Notes to the accounts

1 Principal accounting policies

A Basis of preparation of accounts

(i) These accounts have been prepared in compliance with the Hong Kong Companies Ordinance. The accounts have also been prepared in accordance with all applicable Statements of Standard Accounting Practice ("SSAPs") and Interpretations issued by the Hong Kong Society of Accountants ("HKSA"), accounting principles generally accepted in Hong Kong and the applicable disclosure provisions of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Stock Exchange").

(ii) The measurement basis used in the preparation of the accounts is historical cost modified by the revaluation of investment properties and self-occupied office land and buildings.

B Basis of consolidation

The consolidated accounts include the accounts of the Company and all its subsidiaries except for a non-controlled subsidiary (see note 1D) (the "Group") made up to 31 December each year. The results of subsidiaries acquired or disposed of during the year are included in the consolidated profit and loss account from or to the date of their acquisition or disposal, as appropriate. All material inter-company transactions and balances are eliminated on consolidation.

C Subsidiaries

A subsidiary in accordance with the Hong Kong Companies Ordinance is a company in which the Group, directly or indirectly, holds more than half of the issued share capital, or controls more than half of the voting power, or controls the composition of the board of directors. Subsidiaries are considered to be controlled if the Company has the power, directly or indirectly, to govern the financial and operating policies, so as to obtain benefits from their activities. Investments in subsidiaries are carried in the Company's balance sheet at cost less any impairment losses (see note 1G).

D Non-controlled subsidiary

Octopus Cards Limited ("OCL") is regarded as a jointly controlled entity as the Group does not have effective control over the Board of OCL. The investment in OCL is accounted for in the consolidated accounts of the Company using the equity method as described in SSAP 21 "Accounting for interests in joint ventures."

E Revenue recognition

Provided it is probable that the economic benefits associated with the transactions will flow to the Group and the amount of revenue can be measured reliably, revenue is recognised in the profit and loss account as follows:

(i) Fare revenue is recognised when the journey is provided.

(ii) Advertising income and service fees from telecommunication services provided within the railway are recognised when the services are provided.

(iii) Rental income from investment properties, station kiosks and other railway premises under operating leases is accounted for in accordance with the terms of the leases. Contingent rentals are recognised as income in the accounting period in which they are earned. Property management income is recognised when the services are provided.

F Fixed assets

(i) Investment properties are stated in the balance sheet at open market value as determined annually by independent professionally qualified valuers.

Changes in the value of investment properties arising upon revaluations are treated as movements in the investment property revaluation reserve, except:

- where the balance of the investment property revaluation reserve is insufficient to cover a revaluation deficit on a portfolio basis, the excess of the deficit is charged to the profit and loss account; and
- where a revaluation deficit had previously been charged to the profit and loss account and a revaluation surplus subsequently arises, this surplus is firstly credited to the profit and loss account to the extent of the deficit previously charged to the profit and loss account, and is thereafter taken to the investment property revaluation reserve.

On disposal of an investment property, the related portion of the investment property revaluation reserve is transferred to the profit and loss account.

(ii) Leasehold land and buildings comprise leasehold land for railway depots and self-occupied office land and buildings:

(a) Leasehold land for railway depots is stated at cost less accumulated depreciation and impairment losses.

1 Principal accounting policies (continued)

(b) Self-occupied office land and buildings are stated in the balance sheet at open market value on the basis of their existing use at the date of revaluation less any subsequent accumulated depreciation. Revaluations are performed by independent qualified valuers every year. Changes in the value of self-occupied office land and buildings arising upon revaluations are treated as movements in the fixed asset revaluation reserve, except:

- where the balance of the fixed asset revaluation reserve relating to a self-occupied office land and building is insufficient to cover a revaluation deficit of that property, the excess of the deficit is charged to the profit and loss account; and
- where a revaluation deficit had previously been charged to the profit and loss account and a revaluation surplus subsequently arises, this surplus is firstly credited to the profit and loss account to the extent of the deficit previously charged to the profit and loss account, and is thereafter taken to the fixed asset revaluation reserve.

(iii) Civil works and plant and equipment are stated at cost less accumulated depreciation and impairment losses.

(iv) Assets under construction for the operational railway are stated at cost less impairment losses. Cost comprises direct costs of construction, such as materials, staff costs and overheads, together with interest expense capitalised during the period of construction or installation and testing. Capitalisation of these costs ceases and the asset concerned is transferred to fixed assets when substantially all the activities necessary to prepare the asset for its intended use are completed.

(v) Leases of assets under which the lessee assumes substantially all the risks and benefits of ownership are classified as finance leases. Where the Group acquires the use of assets under finance leases, the amounts representing the fair value of the leased asset, or, if lower, the present value of the minimum lease payments (computed using the rate of interest implicit in the lease), of such assets are included in fixed assets and the corresponding liabilities, net of finance charges, are recorded as obligations under finance leases.

Leases of assets under which the lessor has not transferred all the risks and benefits of ownership are classified as operating leases. Where the Group leases out assets under operating leases, the assets are included in the balance sheet according to their nature and, where applicable, are depreciated in accordance with the Group's depreciation policies. Impairment losses are accounted for in accordance with the accounting policies on impairment of assets. Revenue arising from operating leases is recognised in accordance with the Group's revenue recognition policies as set out in note 1E.

(vi) Subsequent expenditure relating to an existing fixed asset is added to the carrying amount of the asset if it is probable that future economic benefit in excess of the originally assessed standard of performance of the asset will flow to the Group.

Expenditure on repairs or maintenance of an existing fixed asset to restore or maintain the originally assessed standard of performance of that asset is charged as an expense when incurred.

(vii) Gains or losses arising from the retirement or disposal of a fixed asset other than an investment property are determined as the difference between the estimated net disposal proceeds and the carrying amount of the asset and are recognised as income or expense in the profit and loss account on the date of retirement or disposal. Any related revaluation surplus is transferred from the fixed asset revaluation reserve to retained profits.

G Impairment of assets

Internal and external sources of information are reviewed at each balance sheet date to identify indications that the following assets may be impaired or an impairment loss previously recognised no longer exists or may have decreased:

- fixed assets (other than properties carried at revalued amounts);
- railway construction in progress;
- property development in progress;
- deferred expenditure; and
- investments in subsidiaries.

If any such indication exists, the asset's recoverable amount is estimated.

The recoverable amount of an asset is the greater of its net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of time value of money and the risks specific to the asset. Where an asset does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the smallest group of assets that generates cash inflows independently (ie a cash-generating unit).

An impairment loss is recognised whenever the carrying amount of an asset exceeds its recoverable amount.

An impairment loss is reversed if there has been a favourable change in the estimates used to determine the recoverable amount of the asset.

A reversal of impairment losses is limited to the asset's carrying amount that would have been determined had no impairment loss been recognised in prior years. Reversals of impairment losses are credited to the profit and loss account in the year in which the reversals are recognised.

1 Principal accounting policies (continued)

H Depreciation

(i) Investment properties with an unexpired lease term of more than 20 years are not depreciated.

(ii) Fixed assets other than investment properties and assets under construction are depreciated on a straight line basis at rates sufficient to write off their cost or valuation over their estimated useful lives as follows:

Leasehold land and buildings

Self-occupied office land and buildings	the shorter of 50 years and the unexpired term of the lease
Leasehold land for railway depots	the unexpired term of the lease

Civil works

Rails (initial cost)	Indefinite *
Excavation and boring	Indefinite
Tunnel linings, underground civil structures, overhead structures and immersed tubes	100 years
Station building structures	80–100 years
Depot structures	80 years
Concrete kiosk structures	20 years
Station architectural finishes	20–25 years

Plant and equipment

Rolling stock (electrical)	35–40 years
Platform screen doors	35 years
Environmental control systems, lifts and escalators and drainage system	20–30 years
Power supply equipment, metal station kiosks, fire protection system, rolling stock (battery operated) and other mechanical equipment	20 years
Train control and signalling equipment, automatic fare collection systems and advertising panels	15 years
Rolling stock (diesel), telecommunication systems, maintenance equipment, office furniture and equipment	10 years
Computer software licences	7 years
Cleaning equipment, computer equipment and tools	5 years
Motor vehicles	4 years

* Replacement costs of rails are charged to the profit and loss account as revenue expenses.

The useful lives of the various categories of fixed assets are reviewed regularly in the light of actual asset condition, usage experience and the current asset replacement programme. The depreciation charge for the current and future periods is adjusted if there are significant changes from previous estimates.

(iii) No depreciation is provided on assets under construction until construction is completed and the assets are ready for their intended use.

(iv) Depreciation on assets held under finance leases is provided at rates designed to write off the cost of the asset in equal annual amounts over the shorter of the lease term or the anticipated useful life of the asset as set out above, except in cases where title to the asset will be acquired by the Group at the end of the lease where depreciation is provided at rates designed to write off the cost of the asset in equal amounts over the anticipated useful life of the asset.

I Construction costs

(i) Costs incurred by the Group in respect of feasibility studies on proposed railway related construction projects (including consultancy fees, in-house staff costs and overheads) are dealt with as follows:

- where the proposed projects are at a preliminary review stage with no certainty of materialising, the costs concerned are written off to the profit and loss account; and
- where the proposed projects are at a detailed study stage, having been agreed in principle by the Board of Directors based on a feasible financial plan, the costs concerned are dealt with as deferred expenditure until such time as a project agreement is reached with the Government, whereupon the costs are transferred to railway construction in progress.

(ii) After entering into a project agreement with the Government, all costs incurred in the construction of the railway are dealt with as railway construction in progress until commissioning of the railway line, whereupon the relevant construction costs are transferred to fixed assets.

1 Principal accounting policies (continued)

J Property development

(i) Costs incurred by the Group in the preparation of sites for property development are dealt with as property development in progress.

(ii) Payments received from developers in respect of developments are offset against the amounts in property development in progress attributable to that development. Any surplus amounts of payments received from developers in excess of the balance in property development in progress are transferred to deferred income. In these cases, further costs subsequently incurred by the Group in respect of that development are charged against deferred income.

(iii) Expenditure incurred on the development of properties for retention by the Group is transferred to fixed assets when the occupation permits are issued and the properties are put into use.

(iv) When agreement is reached with a developer to redevelop an existing self-occupied property, the relevant property is revalued on an existing use basis prior to commencement of redevelopment. The surplus arising on revaluation is credited to fixed asset revaluation reserve. On commencement of redevelopment, the net book value of the property is transferred to property development in progress.

(v) Profits arising from the development of properties undertaken in conjunction with property developers are recognised in the profit and loss account as follows:

- where the Group receives payments from developers at the commencement of the project, profits arising from such payments are recognised when the foundation and site enabling works are complete and acceptable for development, and after taking into account the outstanding risks and obligations, if any, retained by the Group in connection with the development;
- where the Group receives sharing of proceeds from sale of the development, profits arising from such proceeds are recognised upon the issue of occupation permits provided the amounts of revenue and costs can be measured reliably; and
- where the Group receives a distribution of the assets of the development upon completion of construction, profit is recognised based on the fair value of such assets at the time of receipt.

Upon recognition of profit, the balance of deferred income or property development in progress related to that development is credited or charged to the profit and loss account, as the case may be.

(vi) Where the Group is liable to pay the developer consideration for the retention of part of a property to be redeveloped, profit attributable to the Group in respect of the redevelopment (including any payment received from the developer) will be recognised in the profit and loss account when the quantum of the obligation of the Group and the amount of realised profit can be determined with reasonable accuracy.

(vii) Where properties are received as a profit distribution upon completion of development and are held for sale, those properties are stated at their estimated net realisable value upon receipt. Net realisable value represents the estimated selling price less costs to be incurred in selling the properties. When properties are sold, the carrying amount of those properties is recognised as cost of properties sold in the period in which the related revenue is recognised. The amount of any write-down of properties to net realisable value is recognised as an expense in the period the write-down occurs. The amount of any reversal of any write-down of properties, arising from an increase in net realisable value, is recognised as a reduction in the cost of properties sold in the period in which the reversal occurs.

K Operating lease charges

Rentals payable under operating leases are charged on a straight-line basis over the period of the lease to the profit and loss account, except for rentals payable in respect of railway construction, property development in progress and proposed capital projects which are capitalised as part of railway construction in progress, property development in progress and deferred expenditure respectively.

L Stores and spares

Stores and spares are categorised as either revenue or capital. Revenue items are stated in the balance sheet at cost, using the weighted average cost method. Provision is made for obsolescence where appropriate. Capital items are included in fixed assets and stated at cost less aggregate depreciation and impairment losses. Depreciation is charged at the rates applicable to the relevant fixed assets against which the capital spares are held in reserve.

M Cash equivalents

Cash and cash equivalents comprise cash at banks and in hand, demand deposits with banks and other financial institutions, and short-term, highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value, having been within three months of maturity at acquisition. Bank overdrafts that are repayable on demand and form an integral part of the Group's cash management are also included as a component of cash and cash equivalents for the purpose of the consolidated cash flow statement.

1 Principal accounting policies (continued)

N Interest and finance charges

Interest expense directly attributable to the financing of assets under construction prior to their completion or commissioning is capitalised. Exchange differences arising from foreign currency borrowings related to the acquisition of assets are capitalised to the extent that they are regarded as an adjustment to interest costs. Interest expense attributable to other purposes is charged to the profit and loss account.

Finance charges implicit in the lease payments on assets held under finance leases are charged to the profit and loss account over the period of the lease so as to produce an approximately constant periodic rate of charge on the remaining balance of the obligations for each accounting period.

The differentials paid and received on interest rate swap agreements are accrued and recognised as adjustments to interest expense.

