Notes to Financial Statements

31 December 2003

1. COMPANY REORGANISATION AND BASIS OF PRESENTATION

The Company was incorporated on 7 July 2003 as a joint stock company with limited liability in the People's Republic of China (the "PRC") as part of the reorganisation (the "Reorganisation") of People's Insurance Company of China (now known as the "PICC Holding Company"), a state-owned enterprise engaged in the commercial insurance business in the PRC.

As part of the Reorganisation, which took effect as of 30 September 2002, PICC Holding Company injected into the Company all of its commercial insurance business and operations together with the related assets and liabilities, excluding certain assets and liabilities, by way of capital contribution. In consideration of such injection, the Company issued 8,000 million domestic shares of RMB 1.00 each to PICC Holding Company.

Further details of the Reorganisation are set out in the Company's prospectus dated 27 October 2003 issued in respect of the listing of the Company's shares on the Main Board of The Stock Exchange of Hong Kong Limited (the "HKSE").

The Company's financial statements include the results of the Company for the period from 7 July 2003 (date of incorporation) to 31 December 2003.

The Reorganisation involved companies under common control, and the Company's principal activities were carried out by PICC Holding Company prior to the Reorganisation. Accordingly, the directors consider that it is appropriate, for information purposes, to present supplementary pro forma financial statements. Such supplementary pro forma financial statements comprise a pro forma profit and loss account, a pro forma balance sheet, a pro forma statement of changes in equity and a pro forma cash flow statement, prepared as if the Company had been in existence throughout the two years ended 31 December 2003 and as if the Reorganisation was effective prior to the earliest date presented therein.

2. CORPORATE INFORMATION

The registered office of the Company is located at 69 Dongheyanjie, Xuanwumen, Beijing 100052, the PRC.

The Company is a provider of commercial insurance coverage in the PRC, and provides a wide range of property and casualty ("P&C") insurance consisting of property loss and damage insurance, liability insurance, credit and guarantee insurance, accidental injury insurance, short term health insurance and other P&C insurance as well as related reinsurance.

In the opinion of the directors, the ultimate holding company is PICC Holding Company, which is incorporated in the PRC.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of preparation

These financial statements have been prepared in accordance with Hong Kong Statements of Standard Accounting Practice, accounting principles generally accepted in Hong Kong and the disclosure requirements of the Hong Kong Companies Ordinance. They have been prepared under the historical cost convention, except for the periodic remeasurement of certain fixed assets and investments in securities as further explained below.

Revenue recognition

Revenue is recognised when it is probable that the economic benefits will flow to the Company and when the revenue can be measured reliably, on the following basis:

(a) premium income, at the inception of risk resulting from a policy being written;

(b) rental income, on a time proportion basis over the lease term;

(c) interest income, on a time proportion basis taking into account the principal outstanding and the effective interest rate applicable; and

(d) dividend income, when the shareholders' right to receive payment has been established.

Reinsurance

Assets and liabilities related to reinsurance contracts are reported on a gross basis unless a right of offset exists. Reinsurance premiums ceded and reinsurance recoveries on loss incurred are deducted from the respective revenue and expense accounts. Unearned premium reserves - reinsurers' share represents the ceded portion of unearned premium reserves. Payable to reinsurers includes ceded premiums retained by the Company to fund ceded losses as they become due pursuant to reinsurance agreements. Amounts recoverable from reinsurers are estimated in a manner consistent with the claim liability associated with the reinsured risks. Accordingly, revenues and expenses related to reinsurance agreements are recognised consistently with the underlying risk of the business reinsured.

Unearned premium reserves

Unearned premium reserves are recognised to cover the unexpired portion of the premiums written. Premiums are earned on a time-apportioned basis over the terms of the related insurance contracts.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(CONTINUED)*

Loss and loss adjustment expense reserves

The loss and loss adjustment expense reserves are for future payment obligations under insurance loss.

The loss and loss adjustment expense reserves are recorded on an undiscounted basis and comprise estimated provisions for losses reported at the balance sheet date, losses incurred but not yet reported at the balance sheet date, and loss adjustment expenses that can be directly attributable to individual claims.

The loss and loss adjustment reserves are calculated at the realistically estimated amount considered necessary to settle the loss in full less a deduction for the estimated value of salvage and other recoveries, using recognised actuarial methods. Past experience is taken into account as well as current and future expected social and economic factors.

Changes in estimates of the loss and loss adjustment expense reserves are recognised in the profit and loss account in the period in which the estimates are changed. The directors believe that the loss and loss adjustment expense reserves at the balance sheet date are adequate to cover the ultimate cost of all incurred losses and direct loss adjustment expenses to that date, but the reserves are necessarily based on estimates and no representation is made that the ultimate liability may not exceed or be less than such estimates.

Net claims incurred

Net claims incurred represents the actual amount of claims payable and claims handling expenses, net of claims recovered from reinsurance, and adjusted by changes in net loss and loss adjustment expenses reserves and net provision for premium deficiency.

Provision for premium deficiency

A provision for premium deficiency is recognised if the sum of expected losses and loss adjustment expenses, unamortised deferred acquisition costs and maintenance costs exceeds related unearned premium reserves. The premium deficiency is first recognised by writing off deferred acquisition costs to the extent required to eliminate the deficiency. If the premium deficiency is greater than the unamortised deferred acquisition costs, a provision is made for the excess deficiency. The amount of provision is made for each class of business individually.

Deferred acquisition costs

Policy acquisition costs which vary with and are primarily related to the production of new and renewal business (consisting principally of commission expenses and underwriting personnel expenses), net of reinsurance commissions, are deferred and amortised on a time-apportioned basis over the terms of the related insurance policies. Deferred acquisition costs are limited to the excess of unearned premium reserves over the sum of expected claim costs, claim adjustment related expenses and policy maintenance expenses.

Operating leases

Leases where substantially all the rewards and risks of ownership of assets remain with the lessor are accounted for as operating leases. Where the Company is the lessor, assets leased by the Company under operating leases are included in non-current assets and rentals receivable under the operating leases are credited to the profit and loss account on a straight-line basis over the lease terms. Where the Company is the lessee, rentals payable under the operating leases are charged to the profit and loss account on a straight-line basis over the lease terms.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(CONTINUED)*

Employee benefits

The Company's contributions to the defined contribution plans administered by the PRC government are recognised as an expense in the profit and loss account as incurred.

Related parties

Parties are considered to be related if one party has the ability, directly or indirectly, to control the other party or exercise significant influence over the other party in making financial and operating decisions. Parties are also considered to be related if they are subject to common control or common significant influence. Related parties may be individuals or corporate entities.

Income tax

Income tax comprises current tax and deferred tax. Income tax is recognised in the profit and loss account or in equity if it relates to items that are recognised in the same or a different period directly to equity.

