## 1 PRINCIPAL ACCOUNTING POLICIES

The principal accounting policies adopted in the preparation of these accounts are set out below.

### (a) Basis of preparation

The accounts have been prepared under the historical cost convention as modified by the revaluation of investment properties and other investments, in accordance with accounting principles generally accepted in Hong Kong and comply with accounting standards issued by the Hong Kong Society of Accountants.

### (b) Consolidation

The consolidated accounts comprise the accounts of the Company and all its subsidiaries made up to 31 December. All significant inter-company transactions and balances within the Group are eliminated on consolidation.

A subsidiary is a company in which the Company, directly or indirectly, controls more than half of the voting power or issued share capital or of whose board of directors it controls the composition.

The results of subsidiaries acquired or disposed of during the year are included in the group accounts from the effective date of acquisition or up to the effective date of disposal, as appropriate.

Goodwill represents the excess of the purchase consideration over the fair value ascribed to the net assets of subsidiaries acquired. Reserve on consolidation represents the excess of fair value of the net assets of subsidiaries acquired over the purchase consideration. Any goodwill or reserve on consolidation is charged or credited, as appropriate, directly to reserves.

The gain or loss on the disposal of a subsidiary represents the difference between the proceeds of the sale and the Group's share of its net assets together with any goodwill or reserve on consolidation which was not previously charged or recognised in the consolidated profit and loss account.

Minority interests represent the interests of outside shareholders in the operating results and net assets of subsidiaries.

Investments in subsidiaries are recorded in the Company's accounts at cost, being the fair value of the consideration given plus related acquisition costs, less any provision required for permanent diminution in value. The results of subsidiaries are accounted for by the Company on the basis of dividends received and receivable.

### (c) Associated companies

Associated companies are companies other than subsidiaries in which the Group effectively holds a long term equity investment and over whose management it is able to exercise significant influence.

The consolidated profit and loss account includes the Group's share of the results of associated companies for the year, and the consolidated balance sheet includes the Group's share of the net assets of associated companies.

Premium on acquisition, which represents the excess of purchase consideration over the fair values ascribed to the separable net assets of associated companies, is recognised as an asset and amortised through the consolidated profit and loss account over their estimated economic lives to the Group of between three and fifteen years as deemed appropriate by the directors.

## 1 PRINCIPAL ACCOUNTING POLICIES (CONT'D)

### (d) Revenue recognition

Revenue from sales is recognised on the transfer of risks and rewards of ownership, which generally coincides with the time of shipment.

Interest income is recognised on a time proportion basis, taking into account the principal amounts outstanding and the interest rates applicable.

Dividend income is recognised when the right to receive payment is established.

Rental income from letting the Group's investment property is recognised on a straight line basis.

### (e) Deferred taxation

Deferred taxation is accounted for at the current tax rate in respect of timing differences between profit as computed for taxation purposes and profit as stated in the accounts to the extent that a liability or an asset is expected to be payable or recoverable in the foreseeable future.

### (f) Advertising and marketing expenses, advanced royalties and product development costs

Advertising and marketing expenses are written off as incurred, except for the production costs of commercials and related programming costs which are deferred and written off in the year the commercial is first aired.

Advanced royalties represent prepayments made to licensors of intellectual properties under licensing agreements. All prepayments with respect to these agreements are recoupable against future royalties. Advanced royalties are amortised at the contractual royalty rate based on actual product sales. Management evaluates the future realisation of advanced royalties periodically and charges to expense any amounts that management deems unlikely to be recoupable at the contractual royalty rate through product sales. All advanced royalties are amortised within the term of the license agreement and are written off upon the abandonment of the product or upon the determination that there is significant doubt as to the success of the product.

Expenses relating to product development are deferred and charged to the profit and loss account in the year of initial product shipment.

**(g) Investment property**

Investment property is interests in land and buildings in respect of which construction work and development have been completed and which is held for their long term investment potential, any rental income being negotiated at arm's length.

Investment property is revalued annually by independent valuers and stated at its open market value at the balance sheet date. Changes in the value of investment property is dealt with as movements in the investment property revaluation reserve. If the total of this reserve is insufficient to cover a deficit on a portfolio basis, the excess of the deficit is charged to the profit and loss account. Where such a deficit has previously been charged to the profit and loss account and a revaluation surplus subsequently arises, this surplus is credited to the profit and loss account to the extent of the deficit previously charged. On disposal of an investment property, any revaluation reserve held in respect of the property is released to the profit and loss account.