O Foreign currency translation

Foreign currency transactions during the year are translated into Hong Kong dollars and recorded at exchange rates ruling at the transaction dates. Foreign currency monetary assets and liabilities are translated into Hong Kong dollars at the exchange rates ruling at the balance sheet date. Forward foreign exchange contracts, swaps and options used as a hedge against foreign currency liabilities are revalued at the balance sheet date at the exchange rates ruling at that date. Gains and losses on currency hedging transactions are used to offset gains and losses resulting from currency fluctuations inherent in the underlying foreign currency liabilities. Differences arising on foreign currency translation and revaluation of forward foreign exchange contracts, swaps and options are dealt with in the profit and loss account.

The results of foreign enterprises are translated into Hong Kong dollars at the average exchange rates for the year; balance sheet items are translated into Hong Kong dollars at the rates of exchange ruling at the balance sheet date. The resulting exchange differences are dealt with as a movement in reserves.

P Deferred taxation

Deferred taxation is provided using the liability method in respect of the taxation effect arising from all material timing differences which are expected with reasonable probability to crystallise in the foreseeable future.

A deferred tax asset in respect of carried forward tax losses is only recognised if it is assured beyond reasonable doubt that the Group will have taxable profits sufficient to offset the available losses in the foreseeable future.

No deferred tax is provided on earnings retained overseas.

Q Employee benefits

(i) Salaries, annual leave, leave passage allowance and other costs of non-monetary benefits are accrued and recognised as an expense in the year in which the associated services are rendered by employees of the Group, except those benefits incurred for project staff in respect of construction projects and capital works, which are capitalised as part of the cost of the qualifying assets.

(ii) Contributions to defined contribution retirement plans, including contributions to Mandatory Provident Funds ("MPF") as required under the Hong Kong Mandatory Provident Fund Schemes Ordinance, are recognised as an expense in the profit and loss account as incurred, except those contributions on project staff incurred in respect of construction projects and capital works, which are capitalised as part of the cost of the qualifying assets.

(iii) The Group's net obligation in respect of defined benefit retirement plans is calculated separately for each plan by estimating the amount of future benefit that employees have earned in return for their service in the current and prior years; that benefit is discounted to determine the present value, and the fair value of any plan assets is deducted. The discount rate is the yield at balance sheet date on high quality corporate bond that have maturity dates approximating the terms of the Group's obligations. If there is no deep market in such bonds, the market yield on government bonds would be used. The calculation is performed by a qualified actuary using the projected unit credit method.

When the benefits of a plan are improved, the portion of the increased benefit relating to past service by employees is recognised either as an expense in the profit and loss account, or capitalised as part of the cost of the relevant construction projects or capital works in the case of project related employees, as the case may be, on a straight-line basis over the average period until the benefits become vested. To the extent that the benefits vest immediately, the expense is recognised immediately in a similar manner.

In calculating the Group's obligation in respect of a plan, to the extent that any cumulative unrecognised actuarial gain or loss exceeds ten percent of the greater of the present value of the defined benefit obligation and the fair value of plan assets, that portion is recognised in the profit and loss account over the expected average remaining working lives of the employees participating in the plan. Otherwise, the actuarial gain or loss is not recognised.

Where the calculation of the Group's net obligation results in a negative amount, the asset recognised is limited to the net total of any cumulative unrecognised net actuarial losses and past service costs and the present value of any future refunds from the plan or reductions in future contributions to the plan.

1 Principal accounting policies (continued)

(iv) When the Group grants employees options to acquire shares of the Company, no employee benefit cost or obligation is recognised at the date of grant. When the options are exercised, equity is increased by the amount of the proceeds received.

(v) Termination benefits are recognised when, and only when, the Group demonstrably commits itself to terminate employment or to provide benefits as a result of voluntary redundancy by having a detailed formal plan which is without realistic possibility of withdrawal.

R Retirement Schemes

The Group operates an Occupational Retirement Scheme (the "MTR Corporation Limited Retirement Scheme"), which is supplemented by a top-up scheme ("MTR Corporation Limited Retention Bonus Scheme") mainly for project staff to provide extra benefits in the event of redundancy.

In addition, the Group has set up a MPF Scheme by participating in a master trust scheme provided by an independent MPF service provider to comply with the requirements under the MPF Ordinance.

Employer's contributions to the defined contribution section of the MTR Corporation Limited Retirement Scheme and the MPF Scheme are recognised in the accounts in accordance with the policy set out in note 1Q(ii).

The employer's contributions paid and payable in respect of employees of the hybrid benefit section of the MTR Corporation Limited Retirement Scheme, as calculated annually by independent actuaries in accordance with the Retirement Scheme Rules and provisions of the Occupational Retirement Schemes Ordinance, are used to satisfy the pension expenses recognised in the accounts according to note 1Q(iii). Any deficit or surplus thereof will be dealt with in the balance sheet as accrued or prepaid benefit expenses, as the case may be.

S Provisions and contingent liabilities

Provisions are recognised for liabilities of uncertain timing or amount when the Company or Group has a legal or constructive obligation arising as a result of a past event, it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made. Where the time value of money is material, provisions are stated at the present value of the expenditures expected to settle the obligation.

Where it is not probable that an outflow of economic benefits will be required, or the amount cannot be estimated reliably, the obligation is disclosed as a contingent liability, unless the probability of outflow of economic benefits is remote. Possible obligations, whose existence will only be confirmed by the occurrence or non-occurrence of one or more future events are also disclosed as contingent liabilities unless the probability of outflow of economic benefits is remote.

T Jointly controlled operations

The arrangements entered into by the Group with developers for property developments along the Airport Railway and the Tseung Kwan O Line are considered to be jointly controlled operations pursuant to SSAP 21 "Accounting for interests in joint ventures". Pursuant to the development arrangements, the Group is normally responsible for its own costs, including in-house staff costs and the costs of enabling works, and the developers normally undertake to pay for all other project costs such as land premium, construction costs, professional fees, etc. Such costs are deductible from the proceeds of sale before surplus proceeds are shared. In respect of its interests in such operations, the Group accounts for the costs of enabling works net of up-front payments received as property development in progress. In cases where up-front payments received from developers exceed the related expenditures incurred by the Group, such excess is recorded as deferred income. Expenses incurred by the Group on staff, overhead and consultancy fees in respect of these developments are also capitalised as property development in progress. The Group's share of income earned from such operations is recognised in the profit and loss account in accordance with note 1J after netting off any related balance in the property development in progress account at that time.

U Segment reporting

A segment is a distinguishable component of the Group that is engaged either in providing products or services (business segment), or in providing products or services within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those of other segments.

In accordance with the Group's internal financial reporting system, the Group has chosen business segment information as the primary reporting format. As substantially all the principal activities of the Group are carried out in Hong Kong, no geographical segment information is provided.

Segment revenue, expenses, results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis to that segment. Segment revenue, expenses, assets and liabilities are determined before intra-group balances and intra-group transactions are eliminated as part of the consolidation process, except to the extent that such intra-group balances and transactions are between group enterprises within a single segment.

Segment capital expenditure is the total cost incurred during the year to acquire segment assets that are expected to be used for more than one year.

Unallocated items mainly comprise financial and corporate assets, interest-bearing loans, borrowings, share of results of non-controlled subsidiary, corporate and financing expenses and minority interests.

1 Principal accounting policies (continued)

V Related parties

For the purposes of these financial statements, parties are considered to be related to the Group if the Group has the ability, directly or indirectly, to control the party or exercise significant influence over the party in making financial and operating decisions, or vice versa, or where the Group and the party are subject to common control or common significant influence. Related parties may be individuals or other entities.

W Government grants

Government grants are assistance by Government in the form of transfer of resources in return for the Company's compliance to the conditions attached to it. Government grant, which represents compensation for the cost of an asset, will be deducted from the cost of the asset in arriving at its carrying value to the extent of the amounts received and receivable as at the date of the balance sheet. Any excess of the amount of grant received or receivable over the cost of the asset at the balance sheet date will be carried forward as deferred income to set off future cost of the asset.

2 Fare revenue

The MTR Lines comprise the Kwun Tong, Tsuen Wan, Island, Tung Chung and Tseung Kwan O Lines. The fare revenue attributable to the Tseung Kwan O Line relates to the period after the line commenced operation on 18 August 2002.

3 Non-fare revenue

A Station commercial and other revenue

in HK$ million	**2002**	2001
Station commercial and other revenue comprises:		
Advertising	**399**	428
Kiosk rental	**238**	221
Telecommunication income	**186**	173
Miscellaneous business revenue	**156**	151
	979	973

B Rental and management income

in HK$ million	**2002**	2001
Rental income was attributable to:		
Telford Plaza	**371**	353
Luk Yeung Galleria	**105**	104
Paradise Mall	**113**	80
Maritime Square	**181**	176
Other properties	**127**	104
	897	817
Management income	**85**	73
Property agency income	**5**	1
	987	891

4 Operating expenses before depreciation

A Included in staff costs and related expenses are the following retirement expenses:

in HK$ million	**2002**	2001 (Note 42A)
Contributions to defined contribution plans and Mandatory Provident Fund	**13**	12
Increase in liability for defined benefit plans (Note 36C)	**149**	176
	162	188

The defined benefit expense recognised in respect of 2001 was not restated as an independent actuarial valuation in accordance with SSAP 34 had not been conducted to ascertain the Scheme's position as of 1 January 2001. The amount recognised in the consolidated profit and loss account for the year ended 31 December 2001 was based on the Group's actual contributions made to the Scheme during that year.

B Repairs and maintenance costs relate mainly to contracted maintenance and revenue works. Other routine repairs and maintenance works are performed by in-house operations, the costs of which are included under staff costs and stores and spares consumed.

C Project study and deferred expenditures written off comprise:

in HK$ million	**2002**	2001
Shatin Central Link (Note 17)	**42**	–
North Island Link (Note 17)	**85**	–
Airport Railway improvement works in connection with North Island Link	**63**	–
Others	**28**	16
	218	16

D Included in other expenses are the following charges:

in HK$ million	**2002**	2001
Auditors' remuneration		
– audit services	**3**	3
– other services	**1**	1
Loss on disposal of fixed assets	**17**	6
Operating lease expenses:		
Office buildings and staff quarters	**12**	15
Less: Amount capitalised	**9**	10
	3	5

5 Remuneration of Members of the Board and the Executive Directorate

A Remuneration of Members of the Board and the Executive Directorate

The aggregate emoluments of the Members of the Board and the Executive Directorate of the Company disclosed pursuant to section 161 of the Hong Kong Companies Ordinance were as follows:

in HK$ million	**2002**	2001
Fees	**2**	2
Salaries, allowances and benefits-in-kind	**32**	33
Retirement scheme contributions	**4**	4
	38	39

Included in salaries, allowances and benefits-in-kind are realised gains on exercise of share options amounting to HK$0.2 million *(2001: HK$0.6 million)* in respect of certain Members of the Executive Directorate. Details of the share options granted to the Executive Directorate are disclosed in note 5B. Allowances and benefits-in-kind also include housing, medical and education allowances.

Non-executive directors of the Company are not appointed for a specific term but are subject (save as those appointed pursuant to Section 8 of the Mass Transit Railway Ordinance (Chapter 556 of the Laws of Hong Kong)) to retirement by rotation and re-election at the Company's annual general meetings in accordance with Articles 87 and 88 of the Company's Articles of Association.

The gross emoluments of the Members of the Board and the Members of the Executive Directorate were within the following bands:

Emoluments	**2002 Number**	2001 Number
HK$0 – HK$250,000	**13**	9
HK$500,001 – HK$1,000,000	**1**	–
HK$3,500,001 – HK$4,000,000	**1**	–
HK$4,500,001 – HK$5,000,000	**5**	5
HK$5,000,001 – HK$5,500,000	**–**	1
HK$7,500,001 – HK$8,000,000	**1**	1
	21	16

The information shown in the above table includes the five highest paid employees. The independent non-executive directors' emoluments are included in the first remuneration band.

B Share options

Under the Company's Pre-Global Offering Share Option Scheme ("Share Option Scheme") described in note 41A, Mr. Jack So Chak-kwong and each of the other Members of the Executive Directorate, except Mr. Lincoln Leong Kwok-kuen, were granted options on 20 September 2000 to acquire 1,599,000 and 1,066,000 shares respectively. Mr. Lincoln Leong Kwok-kuen joined the Company on 1 February 2002 and is not a beneficiary of the Share Option Scheme.

Under the vesting terms of the Share Option Scheme, each eligible Member of the Executive Directorate must continue to beneficially own (i) at all times after 26 October 2001, at least 40,000 shares in the case of the Chairman and at least 23,000 shares in the case of other Members of the Executive Directorate, and (ii) at all times after 26 October 2002, at least 80,000 shares in the case of the Chairman and at least 46,000 shares in the case of other Members of the Executive Directorate.

Options exercised and outstanding in respect of each Member of the Executive Directorate as at 31 December 2002 are set out under the paragraph "Board Members and Executive Directorate's Interest in Shares" of the Report of the Members of the Board.

6 Profit on property developments

in HK$ million	**2002**	2001
Profit on property developments comprises:		
Transfer from deferred income (Note 16B)	**2,548**	2,110
Share of surplus from development	**6**	1,096
Profit recognised from sharing in kind	**1,203**	56
Other overhead costs	**(2)**	(14)
	3,755	3,248

Included in share of surplus from development are write-down provision of properties held for sale of HK$44 million *(2001: Nil)* and cost of properties sold of HK$118 million *(2001: Nil)*.