Deferred tax is provided, using the liability method, on all temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax liabilities are recognised for all taxable temporary differences, except where the deferred tax liability arises from the initial recognition of an asset or liability and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

Deferred tax assets are recognised for all deductible temporary differences and the carryforward of unused tax assets and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carryforward of unused tax assets and unused tax losses can be utilised, except where the deferred tax asset relating to the deductible temporary differences arises from the initial recognition of an asset or liability and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. Conversely, previously unrecognised deferred tax assets are recognised to the extent that it is probable that sufficient taxable profits will be available to allow all or part of the deferred tax asset to be utilised.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates and tax laws that have been enacted or substantively enacted at the balance sheet date and interpretations and practices in respect thereof.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(CONTINUED)*

Dividends

Final dividends proposed by the directors are classified as a separate allocation of retained profits within the capital and reserves section of the balance sheet, until they have been approved by the shareholders in a general meeting. When these dividends have been approved by the shareholders and declared, they are recognised as a liability.

Interim and special dividends are simultaneously proposed and declared. Consequently, interim and special dividends are recognised immediately as a liability when they are proposed and declared.

Profit appropriation

Under the PRC Company Law and the Company's articles of association, net profit after tax as determined in accordance with PRC Accounting Regulations can only be distributed as dividends after making up prior years' cumulative losses, if any, and making allowance for the following statutory reserve funds, which cannot be used for purposes other than those for which they are created and are not distributable as cash dividends:

(a) Statutory surplus reserve

In accordance with the PRC Company Law and the Company's articles of association, the Company is required to appropriate 10% of the annual statutory net profit after tax (after offsetting any prior years' losses), determined in accordance with PRC Accounting Regulations, to the statutory surplus reserve. When the balance of such reserve fund reaches 50% of capital, any further appropriation is optional. The statutory surplus reserve can be utilised to offset prior years' losses or to increase capital. However, such balance of the statutory surplus reserve must be maintained at a minimum of 25% of capital after any such usage.

(b) Statutory public welfare fund

In accordance with the PRC Company Law and the Company's articles of association, the Company is required to appropriate 5% to 10% of the annual statutory net profit after tax (after offsetting any prior years' losses), determined in accordance with PRC Accounting Regulations, to the statutory public welfare fund, which will be utilised to build or acquire capital items, such as dormitories and other facilities for the employees of the Company, and cannot be used to settle staff welfare expenses.

In accordance with the PRC relevant regulations and the Company's articles of association, the retained profits of the Company for the purpose of profit distribution are deemed to be the lower of the amount determined in accordance with PRC accounting standards and regulations, and the amount determined in accordance with generally accepted accounting principles in Hong Kong.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(CONTINUED)*

Cash and cash equivalents

For the purpose of the cash flow statement, cash and cash equivalents comprise cash on hand and demand deposits, and short term highly liquid investments which are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value, and have a short maturity of generally within three months when acquired.

For the purpose of the balance sheet, cash and cash equivalents comprise cash on hand and at banks, which are not restricted as to use.

Foreign currencies

Foreign currency transactions are recorded at the applicable exchange rates ruling at the transaction dates. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated at the applicable exchange rates ruling at that date. Exchange differences are dealt with in the profit and loss account.

Trading securities

Trading securities are investments in securities held for trading purposes and are stated at their fair values on the basis of their quoted market prices at the balance sheet date, on an individual investment basis. The gains or losses arising from changes in the fair value of a security are credited or charged to the profit and loss account in the period in which they arise.

Investments in securities

Investments in securities are non-trading investments in listed and unlisted securities intended to be held on a long term basis.

Listed securities are stated at their fair values on the basis of their quoted market prices at the balance sheet date, on an individual investment basis. Unlisted securities are stated at their estimated fair values, on an individual basis. The estimated fair values of unlisted investments are determined by the directors having regard to, inter alia, the prices of the most recent reported sales or purchases of the securities, or comparison of price/earnings ratios and dividend and interest yields of the securities with those of similar listed securities, with allowance made for the lower liquidity of the unlisted securities.

The gains or losses arising from changes in the fair value of a security are dealt with as movements in the non-trading investment securities revaluation reserve, until the security is sold, collected, or otherwise disposed of, or until the security is determined to be impaired, when the cumulative gain or loss derived from the security recognised in the non-trading investment securities revaluation reserve, together with the amount of any further impairment, is charged to the profit and loss account in the period in which the impairment arises.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(CONTINUED)*

Investments in securities *(continued)*

Securities purchased under purchase and resale agreements are recorded at their costs. The difference between the purchase cost and the reselling price is credited as interest income over the period from the date of purchase to the date of resale using the effective interest method.

Securities sold under sale and repurchase agreements in which the Company maintains effective control of the securities are accounted for as secured borrowings. Such securities are maintained on the balance sheet with the proceeds of the sale included in other liabilities and accruals. The difference between the selling price and the repurchase price is amortised as interest expense over the period from the date of sale to the date of repurchase using the effective interest method.

Premiums receivable and agents' balances

Premiums receivable and agents' balances represent amounts due from policyholders and agents and are stated at cost less allowance for doubtful accounts. An allowance for doubtful accounts is provided based on an evaluation of the recoverability of these accounts at the balance sheet date.

Fixed assets, construction in progress and depreciation

Fixed assets, other than construction in progress, are stated at cost or valuation less accumulated depreciation and any impairment losses. The cost of an asset comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use. Expenditure incurred after fixed assets have been put into operation, such as repairs and maintenance, is normally charged to the profit and loss account in the period in which it is incurred. In situations where it can be clearly demonstrated that the expenditure has resulted in an increase in the future economic benefits expected to be obtained from the use of a fixed asset, the expenditure is capitalised as an additional cost of that asset.

Changes in the values of fixed assets are dealt with as movements in the revaluation reserve. If the total of this reserve is insufficient to cover a deficit, on an individual asset basis, the excess of the deficit is charged to the profit and loss account. Any subsequent revaluation surplus is credited to the profit and loss account to the extent of the deficit previously charged. On disposal of a revalued asset, the relevant portion of the revaluation reserve realised in respect of previous valuations is transferred to retained profits as a movement in reserves.

Depreciation is calculated on a straight-line basis after taking into account the estimated residual values, to write off the cost or valuation of each asset over its estimated useful life, as follows:

Land and buildings	30 - 70 years
Motor vehicles	4 - 9 years
Office equipment, furniture and fixtures	3 - 14 years

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(CONTINUED)*

Fixed assets, construction in progress and depreciation *(continued)*

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

Construction in progress represents a building under construction, which is stated at cost less any impairment losses, and is not depreciated. Cost comprises the direct costs of construction and capitalised borrowing costs on related borrowed funds during the period of construction. Construction in progress is reclassified to the appropriate category of fixed assets when completed and ready for use.

