

NOTES TO THE ACCOUNTS

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 in accordance with accounting principles generally accepted in Hong Kong and comply with accounting standards issued by the Hong Kong Society of Accountants ("HKSA"). They have been prepared under the historical cost convention.

In the current year, the Group adopted the following new or revised Statements of Standard Accounting Practice ("SSAPs") issued by the HKSA which are effective for accounting periods commencing on or after 1 January 2001:

SSAP 9 (revised)	:	Events after the balance sheet date
SSAP 26	:	Segment reporting
SSAP 28	:	Provisions, contingent liabilities and contingent assets
SSAP 29	:	Intangible assets
SSAP 30	:	Business combinations
SSAP 31	:	Impairment of assets
SSAP 32	:	Consolidated financial statements and accounting for investments in subsidiaries

The adoption of the above SSAPs had no material impact on the preparation of the accounts as the Group was already adopting the recognition and measurement principles embodied in these new or revised standards.

(b) Group accounting

(i) Consolidation

The consolidated accounts include the accounts of the Company and its subsidiaries made up to 31st August. Subsidiaries are those entities in which the Group controls the composition of the board of directors, controls more than half the voting power or holds more than half of the issued share capital.

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

All significant inter-company transactions and balances within the Group are eliminated on consolidation.

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 unamortised goodwill or negative goodwill or goodwill/negative goodwill taken to reserves and 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.

In the Company's balance sheet the investments in subsidiaries are stated at cost less provision for impairment losses. The results of subsidiaries are accounted for by the Company on the basis of dividends received and receivable.

1. PRINCIPAL ACCOUNTING POLICIES (Cont'd)

(b) Group accounting (Cont'd)

(ii) Translation of foreign currencies

Transactions in foreign currencies are recorded 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 balance sheets of subsidiaries expressed in foreign currencies are translated at the rates of exchange ruling at the balance sheet date whilst the profit and loss accounts are translated at an average rate for the period. Exchange differences are dealt with as a movement in reserves.

(c) Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net assets of the acquired subsidiary at the date of acquisition.

In accordance with the new SSAP 30, goodwill on acquisitions occurring on or after 1st September 2001 is separately shown on the consolidated balance sheet and is amortised using the straight-line method over its estimated useful life. Goodwill arising on major strategic acquisitions of the Group to expand its product or geographical market coverage is amortised over a period of not more than 20 years.

Goodwill on acquisitions that occurred prior to 1st September 2001 was written off against reserves. This represents a change of policies. The Group has taken advantage of the transitional provisions in SSAP 30 and goodwill previously written off against reserves of approximately HK\$5,092,000 has not been restated.

Where an indication of impairment exists, the carrying amount of goodwill, including goodwill previously written off against reserves, is assessed and written down immediately to its recoverable amount.

(d) Fixed assets

Fixed assets are stated at cost less accumulated depreciation and accumulated impairment losses.

Leasehold land is depreciated over the period of the lease while other tangible fixed assets are depreciated at rates sufficient to write off their costs less accumulated impairment losses over their estimated useful lives on a straight-line basis. The principal annual rates are as follows:

Leasehold land	2%
Leasehold buildings	2%
Furniture, fixtures and fittings	25%
Telecommunications, computer and office equipment	7% – 25%
Auto-diallers	25%
Motor vehicles	25%

Depreciation of leasehold improvements is calculated to write off their cost less accumulated impairment losses over the unexpired periods of the leases or their expected useful lives to the Group whichever is shorter.

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.

NOTES TO THE ACCOUNTS

1. PRINCIPAL ACCOUNTING POLICIES (Cont'd)

(d) Fixed assets (Cont'd)

At each balance sheet date, both internal and external sources of information are considered to assess whether there is any indication that fixed assets are impaired. If any such indication exists, the recoverable amount of the asset is estimated and where relevant, an impairment loss is recognised to reduce the asset to its recoverable amount. Such impairment losses are recognised in the profit and loss account.

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.

(e) Assets held under leases

(i) Finance leases

Leases that substantially transfer to the Group all the risks and rewards of ownership of assets are accounted for as finance leases. Finance leases are capitalised at the inception of the leases at the lower of the fair value of the leased assets or the present value of the minimum lease payments. Each lease payment is allocated between capital and finance charges so as to achieve a constant rate on the capital balances outstanding. The corresponding rental obligations, net of finance charges, are included in long-term liabilities. The finance charges are charged to the profit and loss account over the lease periods.

Assets held under finance leases are depreciated over the shorter of lease periods or their estimated useful lives.

(ii) Operating leases

Leases where substantially all the risks and rewards of ownership of assets remain with the leasing company are accounted for as operating leases. Payments made under operating leases net of any incentives received from the leasing company are charged to the profit and loss account on a straight-line basis over the lease periods.

(f) Accounts receivable

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

(g) Cash and cash equivalents

Cash and cash equivalents are short-term highly liquid investments, which are readily convertible into cash and have original maturity of three months or less at the date of acquisition, and short-term loans and overdrafts repayable within three months. Cash equivalents are stated at cost, which approximates fair value because of the short-term maturity of these instruments.

(h) Provisions

Provisions are recognised when the group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate of the amount can be made. Where the group expects a provision to be reimbursed, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain.

1. PRINCIPAL ACCOUNTING POLICIES (Cont'd)

(i) Contingent liabilities and assets

A contingent liability is a possible obligation that arises from past events and whose existence will only be confirmed by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Group. It can also be a present obligation arising from past events that is not recognised because it is not probable that outflow of economic resources will be required or the amount of obligation cannot be measured reliably.