7 Depreciation

in HK$ million	**2002**	2001
Depreciation comprised charges on:		
Railway operations		
– on fixed assets held under finance leases	**19**	19
– on other railway fixed assets	**2,321**	2,036
Assets relating to station advertising, kiosk and miscellaneous businesses	**106**	97
Unallocated corporate assets	**24**	26
	2,470	2,178

8 Interest and finance charges

in HK$ million	**2002**	2001
Interest expenses in respect of:		
Bank loans and overdrafts, and capital market instruments wholly repayable within 5 years	**823**	910
Capital market instruments not wholly repayable within 5 years	**867**	861
Obligations under finance leases	**53**	64
Finance charges	**28**	88
Exchange gain	**–**	(1)
Interest expenses capitalised:		
Tseung Kwan O Extension Project	**(423)**	(661)
Property projects	**(86)**	(144)
Other capital projects	**(81)**	(167)
Assets under construction	**(28)**	(54)
	(618)	(1,026)
	1,153	896
Interest income in respect of:		
Deposits with banks and other financial institutions	**(25)**	(2)
Staff housing loans	**(3)**	(20)
	(28)	(22)
	1,125	874

Interest expenses have been capitalised at the average cost of funds to the Group calculated on a monthly basis. The average interest rates for each month varied from 5.2% to 5.4% per annum during the year *(2001: 5.4% to 7.5% per annum)*.

9 Profit attributable to shareholders

The consolidated profit attributable to shareholders includes a profit of HK$4,142 million *(2001: HK$4,242 million, as restated)* which has been dealt with in the accounts of the Company.

10 Dividends

Dividends paid and proposed during the year comprised:

in HK$ million	**2002**	2001
Dividend approved and paid		
– 2001 final dividend of 28 cents *(2000: 10 cents)* per share approved and paid in 2002	**1,415**	500
– 2002 interim dividend of 14 cents *(2001: 14 cents)* per share	**717**	703
	2,132	1,203
Dividend proposed		
– Final dividend proposed after the balance sheet date of 28 cents *(2001: 28 cents)* per share	**1,444**	1,415

The final dividend proposed after the balance sheet date has not been recognised as a liability at the balance sheet date.

During the year, scrip dividend elections were offered to shareholders with Hong Kong addresses. The Company's majority shareholder, the Financial Secretary Incorporated ("FSI"), had elected to receive part of its entitlement to dividends in the form of scrip to the extent necessary to ensure that the amount payable in cash would not exceed 50% of the total dividend payable. Details of dividends paid to the FSI are disclosed in note 39J.

Pursuant to the financing arrangement under the Penny's Bay Rail Link Project Agreement entered into between the Group and the Government, HK$219 million *(2001: Nil)* interim cash dividend declared and payable to the Government during the year had been waived (Note 39F).

11 Earnings per share

The calculation of basic earnings per share is based on the profit for the year attributable to shareholders of HK$4,212 million *(2001: HK$4,278 million, as restated)* and the weighted average number of ordinary shares of 5,098,511,864 in issue during the year *(2001: 5,015,601,057)*.

The calculation of diluted earnings per share is based on the profit for the year attributable to shareholders of HK$4,212 million *(2001: HK$4,278 million, as restated)* and the weighted average number of ordinary shares of 5,105,400,689 *(2001: 5,030,188,894)* after adjusting for the number of dilutive potential ordinary shares under the employee share option scheme calculated as follows:

	2002	2001
Weighted average number of ordinary shares used in calculating basic earnings per share	**5,098,511,864**	5,015,601,057
Number of ordinary shares deemed to be issued for no consideration	**6,888,825**	14,587,837
Weighted average number of ordinary shares used for calculating the diluted earnings per share	**5,105,400,689**	5,030,188,894

12 Taxation

A Profits tax

Taxation in the consolidated profit and loss account and consolidated balance sheet comprised overseas tax liabilities in respect of consultancy services income earned offshore, chargeable at the appropriate current rates of taxation ruling in the relevant countries.

No provision for Hong Kong profits tax has been made in the consolidated profit and loss account in respect of the Company and its local subsidiaries, as the Company and its local subsidiaries either have substantial accumulated tax losses brought forward which are available for set off against current year's assessable profits or have sustained tax losses as at 31 December 2002.

B Deferred tax

Provision for deferred taxation is not required as any potential liability arising from tax depreciation allowances in excess of related depreciation is not expected to crystallise in the foreseeable future.

The major components of unprovided deferred taxation are:

in HK$ million	**2002**	2001
Depreciation allowances in excess of related depreciation	**6,467**	5,932
Future benefit of tax losses	**(4,342)**	(4,450)
Other timing differences	**1,117**	1,117
Net deferred tax liabilities	**3,242**	2,599

No deferred taxation has been provided on the surpluses arising on the revaluation of properties as the disposal of these assets at their carrying value would result in capital gains which are not subject to taxation.

13 Segmental information

The results of major business activities are summarised below:

in HK$ million	Railway operations	Station commercial and other businesses	Property ownership and management	Total railway operations and related activities	Property developments	Total
2002						
Revenue	5,720	979	987	7,686	–	7,686
Less: Operating expenses before depreciation	2,804	185	167	3,156	–	3,156
	2,916	794	820	4,530	–	4,530
Profit on property developments	–	–	–	–	3,755	3,755
Operating profit before depreciation	2,916	794	820	4,530	3,755	8,285
Less: Depreciation	2,339	106	1	2,446	–	2,446
	577	**688**	**819**	**2,084**	**3,755**	5,839
Unallocated corporate expenses						(540)
Interest and finance charges (net)						(1,125)
Share of profit of non-controlled subsidiary						39
Taxation						(1)
Profit for the year ended 31 December 2002						**4,212**
Assets						
Operational assets	80,216	1,327	10,380	91,923	104	92,027
Railway construction in progress	109	–	–	109	–	109
Railway assets under construction	2,453	1	–	2,454	–	2,454
Property development in progress	–	–	–	–	2,870	2,870
Properties held for sale	–	–	–	–	794	794
	82,778	1,328	10,380	94,486	3,768	98,254
Interest in non-controlled subsidiary						88
Unallocated assets						2,778
Total assets						101,120
Liabilities						
Segmented liabilities	3,690	182	367	4,239	312	4,551
Deferred income	–	–	–	–	6,226	6,226
	3,690	182	367	4,239	6,538	10,777
Unallocated liabilities						33,508
Minority interests						8
Total liabilities						44,293
Other Information						
Capital expenditure on:						
Operational assets and assets under construction	4,215	722	39			
Railway construction in progress	220					
Property development in progress					356	
Non-cash expenses other than depreciation	14	3	–			

13 Segmental information (continued)

in HK$ million	Railway operations	Station commercial and other businesses	Property ownership and management	Total railway operations and related activities	Property developments	Total (Note 42A)
2001						
Revenue	5,728	973	891	7,592	–	7,592
Less: Operating expenses before depreciation	2,856	197	159	3,212	–	3,212
	2,872	776	732	4,380	–	4,380
Profit on property developments	–	–	–	–	3,248	3,248
Operating profit before depreciation	2,872	776	732	4,380	3,248	7,628
Less: Depreciation	2,053	97	2	2,152	–	2,152
	819	679	730	2,228	3,248	5,476
Unallocated corporate expenses						(353)
Interest and finance charges (net)						(874)
Share of profit of non-controlled subsidiary						29
Profit for the year ended 31 December 2001						4,278
Assets						
Operational assets	64,415	1,207	10,417	76,039	301	76,340
Railway construction in progress	12,873	–	–	12,873	–	12,873
Railway assets under construction	3,024	–	–	3,024	–	3,024
Property development in progress	–	–	–	–	3,361	3,361
Properties held for sale	–	–	–	–	689	689
	80,312	1,207	10,417	91,936	4,351	96,287
Interest in non-controlled subsidiary						49
Unallocated assets						1,790
Total assets						98,126
Liabilities						
Segmented liabilities	3,773	164	359	4,296	141	4,437
Deferred income	–	–	–	–	8,411	8,411
	3,773	164	359	4,296	8,552	12,848
Unallocated liabilities						31,385
Total liabilities						44,233
Other Information						
Capital expenditure on:						
Operational assets and assets under construction	2,201	581	196			
Railway construction in progress	3,679					
Property development in progress					789	
Non-cash expenses other than depreciation	6	1	3			

No geographical analysis is shown as substantially all the principal activities of the Company and its subsidiaries are carried out in Hong Kong.

14 Fixed assets

The Group

in HK$ million	Investment properties	Leasehold land and buildings	Civil works	Plant and equipment	Assets under construction	Total
Cost or Valuation						
At 1 January 2002	10,363	1,603	36,191	43,423	3,024	94,604
Additions	16	–	–	62	1,928	2,006
Disposals / Write-offs	–	–	(3)	(122)	(91)	(216)
Deficit on revaluation (Note 33)	(112)	(115)	–	–	–	(227)
Reclassification	–	–	(13)	13	–	–
Tseung Kwan O Extension Project commissioned (Note 15)	–	150	8,374	7,279	–	15,803
Other assets commissioned	–	–	543	1,864	(2,407)	–
At 31 December 2002	10,267	1,638	45,092	52,519	2,454	111,970
At Cost	–	731	45,092	52,519	2,454	100,796
At 31 December 2002 Valuation	10,267	907	–	–	–	11,174
Aggregate depreciation						
At 1 January 2002	–	73	1,969	13,319	–	15,361
Charge for the year	–	34	357	2,079	–	2,470
Written back on disposal	–	–	(2)	(106)	–	(108)
Written back on revaluation (Note 33)	–	(23)	–	–	–	(23)
At 31 December 2002	–	84	2,324	15,292	–	17,700
Net book value at 31 December 2002	**10,267**	**1,554**	**42,768**	**37,227**	**2,454**	**94,270**
Net book value at 31 December 2001	10,363	1,530	34,222	30,104	3,024	79,243

14 Fixed assets (continued)

The Company

in HK$ million	Investment properties	Leasehold land and buildings	Civil works	Plant and equipment	Assets under construction	Total
Cost or Valuation						
At 1 January 2002	10,363	1,603	36,191	43,423	3,024	94,604
Additions	16	–	–	59	1,926	2,001
Disposals / Write-offs	–	–	(3)	(122)	(91)	(216)
Transfer to subsidiary	–	–	–	(609)	(2)	(611)
Deficit on revaluation (Note 33)	(112)	(115)	–	–	–	(227)
Reclassification	–	–	(13)	13	–	–
Tseung Kwan O Extension Project commissioned (Note 15)	–	150	8,374	7,279	–	15,803
Other assets commissioned	–	–	543	1,864	(2,407)	–
At 31 December 2002	10,267	1,638	45,092	51,907	2,450	111,354
At Cost	–	731	45,092	51,907	2,450	100,180
At 31 December 2002 Valuation	10,267	907	–	–	–	11,174
Aggregate depreciation						
At 1 January 2002	–	73	1,969	13,319	–	15,361
Charge for the year	–	34	357	2,020	–	2,411
Written back on disposal	–	–	(2)	(106)	–	(108)
Written back on transfer to subsidiary	–	–	–	(320)	–	(320)
Written back on revaluation (Note 33)	–	(23)	–	–	–	(23)
At 31 December 2002	–	84	2,324	14,913	–	17,321
Net book value at 31 December 2002	**10,267**	**1,554**	**42,768**	**36,994**	**2,450**	**94,033**
Net book value at 31 December 2001	10,363	1,530	34,222	30,104	3,024	79,243

A The remaining lease periods in respect of the investment properties and leasehold land and buildings held in Hong Kong are as follows:

The Group and The Company

	Investment properties		Leasehold land and buildings: Leasehold land for railway depots		Leasehold land and buildings: Office land and buildings	
in HK$ million	**2002**	2001	**2002**	2001	**2002**	2001
Net book value or valuation						
Over 50 years	**1,436**	1,522	**169**	172	**15**	16
10 to 50 years	**8,831**	8,841	**478**	336	**892**	1,006
	10,267	10,363	**647**	508	**907**	1,022

The Group has no investment properties with an unexpired lease term of 20 years or less.

14 Fixed assets (continued)

B The lease of the land on which the civil works, plant and equipment are situated for the operation of the railway was granted to the Company under a running line lease for the period up to 30 June 2047, which has been extended to 29 June 2050. It is assumed that the lease will be renewed and that the operation of the railway will continue after 2050.

Under the terms of the lease, the Company undertakes to keep and maintain all the leased areas, including underground and overhead structures, at its own cost. With respect to parts of the railway situated in structures where access is shared with other users, such as the Lantau Fixed Crossing, the Company's obligation for maintenance is limited to the railway only. All maintenance costs incurred under the terms of the lease have been dealt with as railway operating costs in the profit and loss account.

C All the investment properties of the Group were revalued at 31 December 2002 by DTZ Debenham Tie Leung, Chartered Surveyors, at open market value. The majority of the valuations are based on capitalisation of the net income receivable at an appropriate capitalisation rate, taking into account the reversionary income potential. The net revaluation deficit of HK$112 million *(2001: surplus of HK$17 million)* arising from the revaluation has been charged against the investment property revaluation reserve (note 33).

D All self-occupied office land and buildings were revalued at 31 December 2002 by DTZ Debenham Tie Leung, Chartered Surveyors, at open market value on an existing use basis. The net revaluation deficit of HK$92 million *(2001: deficit of HK$23 million)* arising from the revaluation has been transferred to the fixed asset revaluation reserve to offset against prior period revaluation surpluses (note 33).

The carrying amount of the self-occupied land and buildings at 31 December 2002 would have been HK$928 million *(2001: HK$949 million)* had the office land and buildings been stated at cost less accumulated depreciation.

E Fixed assets include the following assets held under agreements which are treated as finance leases:

The Group and The Company

in HK$ million	Cost **2002**	Aggregate depreciation **2002**	Net book value **2002**	Net book value 2001
Civil works				
– Eastern Harbour Crossing	**1,254**	**230**	**1,024**	1,043

The Company has entered into a Management Agreement (the "Agreement") with New Hong Kong Tunnel Company Limited to operate the Eastern Harbour Crossing until 2008. Included in the assets held under the Agreement are railway and ancillary works relating to the rail tunnel.