Impairment

Internal and external sources of information are reviewed at each balance sheet date to determine whether fixed assets, construction in progress and investments in securities are impaired or an impairment loss previously recognised no longer exists or has decreased. If any such indication exists, the asset's recoverable amount is estimated. An impairment loss is recognised as a charge to the profit and loss account when the carrying amount of an asset exceeds its recoverable amount. 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 (i.e. a cash-generating unit).

An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. 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. A reversal of impairment losses is recognised as a credit to the profit and loss account.

Policyholders' deposits

Policyholders' deposits represent deposits received from policyholders which are refundable under maturity refund type commercial insurance policies. Interest credited to these deposits is recognised as an expense in the profit and loss account.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(CONTINUED)*

Provisions and contingent liabilities

Provisions are recognised for liabilities of uncertain timing or amount when the Company has a legal or constructive obligation 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 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.

Subordinated loan

Subordinated loan is included in the balance sheet at the value of the net proceeds received upon issue, adjusted for the amortisation of any premium or discount arising on issue.

Interest on subordinated loan is charged to the profit and loss account at the coupon rate adjusted for the amortisation of any premium or discount arising on issue, so as to achieve a constant rate of charge over the period from the date of issue to the date of redemption.

When subordinated loan issued is settled before maturity, any difference between the amount repaid and the carrying amount is recognised immediately in the profit and loss account.

4. SEGMENT INFORMATION

Segment information is presented by way of the Company's primary segment reporting basis, by business segment. No further geographical segment information is presented as the Company's customers and operations are located in Mainland China.

Summary details of the business segments are as follows:

(a) the motor vehicle segment provides insurance products to cover motor vehicles;
(b) the commercial property segment provides insurance products to cover commercial properties;
(c) the homeowners segment provides insurance products covering homes and their contents;
(d) the cargo segment provides insurance products covering vessels, crafts or conveyances;
(e) the liability segment provides insurance products covering policyholders' liability;
(f) the accidental injury segment provides insurance products covering accidental injury; and
(g) the "other" segment mainly represents insurance products related to marine hull, aviation and oil and gas.

4. SEGMENT INFORMATION *(CONTINUED)*

Information on the Company's reportable business segments is as follows:

	7 July to 31 December 2003 *RMB million*	Pro forma 2003 *RMB million*	Pro forma 2002 *RMB million*
Turnover			
Motor vehicle	15,466	35,294	31,436
Commercial property	2,789	8,090	8,744
Homeowners	670	1,425	1,642
Cargo	1,072	2,657	2,966
Liability	967	2,406	2,752
Accidental injury	871	1,745	—
Other	1,808	3,351	3,031
	23,643	54,968	50,571
Net premiums earned			
Motor vehicle	13,525	26,930	23,928
Commercial property	2,915	6,437	6,346
Homeowners	429	1,045	1,105
Cargo	1,106	2,314	2,248
Liability	977	2,116	1,817
Accidental injury	464	514	-
Other	507	1,053	937
	19,923	40,409	36,381
Interest and dividend income			
Homeowners	(73)	26	29
Net gains/(losses) on trading and non-trading securities			
Homeowners	6	64	(83)

4. SEGMENT INFORMATION *(CONTINUED)*

	7 July to 31 December 2003 *RMB million*	Pro forma 2003 *RMB million*	Pro forma 2002 *RMB million*
Net claims incurred			
Motor vehicle	(10,641)	(21,618)	(18,701)
Commercial property	(1,639)	(3,285)	(4,127)
Homeowners	(158)	(340)	(351)
Cargo	(520)	(1,107)	(1,001)
Liability	(591)	(1,401)	(1,396)
Accidental injury	(299)	(338)	—
Other	(596)	(974)	(1,058)
	(14,444)	(29,063)	(26,634)
Amortisation of deferred acquisition costs			
Motor vehicle	(1,140)	(2,053)	(1,520)
Commercial property	(64)	(125)	(101)
Homeowners	(56)	(134)	(116)
Cargo	(84)	(147)	(122)
Liability	(81)	(124)	(71)
Accidental injury	(76)	(80)	—
Other	74	184	236
	(1,427)	(2,479)	(1,694)
Insurance protection expense			
Motor vehicle	(150)	(323)	(269)
Commercial property	(17)	(59)	(67)
Homeowners	(10)	(17)	(14)
Cargo	(9)	(22)	(24)
Liability	(8)	(20)	(22)
Accidental injury	(12)	(19)	—
Other	2	(8)	(11)
	(204)	(468)	(407)
Interest expense credited to policyholders' deposits			
Homeowners	(65)	(123)	(54)
Segment profit before unallocated income and expenses			
Motor vehicle	1,594	2,936	3,438
Commercial property	1,195	2,968	2,051
Homeowners	73	521	516
Cargo	493	1,038	1,101
Liability	297	571	328
Accidental injury	77	77	—
Other	(13)	255	104
	3,716	8,366	7,538

4. SEGMENT INFORMATION *(CONTINUED)*

	7 July to 31 December 2003 *RMB million*	Pro forma 2003 *RMB million*	Pro forma 2002 *RMB million*
Unallocated operating income and expenses			
Interest and dividend income	462	664	619
Net gains/(losses) on trading and non-trading securities	24	196	(562)
General and administrative expenses	(3,837)	(6,903)	(6,566)
Finance costs	(23)	(35)	(35)
	(3,374)	(6,078)	(6,544)
Profit before tax	342	2,288	994
Tax	(235)	(837)	(716)
Net profit	107	1,451	278

Interest and dividend income and net gains/(losses) on trading and non-trading securities attributed to the homeowners insurance product (see note 27), which can be separately identified based on the results of its designated pool of investments, are separately disclosed. The remaining amounts that are not attributed to particular insurance products are not allocated and are included under unallocated operating income and expenses.

4. SEGMENT INFORMATION *(CONTINUED)*

	31 December 2003	Pro forma 31 December 2002
	RMB million	*RMB million*
Segment assets		
Motor vehicle	6,764	7,053
Commercial property	3,567	3,435
Homeowners	3,712	3,818
Cargo	564	659
Liability	572	668
Accidental injury	253	—
Other	4,338	5,280
	19,770	20,913
Unallocated assets	64,802	50,713
Total assets	84,572	71,626
Segment liabilities		
Motor vehicle	30,622	27,103
Commercial property	9,688	7,445
Homeowners	8,789	9,898
Cargo	1,972	2,259
Liability	2,022	2,400
Accidental injury	1,335	—
Other	6,792	6,364
	61,220	55,469
Unallocated liabilities	4,595	5,864
Total liabilities	65,815	61,333

5. TURNOVER AND REVENUE

Turnover represents direct premiums written and reinsurance premiums assumed, net of government levies and surcharges, i.e., gross premium written.

