

NOTES TO THE FINANCIAL STATEMENTS

for the year ended 31 December 2001

1. GENERAL

The Bank is a listed public limited company incorporated in Hong Kong and is engaged in the provision of banking and related financial services.

2. ADOPTION OF STATEMENTS OF STANDARD ACCOUNTING PRACTICE

In the current year, the Group has adopted, for the first time, a number of new and revised Statements of Standard Accounting Practice (“SSAPs”) issued by the Hong Kong Society of Accountants. Adoption of these Standards has led to a number of changes in the Group’s accounting policies. The revised accounting policies are set out in note 3. In addition, the new and revised Standards have introduced additional and revised disclosure requirements which have been adopted in these financial statements. Comparative amounts for the prior year have been restated in order to achieve a consistent presentation.

The adoption of these new and revised Standards has resulted in the following changes to the Group’s accounting policies that have affected the amounts reported for the current or prior periods.

- (i) In accordance with SSAP 9 (Revised) “Events after the Balance Sheet Date”, dividends proposed or declared after the balance sheet date are not recognised as a liability at the balance sheet date, but are disclosed as a separate component of equity in the notes to the financial statements. This change in accounting policy has been applied retrospectively, resulting in a prior year adjustment on derecognition of liability for final dividend for 1999 amounting to HK\$117,450,000. The effect of this change has been to increase the reserves at 1 January 2000 by HK\$117,450,000 and the shareholders’ funds from HK\$5,272,548,000 to HK\$5,389,998,000.
- (ii) In adopting SSAP 30 “Business Combinations”, the Group has elected not to restate goodwill previously eliminated against reserves. Accordingly, goodwill arising on acquisitions prior to 1 January 2001 is held in reserves and will be charged to the income statement at the time of disposal of the relevant subsidiary, associate or jointly controlled entity, or at such time as the goodwill is determined to be impaired.

Goodwill arising on acquisitions after 1 January 2001 is capitalised and amortised over its estimated useful life. Negative goodwill arising on acquisitions after 1 January 2001 is presented as a deduction from assets and will be released to income based on an analysis of the circumstances from which the balance resulted.

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for the year ended 31 December 2001

3. SIGNIFICANT ACCOUNTING POLICIES

The financial statements have been prepared under the historical cost convention as modified for the revaluation of certain properties and investments in securities.

The financial statements have been prepared in accordance with accounting principles generally accepted in Hong Kong. The principal accounting policies adopted are as follows:

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Bank and its subsidiaries made up to 31 December each year.

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

Goodwill

Goodwill arising on consolidation represents the excess of the cost of acquisition over the Group's interest in the fair value of the identifiable assets and liabilities of a subsidiary, associate or jointly controlled entity at the date of acquisition.

Goodwill arising on acquisitions after 1 January 2001 is capitalised and amortised on a straight-line basis over its useful economic life. Goodwill arising on the acquisition of an associate or a jointly controlled entity is included within the carrying amount of the associate or jointly controlled entity. Goodwill arising on the acquisition of subsidiaries is presented separately in the balance sheet.

Goodwill arising on acquisitions prior to 1 January 2001 continues to be held in reserves, and will be charged to the income statement at the time of disposal of the relevant subsidiary, associate or jointly controlled entity, or at such time as the goodwill is determined to be impaired.

Negative goodwill represents the excess of the Group's interest in the fair value of the identifiable assets and liabilities of a subsidiary, associate or jointly controlled entity at the date of acquisition over the cost of acquisition.

Negative goodwill arising on acquisition after 1 January 2001 is presented as deduction from assets and will be released to income based on an analysis of the circumstances from which the balance resulted. Negative goodwill arising on the acquisition of an associate or a jointly controlled entity is deducted from the carrying value of that associate or jointly controlled entity. Negative goodwill arising on the acquisition of subsidiaries is presented separately in the balance sheet as a reduction from assets.

Investments in subsidiaries

Investments in subsidiaries are included in the Bank's balance sheet at cost less any identified impairment loss.

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3. SIGNIFICANT ACCOUNTING POLICIES – continued

Interests in associates

The consolidated income statement includes the Group's share of the post-acquisition results of its associates for the year. In the consolidated balance sheet, interests in associates are stated at the Group's share of the net assets of the associates, less any identified impairment loss.

The results of associates are accounted for by the Bank on the basis of dividends received and receivable during the year. In the Bank's balance sheet, investments in associates are stated at cost as reduced by any identified impairment loss.

Jointly controlled entities

Joint venture arrangements which involve the establishment of a separate entity in which each venturer has an interest are referred to as jointly controlled entities.

The Group's interests in jointly controlled entities are included in the consolidated balance sheet at the Group's share of the net assets of the jointly controlled entities less any identified impairment loss. The Group's share of the post-acquisition results of its jointly controlled entities is included in the consolidated income statement.

The Bank's investments in jointly controlled entities are stated at cost, as reduced by any identified impairment loss. The results of jointly controlled entities are accounted for by the Bank on the basis of dividends received and receivable.

Advances and other accounts

Advances to customers, banks and other financial institutions and accrued interest and other accounts are stated in the balance sheet after deducting provision for estimated losses.

Provision for bad and doubtful debts is made, having regard to both specific and general risks.

The specific element of the provision relates to those loans that have been individually reviewed and specifically identified as bad or doubtful. Factors which are considered include expected cashflows, financial condition of the borrower and current economic conditions. The general element of the provision relates to those losses that, although not yet specifically identified, are known from experience to be present in the Group's portfolio of loans and advances. In determining the level of the provision required, management considers numerous factors including, but not limited to, domestic and international economic conditions, the composition of the loan portfolio and prior loan loss experience.

Provisions are applied to write off advances when all security has been realised and further recoveries are considered unlikely.

Loans with a specific due date are classified as overdue when the principal or interest is overdue and remains unpaid as at the year-end date. Loans repayable by regular instalments are treated as overdue when an instalment payment is overdue and remains unpaid as at the year-end date. Loans repayable on demand are categorised as overdue either when a demand for repayment has been served on the borrower but repayment has not been made in accordance with the instruction or, the loan has remained continuously outside the approved limit that was advised to the borrower for more than three months.