Investment property is not depreciated except where the unexpired term of the lease is twenty years or less, in which case depreciation is provided on the carrying amount over the remaining term of the lease.

**(h) Other fixed assets**

Fixed assets other than investment properties are stated at cost less accumulated depreciation. Depreciation is calculated to write off the costs of these assets on a straight line basis over their expected useful lives to the Group. The principal annual rates used for this purpose are:–

| | *Percent* |
|---|---|
| Machinery and equipment | 12.5 to 20 |
| Office equipment, furniture and fixtures | 15 to 20 |
| Motor vehicles | 20 |
| Computer equipment | 25 to 33 |
| Computer software | 20 |

The Group owns the moulds and tools used in the production of the Group's products by third party manufacturers. Substantially all moulds and tools expenditure is depreciated in full in the year of initial product shipment.

Major costs incurred in restoring fixed assets to their normal working condition are charged to the profit and loss account. Improvements are capitalised and depreciated over their expected useful lives to the Group.

The carrying amounts of fixed assets are reviewed regularly to assess whether their recoverable amounts have declined below their carrying amounts. When such a decline has occurred, their carrying amount is reduced to their recoverable amount.

The gain or loss on disposal of a fixed asset is the difference between the net sales proceeds and the carrying amount of the relevant asset, and is recognised in the profit and loss account.

## 1 PRINCIPAL ACCOUNTING POLICIES (CONT'D)

### (i) Investment in securities

(i) *Investment securities*

Investment securities are securities which are intended to be held on a continuing basis for an identified long term purpose and are stated at cost or, in the case of investments previously treated as investments in associated companies, at their carrying value at the date of change of classification, less any provision for permanent diminution in value considered necessary by the directors.

The carrying value at the date of change of classification of investments previously classified as associated companies was the carrying value on the equity basis of accounting at that date. Any excess in the carrying value over cost at the date of change is carried as investments reserve. Upon the disposal of investment securities, profits or losses on disposal, representing the difference between the net sales proceeds and the carrying amounts, are recognised in the profit and loss account and the relevant portion of the investments reserve realised is transferred from the investments reserve to retained profits.

The carrying amounts of individual investments are reviewed at each balance sheet date to assess whether the fair values have declined below the carrying amounts. When a decline other than temporary has occurred, the carrying amount of such securities will be reduced to its fair value. The amount of the reduction is recognised as an expense in the profit and loss account and the relevant portion of the investments reserve is transferred from the investments reserve to retained profits.

(ii) *Other investments*

Other investments are carried at fair value. At each balance sheet date, the net unrealised gains or losses arising from the changes in fair value of other investments are recognised in the profit and loss account. Profits or losses on disposal of other investments, representing the difference between the net sales proceeds and the carrying amounts, are recognised in the profit and loss account as they arise.

### (j) Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined on a weighted average basis. Net realisable value is determined on the basis of anticipated sales proceeds less estimated selling expenses.

### (k) Accounts receivable

Provision is made against accounts receivable to the extent which they are considered to be doubtful. Accounts receivable in the balance sheet are stated net of such provision.

**(l) Operating leases**

Operating leases are leases where substantially all the rewards and risks of ownership of assets remain with the lessors. Related rental payments are charged to the profit and loss account on a straight line basis over the lease term.

**(m) Translation of foreign currencies**

Transactions in foreign currencies are translated at exchange rates ruling at the transaction dates. Monetary assets and liabilities expressed in foreign currencies at the balance sheet date are translated at rates of exchange ruling at the balance sheet date. Exchange differences arising in these cases are dealt with in the profit and loss account.

The accounts of subsidiaries expressed in foreign currencies are translated at the rates of exchange ruling at the balance sheet date. Exchange differences arising therefrom are dealt with as a movement in exchange fluctuation reserve.

**(n) Retirement benefits**

The Group's contributions to the mandatory provident fund scheme and the defined contribution retirement schemes are expensed as incurred. The contributions to the schemes are reduced by employers' contributions forfeited by those employees who leave the schemes prior to vesting fully in the contributions. The assets of all schemes are held separately from those of the Group in independently administered funds.

**(o) Borrowing costs**

Borrowing costs are charged to the profit and loss account in the year in which they are incurred.