An analysis of turnover, interest and dividend income and net gains/(losses) on trading and non-trading securities is as follows:

	7 July to 31 December 2003 *RMB million*	Pro forma 2003 *RMB million*	Pro forma 2002 *RMB million*
Turnover			
Direct premiums written	24,969	58,074	54,081
Reinsurance premiums assumed	7	11	13
	24,976	58,085	54,094
Less: Government levies and surcharges	(1,333)	(3,117)	(3,523)
	23,643	54,968	50,571
Net premiums earned			
Turnover	23,643	54,968	50,571
Less: Reinsurance premiums ceded	(5,289)	(11,116)	(13,441)
Net premiums written	18,354	43,852	37,130
Less: Changes in net unearned premium reserves	1,569	(3,443)	(749)
Net premiums earned	19,923	40,409	36,381
Interest and dividend income			
Interest income from trading and non-trading securities	35	164	126
Interest income from bank deposits	332	474	396
Dividend income from trading and non-trading securities	22	52	126
	389	690	648
Net gains/(losses) on trading and non-trading securities			
Realised gains on trading securities - Mutual funds	3	11	10
Realised gains/(losses) on trading securities - Debts	(4)	3	125
Unrealised gains/(losses) on trading securities - Mutual funds	22	192	(798)
Unrealised gains/(losses) on trading securities - Debts	(17)	10	(17)
Net gains/(losses) on disposal of non-trading securities:			
Realisation of revaluation reserve previously recognised	(5)	—	(1)
Recognised gain arising in the period/year	31	44	36
	30	260	(645)

6. NET CLAIMS INCURRED

	7 July to 31 December 2003 *RMB million*	Pro forma 2003 *RMB million*	Pro forma 2002 *RMB million*
Gross claims expenses	17,295	35,114	31,849
Less: Loss recovered from reinsurance	(4,067)	(7,444)	(7,022)
Net claims expenses	13,228	27,670	24,827
Add: Change in net loss and loss adjustment expense reserves (note 26)	1,217	1,395	1,805
Add: Change in net provision for premium deficiency	(1)	(2)	2
Net claims incurred	14,444	29,063	26,634

7. GENERAL AND ADMINISTRATIVE EXPENSES

The Company's operating profit is arrived at after charging:

	Notes	7 July to 31 December 2003 *RMB million*	Pro forma 2003 *RMB million*	Pro forma 2002 *RMB million*
Personnel expenses		515	921	931
Depreciation	22	680	1,560	1,432
Office expenses		806	1,516	1,505
Provision for doubtful accounts		63	66	11
Repairs and maintenance		141	259	323
Impairment loss on construction in progress	23	21	21	—
Net loss on disposal of fixed assets		6	7	113
Minimum lease payments under operating leases - land and buildings		172	221	126
Auditors' remuneration		9	9	—
Others		1,424	2,323	2,125
		3,837	6,903	6,566

7. GENERAL AND ADMINISTRATIVE EXPENSES *(CONTINUED)*

Total personnel expenses of the Company for the relevant period are as follows:

	7 July to 31 December 2003 *RMB million*	Pro forma 2003 *RMB million*	Pro forma 2002 *RMB million*
Included in net claims incurred	310	794	807
Included in deferred acquisition costs	604	1,538	1,609
Included in general and administrative expenses	515	921	931
Total personnel expenses	1,429	3,253	3,347

8. FINANCE COSTS

	7 July to 31 December 2003 *RMB million*	Pro forma 2003 *RMB million*	Pro forma 2002 *RMB million*
Interest on bank loans wholly repayable within five years	14	25	34
Interest on subordinated loan (note 33)	9	9	—
Other finance costs	—	1	1
	23	35	35

9. DIRECTORS' AND SUPERVISORS' REMUNERATION

Directors' and supervisors' remuneration for the period, disclosed pursuant to the Listing Rules and Section 161 of the Companies Ordinance, is as follows:

	7 July to 31 December 2003	**Pro forma 2003**	Pro forma 2002
	RMB'000	***RMB'000***	*RMB'000*
Fees	1,739	1,739	—
Other emoluments:			
Salaries, allowances and benefits in kind	1,215	1,638	852
Performance related bonuses	2,111	2,969	1,621
Pension scheme contributions	41	99	92
	5,106	6,445	2,565

The number of directors and supervisors whose remuneration fell within the following band is as follows:

	7 July to 31 December 2003	**Pro forma 2003**	Pro forma 2002
Nil to HK$1,000,000 (equivalent to approximately RMB1,065,700)	14	14	11

There was no arrangement under which a director or a supervisor waived or agreed to waive any remuneration during 2003 and 2002.

Fees include approximately HK$600,000 (equivalent to approximately RMB639,000) (2002: Nil) payable to the independent non-executive directors. There were no other emoluments payable to the independent non-executive directors during 2003 (2002: Nil).

The shareholders of the Company adopted a scheme of share appreciation rights of senior management on 30 July 2003. The share appreciation rights scheme is designed to link the interests of the senior management with growth of the Company's results of operations and the Company's value (market price of the H Shares). The Board of Directors of the Company is responsible for making decisions under the scheme and administering the scheme. No shares will be issued under this scheme. Therefore, the shareholdings of shareholders will not be diluted as a result of the issuance of share appreciation rights.

Under the share appreciation rights scheme, members of the Board of Directors (excluding independent non-executive directors) and the Supervisory Committee, president, vice presidents, chief financial officer, division managers of the Company, presidents of provincial level branch offices, employees with special contribution to the Company as determined by the nomination, remuneration and review committee and other senior management at equivalent levels are eligible to receive share appreciation rights.

During the period up to 30 December 2003, the Company did not grant any share appreciation rights pursuant to the share appreciation rights scheme.

10. FIVE HIGHEST PAID EMPLOYEES

The five highest paid employees during the period included three (2002: one) directors and supervisors, details of whose remuneration are set out in note 9 above. Details of the remuneration of the remaining two (2002: four) non-director or supervisor, highest paid employees for the period are as follows:

	7 July to 31 December 2003 ***RMB'000***	**Pro forma 2003** ***RMB'000***	Pro forma 2002 *RMB'000*
Salaries, allowances and benefits in kind	331	470	556
Performance related bonuses	559	861	1,138
Pension scheme contributions	12	18	43
	902	1,349	1,737

The number of non-director or supervisor, highest paid employees whose remuneration fell within the following band is as follows:

	Number of employees		
	7 July to 31 December 2003	**Pro forma 2003**	Pro forma 2002
Nil to HK$1,000,000 (equivalent to approximately RMB1,065,700)	2	2	4

There was no arrangement under which any of these highest paid employees waived or agreed to waive any remuneration during 2003 and 2002.

