

Notes to the Condensed Consolidated Financial Statements

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of preparation

The unaudited condensed interim financial statements have been prepared in accordance with Statement of Standard Accounting Practice (“SSAP”) No.2.125 “Interim Financial Reporting” issued by the Hong Kong Society of Accountants and the disclosure requirements set out in Appendix 16 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (“the Listing Rules”). The accounting policies adopted are consistent with those set out in the Group’s annual financial statements for the year ended December 31, 2001.

Premium receivables

Premium receivables represent premiums which are due for payment. The Group normally allows policyholders to make the payment within a grace period of one month from the due date. The grace period may be further extended by one further month by management purely on a discretionary basis. The insurance policies continue if the default premiums are settled before the expiry of the grace period.

2. TURNOVER

Turnover represents gross insurance premiums written and contributions received in respect of retirement scheme management, commissions received and receivable in respect of general insurance business conducted under an agency agreement, and service fees from asset management business.

Revenue from the following activities has been included in turnover.

	Unaudited six months ended	
	6/30/2002 HK\$’000	6/30/2001 HK\$’000
Revenue from:		
Long term insurance business	831,298	952,355
General insurance business under an agency agreement	4,863	4,605
Asset management business	1,563	566
Turnover	837,724	957,526

The Group’s income all arises from its activities which are conducted in Hong Kong.

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3. OPERATING PROFIT BEFORE TAX

Operating profit before tax is arrived at after charging:

	Unaudited six months ended	
	6/30/2002 HK\$'000	6/30/2001 HK\$'000
Auditors' remuneration	34	511
Depreciation	12,591	12,322
Amortisation of deferred acquisition costs	140,294	128,254
Operating lease rentals on land and buildings	26,456	26,103
Staff costs (directors' remuneration included)	79,248	86,124
Net retirement benefit scheme contributions	5,942	8,001
Charge for bad and doubtful debts	2,791	—
Unrealised losses less gains on other investments:		
Listed	—	—
Unlisted	—	20,404
Realised losses less gains on other listed investments	—	1,535
Provision for amount due from an associate	2,036	—
and after crediting:		
Dividend income from listed investments	9,193	3,600
Unrealised gains less losses arising from dealing in foreign currencies	525	—
Unrealised gains less losses on other investments:		
Listed	30,174	36,895
Unlisted	37,026	—
Realised gains less losses on other listed investments	61,176	—
Realised gains less losses arising from derivative financial instruments (note (i) below)	—	976
Realised gains less losses on equity-linked financial products	—	1,386
Interest income from listed investments	70,757	40,547
Other interest income	16,266	46,156

Notes:

- (i) The Group's insurance liabilities are predominantly in United States dollars. It is the Group's policy to keep adequate assets in United States dollars in order to match its insurance liabilities. Where fixed interest securities are denominated in currencies other than United States dollars and Hong Kong dollars, foreign currency forward contracts are bought to hedge back into United States dollars.

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3. OPERATING PROFIT BEFORE TAX (Continued)

The operating profit before tax by the following activity is analysed as follows:

	Unaudited six months ended	
	6/30/2002 HK\$'000	6/30/2001 HK\$'000
Long term insurance business	88,229	73,970
General insurance business under an agency agreement	(140)	(836)
Asset management business (note (ii) below)	(3,226)	(3,168)
Operating profit before tax	84,863	69,966
Notes:		
(ii) Income from operations - asset management	9,988	5,818
Less: Intragroup Income	(8,268)	(4,939)
	1,720	879
Operating expenses before tax	(4,946)	(4,047)
	(3,226)	(3,168)

The Group's operating profit before tax arises from its direct underwriting activities conducted in Hong Kong.

4. TAX

	Unaudited six months ended	
	6/30/2002 HK\$'000	6/30/2001 HK\$'000
Group:		
Hong Kong profits tax	806	—
Overseas tax	29	51
Underprovision in prior year		
-Hong Kong	—	230
-Overseas	—	559
Associate	—	—
Tax charge for the period	835	840

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4. TAX (Continued)

The assessable profits of a wholly-owned subsidiary, which is engaged in the long term insurance business and retirement scheme management, are computed in accordance with the special provisions of the Hong Kong Inland Revenue Ordinance. This subsidiary had sufficient agreed tax losses brought forward from prior years to offset against any assessable profits for long term insurance business and retirement scheme management arising in Hong Kong during the year.

Hong Kong profits tax has been provided at the rate of 16% on the estimated assessable profits solely arising from asset management business conducted in Hong Kong during the year. Overseas tax has been calculated on the estimated assessable profits for the year at the rates of tax prevailing in the countries in which the Group operates based on existing legislation, interpretations and practices in respect thereof.