A contingent liability is not recognised but is disclosed in the notes to the accounts. When a change in the probability of an outflow occurs so that outflow is probable, they will then be recognised as a provision.

A contingent asset is a possible asset that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain events not wholly within the control of the Group.

Contingent assets are not recognised but are disclosed in the notes to the accounts when an inflow of economic benefits is probable. When inflow is virtually certain, an asset is recognised.

(j) Deferred taxation

Deferred taxation is accounted for at the current taxation 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. In determining whether a liability is expected to be payable in the foreseeable future the Group assesses the effect of its capital expenditure and other plans. If these plans indicate that sufficient accelerated tax allowances will be available to offset the effect of the reversal of timing differences a deferred tax liability is not established for such timing differences.

(k) Revenue recognition

- (i) Revenue for the provision of international telecommunications and fixed telecommunications network services is recognised, net of discounts, when the services are rendered.
- (ii) Revenue received in advance for the provision of international telecommunications services using calling cards is deferred and amortised based on the estimated actual usage by customers. Revenue received in advance for the provision of fixed telecommunications network services is deferred and amortised on a straight-line basis over the life of the subscriber agreement.
- (iii) Advertising and commission income for the provision of internet content and e-commerce services are recognised when the services are rendered.
- (iv) Interest income is recognised on a time proportion basis, taking into account the principal amounts outstanding and the interest rates applicable.

(l) Retirement benefit costs

The Group contributes to defined contribution retirement schemes which are available to all employees. Contributions to the schemes by the Group and employees are calculated as a percentage of employees' basic salaries. The retirement benefit scheme cost charged to the profit and loss account represents contributions payable by the Group to the fund.

The assets of the scheme are held separately from those of the Group in an independently administered fund.

(m) Research and development costs

Research and development costs of new services and enhancements to existing services are charged to the profit and loss account as incurred.

NOTES TO THE ACCOUNTS

1. PRINCIPAL ACCOUNTING POLICIES *(Cont'd)*

(n) Borrowing costs

Borrowing costs that are directly attributable to the acquisition, construction or production of an asset that necessarily takes a substantial period of time to get ready for its intended use or sale are capitalised as part of the cost of that asset.

All other borrowing costs are charged to the profit and loss account in the year in which they are incurred.

(o) Segment reporting

In accordance with the Group's internal financial reporting, the Group has determined that business segments be presented as the primary reporting format and geographical as the secondary reporting format.

Unallocated costs represent corporate expenses. Segment assets consist primarily of fixed assets, receivables and operating cash and exclude goodwill. Segment liabilities comprise operating liabilities and exclude items such as taxation and certain corporate borrowings. Capital expenditure comprises additions to fixed assets.

In respect of geographical segment reporting, sales are based on the country in which the customer is located. Total assets and capital expenditure are where the assets are located.

(p) Dividends

In accordance with the revised SSAP 9, the Group no longer recognises dividends proposed or declared after the balance sheet date as a liability at the balance sheet date. This change in accounting policy has been applied retrospectively; however, as the Group did not distribute any final dividend for the year ended 31 August 2000 and 31 August 2001, no adjustment had been made to the opening retained earnings at September 2001 and September 2002.

(q) Use of estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the year. Actual results could differ from these estimates.

2. TURNOVER, REVENUES AND SEGMENTAL INFORMATION

The Group is principally engaged in the provision of international telecommunications services to customers in Hong Kong, Japan and Canada, and fixed telecommunications network services to customers in Hong Kong and Canada. Revenues recognised during the year are as follows:

	2002	2001
	HK\$'000	HK\$'000
Turnover		
International telecommunications services	908,981	861,338
Fixed telecommunications network services	241,219	154,262
Internet advertising services	–	1,034
	1,150,200	1,016,634
Other revenues		
Interest income	10,870	35,438
Other income	1,010	10,935
	11,880	46,373
Total revenues	1,162,080	1,063,007

(a) Business segments:

The Group is organised on a worldwide basis into three business segments:

- International telecommunications – provision of international long distance calls services
- Fixed telecommunications network – provision of dial up and broadband internet access services, and local IP telephony services
- Internet advertising – provision of internet advertising services

The Group's internet advertising services were discontinued at the beginning of the year (Note 2(c)).

The Group's inter-segment transactions mainly consist of provision of leased lines services. It was entered into at similar terms as that contracted with third parties.

NOTES TO THE ACCOUNTS

2. TURNOVER, REVENUES AND SEGMENTAL INFORMATION (Cont'd)

(a) Business segments: (Cont'd)

2002

	International telecommunications services HK\$'000	Fixed telecommunications network services HK\$'000	Elimination HK\$'000	Group HK\$'000
Turnover				
External sales	908,981	241,219	–	1,150,200
Inter-segment sales	8,100	25,786	(33,886)	–
	917,081	267,005	(33,886)	1,150,200
Segment results	222,651	(121,686)		100,965
Finance costs				(3,504)
Profit before taxation				97,461
Taxation				(14,566)
Profit after taxation				82,895
Minority interests				8,234
Profit attributable to shareholders				91,129
Segment assets	581,253	741,771	–	1,323,024
Unallocated assets				4,261
Total assets				1,327,285
Segment liabilities	205,542	152,401	–	357,943
Unallocated liabilities				59,159
Total liabilities				417,102
Capital expenditure	138,521	440,545	–	579,066
Depreciation	32,951	95,339	–	128,290
Amortisation charge	–	–	–	1,065

2. TURNOVER, REVENUES AND SEGMENTAL INFORMATION (Cont'd)

(a) Business segments: (Cont'd)