11. TAX

	7 July to 31 December 2003 *RMB million*	Pro forma 2003 *RMB million*	Pro forma 2002 *RMB million*
Current - PRC			
Charge for the period/year	323	367	—
Overprovision in prior years	—	—	(683)
	323	367	(683)
Deferred	(88)	470	1,399
Total tax charge for the period/year	235	837	716

A reconciliation of the tax expense applicable to profit before tax using the statutory rate for the PRC, in which the Company is domiciled, to the tax expense at the effective tax rate is as follows:

	7 July to 31 December 2003 *RMB million*	%	Pro forma 2003 *RMB million*	%	Pro forma 2002 *RMB million*	%
Profit before tax	342		2,288		994	
Tax at the statutory tax rate of 33% (i)	113	33	755	33	328	33
Lower tax rate for specific provinces or local authority (i)	—	—	—	—	19	1.9
Income not subject to tax (ii)	(13)	(3.8)	(59)	(2.6)	(76)	(7.6)
Expenses not deductible for tax (iii)	135	39.5	141	6.2	445	44.7
Tax charge for the period/year	235	68.7	837	36.6	716	72.0

(i) The provision for PRC income tax is calculated based on the statutory rate of 33% in accordance with the relevant PRC income tax rules and regulations for all periods presented, except for certain branches of the Company, which are taxed at lower rates or exempted from PRC income tax.

(ii) This primarily comprises interest income from government bonds and distributions from open-ended mutual funds which are not subject to PRC income tax.

(iii) This primarily represents expenses in excess of the statutory deductible amount which are not tax deductible.

12. DIVIDENDS

	7 July to 31 December 2003 *RMB million*	Pro forma 2003 *RMB million*	Pro forma 2002 *RMB million*
Special	650	650	—

Pursuant to the Reorganisation and the "Provisional Regulation Relating to Corporate Reorganisation of Enterprises and Related Management of State-owned Capital and Financial Treatment," which was issued by the PRC Ministry of Finance and became effective on 27 August 2002, the Company agreed to distribute special dividends equivalent to the net profit arising from the commercial insurance business injected into the Company pursuant to the Reorganisation for the period from 1 October 2002 (being the first day after the effective date of the Reorganisation) to 6 July 2003 (being the day immediately prior to the date of its incorporation) determined in accordance with PRC GAAP in two installments as follows:

- The Company distributed RMB5.4 million on 28 October 2003 in cash, representing the net profit under PRC GAAP for the three-month period ended 31 December 2002, to PICC Holding Company; and

- Within 30 days following the date on which the Company publishes its 2003 audited financial statements, the Company will distribute RMB644 million in cash to PICC Holding Company, which represents the net profit for the period from 1 January 2003 to 6 July 2003 calculated as 187/365 of the net profit for 2003 under PRC GAAP. This amount is included in the balance of the amounts due to the ultimate holding company as at 31 December 2003 (note 30).

13. EARNINGS PER SHARE

The calculations of basic earnings per share for the period from 7 July 2003 to 31 December 2003 and for the year ended 31 December 2003 and 2002, are based on:

	7 July to 31 December 2003 *RMB million*	Pro forma 2003 *RMB million*	Pro forma 2002 *RMB million*
Earnings			
Net profit attributable to shareholders used in the basic earnings per share calculation	107	1,451	278

		Number of shares	
	7 July to 31 December 2003 million	Pro forma 2003 million	Pro forma 2002 million
Shares			
Weighted average number of ordinary shares used in the basic earnings per share calculation	9,000	8,482	8,000

The weighted average number of ordinary shares in issue used for the years ended 31 December 2003 and 31 December 2002 have taken into account the issue of 8,000 million ordinary shares upon the incorporation of the Company as if such shares have been outstanding since 1 January 2002.

The Company has had no dilutive potential shares outstanding since 1 January 2002.

14. EMPLOYEE RETIREMENT BENEFITS

As stipulated by the labour regulations of the PRC, the Company participates in various defined contribution retirement plans organised by municipal and provincial governments for its staff. The Company is required to make contributions to the retirement plans at rates ranging from 13% to 39.5% of the salaries, bonuses and certain allowances of its staff. Under the plans, its staff is entitled to a pension equal to a fixed proportion of the salary prevailing at his or her retirement date. The Company has no other material obligation for the payment of its staff's retirement and other post-retirement benefits other than the contributions described above. The Company's contributions for the for the period from 7 July to 31 December 2003, and for each of the two years ended 31 December 2003 and 2002 were RMB191 million, RMB362 million and RMB238 million, respectively.

15. CASH AND CASH EQUIVALENTS AND TERM DEPOSITS

	31 December 2003	Pro forma 31 December 2002
	RMB million	*RMB million*
Cash at banks	11,529	8,900
Cash in hand	32	27
Securities purchased under resale agreements with original maturity of less than 3 months	3,327	345
Deposits with banks and other financial institutions with original maturity of less than 3 months	3,116	2,357
Cash and cash equivalents	18,004	11,629
Term deposits, representing deposits with banks with original maturity of more than three months and other balances with banks	12,562	8,286
Total	30,566	19,915

16. TRADING SECURITIES

	31 December 2003	Pro forma 31 December 2002
	RMB million	*RMB million*
Listed investments:		
Debt securities issued by the PRC central government	1,813	3,052
Debt securities issued by corporate entities	66	273
Mutual funds issued by banks and other financial institutions	3,690	3,009
	5,569	6,334
Unlisted investments:		
Debt securities issued by the PRC central government	525	2,460
Debt securities issued by corporate entities	—	643
Debt securities issued by banks and other financial institutions	—	835
	525	3,938
Total	6,094	10,272

16. TRADING SECURITIES *(CONTINUED)*

A maturity profile of the debt securities classified as trading securities according to their contractual maturity dates is as follows:

	31 December 2003 *RMB million*	Pro forma 31 December 2002 *RMB million*
Less than 3 months but not on demand	199	—
Less than 1 year but more than 3 months	326	149
Less than 5 years but more than 1 year	1,813	3,172
More than 5 years	66	3,942
	2,404	7,263

17. INVESTMENTS IN SECURITIES

	31 December 2003 *RMB million*	Pro forma 31 December 2002 *RMB million*
Listed investments:		
Debt securities issued by the PRC central government	1,864	67
Debt securities issued by corporate entities	280	—
	2,144	67
Unlisted investments:		
Debt securities issued by the PRC central government	5,583	493
Debt securities issued by corporate entities	1,373	420
Mutual funds issued by banks and other financial institutions	1,665	1,314
	8,621	2,227
	10,765	2,294

As at 31 December 2003 and 2002, investments in securities represented non-trading securities and are carried at fair value. The unlisted investments are traded on over-the-counter market in the PRC.