At the expiry of the Agreement, title to the assets will, pursuant to the Eastern Harbour Crossing Ordinance, be vested in the Government which has in turn entered into a Memorandum of Understanding dated 17 October 1986 with the Company to the effect that the assets will be vested in the Company on terms to be agreed between the Company and the Government. On 30 June 2000, the Company entered into a further agreement with the Government pursuant to which the relevant assets will be vested by the Government into the Company in 2008 for a nominal consideration and the Company agreed to indemnify the Government for certain amounts which are expected to be nominal. On this basis, the semi-annual payments made by the Company to New Hong Kong Tunnel Company Limited in respect of the Eastern Harbour Crossing are dealt with in these accounts as payments under a finance lease.

F The Group leases out investment properties and station kiosks under operating leases. The leases typically run for an initial period of one to six years, with an option to renew the lease after that date at which time all terms will be renegotiated. Lease payments are usually adjusted annually to reflect market rentals. Certain leases carry additional rental based on turnover.

The gross carrying amounts of investment properties of the Group and the Company held for use in operating leases were HK$10,267 million *(2001: HK$10,363 million)*. The gross carrying amounts of station kiosks held for use in operating leases were HK$314 million *(2001: HK$208 million)* and the related accumulated depreciation charges were HK$52 million *(2001: HK$45 million)*.

The Group's total future minimum lease payments under non-cancellable operating leases are receivable as follows:

The Group and The Company

in HK$ million	**2002**	2001
Within 1 year	**910**	842
After 1 year but within 5 years	**1,261**	1,408
Later than 5 years	**168**	226
	2,339	2,476

15 Railway construction in progress

The Group and The Company

in HK$ million	Balance at 1 Jan 2002	Transferred from deferred expenditure (Note 17)	Expenditure during the year	Capitalised on commissioning (Note 14)	Balance at 31 Dec 2002
Tseung Kwan O Extension Project					
Main contracts					
– Civil works	**5,866**	**–**	**804**	**(6,670)**	**–**
– Plant and equipment	**2,359**	**–**	**958**	**(3,317)**	**–**
– Works entrusted to Government	**378**	**–**	**85**	**(463)**	**–**
Associated construction costs					
– Site investigation	**74**	**–**	**3**	**(77)**	**–**
– Rental of work sites	**184**	**–**	**349**	**(533)**	**–**
Overheads					
– Consultancy fees	**801**	**–**	**36**	**(837)**	**–**
– Staff costs and general expenses	**1,742**	**–**	**312**	**(2,054)**	**–**
Finance costs	**1,429**	**–**	**423**	**(1,852)**	**–**
	12,833	**–**	**2,970**	**(15,803)**	**–**
Tseung Kwan O Extension Further Capital Works Project					
Construction costs	**1**	**–**	**–**	**–**	**1**
Consultancy fees	**22**	**–**	**1**	**–**	**23**
Staff costs and general expenses	**14**	**–**	**1**	**–**	**15**
Finance costs	**3**	**–**	**1**	**–**	**4**
	40	**–**	**3**	**–**	**43**
Penny's Bay Rail Link Project					
Construction costs	**–**	**9**	**130**	**–**	**139**
Consultancy fees	**–**	**18**	**17**	**–**	**35**
Staff costs and general expenses	**–**	**41**	**68**	**–**	**109**
Finance costs	**–**	**–**	**2**	**–**	**2**
	–	**68**	**217**	**–**	**285**
Government grant received (Note 39F)					**(219)**
					66
Total	**12,873**	**68**	**3,190**	**(15,803)**	**109**

16 Property development in progress and deferred income

Under the Airport Railway Agreement related to the construction of the Airport Railway, the Government had granted to the Company land on five station sites along the railway at full market value for property development. In preparing the sites for development, the Company incurs costs related to foundation and site enabling works and expects the costs to be reimbursed by property developers in the form of up-front cash payments when development packages are awarded. In accordance with the development agreements entered into with property developers, the developers are also responsible for the balance of the development costs.

Despite having entered into the development agreements with the developers, the Company being the grantee of the land remains primarily responsible for the fulfilment of all the conditions and obligations in the Land Grant. Such conditions and obligations include the type and quantity of the developments that must be built, public facilities to be provided, and the completion date of the project.

Costs of foundation and site enabling works incurred by the Company are capitalised as property development in progress and payments received from developers are credited to property development in progress to offset costs incurred in respect of the same development. In cases where payments received from developers exceed the related expenditure incurred by the Company, such excess is recorded as deferred income (note 16B). In these cases, any subsequent expenditure incurred by the Company in respect of that development will be charged against deferred income. It is expected that the majority of deferred income will be recognised as profits of the Company at the appropriate time after charging any remaining costs related to foundation and site enabling works, and after taking into account the outstanding risks and obligations retained by the Company relating to each development. Until such time as deferred income is recognised as profit, it is recorded as a liability of the Company in recognition of the Company's obligations under the Land Grant.

The TKE Project Agreement entered into between the then Secretary for Transport, for and on behalf of the Government, and the Company in respect of the construction of the Tseung Kwan O Extension provides the Company with the right to undertake property developments at four station and depot sites along the Tseung Kwan O Line ("Tseung Kwan O Extension Property Projects"). The basis of accounting for development costs incurred by the Company and payments received by the Company related thereto is consistent with that for the property developments along the Airport Railway ("Airport Railway Property Projects").

A Property development in progress

The Group and The Company

in HK$ million	Balance at 1 Jan	Expenditure	Offset against payments received from developers (Note 16B)	Balance at 31 Dec
2002				
Airport Railway Property Projects	**583**	**76**	**(62)**	**597**
Tseung Kwan O Extension and other property projects	**2,778**	**280**	**(785)**	**2,273**
	3,361	**356**	**(847)**	**2,870**
2001				
Airport Railway Property Projects	634	51	(102)	583
Tseung Kwan O Extension and other property projects	2,065	738	(25)	2,778
	2,699	789	(127)	3,361

16 Property development in progress and deferred Income (continued)

B Deferred income

The Group and The Company

in HK$ million	Balance at 1 Jan	Payments received from developers	Offset against property development in progress (Note 16A)	Amount recognised as profit (Note 6)	Balance at 31 Dec
2002					
Airport Railway Property Projects	**8,401**	**425**	**(62)**	**(2,548)**	**6,216**
Tseung Kwan O Extension Property Projects	**10**	**785**	**(785)**	**–**	**10**
	8,411	**1,210**	**(847)**	**(2,548)**	**6,226**
2001					
Airport Railway Property Projects	10,388	225	(102)	(2,110)	8,401
Tseung Kwan O Extension Property Projects	15	20	(25)	–	10
	10,403	245	(127)	(2,110)	8,411

C Stakeholding funds

As stakeholder under certain Airport Railway Property Projects, the Company receives and manages deposit monies and sales proceeds in respect of sales of properties under those developments. These monies are placed in separate designated bank accounts and, together with any interest earned, will be released to the developers for the reimbursement of costs of the respective developments in accordance with the terms and conditions of the Government Consent Schemes and development agreements. Accordingly, the balances of the stakeholding funds and the corresponding bank balances have not been included in the Group's and the Company's balance sheets. Movements in stakeholding funds during the year were as follows:

The Group and The Company

in HK$ million	**2002**	2001
Balance as at 1 January	**5,686**	4,011
Stakeholding funds received and receivable	**8,399**	11,482
Add: Interest earned thereon	**65**	137
	14,150	15,630
Disbursements during the year	**(10,919)**	(9,944)
Balance as at 31 December	**3,231**	5,686
Represented by :		
Balances in designated bank accounts as at 31 December	**3,229**	5,684
Retention receivable	**2**	2
	3,231	5,686

17 Deferred expenditure

The Group and The Company

in HK$ million	Balance at 1 Jan	Transfer to railway construction in progress (Note 15)	Premium on bond issue	Expenditure/ (Amortisation) during the year	Amount written off to profit and loss account (Note 4C)	Balance at 31 Dec
2002						
Deferred finance charges	**133**	**–**	**(53)**	**(8)**	**–**	**72**
Expenditure on proposed capital projects						
– Penny's Bay Rail Link	**68**	**(68)**	**–**	**–**	**–**	**–**
– North Island Link	**77**	**–**	**–**	**8**	**(85)**	**–**
– Shatin Central Link	**42**	**–**	**–**	**–**	**(42)**	**–**
– Tung Chung Cable Car Project	**6**	**–**	**–**	**11**	**–**	**17**
– West Island Link	**–**	**–**	**–**	**16**	**–**	**16**
– Interchange – Shatin Central Line	**–**	**–**	**–**	**1**	**–**	**1**
	326	**(68)**	**(53)**	**28**	**(127)**	**106**
2001						
Deferred finance charges	149	–	–	(16)	–	133
Expenditure on proposed capital projects						
– Penny's Bay Rail Link	21	–	–	47	–	68
– North Island Link	17	–	–	60	–	77
– Shatin Central Link	–	–	–	42	–	42
– Tung Chung Cable Car Project	–	–	–	6	–	6
	187	–	–	139	–	326

Deferred expenditures relating to the Penny's Bay Rail Link were transferred to Railway Construction in Progress upon signing of the Penny's Bay Rail Link Project Agreement with the Government during the year.

Expenditures incurred in respect of the Shatin Central Link and the North Island Link were written off to the profit and loss account following an unsuccessful bid for the construction and operation of the Shatin Central Link, and Government's decision to defer the completion of the North Island Link to beyond 2016.

18 Interest in non-controlled subsidiary

The Group and the Company had the following interest in a non-controlled subsidiary at 31 December 2002:

	The Group		The Company	
in HK$ million	**2002**	2001	**2002**	2001
Unlisted shares, *at cost*	**–**	–	**24**	24
Share of net assets	**88**	49	**–**	–
	88	49	**24**	24

Name of company	Issued and paid up ordinary share capital	Interest in equity shares held by the Company	Place of incorporation	Principal activities
Octopus Cards Limited	HK$42,000,000	57.4%	Hong Kong	Development and operation of smart card system

In June 1994, the Company entered into an agreement with four local transport companies, Kowloon-Canton Railway Corporation, The Kowloon Motor Bus Company (1933) Limited, Citybus Limited and The Hongkong and Yaumati Ferry Co., Limited, to incorporate a company, Creative Star Limited, now Octopus Cards Limited ("OCL"), to undertake the development and operation of the "Octopus" contactless smart card ticketing system, which was initially used by the shareholding transport companies. Although the Company holds a majority interest in the issued shares of OCL, its appointees to the Board of Directors of OCL are limited to 49% of the voting rights at board meetings. The shareholders have agreed to provide the necessary funding to OCL for its operations and for the development of the "Octopus" system.

On 20 April 2000, OCL received approval from The Hong Kong Monetary Authority to become a deposit-taking company ("DTC") for purposes of extending the use of Octopus cards to a wider range of services, including those that are non-transport related. Prior to becoming a DTC, the Octopus card was exempted from the definition of "multi-purpose card" under the Banking Ordinance (Chapter 155 of the Laws of Hong Kong) on the basis that its use was restricted to transport related services only. In connection with the application, the Company and the other shareholders of OCL injected HK$28 million and HK$42 million in the form of subordinated loan and share capital respectively into OCL on 18 April 2000 in order to fulfill the capital requirements pursuant to the Banking Ordinance. The contributions were made in proportion to each shareholder's interest in the shares of OCL.

On 17 January 2001, the Company entered into a new Shareholders' Agreement with the other shareholders of OCL. Under this agreement, the Company disposed of a shareholding interest of 10.4% in OCL to certain other shareholders of OCL for a consideration of HK$16 million, together with a deferred consideration to be received in the event of OCL subsequently becoming a stock exchange listed company. On 17 October 2001, OCL repaid half, or HK$9.5 million of the Company's subordinated loans granted to OCL in connection with the above mentioned application to become a DTC. In January 2002, OCL repaid the remaining balance of the Company's subordinated loans.

During the year ended 31 December 2002, a total amount of HK$45 million *(2001: HK$44 million)* was paid by the Company to OCL in respect of the central clearing services provided by OCL to the Company. During the same period, load agent fees amounting to HK$11 million *(2001: HK$12 million)* were received from OCL in respect of services and facilities provided by the Company at various MTR stations to enable customers to add value to the Octopus cards.

In addition, services fees amounting to HK$2 million *(2001: HK$2 million)* were received from OCL in respect of rental of computer equipment and services and warehouse storage space payable to the Company under a service agreement.