2001

	International tele- communications services HK\$'000	Fixed tele- communications network services HK\$'000	Internet advertising services HK\$'000	Elimination HK\$'000	Group HK\$'000
Turnover					
External sales	861,338	154,262	1,034	–	1,016,634
Inter-segment sales	5,400	–	–	(5,400)	–
	866,738	154,262	1,034	(5,400)	1,016,634
Segment results	146,611	(72,123)	(10,968)		63,520
Finance costs					(4,542)
Profit before taxation					58,978
Taxation					(18,775)
Profit after taxation					40,203
Minority interests					13,724
Profit attributable to shareholders					53,927
Segment assets	645,948	497,209	1,461	–	1,144,618
Unallocated assets					–
Total assets					1,144,618
Segment liabilities	187,566	62,166	399	–	250,131
Unallocated liabilities					89,181
Total liabilities					339,312
Capital expenditure	19,940	145,922	175	–	166,037
Depreciation	37,238	45,416	193	–	82,847
Amortisation charge	–	–	–	–	–

NOTES TO THE ACCOUNTS

2. TURNOVER, REVENUES AND SEGMENTAL INFORMATION (Cont'd)

(b) Geographical segments

Although the Group's three business segments are managed on a worldwide basis, they operate in three main geographical areas:

- Hong Kong – international telecommunications, fixed telecommunications network services and internet advertising.
- Japan – international telecommunications.
- Canada – international telecommunications and fixed telecommunications network services.

In presenting information on the basis of geographical segments, turnover and segment results are based on the geographical location of customers. Total assets and capital expenditure are based on the geographical location of the assets.

There were no sales between the geographical segments.

	Turnover	Segment result	Total assets	Capital expenditure
	2002	2002	2002	2002
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Hong Kong	1,107,987	97,622	1,300,528	578,979
Japan	8,386	(135)	4,397	45
Canada	33,827	2,413	18,099	42
	<u>1,150,200</u>	<u>99,900</u>	<u>1,323,024</u>	<u>579,066</u>
Unallocated costs		<u>1,065</u>		
Operating profit		<u>100,965</u>		
Unallocated assets			<u>4,261</u>	
Total assets			<u>1,327,285</u>	

2. TURNOVER, REVENUES AND SEGMENTAL INFORMATION (Cont'd)

(b) Geographical segments (Cont'd)

	Turnover	Segment result	Total assets	Capital expenditure
	2001	2001	2001	2001
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Hong Kong	971,584	63,660	1,130,157	166,004
Japan	9,272	(122)	4,794	7
Canada	35,778	(18)	9,667	26
	<u>1,016,634</u>	<u>63,520</u>	<u>1,144,618</u>	<u>166,037</u>
Unallocated costs		-		
Operating profit		<u>63,520</u>		
Unallocated assets			-	
Total assets			<u>1,144,618</u>	

(c) In current year, the Group's internet advertising operation has been discontinued. The revenue and operating loss relating to the internet advertising segment are disclosed above and are included in the Hong Kong reporting segment. The contribution to turnover and the loss from ordinary activities in respect of the discontinued operation, amounted for up to the date of discontinuance, are as follows:

	2002	2001
	HK\$'000	HK\$'000
Sales	-	1,034
Loss from ordinary activities	<u>-</u>	<u>10,968</u>

NOTES TO THE ACCOUNTS

3. OTHER OPERATING EXPENSES

	2002	2001
	HK\$'000	HK\$'000
Advertising and marketing expenses	168,441	86,574
Amortisation of goodwill	1,065	–
Depreciation	128,290	82,847
Equipment rental	5,141	7,715
Loss on disposal of fixed assets	2,414	3,512
Office rental and utilities	19,474	23,628
Provision for doubtful debts	10,277	9,663
Staff costs (including directors' emoluments)	196,158	149,237
Others	71,892	51,959
	603,152	415,135

4. OPERATING PROFIT

The operating profit is stated after crediting and charging the following:

	2002	2001
	HK\$'000	HK\$'000
Crediting		
Net exchange gains	–	2,694
Charging		
Amortisation of goodwill	1,065	–
Auditors' remuneration	1,261	870
Depreciation of owned fixed assets	124,563	77,187
Depreciation of fixed assets held under finance leases	3,727	5,660
Loss on disposal of fixed assets	2,414	3,512
Operating lease charges in respect of land and buildings	11,486	17,908
Operating lease charges in respect of computer equipment	5,141	7,715
Provisions for doubtful debts	10,277	9,663
Research and development costs	2,166	2,791
Retirement benefit costs (Note 10)	11,335	4,082
Net exchange losses	508	–
Staff costs (including directors' emoluments)	218,144	168,156
Less: staff costs capitalised as fixed assets	(21,986)	(18,919)
	196,158	149,237

NOTES TO THE ACCOUNTS

5. FINANCE COSTS

	2002	2001
	HK\$'000	HK\$'000
Interest on bank overdrafts	235	928
Interest element of finance leases	225	688
Interest paid to a minority shareholder	846	1,458
Interest paid to third parties	2,198	1,468
	3,504	4,542

6. TAXATION

The amount of taxation charged to the consolidated profit and loss account represents:

	2002	2001
	HK\$'000	HK\$'000
Hong Kong profits tax		
– current (Note (a))	18,000	21,746
– overprovisions in prior years	(10,665)	(4,200)
– deferred taxation (Note 19 (b))	9,515	1,000
Overseas taxation		
– current (Note (b))	116	229
– overprovisions in prior years	(2,400)	–
	14,566	18,775

- (a) Hong Kong profits tax has been provided at the rate of 16% (2001: 16%) on the estimated assessable profit for the year.
- (b) Taxation on overseas profits has been calculated on the estimated assessable profits for the year at the rates of taxation prevailing in the overseas countries in which the Group operates.