17. INVESTMENTS IN SECURITIES *(CONTINUED)*

A maturity profile of the debt securities classified as non-trading securities according to their contractual maturity dates is as follows:

	31 December 2003	Pro forma 31 December 2002
	RMB million	*RMB million*
Less than 3 months but not on demand	—	1
Less than 1 year but more than 3 months	201	151
Less than 5 years but more than 1 year	3,696	398
More than 5 years	5,203	430
	9,100	980

18. PREMIUMS RECEIVABLES AND AGENTS' BALANCES, NET

	31 December 2003	Pro forma 31 December 2002
	RMB million	*RMB million*
Premiums receivables and agents' balances	2,095	2,350
Less: Allowance for doubtful accounts	(83)	(11)
	2,012	2,339

An aged analysis of the premiums receivable and agents' balances as at the balance sheet date, based on payment due date, and net of provisions, is as follows:

	31 December 2003	Pro forma 31 December 2002
	RMB million	*RMB million*
Within 3 months	1,622	2,252
Over 3 months but less than 6 months	345	70
Over 6 months	45	17
	2,012	2,339

18. PREMIUMS RECEIVABLES AND AGENTS' BALANCES, NET *(CONTINUED)*

Movements in the allowance for doubtful accounts are as follows:

	7 July to 31 December 2003 *RMB million*	Pro forma 2003 *RMB million*	Pro forma 2002 *RMB million*
At beginning of the period/year	14	11	17
Provision for the period/year	69	72	11
Written-off	—	—	(17)
At end of the period/year	83	83	11

19. RECEIVABLES FROM REINSURERS

An aged analysis of the receivables from reinsurers as at the balance sheet date is as follows:

	31 December 2003 *RMB million*	Pro forma 31 December 2002 *RMB million*
Within 3 months	536	764
Over 3 months but less than 6 months	70	25
Over 6 months	50	122
	656	911

As at 31 December 2002 and 2003, the amount of receivables from reinsurers net of reinsurance premiums ceded was current and in accordance with the terms of the relevant reinsurance contracts. None of the Company's reinsurance contracts contains any contractual provisions for the delay of any reimbursement of incurred losses to the Company. Reinsurance adjustment commission and profit commission totaling RMB318 million and RMB395 million as at 31 December 2003 and 31 December 2002, respectively, are included in the receivables due from reinsurers that are due from certain reinsurers when the underwriting year of account closes, which under the terms of the relevant reinsurance contracts is normally on a three-year basis.

20. PREPAYMENTS AND OTHER RECEIVABLES

	31 December 2003	Pro forma 31 December 2002
	RMB million	*RMB million*
Amount due from provincial and municipal governments (i)	**1,210**	1,210
Amount due from the ultimate holding company (ii)	**—**	78
Amounts due from other third parties	**151**	109
Interest receivables	**190**	199
Prepayments and deposits	**77**	131
Income tax recoverable	**—**	200
Others	**439**	175
	2,067	2,102

(i) During 1999, pursuant to the instruction from the State Council as part of the restructuring of the PRC insurance industry, the Company acquired the commercial insurance business of certain provincial and municipal governments. On the date of the acquisition, the net liabilities assumed amounted to RMB1,210 million, which mainly consisted of unearned premium reserves and loss and loss adjustment expense reserves, net of cash and cash equivalents.

On 30 May 2003, the Ministry of Finance issued a notice to the provincial and municipal governments instructing them to settle the amount with the Company by 31 December 2003. At present, the Company is in the process of negotiating with the relevant provincial and municipal governments to settle the amount. PICC Holding Company has undertaken to the Company that the amount will be fully recovered by the Company. Accordingly, no provision has been made against this amount as at 31 December 2003.

(ii) The amount due from the ultimate holding company is unsecured, interest-free and has no fixed repayment terms.

21. CAPITAL SECURITY FUND

In accordance with the PRC Insurance Law, the Company is required to maintain a deposit equivalent to 20% of its registered capital with banks designated by the China Insurance Regulatory Commission ("the CIRC") as a security fund. Based on the registered capital of the ultimate holding company, a bank deposit of RMB1,540 million was maintained as the security fund as at 31 December 2002. The use of the security fund is subject to the approval of the CIRC. The amount of this security fund has been increased to RMB2,228 million subsequent to the Company's initial public offering, representing 20% of the Company's current issued share capital.

22. FIXED ASSETS

	Land and buildings	Motor vehicles	Office equipment, furniture and fixtures	Total
	RMB million	*RMB million*	*RMB million*	*RMB million*
The Company				
Cost:				
Acquired pursuant to the Reorganisation	13,836	1,460	1,604	16,900
Additions	115	30	295	440
Transfers (note 23)	152	—	11	163
Disposals	—	(13)	(1)	(14)
At 31 December 2003	14,103	1,477	1,909	17,489
Accumulated depreciation:				
Acquired pursuant to the Reorganisation	(353)	(435)	(384)	(1,172)
Depreciation	(225)	(204)	(251)	(680)
Disposals	—	8	—	8
At 31 December 2003	(578)	(631)	(635)	(1,844)
Net book value:				
As 31 December 2003	13,525	846	1,274	15,645
Pro forma				
Cost or valuation:				
At 1 January 2003	13,828	1,460	1,548	16,836
Additions	135	36	359	530
Transfers (note 23)	152	—	11	163
Disposals	(12)	(19)	(9)	(40)
At 31 December 2003	14,103	1,477	1,909	17,489
Analysis of cost or valuation:				
At cost	389	64	826	1,279
Valuation - 2002	13,714	1,413	1,083	16,210
	14,103	1,477	1,909	17,489
Accumulated depreciation:				
At 1 January 2003	(116)	(116)	(78)	(310)
Depreciation	(472)	(524)	(564)	(1,560)
Disposals	10	9	7	26
At 31 December 2003	(578)	(631)	(635)	(1,844)
Net book value:				
As 31 December 2003	13,525	846	1,274	15,645
As 31 December 2002	13,712	1,344	1,470	16,526

22. FIXED ASSETS *(CONTINUED)*

As required by the relevant PRC rules and regulations with respect to the Reorganisation, the fixed assets of the Company as at 30 September 2002 were valued for each asset class by China Enterprise Appraisals Co., Ltd., independent professionally qualified valuers registered in the PRC, on a depreciated replacement cost basis or fair market valuation basis as appropriate. The surplus on revaluation of approximately RMB3,716 million was dealt with in reserves and was considered as part of the Company's acquisition cost of fixed assets upon the Reorganisation. The Company's properties were also valued separately as at 31 July 2003 by Sallmanns (Far East) Limited, independent professionally qualified valuers in Hong Kong who have among their staff Fellows of the Hong Kong Institute of Surveyors and the Royal Institution of Chartered Surveyors. The value arrived at by these valuers was approximately the same as that arrived at by the PRC valuers.

For the purpose of the pro forma financial statements, had the fixed assets been carried at historical cost less accumulated depreciation and impairment losses, their carrying amounts as at 31 December 2002 would have been approximately RMB11,813 million as follows:

	Pro forma 31 December 2002 *RMB million*
Land and buildings	9,698
Motor vehicles	760
Office equipment, furniture and fixtures	1,355
	11,813

The land and buildings are all located in the PRC. The land is held under lease terms ranging from 30 years to 70 years.