5. DIVIDEND

The directors do not recommend the payment of an interim dividend for the six months ended June 30, 2002 (June 2001: Nil).

6. EARNINGS PER SHARE

The calculation of basic earnings per share is based on the net profit attributable to shareholders for the period of HK\$84,028,000 (June 2001: HK\$68,903,000) and the weighted average number of 824,747,000 shares (June 2001: 827,100,000 shares) in issue during the period.

The diluted earnings per share for the periods ended June 30, 2001 and 2002 have not been presented because the effect arising from the deemed exercise of share options outstanding during these periods would have had an anti-dilutive effect on the basic earnings per share.

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7. SHARE CAPITAL

	Unaudited as at 6/30/2002		Audited as at 12/31/2001	
	Number of shares	Nominal value HK\$'000	Number of shares	Nominal value HK\$'000
<i>Authorised:</i>				
Ordinary shares of HK\$1.00 each	3,000,000,000	3,000,000	3,000,000,000	3,000,000
<i>Issued and fully paid:</i>				
Ordinary shares of HK\$1.00 each	827,100,000	827,100	827,100,000	827,100
Shares repurchased and cancelled (i)	(2,942,000)	(2,942)	—	—
	824,158,000	824,158	827,100,000	827,100

Note:

- (i) 2,612,000 and 330,000 ordinary shares of HK\$1.00 each were repurchased by the Company from The Stock Exchange of Hong Kong Limited on February 6 and 8, 2002 at a price from HK\$1.72 to HK\$1.85 and HK\$1.79 to HK\$1.80 per share respectively. The aggregate price paid by the Company for such repurchases was HK\$5,256,960.

8. DEFERRED ACQUISITION COSTS

	Unaudited as at 6/30/2002 HK\$'000	Audited as at 12/31/2001 HK\$'000
Balance at beginning of period	1,673,418	1,640,930
Additions	86,472	298,707
Less: Amortisation	(140,294)	(266,219)
Balance at end of period	1,619,596	1,673,418
Portion reclassified as current assets	(284,018)	(275,371)
Non-current portion	1,335,578	1,398,047

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9. PREMIUM DEPOSIT

Premium deposits are amounts that are left on deposit with the Group for the payment of future premiums.

10. FUTURE INSURANCE LIABILITIES

	Unaudited as at 6/30/2002 HK\$'000	Audited as at 12/31/2001 HK\$'000
As at beginning of period	3,578,132	3,133,667
Increase for the period	172,294	445,367
Currency realignment	609	(902)
	3,751,035	3,578,132
Non-current portion of amounts payable under financial reinsurance contracts	—	8,967
At end of period	3,751,035	3,587,099

As at June 30, 2002, the current portion of amounts payable under financial reinsurance contracts amounted to HK\$24,733,000 (December 2001: HK\$45,759,000), which was included in other insurance liabilities.

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11. INVESTMENTS

	Note	Unaudited as at 6/30/2002 HK\$'000	Audited as at 12/31/2001 HK\$'000
Listed bonds, at market value	12		
Hong Kong		522,925	685,737
Elsewhere		1,545,629	2,000,572
		2,068,554	2,686,309
Listed equities, at market value:			
Hong Kong		50,506	34,357
Elsewhere		14,321	15,187
		64,827	49,544
Unlisted unit trusts, at fair value		663,389	523,377
Investments - current assets		2,796,770	3,259,230

All investments, being available for sale, are classified as current assets.

In the period January to June 2002, the Group has sold US\$23,000,000 amount of nominal value of its holding of PCCW Capital Limited and PCCW-HKTC Capital Limited, recording a gain of HK\$8,839,000.

As at June 30, 2002, the Group continues to hold a total nominal amount of US\$14,000,000 bonds issued by PCCW Capital Limited, with maturity date in 2005. The market value of these bonds amounted to HK\$114,383,000 (December 2001: HK\$106,741,000).

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12. LISTED BONDS

The listed bonds analysed by issuer as at the balance sheet date were as follows:

	Unaudited as at 6/30/2002 HK\$'000	Audited as at 12/31/2001 HK\$'000
Governments	106,320	477,832
Banks and other financial institutions	699,725	715,835
Corporate entities	1,262,509	1,492,642
Listed bonds	2,068,554	2,686,309

The maturity profile of the listed bonds as at the balance sheet date was as follows:

	Unaudited as at 6/30/2002 HK\$'000	Audited as at 12/31/2001 HK\$'000
With a residual maturity of:		
Three months or less	38	29,951
One year or less but over three months	33,998	62,166
Five years or less but over one year	1,364,033	1,476,454
Over five years	670,485	1,117,738
Listed bonds	2,068,554	2,686,309

13. CONTINGENT LIABILITIES

As at June 30, 2002, the Group and the Company had no material contingent liabilities other than contingencies arising from the ordinary course of the long term insurance business (December 2001: Nil).