6. TAXATION (Cont'd)

As at 31st August 2002, potential deferred taxation assets/(liabilities) for the year have not been recognised/(provided) in respect of the following:

	2002	2001
	HK\$'000	HK\$'000
Accelerated depreciation allowances	(31,878)	(18,277)
Tax losses	34,721	38,276
	2,843	19,999

7. PROFIT ATTRIBUTABLE TO SHAREHOLDERS

The profit attributable to shareholders is dealt with in the accounts of the Company to the extent of HK\$154,199,000 (2001: HK\$99,208,000).

8. DIVIDENDS

	2002	2001
	HK\$'000	HK\$'000
Interim, paid, of HK\$Nil (2001: HK\$0.01) per ordinary share	–	4,907

NOTES TO THE ACCOUNTS

9. EARNINGS PER SHARE

	2002	2001
	HK\$'000	HK\$'000
Profit attributable to shareholders	91,129	53,927
	No of shares in thousand	No of shares in thousand
Weighted average number of shares in issue	495,181	490,679
Incremental shares from assumed exercise of share options	11,219	3,770
Incremental shares from assumed exercise of warrants	59,489	–
Diluted weighted average number of shares	565,889	494,449
Basic earnings per share	HK\$18.4 cents	HK\$11.0 cents
Diluted earnings per share	HK\$16.1 cents	HK\$10.9 cents

10. RETIREMENT BENEFIT COSTS

The Group contributes to a defined contribution retirement scheme, an Occupational Retirement Scheme ("the ORSO Scheme"), which is available to some of its employees. Under the ORSO Scheme the employees are required to contribute 5% of their monthly salaries, while the Group's contributions are calculated at 10% and 5% of the monthly salaries of senior management staff and all other staff respectively. The employees are entitled to 100% of the employer's contributions after 10 years of completed service, or at a reduced scale after completion of 3 to 9 years' service. Contributions to the ORSO Scheme are reduced by contributions forfeited by those employees who leave the ORSO Scheme prior to vesting fully in the Group's contributions.

A mandatory provident fund scheme (the "MPF Scheme") has been established under the Hong Kong Mandatory Provident Fund Scheme Ordinance in December 2000. Commencing on 1st December 2000, the existing employees of the Group in Hong Kong may elect to join the MPF Scheme, and all new employees of the Group in Hong Kong are required to join the MPF Scheme. Both the Group and the employees are required to contribute 5% of each individual's relevant income with a maximum amount of HK\$1,000 per month as a mandatory contribution. Employer's mandatory contributions are 100% vested in the employees as soon as they are paid to the MPF Scheme. Employees may also elect to contribute more than the minimum as a voluntary contribution.

The retirement schemes for staff of the Group in other countries follow the local statutory requirements of the respective countries.

The aggregate employer's contributions, net of forfeited contributions, which have been dealt with in the profit and loss account during the year are as follows:

	2002	2001
	HK\$'000	HK\$'000
Gross contributions	11,965	7,616
<i>Less:</i> forfeited contributions utilised to offset the Group's contributions during the year	(630)	(3,534)
Net contributions charged to profit and loss account	11,335	4,082

At 31st August 2002, the forfeited contributions available to offset future contributions by the Group to the scheme amounted to approximately HK\$21,000 (2001: HK\$31,000).

NOTES TO THE ACCOUNTS

11. DIRECTORS' AND SENIOR MANAGEMENT'S EMOLUMENTS

(a) Directors' remuneration

The aggregate amounts of emoluments payable to directors of the Company during the year are as follows:

	2002	2001
	HK\$'000	HK\$'000
Executive		
Basic salaries, other allowances and benefits in kind	15,883	13,559
Discretionary bonuses	6,000	6,000
Allowances for directors' quarters	2,412	2,321
Contributions to pension schemes	1,461	1,274
	25,756	23,154
Independent non-executive		
Fees	336	320
	26,092	23,474

During the year, the benefits arising from the exercise of share options granted to the directors amounted to approximately HK\$1,159,000 (2001: HK\$205,000).

The emoluments of the directors fell within the following bands:

	Number of directors	
	2002	2001
Nil – HK\$1,000,000	3*	3*
HK\$1,000,001 – HK\$1,500,000	1	2
HK\$1,500,001 – HK\$2,000,000	1	–
HK\$2,000,001 – HK\$2,500,000	–	1
HK\$2,500,001 – HK\$3,000,000	1	–
HK\$3,000,001 – HK\$3,500,000	1	1
HK\$7,000,001 – HK\$7,500,000	–	2
HK\$8,000,001 – HK\$8,500,000	2	–

* Including three independent non-executive directors.

No director waived any emoluments in respect of the years ended 31st August 2001 and 2002.

(b) Five highest paid individuals

The five individuals whose emoluments were the highest in the Group for both years were also directors and their emoluments are reflected in the analysis presented above.

12. GOODWILL – GROUP

	Note	HK\$'000
Deemed acquisition of additional interest in a subsidiary through subscription of rights issue	(i)	4,309
Acquisition of additional interest in a subsidiary from a minority shareholder (Note 20(c))	(ii)	1,017
Amortisation charge (Note 4)		(1,065)
Closing net book amount		4,261
At 31st August 2002		
Cost		5,326
Accumulated amortisation		(1,065)
Net book amount		4,261
At 31st August 2001		
Cost		–
Accumulated amortisation		–
Net book amount		–

- (i) On 10th January 2002, the Group increased its shareholdings in a subsidiary, Hong Kong Broadband Network Limited (“HKBN”), from 85% to 96% through the subscription of shares under a rights issue. The subscription price of HK\$169,829,400 was settled in cash.
- (ii) On 13th March 2002, the Group purchased the remaining 15,000 ordinary shares in HKBN from a minority shareholder, KDDI Corporation, for cash consideration of HK\$7,500,000. As a result, HKBN became the wholly owned subsidiary of the Company.