18 Interest in non-controlled subsidiary (continued)

The condensed profit and loss account and the balance sheet for OCL are shown below:

Profit and loss account

Year ended 31 December *in HK$ million*	**2002 (Audited)**	2001 (Audited and restated)
Turnover	**175**	152
Other operating income	**53**	42
	228	194
Staff costs	**(53)**	(51)
Load agent fees	**(21)**	(21)
Other expenses	**(55)**	(46)
Operating profit before depreciation	**99**	76
Depreciation	**(61)**	(55)
Operating profit before interest and finance charges	**38**	21
Net interest income	**30**	29
Profit before taxation	**68**	50
Taxation	**–**	–
Profit for the year	**68**	50
Group's share of profit	**39**	29

Balance sheet

At 31 December *in HK$ million*	**2002 (Audited)**	2001 (Audited and restated)
Assets		
Fixed assets	**306**	333
Investments	**590**	452
Cash at banks and in hand	**236**	183
Other assets	**67**	79
	1,199	1,047
Liabilities		
Card floats and card deposits due to cardholders	**(996)**	(899)
Amounts due to shareholders	**(18)**	(19)
Other liabilities	**(31)**	(29)
Shareholders' loans	**–**	(14)
	(1,045)	(961)
Net assets	**154**	86
Shareholders' funds		
Share capital	**42**	42
Retained profits	**112**	44
	154	86
Group's share of net assets	**88**	49

19 Investments in subsidiaries

The Company

in HK$ million	**2002**	2001
Unlisted shares, *at cost*	**166**	52
Less: Impairment losses	**3**	3
	163	49

Details of subsidiaries as at 31 December 2002, other than the non-controlled subsidiary the relevant details of which are disclosed in note 18, are as follows:

		Proportion of ownership interest				
Name of company	Issued and paid up ordinary/registered share capital	Group's effective interest	Held by the Company	Held by subsidiary	Place of incorporation and operation	Principal activities
Fasttrack Insurance Ltd.	HK$77,500,000	100%	100%	–	Bermuda	Insurance underwriting
MTR Corporation (C.I.) Limited	US$1,000	100%	100%	–	Cayman Islands	Finance
MTR Engineering Services Limited	HK$1,000	100%	100%	–	Hong Kong	Engineering services
MTR Property Agency Co. Limited	HK$2	100%	100%	–	Hong Kong	Property agency
MTR Travel Limited	HK$2,500,000	100%	100%	–	Hong Kong	Travel services
MTR Consultancy (Shenzhen) Limited	HK$1,000,000	100%	100%	–	The People's Republic of China (Incorporated)	Railway consultancy services
MTR Corporation (Singapore) Pte. Ltd.	S$50,000	100%	100%	–	Singapore	Railway consultancy services
MTR (Shanghai Consultancy) Company Limited	HK$1,000	100%	100%	–	Hong Kong	Railway consultancy services
MTR (Shanghai Metro Management) Limited	HK$1,000	100%	100%	–	Hong Kong	Project management services
MTR (Shanghai Project Management) Limited	HK$1,000	100%	100%	–	Hong Kong	Railway consultancy services
Shanghai Hong Kong Metro Construction Management Co. Ltd.	HK$15,000,000	60%	–	60%	The People's Republic of China (Incorporated)	Railway construction management
MTR China Property Limited	HK$1,000	100%	100%	–	Hong Kong	Property management
Shenzhen Donghai Anbo Property Management Co. Ltd.	RMB3,000,000	51%	–	51%	The People's Republic of China (Incorporated)	Property management
MTR Telecommunication Company Limited	HK$100,000,000	100%	100%	–	Hong Kong	Radio communication services
TraxComm Limited	HK$1,000	100%	100%	–	Hong Kong	Fixed telecommunication network services
Hong Kong Cable Car Limited	HK$1,000	100%	100%	–	Hong Kong	Dormant
Lantau Cable Car Limited	HK$1,000	100%	100%	–	Hong Kong	Dormant
MTR (Estates Management) Limited	HK$1,000	100%	100%	–	Hong Kong	Dormant

19 Investments in subsidiaries (continued)

No dividend has been paid or is payable to the Company by the subsidiaries for the year up to 31 December 2002.

In May 2002 and June 2002, the Group acquired 51% and 60% interests in Shenzhen Donghai Anbo Property Management Co. Ltd. and Shanghai Hong Kong Metro Construction Management Co. Ltd. for HK$1 million and HK$9 million respectively, satisfied in cash. As a result, the Group's profit for the year and the net assets as at the year end have both been increased by HK$0.2 million.

20 Staff housing loans

The Group and The Company

in HK$ million	Balance at 1 Jan	New loans drawndown	Redemption	Repayment	Reduction in provision	Balance at 31 Dec
2002						
Housing loans receivable	**128**	**–**	**(34)**	**(10)**	**–**	**84**
Less: General provision	**1**	**–**	**–**	**–**	**(1)**	**–**
	127	**–**	**(34)**	**(10)**	**1**	**84**
2001						
Housing loans receivable	638	3	(487)	(26)	–	128
Less: General provision	3	–	–	–	(2)	1
	635	3	(487)	(26)	2	127

The Group and The Company

in HK$ million	**2002**	2001
Amount receivable:		
– within 1 year	**9**	12
– after 1 year	**75**	115
	84	127

The MTR Staff Housing Loan Scheme, a Company financed scheme, was introduced in 1997 to replace, on a phased basis, the previous arrangements whereby interest subsidies were paid by the Company to eligible employees. All housing loans granted to employees carry interest either at the prevailing Best Lending Rate less 1.75% per annum or at the Company's Average Cost of Borrowings plus 0.75% per annum, and are secured by mortgage over the relevant properties.

21 Properties held for sale

The Group and The Company

in HK$ million	**2002**	2001
Properties held for sale		
– at cost	**271**	689
– at net realisable value	**523**	–
	794	689

The properties held for sale at 31 December 2001 and 2002 comprised residential units, retail and car parking spaces at the Olympic Station and Kowloon Station developments. They are properties received by the Company, either as property sharing in kind or as part of the profit distribution upon completion of the development (note 6). The properties are stated in the balance sheet at the lower of cost, which is deemed to be their net realisable value upon recognition (note 1J(vii)), or their net realisable value at the balance sheet date. Net realisable value represents the estimated selling price less costs to be incurred in selling the properties. The net realisable values as at 31 December 2001 and 2002 are determined by reference to an open market valuation of the properties as at those dates, undertaken by DTZ Debenham Tie Leung, Chartered Surveyors.

Properties held for sale at net realisable value are stated net of general provision, made in order to state these properties at the lower of their cost and estimated net realisable value. The amount of write-down of properties to estimated net realisable value recognised in the consolidated profit and loss account is HK$44 million *(2001: Nil)*.

22 Stores and spares

The Group and The Company

in HK$ million	**2002**	2001
Stores and spares expected to be consumed:		
– within 1 year	**138**	138
– after 1 year	**127**	130
	265	268
Less: Specific provision for obsolete stock	**6**	7
	259	261

Stores and spares expected to be consumed after 1 year comprise mainly contingency spares and stocks kept to meet cyclical maintenance requirements.

23 Debtors, deposits and payments in advance

	The Group		**The Company**	
in HK$ million	**2002**	2001	**2002**	2001
Debtors (net of specific allowances for bad and doubtful debts), deposits and payments in advance relate to:				
– Tseung Kwan O Extension Project	**1**	21	**1**	21
– Railway operations and other projects	**726**	809	**717**	816
	727	830	**718**	837

The Group's credit policy in respect of receivables arising from its principal activities are as follows:

(i) Rentals, advertising and telecommunications fees are billed monthly with due dates ranging from 7 to 50 days. Tenants of the Group's investment properties and station kiosks are required to pay three months' rental deposit upon the signing of lease agreements.

(ii) Amounts receivable under interest rate and currency swap agreements with financial institutions are due in accordance with the respective terms of the agreements.

(iii) Debtors in relation to capital works entrusted to the Group, subject to any agreed retentions, are due within 21 days upon the certification of work in progress.

Fare revenue is collected either in cash for single and two-ride tickets or through Octopus Cards with daily settlement.

The ageing analysis of debtors included above is as follows:

	The Group		**The Company**	
in HK$ million	**2002**	2001	**2002**	2001
Amount not yet due	**548**	698	**546**	697
Overdue by 30 days	**82**	65	**80**	65
Overdue by 60 days	**10**	9	**10**	9
Overdue by 90 days	**4**	3	**4**	3
Overdue by more than 90 days	**13**	16	**12**	16
Total debtors	**657**	791	**652**	790
Deposits and payments in advance	**70**	39	**66**	47
	727	830	**718**	837

As at 31 December 2002, all debtors, deposits and payments in advance were expected to be recovered within one year except for HK$25 million *(2001: HK$21 million)* included in the amounts relating to railway operations and other projects, which were expected to be recovered after one year.

Included in amount not yet due are HK$70 million *(2001: Nil)* receivable from property purchasers, which are due for payment in accordance with the terms of individual agreements on sales and purchases.

24 Amounts due from the Government and other related parties

	The Group		The Company	
in HK$ million	**2002**	2001	**2002**	2001
Amounts due from:				
– the Government	**57**	78	**57**	78
– the Housing Authority	**30**	65	**30**	65
– the Kowloon-Canton Railway Corporation ("KCRC")	**8**	3	**8**	3
– non-controlled subsidiary	**–**	6	**–**	6
– other subsidiaries of the Company (net of provision for losses)	**–**	–	**198**	30
	95	152	**293**	182

The amount due from the Government relates to outstanding receivable and retention, as well as provision for contract claims recoverable from the Government, in connection with infrastructure works entrusted to the Company.

The amount due from the Housing Authority relates to site formation works entrusted to the Company by the Housing Authority in respect of the Tseung Kwan O Extension Project. The entrustment arrangement enabled early possession of a site by the Group to facilitate railway construction.

The amount due from KCRC relates to works entrusted to the Company in connection with the provision of interchange stations between the MTR and KCRC systems.

As at 31 December 2002, the contract retentions on the above entrusted works due for release after one year were HK$7 million *(2001: HK$16 million)*. All other amounts due from the Government and other related parties were expected to be received within 12 months.

25 Cash and cash equivalents

	The Group		The Company	
in HK$ million	**2002**	2001	**2002**	2001
Deposits with banks and other financial institutions	**1,651**	180	**1,524**	78
Cash at banks and in hand	**67**	35	**39**	34
Cash and cash equivalents in the balance sheet	**1,718**	215	**1,563**	112
Bank overdrafts (Note 26B)	**(34)**	(49)	**(34)**	(49)
Cash and cash equivalents in the cash flow statement	**1,684**	166	**1,529**	63

26 Loans and obligations under finance leases

A By type

The Group

in HK$ million	Balance at year end closing rate **2002**	Exchange (gain)/loss on related forward exchange contracts **2002**	Balance **2002**	Balance 2001
Capital market instruments				
Listed or publicly traded:				
US dollar Yankee notes due 2005	**2,340**	**(16)**	**2,324**	2,324
US dollar Global notes due 2009	**5,850**	**(15)**	**5,835**	5,834
US dollar Global notes due 2010	**4,680**	**(1)**	**4,679**	4,679
Debt issuance programme notes due 2005	**195**	**–**	**195**	195
	13,065	**(32)**	**13,033**	13,032
Unlisted:				
Debt issuance programme notes due 2003 to 2018	**7,538**	**(4)**	**7,534**	7,534
HK dollar note issuance programme notes due 2003	**500**	**–**	**500**	500
HK dollar notes due 2004 to 2008	**2,350**	**–**	**2,350**	2,350
HK dollar retail bonds due 2004 to 2006	**3,500**	**–**	**3,500**	–
	13,888	**(4)**	**13,884**	10,384
Total capital market instruments	**26,953**	**(36)**	**26,917**	23,416
Bank loans and overdrafts	**5,969**	**14**	**5,983**	7,219
	32,922	**(22)**	**32,900**	30,635
Obligations under finance leases (Note 26C)	**608**	**–**	**608**	750
Total	**33,530**	**(22)**	**33,508**	31,385

The Company

in HK$ million	Balance at year end closing rate **2002**	Exchange (gain)/loss on related forward exchange contracts **2002**	Balance **2002**	Balance 2001
Capital market instruments				
Listed or publicly traded:				
US dollar Yankee notes due 2005	**2,340**	**(16)**	**2,324**	2,324
US dollar Global notes due 2009	**5,850**	**(15)**	**5,835**	5,834
US dollar Global notes due 2010	**4,680**	**(1)**	**4,679**	4,679
Debt issuance programme notes due 2005	**195**	**–**	**195**	195
	13,065	**(32)**	**13,033**	13,032
Unlisted:				
Debt issuance programme notes due 2003 to 2018	**4,888**	**(4)**	**4,884**	4,884
HK dollar note issuance programme notes due 2003	**500**	**–**	**500**	500
	5,388	**(4)**	**5,384**	5,384
Total capital market instruments	**18,453**	**(36)**	**18,417**	18,416
Bank loans and overdrafts	**5,969**	**14**	**5,983**	7,219
	24,422	**(22)**	**24,400**	25,635
Obligations under finance leases (Note 26C)	**608**	**–**	**608**	750
Total	**25,030**	**(22)**	**25,008**	26,385

26 Loans and obligations under finance leases (continued)

As at 31 December 2002, the Group had available undrawn committed bank loan facilities amounting to HK$6,000 million *(2001: HK$5,495 million)*. In addition, the Group had a number of uncommitted facilities with undrawn amounts totalling HK$11,943 million *(2001: HK$11,841 million)*, comprising a multi-currency debt issuance programme and short-term bank loan facilities.

B By repayment terms

The Group

in HK$ million	Capital market instruments **2002**	Bank loans and overdrafts **2002**	Obligations under finance leases **2002**	Total **2002**	Total 2001
Long-term loans and obligations under finance leases					
Amounts repayable beyond 5 years	**11,482**	**255**	**–**	**11,737**	12,396
Amounts repayable within a period of between 2 and 5 years	**6,769**	**1,218**	**393**	**8,380**	13,614
Amounts repayable within a period between 1 and 2 years	**4,415**	**4,073**	**112**	**8,600**	4,772
Amounts repayable within 1 year	**4,251**	**403**	**103**	**4,757**	160
	26,917	**5,949**	**608**	**33,474**	30,942
Bank overdrafts	**–**	**34**	**–**	**34**	49
Short-term loans	**–**	**–**	**–**	**–**	394
	26,917	**5,983**	**608**	**33,508**	31,385

The Company

in HK$ million	Capital market instruments **2002**	Bank loans and overdrafts **2002**	Obligations under finance leases **2002**	Total **2002**	Total 2001
Long-term loans and obligations under finance leases					
Amounts repayable beyond 5 years	**10,982**	**255**	**–**	**11,237**	11,896
Amounts repayable within a period of between 2 and 5 years	**2,719**	**1,218**	**393**	**4,330**	9,614
Amounts repayable within a period between 1 and 2 years	**965**	**4,073**	**112**	**5,150**	4,272
Amounts repayable within 1 year	**3,751**	**403**	**103**	**4,257**	160
	18,417	**5,949**	**608**	**24,974**	25,942
Bank overdrafts	**–**	**34**	**–**	**34**	49
Short-term loans	**–**	**–**	**–**	**–**	394
	18,417	**5,983**	**608**	**25,008**	26,385

The amounts repayable within 1 year in respect of long-term loans and obligations under finance leases are included in long-term loans as these amounts are intended to be refinanced on a long-term basis.