As at 31 December 2003, the title certificates of certain land and buildings (net book value: RMB1,062 million) are still in the name of the ultimate holding company, and the change of registration to the registration to the Company's current name is in progress.

23. CONSTRUCTION IN PROGRESS

	7 July to 31 December 2003 *RMB million*	Pro forma 2003 *RMB million*	Pro forma 2002 *RMB million*
As of beginning of the period/year	791	714	1,117
Additions	35	112	280
Transfers (note 22)	(163)	(163)	(636)
Distribution to the owner in connection with the Reorganisation	—	—	(47)
Impairment	(21)	(21)	—
As of end of the period/year	642	642	714

The buildings under construction are all located in the PRC and are held under medium term leases.

24. DEFERRED ACQUISITION COSTS

The movements in deferred acquisition costs during the period from 7 July 2003 to 31 December 2003 and for the year ended 31 December 2003 are as follows:

The Company	Gross *RMB million*	Reinsurance *RMB million*	Net *RMB million*
At 7 July 2003	3,219	(1,936)	1,283
Deferred acquisition costs	3,109	(1,681)	1,428
Amortisation	(2,946)	1,519	(1,427)
At 31 December 2003	3,382	(2,098)	1,284

Pro forma	Gross *RMB million*	Reinsurance *RMB million*	Net *RMB million*
At 1 January 2003	3,091	(2,015)	1,076
Deferred acquisition costs	6,242	(3,555)	2,687
Amortisation	(5,951)	3,472	(2,479)
At 31 December 2003	3,382	(2,098)	1,284

25. UNEARNED PREMIUM RESERVES

	31 December 2003 *RMB million*	Pro forma 31 December 2002 *RMB million*
Gross unearned premium reserves	**30,422**	28,053
Less: Unearned premium reserves - reinsurers' share	**(6,030)**	(7,104)
Net unearned premium reserves	**24,392**	20,949

Unearned premium reserves and loss and loss adjustment expense reserves (note 26) of the Company's commercial insurance business as at 31 December 2002 and 31 December 2003, respectively, were reviewed by a firm of independent internationally based consulting actuaries. Save for RMB1,985 million as at 31 December 2003 (2002: RMB1,600 million). All of the unearned premium reserves are expected to be realised within one year from the balance sheet date.

26. LOSS AND LOSS ADJUSTMENT EXPENSE RESERVES

	Gross loss and loss adjustment expense reserves *RMB million*	Reinsurance recoverable on unpaid losses *RMB million*	Net loss and loss adjustment expense reserves *RMB million*
The Company			
At 7 July 2003	17,467	(7,011)	10,456
Incurred loss and loss adjustment expenses	17,259	(3,330)	13,929
Loss and loss adjustment expenses paid	(16,770)	4,058	(12,712)
At 31 December 2003	17,956	(6,283)	11,673
Pro forma			
At 1 January 2003	16,597	(6,319)	10,278
Incurred loss and loss adjustment expenses	35,114	(7,444)	27,670
Loss and loss adjustment expenses paid	(33,755)	7,480	(26,275)
At 31 December 2003	17,956	(6,283)	11,673

Save for RMB1,801 million as at 31 December 2003 (2002: RMB1,816 million), all of the loss and loss adjustment expense reserves are expected to be settled within one year.

27. POLICYHOLDERS' DEPOSITS

Policyholders' deposits consist of interest-bearing and non-interest-bearing deposits placed by policyholders. The remaining maturities of policyholders' deposits are analysed as follows:

	31 December 2003	Pro forma 31 December 2002
	RMB million	*RMB million*
Due within 1 year	**1,964**	1,728
Due after 1 year but within 5 years	**4,430**	4,768
Due after 5 years or more	**2,896**	1,003
	7,326	5,771
	9,290	7,499

Certain commercial insurance policies offered by the Company require that the policyholders place a deposit with the Company which is refundable upon maturity or termination and bears no interest. Policy terms range from one year to perpetuity. A policyholder can terminate the insurance policy before the maturity date without penalties. The main feature of this insurance product is that the insurance coverage is fixed at the inception of the policy and remains in effect during the policy period or until terminated by the policyholder.

From 2002, the Company has underwritten policies of a new homeowners insurance product containing both insurance and investment features. Policyholders deposit a fixed principal amount which is only refundable upon the maturity of the policy of three years or five years and the policyholder receives a fixed rate of interest. Penalties on early termination are charged according to the terms stated in the insurance contract. The amounts of interest credited to policyholder deposits for the period from 7 July to 31 December 2003, and for each of the two years ended 31 December 2003 and 2002 were RMB65 million, RMB123 million and RMB54 million, respectively. The balances of this type of insurance deposit product as at 31 December 2003 and 31 December 2002 amounted to RMB6,142 million and RMB3,907 million, respectively.

28. PAYABLES TO REINSURERS

Payables to reinsurers are analysed as follows:

	31 December 2003	Pro forma 31 December 2002
	RMB million	*RMB million*
Reinsurance balances payable	1,132	1,252
Reinsurance funds withheld	846	1,051
	1,978	2,303

Payables to reinsurers as at 31 December 2003 and 31 December 2002 are due within three months from the balance sheet date or are repayable on demand. The reinsurance funds withheld as at 31 December 2003 and 31 December 2002 are repayable upon the expiration of the related reinsurance contracts.

29. ACCRUED INSURANCE PROTECTION FUND

The Company is obligated to pay into an insurance protection fund based on 1% of its annual retained premiums in accordance with the relevant PRC insurance law and regulations. No further provision is required once the accumulated balance has reached 6% of the Company's total assets determined in accordance with PRC GAAP. The amount provided for is payable to the CIRC to finance the resolution of failed insurance companies in the PRC and is required to be set aside by investments in debt securities issued by the central government of the PRC and placements of deposits with the four wholly state-owned national commercial banks.

The Company's accrued insurance protection amounts in accordance with the relevant PRC insurance law and regulations as at the balance sheet date is held in form of cash at banks.

The cash at banks is restricted for use until the accrual has been settled with the CIRC. The balance as at the balance sheet date represented the amounts accrued for since 1 October 2002 and the accrued related interest income.

All of the accrued insurance protection amounts is payable at the request of the CIRC.

Pursuant to the Reorganisation and with the approval from the CIRC and the consent of the State Council of the PRC, the entire amount of the accrued insurance protection fund as at 30 September 2002 of RMB2,192 million was extinguished. The extinguishment of the accrued insurance protection fund has been accounted for as a capital transaction in the pro forma statement of changes in equity for the year ended 31 December 2002. Accordingly, RMB1,893 million of investments in debt securities and RMB299 million of deposits with banks with original maturity of more than three months as at 30 September 2002 were released from the restrictions. The extinguishment of this liability did not relieve the Company's obligation to accrue for the insurance protection fund after the effective date of the Reorganisation.