Goodwill was recognised on both transactions for the amount of the excess of the purchase price paid over the net book value (which approximates fair value) of the assets acquired, and is amortised on a straight-line basis over five years.

NOTES TO THE ACCOUNTS

13. FIXED ASSETS

	Group						
	Leasehold land and buildings	Leasehold improve- ments	Furniture, fixtures and fittings	Telecom- munications, computer and office equipment	Autodiallers	Motor vehicles	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Cost:							
At 1st September 2001	45,069	44,351	8,835	500,716	17,190	5,046	621,207
Additions	13,113	9,529	1,034	552,496	80	2,814	579,066
Disposals	–	–	–	(7,920)	–	–	(7,920)
Exchange adjustments	–	(6)	(11)	(145)	(2)	–	(164)
At 31st August 2002	58,182	53,874	9,858	1,045,147	17,268	7,860	1,192,189
Accumulated depreciation:							
At 1st September 2001	1,277	11,488	4,860	158,596	13,788	3,802	193,811
Charge for the year	1,031	5,204	1,449	118,052	1,648	906	128,290
Disposals	–	–	–	(2,951)	–	–	(2,951)
Exchange adjustments	–	(5)	(1)	(51)	–	–	(57)
At 31st August 2002	2,308	16,687	6,308	273,646	15,436	4,708	319,093
Net book value:							
At 31st August 2002	55,874	37,187	3,550	771,501	1,832	3,152	873,096
At 31st August 2001	43,792	32,863	3,975	342,120	3,402	1,244	427,396

13. FIXED ASSETS (Cont'd)

	Company						
	Telecom-						
	munications,						
	Leasehold land and buildings	Leasehold improve- ments	Furniture, fixtures and fittings	computer and office equipment	Autodiallers	Motor vehicles	Total
	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Cost:							
At 1st September 2001	5,197	16,473	6,498	139,733	16,888	3,975	188,764
Additions	–	33	62	133,215	80	2,490	135,880
Disposals	–	–	–	(709)	–	–	(709)
At 31st August 2002	5,197	16,506	6,560	272,239	16,968	6,465	323,935
Accumulated depreciation:							
At 1st September 2001	346	8,051	3,972	74,314	13,691	3,558	103,932
Charge for the year	104	2,140	1,065	22,312	1,621	625	27,867
Disposals	–	–	–	(662)	–	–	(662)
At 31st August 2002	450	10,191	5,037	95,964	15,312	4,183	131,137
Net book value:							
At 31st August 2002	4,747	6,315	1,523	176,275	1,656	2,282	192,798
At 31st August 2001	4,851	8,422	2,526	65,419	3,197	417	84,832

NOTES TO THE ACCOUNTS

13. FIXED ASSETS (Cont'd)

(a) The interests in leasehold land and buildings situated in Hong Kong at their net book values are analysed as follows:

	Group		Company	
	2002	2001	2002	2001
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Leases of between 10 to 50 years	55,874	43,792	4,747	4,851

(b) At 31st August 2002, the net book value of telecommunications, computer and office equipment under finance leases held by the Group and the Company amounted to HK\$4,062,000 (2001: HK\$7,789,000) and HK\$3,361,000 (2001: HK\$5,685,000) respectively.

(c) At 31st August 2002, the net book value of fixed assets pledged as security for a loan from a former minority shareholder (Note 19(c)) amounted to approximately HK\$12,714,000.

14. INVESTMENTS IN SUBSIDIARIES

	Company	
	2002	2001
	HK\$'000	HK\$'000
Unlisted investments, at cost (Note (a))	44,841	36,250
Amounts due from subsidiaries (Note (b))	687,328	430,605
	732,169	466,855
Less: provisions	–	(42,955)
	732,169	423,900

14. INVESTMENTS IN SUBSIDIARIES (Cont'd)

(a) The following is a list of the principal subsidiaries at 31st August 2002:

Name	Place of incorporation	Principal activities and place of operations	Particulars of issued share capital	Percentage of interest held
Attitude Holdings Limited	British Virgin Islands	Inactive	Ordinary US\$1	100
# City Telecom (B.C.) Inc.	Canada	Provision of international telecommunications and dial-up internet access services in Canada	Common CAD501,000	100
# City Telecom (Canada) Inc.	Canada	Maintenance of switching equipment and provision of operational services in Canada	Common CAD100	100
# City Telecom Inc.	Canada	Provision of international telecommunications and dial-up internet access services in Canada	Common CAD1,000	100
City Telecom International Limited	British Virgin Islands	Investment holding in Hong Kong	Ordinary US\$1	*100
# City Telecom (Japan) Co. Limited	Japan	Provision of international telecommunications services in Japan	Ordinary ¥10,000,000	100
# City Telecom (USA) Inc.	The United States of America (the "USA")	Maintenance of switching equipment and provision of operational services in the USA	Common US\$1	100
Automedia Holdings Limited	British Virgin Islands	Investment holding in Hong Kong	Ordinary US\$1	*100
Golden Trinity Holdings Limited	British Virgin Islands	Investment holding in Hong Kong	Ordinary US\$1	*100
Hong Kong Broadband Network Limited	Hong Kong	Provision of fixed telecommunications network services in Hong Kong	Ordinary HK\$383,049	100
CTI Marketing Company Limited (formerly known as iChannel.com Limited)	Hong Kong	Provision of media marketing services in Hong Kong	Ordinary HK\$10,000	100

