

G Capitalisation of certain costs

Under HK GAAP, certain costs of a non-incremental nature are capitalised relative to the Airport Railway Project and other capital projects. Under US GAAP, it is not permissible to capitalise these non-incremental costs. The preponderance of the capitalised costs relating to the Airport Railway Project and other capital projects is incremental in nature and accordingly, is properly capitalised under both HK GAAP and US GAAP.

H Interest

Under HK GAAP, interest earned on funds obtained by the Company specifically for the construction of the Airport Railway prior to the date of expenditure for such purpose is

credited to construction in progress related to the Airport Railway. Interest earned for this purpose includes notional interest on funds temporarily applied by the Company for purposes other than related to the construction of the Airport Railway. Under US GAAP, actual interest earned is included in the determination of profit for such period, and notional interest on funds temporarily applied is not recognised.

I Offsetting amounts related to foreign currency exchange contracts

Under HK GAAP, the accrued gains and losses on foreign currency exchange contracts are used to offset gains and losses resulting from currency fluctuations inherent in the underlying foreign currency liabilities. Under US GAAP, the accrued gains and losses related to the foreign currency exchange contracts cannot be netted against the foreign currency debt as they are two separate legal transactions that do not have the right of setoff. The amount of accrued gains/(losses) related to the foreign currency exchange contracts that was netted against the foreign currency debt amounted to HK\$133 million and HK\$(51) million for the year ended 31 December 1999 and 2000, respectively.

J Stock based compensation

Under HK GAAP, share options granted by the Company and shares granted by the principal shareholder (defined as shareholding larger than 10%) for no consideration to the employees of the Company are not required to be recognised in the profit and loss account of the Company. Under US GAAP, such share options and shares granted are accounted for in accordance with Accounting Principles Board Opinion 25 as contributions to capital with the offsetting charge to the profit and loss account as compensation expense. The compensation expense for the share grants is measured based on the quoted market price of the shares and in case of share options, the difference between the quoted market price of the shares less the exercise price, at a defined measurement date. The measurement date is the first date on which both the number of shares that an individual employee is entitled to receive and the exercise price are known.

K Others

Other adjustments primarily represent the net effect of costs deferred under HK GAAP which are required to be recognised

as expenses under US GAAP, and certain anticipated expenses recognised under HK GAAP which are not recognised as expenses under US GAAP until the related goods or services are received or provided.

L Dividend

Under HK GAAP, dividends to shareholders are recognised in the period during which the income from which the dividend is to be declared was earned. Under US GAAP, dividends are recognised in the period in which they are declared.

M Staff separation payments

Under HK GAAP, employee separation expenses are not included as part of operating expenses and are reported as a separate line caption in the profit and loss account. Under US GAAP, expenses relating to employee separation arrangements

are included as part of operating expenses and are not reported as a separate caption in the profit and loss account.

N Recently issued accounting standards

In June 1998, the United States Financial Accounting Standards Board issued SFAS No. 133 "Accounting for Derivative Instruments and Hedging Activities". SFAS No. 133 requires companies to adopt its provisions for all fiscal quarters of all fiscal years beginning after 15 June 2000, as deferred by SFAS No. 137. Earlier application of all of the provisions of SFAS No. 133 is permitted, but the provisions cannot be applied retroactively to financial statements of prior periods. SFAS No. 133, as amended by SFAS No. 138, standardises the accounting for derivative instrument by requiring that an entity recognise those items as assets or liabilities in the balance sheet and measure at fair value.

Reconciliation of net income to US GAAP

in million	Year ended 31 December		
	1999 HK\$	2000 HK\$	2000 US\$ (note)
Profit for the year in accordance with HK GAAP	2,116	4,055	520
Adjustments required under US GAAP			
Revenue recognition on property developments	635	(13)	(2)
Depreciation on revalued properties and redevelopment	(54)	(57)	(7)
Depreciation on certain fixed assets	(2)	10	1
Difference in periodic pension cost	36	182	23
Deferred tax accounting	(49)	(574)	(73)
Capitalisation of certain costs	(159)	(151)	(19)
Interest	(21)	(21)	(3)
Stock based compensation	-	(25)	(3)
Other	19	3	-
Tax effect of above adjustments	(72)	9	1
Net income for the year in accordance with US GAAP	<u>2,449</u>	<u>3,418</u>	<u>438</u>
Basic and diluted earnings per share	<u>HK\$0.49</u>	<u>HK\$0.68</u>	<u>US\$0.09</u>

Reconciliation of shareholders' equity to US GAAP

in million	1999 HK\$	As of 31 December 2000 HK\$	2000 US\$ (note)
Shareholders' funds in accordance with HK GAAP	45,115	49,828	6,388
Adjustments required under US GAAP			
Revenue recognition on property developments	1,074	1,061	136
Accumulated depreciation on revalued properties and redevelopment	(177)	(234)	(30)
Asset revaluation reserves	(5,482)	(6,640)	(851)
Accumulated depreciation on certain fixed assets	(801)	(791)	(101)
Difference in periodic pension cost	(493)	(311)	(40)
Deferred tax accounting	(1,183)	(1,757)	(225)
Capitalisation of certain costs	(957)	(1,108)	(142)
Interest	718	697	89
Other	35	38	5
Tax effect of above adjustments	30	39	5
Dividend	-	500	64
Shareholders' equity in accordance with US GAAP	<u>37,879</u>	<u>41,322</u>	<u>5,298</u>

Note: For the convenience of readers, the US dollars equivalent was translated at HK\$7.7998 which was the Hong Kong closing buying rate quoted from Reuters at 4 pm of 29 December 2000.