26 Loans and obligations under finance leases (continued)

C Obligations under finance leases

As at 31 December 2002, the Group and the Company had obligations under finance leases repayable as follows:

The Group and The Company

in HK$ million	Present value of the minimum lease payments **2002**	Interest expense relating to future periods **2002**	Total minimum lease payments **2002**	Present value of the minimum lease payments 2001	Interest expense relating to future periods 2001	Total minimum lease payments 2001
Amounts repayable beyond 5 years	**–**	**–**	**–**	141	9	150
Amounts repayable within a period of between 2 and 5 years	**393**	**57**	**450**	364	86	450
Amounts repayable within a period of between 1 and 2 years	**112**	**38**	**150**	103	47	150
Amounts repayable within 1 year	**103**	**47**	**150**	142	58	200
	608	**142**	**750**	750	200	950

Obligations under finance lease are the Group's and the Company's commitments to make future payments to New Hong Kong Tunnel Company Limited under the management agreement for the Eastern Harbour Crossing which is treated as a finance lease (note 14E).

D Bonds and notes issued and redeemed

Bonds and notes issued during the year ended 31 December 2001 and 2002 comprise:

The Group

	2002		2001	
in HK$ million	Principal amount	Net consideration received	Principal amount	Net consideration received
Debt issuance programme notes	**–**	**–**	2,650	2,648
HK dollar retail bonds	**3,500**	**3,553**	–	–
HK dollar notes	**–**	**–**	2,350	2,347
	3,500	**3,553**	5,000	4,995

All the above bonds and notes were issued by a subsidiary, MTR Corporation (C.I.) Limited. The bonds and notes issued are unconditionally and irrevocably guaranteed by the Company; and are direct, unsecured, unconditional and unsubordinated to other unsecured and unsubordinated obligations of MTR Corporation (C.I.) Limited. The obligations of the Company under the guarantee are direct, unsecured, unconditional, and unsubordinated to other unsecured and unsubordinated obligations of the Company. The net proceeds received from the issues were on lent to the Company for general working capital, refinancing or other corporate purposes.

None of the Group's issued debt securities was redeemed during the year ended 31 December 2002.

26 Loans and obligations under finance leases (continued)

E Guarantees

There were no guarantees given by the Government in respect of loan facilities as at 31 December 2002 and 2001.

F Interest rates

The total borrowings, excluding obligations under finance leases, of HK$32,900 million *(2001: HK$30,635 million)* comprise:

The Group

	2002		2001	
	Loan amount HK$ million	Interest rate % p.a.	Loan amount HK$ million	Interest rate % p.a.
Fixed rate loans and loans swapped to fixed rates	**20,325**	**4.3 – 8.4**	15,901	4.5 – 8.4
Variable rate loans and loans swapped from fixed rate	**12,575**	**(Note)**	14,734	(Note)
	32,900		30,635	

The Company

	2002		2001	
	Loan amount HK$ million	Interest rate % p.a.	Loan amount HK$ million	Interest rate % p.a.
Fixed rate loans and loans swapped to fixed rates	**12,075**	**4.3 – 8.4**	11,151	4.5 – 8.4
Variable rate loans and loans swapped from fixed rate	**12,325**	**(Note)**	14,484	(Note)
	24,400		25,635	

Note: Interest rates are determined by reference to either the Hong Kong prime rate, the Hong Kong Interbank Offered Rate or the London Interbank Offered Rate.

27 Off-balance sheet financial instruments

The Group has employed off-balance sheet derivative instruments such as interest rate swaps and currency swaps to manage its interest rate and foreign exchange exposure. These instruments are used solely to reduce or eliminate the financial risk associated with the Group's liabilities and not for trading or speculation purposes.

The contracted notional amounts of derivative instruments outstanding by maturity and type at 31 December 2002 are as follows:

The Group and The Company

	2002				2001
	Maturing in				
Notional amount *in HK$ million*	Less than 2 years	2-5 years	Over 5 years	Total	Total
Foreign exchange forwards	**311**	**184**	**–**	**495**	534
Cross currency and interest rate swaps	**3,892**	**2,775**	**6,847**	**13,514**	8,288
Interest rate swaps and options	**14,750**	**6,100**	**2,060**	**22,910**	10,910
	18,953	**9,059**	**8,907**	**36,919**	19,732

27 Off-balance sheet financial instruments (continued)

There are four main categories of risk related to using derivative instruments, namely market risk, credit risk, operational risk and legal risk. Since the Group employs derivative instruments purely for hedging purposes, it is not exposed to market risk because any change in market values will be offset by an opposite change in the market values of the underlying liabilities being hedged.

The Group manages credit risk by assigning limits to counter-parties and by dealing only with financial institutions with acceptable credit ratings. The Group further monitors its credit exposure by estimating the fair market values plus any potential adverse movement in the values of the derivative instruments employed. The Group has not experienced non-performance by any counter-party.

The Group has internal control measures to safeguard compliance with policies and procedures to minimise operational risk. Standardised or master agreements are used whenever practicable to reduce legal risk and credit exposure.

28 Creditors, accrued charges and provisions

	The Group		The Company	
in HK$ million	**2002**	2001 (Note 42A)	**2002**	2001 (Note 42A)
Creditors, accrued charges and provisions				
– Airport Railway Project	**282**	335	**282**	335
– Tseung Kwan O Extension Project	**814**	479	**814**	479
– Property Projects	**281**	75	**281**	75
– Railway operations and other projects	**2,383**	2,271	**2,305**	2,235
	3,760	3,160	**3,682**	3,124

The above amounts are mainly related to capital projects which are settled upon certification of work in progress and swap interest payable. The Group has no significant balances of trade creditors resulting from its provision of transportation services.

The analysis of creditors included above by due dates is as follows:

	The Group		The Company	
in HK$ million	**2002**	2001 (Note 42A)	**2002**	2001 (Note 42A)
Due within 30 days or on demand	**547**	595	**531**	578
Due after 30 days but within 60 days	**667**	1,106	**654**	1,092
Due after 60 days but within 90 days	**50**	44	**47**	43
Due after 90 days	**2,043**	971	**2,006**	967
	3,307	2,716	**3,238**	2,680
Rental and other refundable deposits	**295**	290	**286**	290
Accrued employee benefits	**158**	154	**158**	154
Total	**3,760**	3,160	**3,682**	3,124

Creditors, accrued charges and provisions in respect of the Airport Railway and Tseung Kwan O Extension projects include provisions for claims on completed contracts, which were capitalised as part of the railway assets upon commissioning of the Tung Chung and Airport Express Lines in 1998 and the Tseung Kwan O Line in August 2002. Most of the claims relating to the Tung Chung and Airport Express Lines have been resolved and claims in respect of the newly commissioned Tseung Kwan O Line are being assessed and resolved as part of the normal process of managing a major construction project. It is anticipated that, subject to unforeseen circumstances, the remaining amount required to be paid will be sufficiently covered by the above mentioned provisions of the respective projects.

As at 31 December 2002, all creditors, accrued charges and provisions were expected to be settled within one year except for HK$382 million *(2001: HK$460 million)* included in the amounts relating to railway operations and other projects, which were expected to be settled after one year. The amounts due after one year are mainly rental deposits received from shop and station kiosk tenants and advance income received from telecommunication services operators.

29 Contract retentions

The Group and The Company

in HK$ million	Due for release after 12 months	Due for release within 12 months	Total
2002			
Tseung Kwan O Extension Project	**–**	**237**	**237**
Property Projects	**–**	**31**	**31**
Railway operations and other projects	**62**	**166**	**228**
	62	**434**	**496**
2001			
Tseung Kwan O Extension Project	201	225	426
Property Projects	32	34	66
Railway operations and other projects	142	164	306
	375	423	798

30 Amounts due to the Government and other related parties

The following are amounts due to the Government and Airport Authority in respect of works entrusted to them by the Group and the amounts due to the subsidiaries:

	The Group		The Company	
in HK$ million	**2002**	2001	**2002**	2001
Amounts due to:				
– the Government	**129**	282	**129**	282
– the Airport Authority	**76**	119	**76**	119
– non-controlled subsidiary	**4**	–	**4**	–
– the Company's subsidiaries	**–**	–	**8,590**	5,031
	209	401	**8,799**	5,432

As at 31 December 2002, all amounts *(2001: HK$401 million)* due to the Government and Airport Authority and HK$90 million *(2001: HK$31 million)* due to the subsidiaries are expected to be settled within one year.

31 Deferred liabilities

The Group and The Company

in HK$ million	**2002**	2001
Estate management funds		
– Refundable deposits on managed properties	**31**	31
– Building maintenance and asset replacement reserve funds	**54**	47
	85	78

32 Share capital, share premium and capital reserve

in HK$ million	**2002**	2001
Authorised:		
6,500,000,000 shares of HK$1.00 each	**6,500**	6,500
Issued and fully paid:		
5,158,748,655 shares *(2001: 5,055,229,742 shares)* of HK$1.00 each	**5,159**	5,055
Share premium	**1,563**	564
Capital reserve	**27,188**	27,188
	33,910	32,807

Pursuant to the Articles of Association of the Company, the capital reserve can only be applied in paying up in full unissued shares to be allotted and distributed as fully paid bonus shares to the shareholders of the Company.

Share premium represents the amount by which the issue price of shares exceeds the par value of those shares. The application of the share premium account is governed by section 48B of the Hong Kong Companies Ordinance.

New shares issued and fully paid up during the year comprise:

			Proceeds credited to		
	Number of shares	Option/ scrip price HK$	Share capital account HK$ million	Share premium account HK$ million	Total HK$ million
Employee share options exercised	4,362,000	8.44	4	33	37
Issued as 2001 final scrip dividends	63,322,970	11.17	64	644	708
Issued as 2002 interim scrip dividends	35,833,943	9.99	36	322	358
	103,518,913		104	999	1,103

Outstanding share options under the Pre-Global Offering Share Option Scheme as at 31 December 2002 are disclosed in note 41A.

33 Other reserves

The Group

in HK$ million	Investment property revaluation reserve	Fixed asset revaluation reserve	Retained profits	Total
2002				
Balance as at 1 January 2002 as previously reported	**6,518**	**116**	**14,608**	**21,242**
Prior period adjustments in respect of annual leave and passage expenses (Note 42A)	**–**	**–**	**(156)**	**(156)**
	6,518	**116**	**14,452**	**21,086**
Prior period adjustments in respect of pension expenses (Note 42A)	**–**	**–**	**(45)**	**(45)**
Balance as at 1 January 2002 as restated	**6,518**	**116**	**14,407**	**21,041**
Dividends paid	**–**	**–**	**(2,132)**	**(2,132)**
Deficits on revaluation	**(112)**	**(92)**	**–**	**(204)**
Profit for the year	**–**	**–**	**4,212**	**4,212**
Balance as at 31 December 2002	**6,406**	**24**	**16,487**	**22,917**
2001				
Balance as at 1 January 2001 as previously reported	6,501	139	11,527	18,167
Prior period adjustments in respect of annual leave and passage expenses (Note 42A)	–	–	(150)	(150)
Balance as at 1 January 2001 as restated	6,501	139	11,377	18,017
Dividends paid	–	–	(1,203)	(1,203)
Surplus/(Deficit) on revaluation	17	(23)	–	(6)
Profit for the year (as restated)	–	–	4,278	4,278
Balance as at 31 December 2001	6,518	116	14,452	21,086

33 Other reserves (continued)

The Company

in HK$ million	Investment property revaluation reserve	Fixed asset revaluation reserve	Retained profits	Total
2002				
Balance as at 1 January 2002 as previously reported	**6,518**	**116**	**14,545**	**21,179**
Prior period adjustments in respect of annual leave and passage expenses (Note 42A)	**–**	**–**	**(154)**	**(154)**
	6,518	**116**	**14,391**	**21,025**
Prior period adjustments in respect of pension expenses (Note 42A)	**–**	**–**	**(45)**	**(45)**
Balance as at 1 January 2002 as restated	**6,518**	**116**	**14,346**	**20,980**
Dividends paid	**–**	**–**	**(2,132)**	**(2,132)**
Deficits on revaluation	**(112)**	**(92)**	**–**	**(204)**
Profit for the year	**–**	**–**	**4,142**	**4,142**
Balance as at 31 December 2002	**6,406**	**24**	**16,356**	**22,786**
2001				
Balance as at 1 January 2001 as previously reported	6,501	139	11,500	18,140
Prior period adjustments in respect of annual leave and passage expenses (Note 42A)	–	–	(148)	(148)
Balance as at 1 January 2001 as restated	6,501	139	11,352	17,992
Dividends paid	–	–	(1,203)	(1,203)
Surplus/(Deficit) on revaluation	17	(23)	–	(6)
Profit for the year (as restated)	–	–	4,242	4,242
Balance as at 31 December 2001	6,518	116	14,391	21,025

The investment property and fixed asset revaluation reserves were set up to deal with the gains or losses arising from the revaluation of investment properties and self-occupied office land and buildings respectively (note 1F).

The investment property and fixed asset revaluation reserves are not available for distribution to shareholders because they do not constitute realised profits. As at 31 December 2002, the total amount of reserves available for distribution to shareholders under the Hong Kong Companies Ordinance amounted to HK$16,356 million *(2001: HK$14,391 million, as restated)*.

Included in the Group's retained profits as at 31 December 2002 is an amount of HK$64 million *(2001: HK$25 million)*, being the retained profits attributable to the non-controlled subsidiary.

34 Acquisition of subsidiaries

During 2002, the Company acquired 51% and 60% interests in Shenzhen Donghai Anbo Property Management Co. Ltd. and Shanghai Hong Kong Metro Construction Management Co. Ltd. for HK$1 million and HK$9 million respectively, both acquisitions were satisfied in cash.