NOTES TO THE ACCOUNTS

14. INVESTMENTS IN SUBSIDIARIES (Cont'd)

Name	Place of incorporation	Principal activities and place of operations	Particulars of issued share capital	Percentage of interest held
iStore.com Limited	Hong Kong	Inactive	Ordinary HK\$10,000	100
CTI International Limited	Hong Kong	Provision of external telecommunications facilities in Hong Kong	Ordinary HK\$10,000,000	100
# 廣州城電客戶服務有限公司 (CTI Guangzhou Customer Service Co. Ltd. (translated but not the registered name))	The People's Republic of China	Provision of administrative support services in Mainland China	Ordinary HK\$1,050,000	*100

* Shares held directly by the Company.

Subsidiaries not audited by PricewaterhouseCoopers. The aggregate net liabilities of the subsidiaries not audited by PricewaterhouseCoopers amounted to approximately 1% (2001: 2%) of the Group's total assets.

(b) The amounts due from subsidiaries are unsecured, interest free and have no fixed terms of repayment.

15. ACCOUNTS RECEIVABLE

At 31st August 2002, the aging analysis of the accounts receivable was as follows:

	Group		Company	
	2002 HK\$'000	2001 HK\$'000	2002 HK\$'000	2001 HK\$'000
Current – 30 days	94,778	91,163	31,553	79,167
31 – 60 days	7,750	5,992	1,843	3,504
61 – 90 days	5,529	3,009	5,057	1,710
Over 90 days	1	–	–	–
	108,058	100,164	38,453	84,381

The majority of the Group's turnover is on open account. Customers are generally required to pay deposits or provide their credit card or other credit information to the Group before they subscribe for the Group's services.

16. ACCOUNTS PAYABLE

At 31st August 2002, the aging analysis of the accounts payable was as follows:

	Group		Company	
	2002	2001	2002	2001
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Current – 30 days	53,613	44,585	34,323	34,485
31 – 60 days	24,939	34,500	23,847	29,922
61 – 90 days	11,587	11,125	10,948	10,567
Over 90 days	36,141	45,556	34,226	44,203
	126,280	135,766	103,344	119,177

17. SHARE CAPITAL

Authorised (Ordinary shares of HK\$0.10 each)

	2002		2001	
	No. of shares	HK\$'000	No. of shares	HK\$'000
At 31st August 2000, 31st August 2001 and 31st August 2002	2,000,000,000	200,000	2,000,000,000	200,000

Issued and fully paid (Ordinary shares of HK\$0.10 each)

	2002		2001	
	No. of shares	HK\$'000	No. of shares	HK\$'000
At 1st September	491,074,000	49,107	489,604,000	48,960
Exercise of share options (Note (a))	3,060,000	306	1,470,000	147
Exercise of warrants (Note (b))	6,729,202	673	–	–
At 31st August	500,863,202	50,086	491,074,000	49,107

NOTES TO THE ACCOUNTS

17. SHARE CAPITAL (Cont'd)

- (a) During the year, 2,120,000 shares were issued at a price of HK\$0.26 per share and 940,000 shares were issued at a price of HK\$0.58 per share to share option holders who exercised their subscription rights. These shares rank pari passu with the existing shares.
- (b) The Company effected a warrant issue at a price of HK\$0.11 per warrant to qualifying shareholders (shareholders domiciled in Hong Kong) for cash. One warrant was offered for every five existing shares held on the date of record. The warrants entitle the holders to subscribe HK\$39,325,920 in cash at any time on or before 1st November 2004 for ordinary shares of the Company at a price of HK\$0.40 per share (subject to adjustment). If the warrants are fully exercised, the Company will be required to issue a further 98,314,800 shares. During the year, 6,729,202 warrants were exercised for an equivalent number of shares and 91,585,598 warrants were outstanding at year end. The shares issued rank pari passu with the existing shares.
- (c) Details of the share options granted by the Company during the year pursuant to the share option scheme approved by the shareholders of the Company on 12th July 1997 and the options outstanding at 31st August 2002, which will lapse not later than 11th July 2007, are as follows:

Date of grant	3rd September 1998	10th September 1999	20th October 2000
Exercise price per share (HK\$)	0.26	2.10	0.58
Number of Share Options outstanding at 1st September 2001	3,010,000	60,000	22,386,000
Granted	–	–	–
Exercised	(2,120,000)	–	(940,000)
Lapsed upon resignation of employees	–	–	(20,000)
Cancelled	–	–	(16,000)
Number of Share Options outstanding at 31st August 2002	890,000	60,000	21,410,000

All of the above share options are immediately exercisable.