*31 December 2000*

## 2 TURNOVER AND REVENUES

The Group is principally engaged in the creation, design, development, marketing and distribution of toys and family entertainment activity products. Revenues recognised during the year were as follows:

| | **2000** | 1999 |
|---|---|---|
| | ***HK$'000*** | *HK$'000* |
| Turnover | | |
| Sales of goods | **971,030** | 1,081,836 |
| Other revenues | | |
| Interest income from: | | |
| Bank deposits | **25,401** | 8,908 |
| Debt securities | **–** | 2,841 |
| Dividend income from: | | |
| Listed investments | **1,060** | 4,137 |
| Unlisted investments | **–** | 4 |
| Gross rental income from investment property | **213** | – |
| | **26,674** | 15,890 |
| Total revenues | **997,704** | 1,097,726 |

A geographical analysis of the Group's turnover and operating (loss)/profit for the year is as follows:

| | **Turnover** | | **Operating (loss)/profit** | |
|---|---|---|---|---|
| | **2000** | 1999 | **2000** | 1999 |
| | ***HK$'000*** | *HK$'000* | ***HK$'000*** | *HK$'000* |
| Principal markets: | | | | |
| North America | **866,079** | 855,654 | **(49,792)** | 12,943 |
| Europe | **88,407** | 216,736 | **12,669** | 8,331 |
| Asia Pacific | **12,654** | 8,640 | **728** | 2,311 |
| Others | **3,890** | 806 | **(396)** | 209 |
| | **971,030** | 1,081,836 | **(36,791)** | 23,794 |

## 3 OPERATING (LOSS)/PROFIT

The operating (loss)/profit is stated after charging and crediting the following:–

| | **2000** | 1999 |
|---|---|---|
| | ***HK$'000*** | *HK$'000* |
| **Charging:** | | |
| Cost of inventories sold | **443,958** | 477,664 |
| Depreciation of fixed assets | **12,872** | 28,814 |
| Staff costs | | |
| – Reversal of provision for discretionary bonus | **–** | (9,510) |
| – Others | **86,127** | 62,826 |
| Operating lease expenses | | |
| – Office and warehouse facilities | **9,638** | 17,079 |
| – Hire of equipment | **286** | 642 |
| Loss on disposal of fixed assets | **1,635** | – |
| Product development costs | **25,176** | 36,875 |
| Auditors' remuneration | **1,436** | 2,228 |
| **Crediting:** | | |
| Gain on disposal of fixed assets | **–** | 262 |

## 4 INTEREST EXPENSE AND BANK CHARGES

| | **2000** | 1999 |
|---|---|---|
| | ***HK$'000*** | *HK$'000* |
| Interest on bank loans and overdrafts | **11,186** | 8,786 |
| Other incidental borrowing costs | **3,005** | 5,766 |
| | **14,191** | 14,552 |

## 5 NET GAIN/(LOSS) ON INVESTMENT IN SECURITIES

| | **2000** | 1999 |
|---|---|---|
| | ***HK$'000*** | *HK$'000* |
| Net realised gain/(loss) on disposal of investment securities | **186,269** | (3,200) |
| Net realised gain/(loss) on disposal of other investments | **937** | (3,464) |
| Net unrealised loss on other investments | **(65,709)** | – |
| | **121,497** | (6,664) |

## 6 TAXATION

(a) The taxation charge in the consolidated profit and loss account comprises:–

| | 2000 HK$'000 | 1999 HK$'000 |
|---|---|---|
| Hong Kong profits tax | | |
| Current year | **1,589** | 1,636 |
| Prior years | **135** | 22,692 |
| Transferred to deferred taxation account | **100** | 890 |
| | **1,824** | 25,218 |
| Overseas taxation | | |
| Current year | **–** | 375 |
| Prior years | **–** | 5,629 |
| | **–** | 6,004 |
| Share of taxation attributable to associated companies | **2,612** | 2,388 |
| | **4,436** | 33,610 |

Hong Kong profits tax has been provided at the rate of 16% (1999: 16%) on the estimated assessable profit for the year. Overseas taxation is provided on the profits/losses of the overseas subsidiaries and branch in accordance with the tax laws of the countries in which these entities operate.