The fair value of assets acquired and liabilities assumed were as follows:

in HK$ million	**2002**
Net assets acquired:	
Prepayments	**1**
Cash at bank and in hand	**16**
Net identifiable assets	**17**
Less: Minority interests	**7**
Total purchase price paid, satisfied in cash	**10**
Less: Cash of subsidiaries acquired	**16**
Net cash inflows in respect of the purchase of subsidiaries	**(6)**

35 Retirement Schemes

The Company operates two occupational retirement schemes, the MTR Corporation Limited Retirement Scheme (the "Retirement Scheme") and a top-up scheme, the MTR Corporation Limited Retention Bonus Scheme (the "RBS"). In addition, in accordance with the Mandatory Provident Fund ("MPF") Schemes Ordinance, the Company has set up an MPF Scheme on 1 December 2000 by participating in a master trust scheme provided by an independent MPF service provider. Employees eligible to join the Retirement Scheme can choose between the Retirement Scheme and the MPF Scheme while temporary employees are required to join the MPF Scheme.

The assets of these schemes are held under the terms of separate trust arrangements. These trusts ensure that the assets are kept separate from those of the Company.

A Retirement Scheme

The Retirement Scheme was established under trust at the beginning of 1977. The Retirement Scheme contains both defined benefit and defined contribution elements. The Retirement Scheme was registered under the Occupational Retirement Schemes Ordinance (Chapter 426 of the Laws of Hong Kong) ("ORSO") with effect from 31 October 1994. On 3 July 2000, exemption was granted by the MPF Authority to maintain the Retirement Scheme and offer it as an alternative to the MPF Scheme.

The Retirement Scheme provides both a hybrid benefit section and a defined contribution benefit section, offering benefits on retirement, permanent disability, death and leaving service to its members. The hybrid benefit section provides benefits based on the greater of a multiple of final salary and accumulated contributions with investment returns. The defined contribution benefit section, which was implemented on 1 April 1999, is a member choice plan which provides retirement benefits based on accumulated contributions and investment returns only. Promotees who are promoted after 1 April 1999 can choose to join either the defined contribution benefit section or to remain in the hybrid benefit section. As the hybrid benefit section was closed to new entrants on 31 March 1999, staff joining the Company on or after 1 April 1999 who would be eligible to join the Retirement Scheme can choose to join either the defined contribution benefit section or, commencing 1 December 2000, the MPF Scheme.

(a) The hybrid benefit section

Members' contributions to the hybrid benefit section are based on a fixed percentage of basic salary. The Company's contributions are determined by the Executive Directorate with reference to an actuarial valuation. At 31 December 2002, the total membership was 6,397 *(2001: 6,715)*. In 2002, members contributed HK$75 million *(2001: HK$78 million)* and the Company contributed HK$256 million *(2001: HK$267 million)* to the hybrid benefit section. The net asset value of the hybrid benefit section as at 31 December 2002 was HK$3,769 million *(2001: HK$3,726 million)*.

35 Retirement Schemes (continued)

(b) The defined contribution benefit section

Both members' and the Company's contributions to the defined contribution benefit section are based on fixed percentages of members' basic salary. As at 31 December 2002, the total membership under this section was 363 *(2001: 368)*. In 2002, total members' contributions were HK$5.2 million *(2001: HK$4.4 million)* and the total contribution from the Company was HK$10.6 million *(2001: HK$9.1 million)*. The net asset value as at 31 December 2002 was HK$28.6 million *(2001: HK$19.7 million)*.

According to the terms of the trust deed, forfeitures were transferred to the reserve account to be utilised at the discretion of the Company.

(c) Actuarial valuations

Actuarial valuations are carried out annually in accordance with the ORSO. A full actuarial valuation of the Retirement Scheme, comprising both the hybrid and the defined contribution benefit sections, was carried out at 31 December 2002 by Towers, Perrin, Forster & Crosby, Inc., an independent firm of consulting actuaries, using the Attained Age Method. The principal actuarial assumptions used included a long-term rate of investment return net of salary increases of 2.25% *(2001: 2%)* per annum, together with appropriate allowances for expected rates of mortality, turnover, redundancy and retirement and an adjustment for salary increases expected over the short term. The actuary confirmed that, at the valuation date:

(i) the solvency ratio of the hybrid benefit section of the Retirement Scheme was 97.2%, the Scheme's assets were not sufficient to meet its aggregate vested liability by HK$110 million, had all members left the scheme; however

(ii) as long as the hybrid benefit section of the Retirement Scheme is funded in accordance with the same contribution rates as in 2002, it is expected that the scheme's assets would be sufficient to eliminate the expected vested liability shortfall within a period of 3 years from date of valuation.

B RBS

The RBS was established under trust as of 1 January 1995. The RBS is a defined benefit scheme and applies to all employees classified by the Company as staff working on designated projects and who are not on gratuity terms. The RBS provides for benefits to be payable only in the event of redundancy for accrued service up to 31 December 2002. The RBS was registered under the Occupational Retirement Schemes Ordinance with effect from 1 December 1995. As at 31 December 2002, there were 520 members *(2001: 692)* under the RBS.

The RBS is non-contributory for members. The Company's contributions are determined by the Executive Directorate with reference to an actuarial valuation and are charged as part of the staff costs to various projects on the basis of the amount contributed. During 2002, the Company's contributions amounted to HK$2 million *(2001: HK$3 million)*. The net asset value of the RBS as at 31 December 2002 was HK$23 million *(2001: HK$45 million)*.

Actuarial valuations are carried out annually. A full actuarial valuation of the RBS was carried out at 31 December 2002 by Towers, Perrin, Forster & Crosby, Inc. using the Attained Age Method. The principal actuarial assumptions used included an expected weighted rate of investment return net of salary increases, of approximately 1.25% *(2001: 0%)* per annum, together with appropriate allowance for expected rates of redundancy. The actuary confirmed that, at the valuation date:

(i) due to the nature of the RBS which provides for benefits only on redundancy, there was no aggregate vested liability, and thus the RBS was technically solvent; and

(ii) the value of the RBS assets, together with the future contributions recommended by the actuary and to be adopted by the Company, would be sufficient to meet the liabilities of the RBS on an on-going basis.

C MPF Scheme

Effective from the MPF commencement date of 1 December 2000, the Company joined The Bank Consortium MPF Plan which has been registered with the Mandatory Provident Fund Schemes Authority and authorised by the Securities and Futures Commission.
As at 31 December 2002, the total number of employees of the Company participating in the MPF Scheme was 502 *(2001: 438)*. In 2002, total members' contributions were HK$2.0 million *(2001: HK$2.5 million)* and total contribution from the Company was HK$2.3 million *(2001: HK$2.7 million)*.

36 Defined benefit retirement plan obligations

The Group makes contributions to two defined benefit plans that provide benefits for employees upon retirement or termination of services for other reasons (note 35). The movements in respect of these defined benefit plans during the year are summarised as follows:

A The amounts recognised in the balance sheets:

The Group and The Company

in HK$ million	Retirement Scheme **2002**	RBS **2002**	Total **2002**	Retirement Scheme 2001	RBS 2001	Total 2001
Present value of funded obligations	**3,775**	**31**	**3,806**	3,717	46	3,763
Fair value of plan assets	**(3,768)**	**(23)**	**(3,791)**	(3,673)	(45)	(3,718)
Net unrecognised actuarial losses	**(6)**	**(6)**	**(12)**	–	–	–
Net liability	**1**	**2**	**3**	44	1	45

The plans had no investment in shares or debt securities issued by the Company.

B Movements in the net liability recognised in the balance sheets:

The Group and The Company

in HK$ million	Retirement Scheme **2002**	RBS **2002**	Total **2002**
At 1 January	**44**	**1**	**45**
Contributions paid to the Schemes	**(256)**	**(2)**	**(258)**
Expense recognised in the profit and loss account (Notes 4A and 36C)	**213**	**3**	**216**
At 31 December	**1**	**2**	**3**

C Expense recognised in the consolidated profit and loss account:

in HK$ million	Retirement Scheme **2002**	RBS **2002**	Total **2002**
Current service cost	**220**	**3**	**223**
Interest cost	**220**	**1**	**221**
Expected return on plan assets	**(227)**	**(1)**	**(228)**
	213	**3**	**216**
Less: Amount capitalised	**64**	**3**	**67**
	149	**–**	**149**

The retirement expense is recognised under staff costs and related expenses in the consolidated profit and loss account.

D Actual gain/(loss) on plan assets

in HK$ million	**2002**
MTRCL Retirement Scheme	**(60)**
MTRCL Retention Bonus Scheme	**1**

36 Defined benefit retirement plan obligations (continued)

E The principal actuarial assumptions used as at 31 December 2002 (expressed as weighted average) are as follows:

	Retirement Scheme **2002**	RBS **2002**	Retirement Scheme 2001	RBS 2001
Discount rate at 31 December	**5.25%**	**1.50%**	6.00%	2.50%
Expected rate of return on plan assets	**6.00%**	**2.00%**	6.00%	2.50%
Future salary increases	**3.75%**	**0.75%**	4.00%	2.50%

Certain comparative information is not provided as an independent actuarial valuation is not required and has not been conducted to ascertain the Schemes' position as at 1 January 2001.

37 Railway projects

A Tseung Kwan O Project

The Project Agreement with the Government related to the design, construction, financing and operation of the Tseung Kwan O Extension was signed on 4 November 1998.

The Agreement also permits the Company to undertake commercial and residential property developments at the proposed development sites in Tseung Kwan O South Area 86, Tiu Keng Leng, Tseung Kwan O Town Centre and Hang Hau, with approximate site areas totalling 42.64 hectares.

The project was completed four months earlier than schedule with service on the Tseung Kwan O Line commencing on 18 August 2002. Although the final accounts of a few contracts are under negotiation with the contractors, it is anticipated that the total cost of the project will be approximately HK$16 billion, as compared to the original budget of HK$30.5 billion.

B Penny's Bay Rail Link

The Project Agreement between the Government and the Company for the design, construction, financing and operation of the Penny's Bay Rail Link was signed on 24 July 2002.

Under the Agreement, the project is scheduled to be completed and opened for service on 1 July 2005. The capital cost estimate for the project based on the defined scope of works and programme is estimated at HK$2 billion.

Following the signing of the Agreement, the Company has awarded 13 major contracts amounting to some HK$928 million for the construction of railway. It is anticipated that the project will be completed within the capital cost estimate of HK$2 billion.

At 31 December 2002, the Company had incurred expenditure of HK$285 million on the project *(2001: HK$68 million regarded as Deferred Expenditure)* and had authorised outstanding commitments on contracts totalling HK$825 million *(2001: HK$22 million)* related to the project.

38 Interests in jointly controlled operations

The Group has the following jointly controlled operations in respect of its property development projects as at 31 December 2002.

Location/ development package	Land use	Total gross floor area (sq. m.)	Actual or expected completion date
Hong Kong Station	Office / Retail / Hotel	415,900	By phases from 1998–2005
Kowloon Station			
Package One	Residential	147,547	Completed in 2000
Package Two	Residential	210,319	By phases from 2002–2003
Package Three	Residential	105,886	2004
Package Four	Residential	128,845	2003
Package Five, Six and Seven	Residential / Office / Retail / Hotel / Serviced Apartment	504,350	By phases from 2005–2008
Olympic Station			
Package One	Residential / Office / Retail	309,069	By phases from 1998–2000
Package Two	Residential / Retail	268,650	By phases from 2001–2002
Package Three	Residential	104,452	2005
Tsing Yi Station	Residential / Retail	292,795	Fully completed in 1999
Tung Chung Station			
Package One	Residential / Office / Retail / Hotel	361,691	By phases from 1999–2005
Package Two	Residential / Retail	255,949	By phases from 2002–2006
Package Three	Residential / Retail	413,154	By phases from 2002–2007
Hang Hau Station	Residential / Retail	142,152	2005
Tiu Keng Leng Station	Residential / Retail	253,765	By phases from 2005–2006
Tseung Kwan O Station			
Area 55b	Residential / Retail	96,797	2006
Area 57a	Residential / Retail	29,642	2005
Choi Hung Park-and-Ride	Residential / Retail	21,582	2005

The Group's assets held in relation to these joint venture operations include various site foundation works and related staff and overhead costs. The costs incurred by the Group on each development package are set off against any up-front payments received from developers in relation to that development package, and the balance is shown on the balance sheet either as property development in progress or deferred income (note 16) as the case may be. As at 31 December 2002, total property development in progress in respect of these jointly controlled operations was HK$1,126 million *(2001: HK$621 million)* and total deferred income was HK$6,226 million *(2001: HK$8,411 million)*.

As the Group is not involved in the financing of the construction of the developments, the only financial liability in respect of these developments as at 31 December 2002 was HK$56 million *(2001: HK$81 million)* in respect of accruals related to property enabling works.

During the year ended 31 December 2002, profits of HK$3,755 million *(2001: HK$3,248 million)* were recognised (note 6).

39 Material related party transactions

The Financial Secretary Incorporated, which holds approximately 76% of the Company's issued share capital on trust for the Government of the Hong Kong SAR, is the majority shareholder of the Company. Transactions between the Group and Government departments, agencies or Government controlled entities, other than those transactions such as the payment of fees, taxes, leases and rates, etc. that arise in the normal dealings between the Government and the Group, are considered to be related party transactions pursuant to SSAP 20 "Related party disclosures" and are identified separately in these accounts.

Members of the Board and Members of the Executive Directorate, and parties related to them, are also considered to be related parties of the Group. Transactions with these parties, except for those involving a Member of the Board or his related parties where the relevant Member abstains from voting, are separately disclosed in the accounts.

Major related party transactions entered into by the Group in prior years include:

A The Company entered into the Airport Railway Agreement with the Government on 5 July 1995 for the construction of the Airport Railway. In addition to specifying the parameters for the design, construction and operation of the Tung Chung and Airport Express Lines, the Agreement also included provisions for the granting of land to the Company for property development (note 16).