18. RESERVES

	Group				
	Share premium HK\$'000	Warrant reserve HK\$'000	Retained profits HK\$'000	Exchange reserve HK\$'000	Total Reserves HK\$'000
At 1st September 2000	568,945	–	138,241	(2,722)	704,464
Profit for the year	–	–	53,927	–	53,927
2001 interim dividend paid	–	–	(4,907)	–	(4,907)
Premium on shares issued upon exercise of share options	235	–	–	–	235
Exchange adjustments on translation of the accounts of overseas subsidiaries	–	–	–	2,480	2,480
At 31st August 2001	569,180	–	187,261	(242)	756,199
At 1st September 2001	569,180	–	187,261	(242)	756,199
Issue of warrants	–	10,815	–	–	10,815
Expenses in connection with issue of new warrants	–	(1,058)	–	–	(1,058)
Profit for the year	–	–	91,129	–	91,129
Exercises of warrants	–	(668)	–	–	(668)
Premium on shares issued upon exercise of share options (Note 17(a))	790	–	–	–	790
Premium on shares issued upon exercise of warrants (Note 17(b))	2,686	–	–	–	2,686
Exchange adjustments on translation of the accounts of overseas subsidiaries	–	–	–	204	204
At 31st August 2002	572,656	9,089	278,390	(38)	860,097

NOTES TO THE ACCOUNTS

18. RESERVES (Cont'd)

	Company			Total Reserves HK\$'000
	Share premium HK\$'000	Warrant reserve HK\$'000	Retained profits HK\$'000	
At 1st September 2000	568,945	–	97,942	666,887
Profit for the year	–	–	99,208	99,208
2001 interim dividend paid	–	–	(4,907)	(4,907)
Premium on shares issued upon exercise of share options	235	–	–	235
At 31st August 2001	569,180	–	192,243	761,423
At 1st September 2001	569,180	–	192,243	761,423
Issue of warrants	–	10,815	–	10,815
Expenses in connection with issue of new warrants	–	(1,058)	–	(1,058)
Profit for the year	–	–	154,199	154,199
Exercises of warrants	–	(668)	–	(668)
Premium on shares issued upon exercise of share options	790	–	–	790
Premium on shares issued upon exercise of warrants	2,686	–	–	2,686
At 31st August 2002	572,656	9,089	346,442	928,187

19. LONG-TERM LIABILITIES

	Note	Group		Company	
		2002 HK\$'000	2001 HK\$'000	2002 HK\$'000	2001 HK\$'000
Obligations under finance leases	(a)	2,949	7,384	2,949	7,384
Deferred taxation	(b)	15,000	5,485	15,000	5,485
Loan from a minority shareholder	(c)	–	22,500	–	–
		17,949	35,369	17,949	12,869
Less: current portion of long-term liabilities		(2,949)	(4,410)	(2,949)	(4,410)
		15,000	30,959	15,000	8,459

19. LONG-TERM LIABILITIES (Cont'd)

(a) Obligations under finance leases

	Group and Company	
	2002	2001
	HK\$'000	HK\$'000
Minimum lease payments:		
– Within one year	3,003	4,727
– In the second year	–	3,042
	3,003	7,769
Future finance charges on finance leases	(54)	(385)
Present value of finance lease liabilities	2,949	7,384
The present value of finance lease liabilities is as follows:		
– Within one year	2,949	4,410
– In the second year	–	2,974
	–	2,974
	2,949	7,384

(b) Deferred taxation

	Group and Company	
	2002	2001
	HK\$'000	HK\$'000
At 1st September	5,485	4,485
Transfer from profit and loss account (Note 6)	9,515	1,000
At 31st August	15,000	5,485

NOTES TO THE ACCOUNTS

19. LONG-TERM LIABILITIES (Cont'd)

(b) Deferred taxation (Cont'd)

As at 31st August 2002, the potential deferred tax liabilities/(assets) and the amounts provided/(recognised) are as follows:

	2002		2001	
	Full potential liabilities/(assets) HK\$'000	Provision made HK\$'000	Full potential liabilities/(assets) HK\$'000	Provision made HK\$'000
Group				
Accelerated depreciation allowances	84,978	15,000	52,448	5,485
Tax losses	(127,522)	–	(92,801)	–
	(42,544)	15,000	(40,353)	5,485
Company				
Accelerated depreciation allowances	20,195	15,000	10,056	5,485

(c) Loan from a minority shareholder – Group

Last year's balance represented the loan from a minority shareholder which was secured by all present and future assets of a subsidiary, interest bearing at a fixed rate of 7% per annum, repayable on 25th June 2003 and convertible into fully paid up ordinary shares in that subsidiary.

During the year, the Company has acquired all the remaining shareholding in the subsidiary from the minority shareholder. The Company has assumed the subsidiary's obligations to repay the loan from the former minority shareholder on or before 25th June 2003 bearing interest at a fixed rate of 7% per annum and the loan has been reclassified as a current liability. The loan is not convertible into fully paid up ordinary shares in that subsidiary. As security for the Company's obligations to the former minority shareholder, the subsidiary has pledged a property in favour of the former minority shareholder (Note 13(c)).

20. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT

(a) Reconciliation of profit before taxation to net cash inflow from operating activities

	2002	2001
	HK\$'000	HK\$'000
Profit before taxation	97,461	58,978
Amortisation of goodwill	1,065	–
Depreciation of owned fixed assets	124,563	77,187
Depreciation of fixed assets held under finance leases	3,727	5,660
Interest income	(10,870)	(35,438)
Interest expenses	3,279	3,854
Interest element of finance leases	225	688
Loss on disposal of fixed assets	2,414	3,512
(Increase)/decrease in accounts receivable, other receivables, deposits and prepayments	(15,211)	39,943
Increase/(decrease) in accounts payable, other payables, accrued charges, deposits received and deferred service income	89,747	(111,091)
Net cash inflow from operating activities	296,400	43,293