Hong Kong profits tax charged for the year ended 31 December 1999 includes assessment for additional tax and interest by the Hong Kong Inland Revenue Department upon the finalisation of their review of the Group's offshore income claims for the seven years ended 31 December 1998.

(b) The movements in the deferred taxation account are as follows:–

| | 2000 HK$'000 | 1999 HK$'000 |
|---|---|---|
| Balance at 1 January | **100** | 990 |
| Transferred from profit and loss account | **(100)** | (890) |
| Balance at 31 December | **–** | 100 |

(c) Details of unprovided deferred tax assets/(liabilities) as at year end are as follows:–

| | 2000 | 1999 |
|---|---|---|
| | ***HK$'000*** | *HK$'000* |
| Differences in depreciation allowances | **367** | (115) |
| Unutilised overseas tax losses | **92,536** | 77,014 |
| Other timing differences | **106,726** | 64,045 |
| | **199,629** | 140,944 |

Unutilised overseas tax losses of HK$12,336,000 as at 31 December 2000 will expire within three years from that date.

## 7 PROFIT ATTRIBUTABLE TO SHAREHOLDERS

Included in profit attributable to shareholders is a profit of HK$290,891,000 (1999: loss of HK$83,732,000) which is dealt with in the Company's own accounts.

## 8 DIVIDENDS

| | 2000 | 1999 |
|---|---|---|
| | ***HK$'000*** | *HK$'000* |
| Interim dividend of HK$0.02 (1999:HK$ nil) per share | **13,454** | – |
| Proposed final dividend of HK$0.01 (1999:HK$0.06) per share | **10,091** | 39,912 |
| | **23,545** | 39,912 |
| Proposed special dividend of HK$ nil (1999:HK$0.25) per share | **–** | 166,302 |
| Underprovision for prior year's final and special dividends | **2,928** | – |
| | **26,473** | 206,214 |

The underprovision for prior year's final and special dividends represent dividends payable on shares issued on exercise of share options after the approval of the Company's accounts and before the closure of the Company's Register of Members.

*31 December 2000*

## 9 EARNINGS PER SHARE

The calculation of basic and diluted earnings per share is based on the following data:

| | 2000 | 1999 |
|---|---|---|
| | ***HK$'000*** | *HK$'000* |
| Profit attributable to shareholders for the purpose of calculating basic and diluted earnings per share | **114,046** | 5,994 |
| | **Number of shares** | |
| Weighted average number of ordinary shares for the purpose of calculating basic earnings per share | **670,094,815** | 661,065,673 |
| Number of potential ordinary shares issuable under share options | **2,057,637** | N/A |
| Weighted average number of ordinary shares for the purpose of calculating diluted earnings per share | **672,152,452** | N/A |

No diluted earnings per share has been presented for 1999 as the exercise of share options would be anti-dilutive.

## 10 RETIREMENT BENEFIT COSTS

The Group operates defined contribution retirement schemes for its employees in Hong Kong and overseas. Contributions to the schemes by the Group and employees are calculated at various funding rates up to a maximum of 15% of the monthly salary and in accordance with the terms stipulated in the schemes.

Pursuant to the Mandatory Provident Fund Scheme Ordinance (Chapter 485 of the Laws of Hong Kong) (the "MPF Ordinance"), companies within the Group in Hong Kong have enrolled all employees in Hong Kong into a mandatory provident fund scheme (the "MPF Scheme") from 1 December 2000. The MPF Scheme is a master trust scheme established under trust arrangement and governed by laws in Hong Kong. Under the MPF Ordinance, employers and employees are required to contribute 5% of the employees' relevant income as defined in the MPF Ordinance up to a maximum of HK$1,000 per employee per month (the "mandatory contributions"). The mandatory contributions are fully and immediately vested in the employees as accrued benefits once they are paid to the approved trustees of the MPF Scheme. Contributions to the MPF Scheme by the Group and employees can be made up to a maximum of 5% of the employees' monthly salary in form of mandatory and voluntary contributions.

The unvested benefits of employees terminating employment forfeited in accordance with the terms of the schemes can be utilised by the Group to reduce future contributions to the schemes.

The amount of forfeited contributions utilised by the Group during the year amounted to HK$570,000 (1999: HK$127,000). There was no unutilised forfeited contributions as at 31 December 2000 (1999: Nil).

Contributions totalling HK$97,000 (1999: Nil) were payable to the schemes at the year end and are included in other payables and accrued charges.