B The Company entered into the TKE Project Agreement with the Government on 4 November 1998 for the design, construction, financing and operation of the Tseung Kwan O Extension and the granting of land for commercial and residential property developments along the railway extension (note 37A).

C On 30 June 2000, the Appointed Day for the purposes of the Mass Transit Railway Ordinance, the Company was granted a franchise, for an initial period of 50 years, to operate the existing mass transit railway, and to operate and construct any extension to the railway. On the same day, the Company entered into an Operating Agreement with the Government which detailed provisions for the design, construction, maintenance and operation of the railway under the franchise. The Government has also acknowledged in the Operating Agreement that the Company will require an appropriate commercial rate of return on its investment in any new railway project (which would ordinarily be between 1% to 3% above the estimated weighted average cost of capital of the Company) and that financial and other support from the Government may be required.

D On 14 July 2000, the Company received a comfort letter from the Government pursuant to which Government agreed to extend the period of certain of the Company's land interests so that they are coterminous with the Company's initial 50-year franchise.

During the year, the Group has had the following material related party transactions:

E In connection with the construction of the Airport Railway and the Tseung Kwan O Extension, certain essential project works are embedded within the infrastructure works to be undertaken by the Government or certain of its related parties. These works have been entrusted to the Government and its related parties and are payable on an actual cost basis according to architectural certifications. The Government and certain of its related parties, on the other hand, have entered into entrustment agreements with the Company for the construction of various other infrastructure works that are also reimbursable according to actual costs certified. Details of the amounts paid and the amounts receivable and payable as at 31 December 2002 are provided in notes 15, 24 and 30 respectively.

F On 24 July 2002, the Company entered into an agreement with the Government specifying the parameters for the design, construction, financing and operation of the Penny's Bay Rail Link (the "PBL Agreement"). In connection with the financing of the PBL Project, the Government agreed to provide financial support to the Company in order to bridge the funding gap between the Company's required rate of return of 11.25% per annum in respect of the PBL Project, and the projected return of the PBL pursuant to the terms of the Operating Agreement (note 39C). Such financial support, which amounted to HK$798 million at net present value on 1 January 2002, is to be provided through the Government waivers of its entitlement to cash dividends in respect of its shareholding, commencing from the financial year ended 31 December 2002 and thereafter as is equivalent to the funding gap. During the year ended 31 December 2002, interim cash dividend amounted to HK$219 million *(2001: Nil)* had been waived by the Government (note 39J). The dividends waived have been recorded as a reduction to shareholders' funds and have been set off against cumulative construction cost of the PBL Project (note 15).

G A Provisional Agreement for the Company to build and operate the Tung Chung Cable Car Project ("Cable Car Project") together with a Theme Village at Ngong Ping on the Lantau Island was entered into between the Company and the Government on 31 July 2002. The Cable Car Project is planned for service opening in August 2005 and the cost estimate of railway works as per the Financial Proposal to Government is HK$750 million. As at 31 December 2002, the Company had incurred expenditure of HK$17 million *(2001: HK$6 million)* on the project which was regarded as deferred expenditure in the balance sheet.

H The Company has business transactions with its non-controlled subsidiary in the normal course of operations, details of which are disclosed in note 18.

39 Material related party transactions (continued)

I The Group has paid remuneration to the Members of the Board and Members of the Executive Directorate. Details of these transactions are described in note 5. In addition, the Members of the Executive Directorate were granted share options under the Company's Pre-Global Offering Share Option Scheme. Details of these benefits in kind are disclosed in note 5B and under the paragraph "Board Members and Executive Directorate's interests in shares" in the Report of the Members of the Board.

J During the year, the following dividends were paid to or waived by the Government:

in HK$ million	2002 Interim dividend	2001 Final dividend	Total
Cash dividends paid	–	470	470
Cash dividends waived (Note 39F)	219	–	219
Shares allotted in respect of scrip dividends	330	614	944
	549	1,084	1,633

40 Commitments

A Capital commitments

(i) Outstanding capital commitments as at 31 December 2002 not provided for in the accounts were as follows:

The Group and The Company

in HK$ million	Railway operations	Tseung Kwan O Extension Project	Penny's Bay Rail Link and Tung Chung Cable Car Projects	Property development projects	Total
2002					
Authorised but not yet contracted for	**499**	**–**	**–**	**1,934**	**2,433**
Authorised and contracted for	**1,321**	**–**	**1,017**	**67**	**2,405**
	1,820	**–**	**1,017**	**2,001**	**4,838**
2001					
Authorised but not yet contracted for	854	4,142	–	1,985	6,981
Authorised and contracted for	1,738	1,025	22	154	2,939
	2,592	5,167	22	2,139	9,920

Included in the amounts authorised but not yet contracted for are costs that will not be subject to construction contracts such as staff costs, overhead expenses and capitalised interest.

(ii) The commitments under railway operations comprise the following:

The Group and The Company

in HK$ million	Improvement and enhancement works	Acquisition of property, plant and equipment	Total
2002			
Authorised but not yet contracted for	**338**	**161**	**499**
Authorised and contracted for	**665**	**656**	**1,321**
	1,003	**817**	**1,820**
2001			
Authorised but not yet contracted for	625	229	854
Authorised and contracted for	908	830	1,738
	1,533	1,059	2,592

40 Commitments (continued)

(iii) Commitments in respect of jointly controlled operations have been included in the commitments for Property Development Projects above and were as follows:

The Group and The Company

in HK$ million	**2002**	2001
Authorised but not yet contracted for	**1,931**	1,983
Authorised and contracted for	**57**	38
	1,988	2,021

B Operating lease commitments

The Group had operating leases on office buildings and staff quarters as at 31 December 2002. The total future minimum lease payments under non-cancellable operating leases are payable as follows:

The Group and The Company

in HK$ million	**2002**	2001
Payable within one year		
Leases expiring within one year	**3**	4
Leases expiring between one to five years	**4**	8
	7	12
Payable after one but within five years	**2**	4
Payable after five years	**–**	–
	9	16

The above includes HK$6 million *(2001: HK$10 million)* in respect of the office accommodation and quarters for construction project staff. The majority of the leases are subject to rent reviews.

C Liabilities and commitments in respect of property management contracts

The Group had, over the years, jointly developed with outside property developers certain properties above or adjacent to railway depots and stations. Under most of the development agreements, the Group retained the right to manage these properties after their completion. The Group, as manager of these properties, enters into services contracts with outside contractors for the provision of security, cleaning, maintenance and other services on behalf of the managed properties. The Group is primarily responsible for these contracts, but any contract costs incurred will be reimbursed by the owners and tenants of the managed properties from the management funds as soon as they are paid.

As at 31 December 2002, the Group had total outstanding liabilities and contractual commitments of HK$445 million *(2001: HK$390 million)* in respect of these works and services. Cash funds totalling HK$530 million *(2001: HK$435 million)* obtained through monthly payments of management service charges from the managed properties are held by the Group on behalf of those properties for settlement of works and services provided.

41 Employee Share Option Schemes

A Pre-Global Offering Share Option Scheme

In connection with the Initial Public Offering ("IPO") and Stock Exchange listing of the Company's shares in October 2000, a Pre-Global Offering Share Option Scheme ("Share Option Scheme") was established. Under the Share Option Scheme, a total of 769 employees including all the Members of the Executive Directorate, except Mr. Lincoln Leong Kwok-kuen who was appointed on 1 February 2002, were granted on 20 September 2000 options to purchase an aggregate of 48,338,000 shares at an exercise price of HK$8.44 per share, which was equivalent to 90% of the IPO offer price of HK$9.38 per share. The options may be exercised prior to 11 September 2010, subject to the vesting provisions under the Scheme, which provide that certain proportions of the underlying shares in respect of which options were granted under the Share Option Scheme will vest at certain specified times, as follows:

Date	Proportion of options vested
Before 5 October 2001	None
5 October 2001 to 4 October 2002	One-third
5 October 2002 to 4 October 2003	Two-thirds
After 4 October 2003	All

In 2002, 14,651,500 options to subscribe for shares were vested and 4,362,000 share options previously vested have been exercised. The weighted average closing price in respect of the share options exercised during the year was HK$10.32 per share. In addition, 2,815,000 share options lapsed as a result of the resignation of certain option holders during the year. As at 31 December 2002, total options to subscribe for 36,763,500 *(2001: 43,940,500)* shares remained outstanding.

41 Employee Share Option Schemes (continued)

B New Joiners Share Option Scheme

In May 2002, the New Joiners Share Option Scheme (the "New Scheme") was adopted at the Annual General Meeting to provide share options to new members of the top and senior management of the Company who did not participate in the Pre-Global Offering Share Option Scheme. Under the Rules of the New Scheme, a maximum of 5,056,431 shares may be issued pursuant to the exercise of options granted under the New Scheme. Options granted will vest in respect of their underlying shares over a period of three years from the date on which the relevant option is granted. The exercise price of the options granted under the New Scheme is to be set at a level which reflects generally the share price of the Company at the time of grant of the options.

As at 31 December 2002, no option has been granted under the New Scheme.

42 Adoption of new accounting standards in Hong Kong

The following new or revised SSAPs issued by the Hong Kong Society of Accountants, which became effective during 2002, were adopted for preparation of the Group's financial statements for the years ended 31 December 2001 and 2002:

- SSAP 34, Employee Benefits
- SSAP 35, Accounting for Government Grants and Disclosure of Government Assistance
- SSAP 1 (revised), Presentation of Financial Statements
- SSAP 15 (revised), Cash Flow Statements

A Adoption of SSAP 34, Employee Benefits

As a result of the first time adoption of SSAP 34 and the transitional provisions prescribed in the Standard, the Group has made the following adjustments to its financial results for the year ended 31 December 2002 which are relevant to the Group:

	The Group			The Company		
	Net movements in entitlements			Net movements in entitlements		
in HK$ million	Balance as at 1 January 2001	Year ended 31 December 2001	Balance as at 1 January 2002	Balance as at 1 January 2001	Year ended 31 December 2001	Balance as at 1 January 2002
Retained profit as previously reported	11,527		14,608	11,500		14,545
Prior period adjustments in respect of:						
Short-term benefits						
– unused annual leave entitlement	(137)	(2)	(139)	(137)	(2)	(139)
– leave passage entitlement	(11)	(4)	(15)	(11)	(4)	(15)
Share of non-controlled subsidiary's unused annual leave entitlement	(2)	–	(2)	–	–	–
	(150)	(6)	(156)	(148)	(6)	(154)
Post-employment benefits	–	–	(45)	–	–	(45)
	(150)		(201)	(148)		(199)
Retained profit as restated	11,377		14,407	11,352		14,346

42 Adoption of new accounting standards in Hong Kong (continued)

(i) Short-term benefits – accrued liabilities on unused annual leave and leave passage expenses

Prior to the issuance of SSAP 34, the Group did not provide for the liabilities in respect of its staffs' vested annual leave and leave passage entitlements. SSAP 34 requires that obligations in respect of these entitlements should be accrued as soon as services are rendered. In accordance with this change in accounting policy and pursuant to SSAP 2 (which outlines the disclosure requirements when a change in accounting policy has a material effect on the current or prior periods presented), the Group has retrospectively restated the opening balances of the retained profits as at 1 January 2001 and 2002 by reductions of HK$150 million and HK$156 million respectively. The previously reported net profit for the year ended 31 December 2001 has also been reduced by HK$6 million to reflect movements in the accrued annual leave and leave passage account during the year.

(ii) Post-employment benefits – defined benefit plans

The Group operates two defined benefit plans, the hybrid benefit section of the Retirement Scheme and the RBS (the "Schemes"). SSAP 34 prescribes the valuation methodology and accounting treatments in respect of defined benefit plans, which differs from those adopted by the Group in previous accounts. On adoption of SSAP 34, actuarial valuations were reconducted by independent professionally qualified actuaries to ascertain the Schemes' position as of 1 January 2002 according to the requirements of the new Standard. The results indicated that the Schemes' present value of the defined benefit obligations exceeded the fair value of the Schemes' assets (transitional liabilities) by HK$44 million and HK$1 million respectively on the same date. Pursuant to the provisions of SSAP 34, the Group has chosen to recognise the entire transitional liabilities immediately at the time of first adoption. In accordance with this change in accounting policy and pursuant to SSAP 2, the total transitional liabilities of HK$45 million has been recognised retrospectively against the opening balance of the retained profits as at 1 January 2002 (note 33) and the liabilities has been carried in the balance sheet as accrued pension expenses. Comparative information has not been restated as an independent actuarial valuation has not been conducted to ascertain the Schemes' position as of 1 January 2001.

B Adoption of SSAP 35, Accounting for Government Grants and Disclosure of Government Assistance

Pursuant to the terms of the PBL Project Agreement entered into in July 2002 between the Company and the Government, the Government will provide financial support in the form of dividend waivers in respect of its cash dividend entitlement commencing from financial year ended 31 December 2002. Details of the dividend waiver and the related accounting treatment are set out in notes 1W and 39F. Such dividend waivers are within the meaning of government grants defined in SSAP 35, which became effective for financial statement beginning on or after 1 July 2002.

C Adoption of SSAP 1 (revised), Presentation of Financial Statements

In order to comply with the revised requirements of SSAP 1 (revised), the Group adopts the new statement "Consolidated Statement of Changes in Equity" which replaces the "Consolidated Statement of Recognised Gains and Losses" included in previous accounts. The new statement reconciles the movement of key components of the shareholders' fund, including share capital, reserves and retained earnings, from the beginning to end of a period.

D Adoption of SSAP 15 (revised), Cash Flow Statements

The format of the Consolidated Cash Flow Statement has been revised to follow the new requirements of SSAP 15 (revised).

43 Comparative figures

Comparative figures have been restated and reclassified based on the requirement of the new accounting standards adopted as set out in note 42.

44 Approval of accounts

The accounts were approved by the Board on 6 March 2003.