NOTES TO THE ACCOUNTS

20. NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT (Cont'd)

(b) Analysis of changes in financing during the year

	Share capital (including share premium) HK\$'000	Minority interest HK\$'000	Obligations under finance leases HK\$'000
Balance at 1st September 2000	617,905	24,131	11,479
Issue of new shares	382	–	–
Share of loss for the year	–	(13,724)	–
Repayment of capital element of finance leases	–	–	(4,095)
Balance at 31st August 2001	618,287	10,407	7,384
Balance at 1st September 2001	618,287	10,407	7,384
Issue of new shares	13,544	–	–
Share of loss for the year	–	(8,234)	–
Gain on dilution of interest in a subsidiary	–	4,310	–
Acquisition of additional interest in a subsidiary	–	(6,483)	–
Repayment of capital element of finance leases	–	–	(4,435)
Balance at 31st August 2002	631,831	–	2,949

(c) Acquisition of additional interest in a subsidiary

	2002 HK\$'000	2001 HK\$'000
Minority interests acquired	6,483	–
Goodwill on acquisition	1,017	–
	7,500	–
Satisfied by:		
Cash	7,500	–

21. COMMITMENTS

(a) Capital commitments

	Group		Company	
	2002	2001	2002	2001
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Purchase of telecommunications, computer and office equipment				
– contracted but not provided for	139,009	119,814	17,985	67,992

(b) Commitments under operating leases

At 31st August 2002, the Group and the Company had future aggregate minimum lease payments under non-cancellable operating leases as follows:

	Group		Company	
	2002	2001	2002	2001
	HK\$'000	HK\$'000	HK\$'000	HK\$'000
Leases in respect of land and buildings which are payable:				
– Within one year	6,970	11,703	3,168	11,703
– Later than one year and not later than five year	1,874	3,037	1,218	3,037
	8,844	14,740	4,386	14,740
Leases in respect of telecommunications facilities and computer equipment which are payable:				
– Within one year	8,199	16,067	3,449	16,067
– Later than one year and not later than five year	528	8,951	–	8,951
	8,727	25,018	3,449	25,018
	17,571	39,758	7,835	39,758

NOTES TO THE ACCOUNTS

22. PLEDGE OF ASSETS

As at 31st August 2002, the Group had deposits of HK\$5,000,000 at a bank as sureties to the Office of the Telecommunications Authority ("OFTA") for the due performance of the terms of the Wireless Fixed Telecommunications Network Services License ("WFTNS"). The amount of the sureties shall reduce and the deposits be refunded upon satisfying the terms stipulated in the license.

As at 31st August 2002, the terms of the licence have been satisfied by the Group and the release of the bank deposits is pending on the approval of the OFTA.

23. RELATED PARTY TRANSACTIONS

Significant related party transactions, which were carried out in the normal course of the Group's business are as follows:

	Note	2002 HK\$'000	2001 HK\$'000
Calling charges payable to KDDI Corporation	(a)	13,161	34,106
Interest expenses payable to KDDI Corporation	(b)	846	1,458

- (a) The calling charges were payable to KDDI Corporation, a minority shareholder of a subsidiary of the Company, pursuant to the service agreements entered into between the Company and KDDI Corporation in 1999. The transactions were conducted in accordance with the terms of the service agreements and the Group believes that the terms are no less favourable than terms available from third parties. The above amount represents the calling charges payable to KDDI Corporation for the period from 1st September 2001 to 13th March 2002. KDDI Corporation ceased to have any interest in the subsidiary on 13th March 2002.
- (b) These represent interest payable on the interest-bearing loan from KDDI Corporation (Note 19(c)) for the period from 1st September 2001 to 13th March 2002.

24. PENDING LITIGATION

- (a) In July 1998, Cable & Wireless HKT, a Hong Kong company, commenced proceedings against the Company and served a statement of claim which alleged that the Company had breached the terms of a contract it had with Cable & Wireless HKT and committed an economic tort. The Company denied these allegations in a comprehensive defence which included a counterclaim against the plaintiff seeking damages for anti-competitive practices conducted by Cable & Wireless HKT in Hong Kong. Neither the claim by Cable & Wireless HKT nor the counterclaim by the Company has been quantified. The directors believe that the allegations against the Company are without merit and intend to defend the litigation vigorously. The case is now in its discovery phase. No provision against the claim has been made in the accounts.

24. PENDING LITIGATION *(Cont'd)*

- (b) In January 1999, Jade Com Development Limited ("Jade Com") commenced proceedings against the Company and two directors of the Company alleging repudiation of the international carrier service agreement between Jade Com and Attitude Holdings Limited, a wholly-owned subsidiary of the Company. Jade Com claimed damages for breach of contract and misrepresentation and alleged that the Company has a remaining commitment of approximately US\$3.6 million under the agreement. The Company filed a defence in May 1999 on the basis that Jade Com had breached a condition of the agreement that they obtain the necessary legal approvals and licenses necessary for the provision of their services. In February 2001, the parties consented to adjourn the case indefinitely with liberty to restore. No provision has been made in the accounts with respect to the litigation.
- (c) In June 1999, New World Telephone Limited ("New World") commenced proceedings against the Company. The dispute arose from contractual arrangements between the parties whereby New World provided carrier services to the Company for the Company's incoming and outgoing international telephone call traffic through the New World's telecommunication network facility and operation system. In the proceedings New World alleged, inter alia, that the Company failed to settle the interconnection fees of the same amount payable to New World and that New World is entitled to recover delivery fees allegedly paid by mistake to the Company. New World's claim is for a total of approximately HK\$96.4 million. The directors believe that the Company is entitled to set off the interconnection fees payable to New World against the delivery fees receivable by the Company. Defences were filed in August and October 1999 to the same effect. The Company has instructed solicitors to defend the case vigorously. The proceedings have reached the stage of discovery but New World have not taken any steps in the proceedings since November 1999. No provision against the claims has been made in the accounts.

25. APPROVAL OF ACCOUNTS

The accounts were approved by the board of directors on 20th November 2002.