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14. PENDING LITIGATION

On September 21, 2000, a writ was issued against a number of persons, including Pacific Century Insurance Company Limited (“PCI”), a wholly-owned subsidiary of the Company, and certain insurance agents of PCI, by certain members of an insurance group operating in Hong Kong (the “Plaintiffs”), whereby the Plaintiffs sought, among other things, injunctive relief and damages against PCI in connection with PCI’s plan matching scheme and the purported use of certain documents and information.

On July 24, 2001, a High Court judge granted the Plaintiffs interim injunctive relief pending the trial of the action or further order. The interim injunctive relief restrains PCI, among others, from disclosing or otherwise making any use of certain documents and information, and accepting applications for life insurance policies in certain circumstances.

Having consulted legal counsel, the Group has determined that it will continue to defend vigorously these proceedings. In the opinion of the directors and based on legal advice, it is unlikely that the final outcome of these proceedings would materially affect the financial position of the Group.

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15. RELATED PARTY TRANSACTIONS

(a) Details of transactions with companies related to the Group are as follows:

	Notes	Unaudited six months ended	
		6/30/2002 HK\$'000	6/30/2001 HK\$'000
Premium income in respect of group life and medical policies issued to:	(i)		
Pacific Century Asset Management (HK) Limited (trading as "Pacific Century Group")		3,096	5,882
PCCW Services Limited		1,884	2,323
Pacific Century Systems Limited		486	507
Morningstar Asia Limited		10	8
Power Logistics Limited		78	126
The HK I-Education Limited		15	—
Premium income in respect of group personal accident policy issued to Pacific Century Systems Limited		37	—
		5,606	8,846
General insurance commission income received from The Ming An Insurance Company (Hong Kong), Limited	(ii)	4,863	4,605

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15. RELATED PARTY TRANSACTIONS (Continued)

Notes:

- (i) The Group entered into a number of group life and medical as well as personal accident policies with certain companies related to the ultimate holding company of the Group, Pacific Century Group (Cayman Islands) Limited and its associates. In the opinion of the directors (including the independent non-executive directors), the group life and medical and personal accident policies for these related companies are negotiated and conducted on terms and conditions similar to those offered to other policyholders of the Group, in the ordinary and usual course of business of the Group and on terms that are fair and reasonable so far as the shareholders of the Company are concerned. The total amount of premium income derived therefrom would not exceed 2% of the total turnover of the Group for the year ending December 31, 2002.
- (ii) Pursuant to an agency agreement dated November 1, 1994 and subsequently replaced by an Agency Agreement effective January 1, 2001, Pacific Century Insurance Company Limited, a wholly-owned subsidiary of the Group, was, effective as from January 1, 2001 appointed as an underwriting agent of The Ming An Insurance Company (Hong Kong), Limited ("Ming An"), with authorisation to underwrite and to settle claims of certain types of general insurance businesses on behalf of Ming An. Ming An is a substantial shareholder of the Company.

The Agency Agreement is based on arm's length commercial terms in accordance with the prevailing market conditions.

- (b) On April 27, 2000, the Group allied with a fellow subsidiary, Pacific Century CyberWorks Limited, and established a company, Advanced Internet Visions Limited ("AIV"). AIV acted as an investment vehicle for the holding of and interest in Morningstar Asia Limited ("MAL"), a company incorporated in Hong Kong. MAL was engaged in providing financial information and related services in Asia (outside Japan) by way of, among other things, printed materials, computer software products and/or Internet products.

The Group's attributable equity interest in MAL is approximately 12%.

- (c) The Group provided secured loans to employees and agents which are interest-bearing at the prevailing bank lending rate, secured by the underlying properties and/or motor vehicles, and repayable on a monthly instalment basis.
- (d) As at June 30, 2002, the Group had a total amount of HK\$11,466,000 (December 2001: HK\$11,420,000) payable to related companies which arose from the ordinary and normal course of business conducted on terms similar to those offered to other customers of the Group.

The transactions mentioned in (a) and (b) above constitute connected transactions under the Listing Rules.

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16. COMMITMENTS

Operating lease commitments

	Unaudited as at 6/30/2002 HK\$'000	Audited as at 12/31/2001 HK\$'000
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The Group had total future minimum lease payments under non-cancellable operating leases in respect of land and buildings, falling due as follows:		
Within one year	48,736	54,704
In the second to fifth years, inclusive	12,080	33,477
	60,816	88,181