30. OTHER LIABILITIES AND ACCRUALS

	31 December 2003 *RMB million*	Pro forma 31 December 2002 *RMB million*
Amounts due to ultimate holding company (note i)	616	—
Amounts due to a fellow subsidiary (note ii)	4	—
Salaries and staff welfare payables	1,549	1,553
Accrued expenses	964	1,107
Securities sold under agreements to repurchase	300	1,500
Accrued capital expenditure	178	1,232
Premiums received in advance	952	768
Others (note iii)	584	638
	5,147	6,798

(i) The amounts due to the ultimate holding company included a special dividend of RMB644.5 million which will be paid within 30 days following the date on which the Company publishes its 2003 audited financial statements (note 12). The other balances with the ultimate holding company are unsecured, interest free and have no fixed terms of repayment.

(ii) The amounts due to a fellow subsidiary are unsecured, interest-free and have no fixed terms of repayment.

(iii) As at 31 December 2002, the balance included bank loan balances of RMB9 million which were unsecured and repayable on demand, and bore interest at one year borrowing rate of the People's Bank of China.

31. DEFERRED TAX

The Company

The movements in deferred tax liabilities and assets during the period are as follows:

Deferred tax liabilities (in RMB million)

	Revaluation of trading securities	Deferred income recognition of trading investment securities	Deferred acquisition cost	Others	Total
At 7 July 2003	(24)	31	422	(5)	424
Deferred tax (credited)/charged to the profit and loss account during the period	53	(30)	2	36	61
Gross deferred tax liabilities at 31 December 2003	29	1	424	31	485

Deferred tax assets (in RMB million)

	Revaluation of not-trading securities	Depreciation of fixed assets	Total
At 7 July 2003	19	—	19
Deferred tax (charged)/credited to the profit and loss account /reserves during the period	(16)	149	133
Gross deferred tax assets at 31 December 2003	3	149	152
Net deferred tax liabilities at 31 December 2003			333

There are no income tax consequences attaching to the payment of dividends by the Company to its shareholders.

The change in respect of the deferred tax asset recognised arising from the revaluation of non-trading securities is taken to the non-trading investment securities revaluation reserve.

31. DEFERRED TAX *(CONTINUED)*

Pro forma

The movements in deferred tax liabilities and assets during the year are as follows:

Deferred tax liabilities (in RMB million)

	Revaluation of trading securities	Deferred income recognition of trading investment securities	Deferred acquisition cost	Others	Total
At 1 January 2003	(37)	39	355	—	357
Deferred tax (credited)/charged to the profit and loss account during the year	66	(38)	69	31	128
Gross deferred tax liabilities at 31 December 2003	29	1	424	31	485

Deferred tax assets (in RMB million)

	Revaluation of not-trading securities	Tax value of of losses carried forward	Depreciation of fixed assets	Total
At 1 January 2003	46	491	—	537
Deferred tax (charged)/credited to the profit and loss account /reserves during the year	(43)	(491)	149	(385)
Gross deferred tax assets at 31 December 2003	3	—	149	152
Net deferred tax liabilities at 31 December 2003				333

There are no income tax consequences attaching to the payment of dividends by the Company to its shareholders.

The change in respect of the deferred tax asset recognised arising from the revaluation of non-trading securities is taken to the non-trading investment securities revaluation reserve.

31. DEFERRED TAX *(CONTINUED)*

Pro forma

Deferred tax liabilities (in RMB million)

	Deferred income recognition of trading investment securities	Deferred acquisition cost	Total
At 1 January 2002	8	237	245
Deferred tax charged to the profit and loss account during the year	31	118	149
Gross deferred tax liabilities at 31 December 2002	39	355	394

Deferred tax assets (in RMB million)

	Revaluation of trading securities	Revaluation of non-trading securities	Tax value of losses carried forward	Provision for other receivables and long term investments	Impairment loss on fixed assets	Provision for premium receivables and agents' balances	Total
At 1 January 2002	1	1	—	1,738	281	39	2,060
Deferred tax (charged)/credited to the profit and loss account/ reserves during the year	36	45	491	(1,738)	(281)	(39)	(1,486)
Gross deferred tax assets at 31 December 2002	37	46	491	—	—	—	574
Net deferred tax assets at 31 December 2002							180

There are no income tax consequences attaching to the payment of dividends by the Company to its shareholders.

The change in respect of the deferred tax asset recognised arising from the revaluation of non-trading securities is taken to the non-trading investment securities revaluation reserve.

32. ISSUED CAPITAL

	31 December 2003	Pro forma 31 December 2002
	RMB million	*RMB million*
Shares		
Registered, issued and fully paid:		
7,685,820,000 domestic shares of RMB1.00 each	**7,686**	—
3,455,980,000 H Shares of RMB1.00 each	**3,456**	—
	11,142	—

The Company does not have a share option scheme.

A summary of the transactions from 7 July 2003 to 31 December 2003 analysing the movements in the Company's share capital is as follows:

	Number of shares in issue		Issued share capital		
	Domestic shares	H Shares	Domestic shares	H Shares	Total
			RMB'000	*RMB'000*	*RMB'000*
Upon incorporation on 7 July 2003 (a)	8,000,000,000	—	8,000,000	—	8,000,000
Issue of H Shares upon listing (b)	—	2,732,000,000	—	2,732,000	2,732,000
Sale of domestic shares by the ultimate holding company and conversion into H Shares upon listing (b)	(273,200,000)	273,200,000	(273,200)	273,200	—
Issue of H Shares upon exercise of over-allotment option (c)	—	409,800,000	—	409,800	409,800
Sale of domestic shares by ultimate holding company and conversion into H Shares upon exercise of over-allotment option (c)	(40,980,000)	40,980,000	(40,980)	40,980	—
At 31 December 2003	7,685,820,000	3,455,980,000	7,685,820	3,455,980	11,141,800

32. ISSUED CAPITAL *(CONTINUED)*

(a) As part of the Reorganisation (note 1), the Company issued 8,000 million domestic shares at a par value of RMB1.00 each to PICC Holding Company, and the Company's registered and paid-up capital became RMB8,000 million accordingly.

(b) The Company's shares were listed on the HKSE on 6 November 2003 and 3,005.2 million H Shares with a par value of RMB1.00 each were issued to the public by way of a placement and offer at a price HK$1.80 (equivalent to approximately RMB1.92) per share. The domestic shares and the H Shares rank pari passu with each other in all respects and, in particular, rank equally for all dividends or distributions declared, paid or made except for the distribution of the special dividends set out in note 12.

(c) The Company's shares were oversubscribed in its initial public offering and hence a further 450.8 million H Shares with a par value of RMB1.00 each were issued to the public pursuant to an over-allotment option.

33. SUBORDINATED LOAN

On 10 October 2003, the Company signed a loan agreement with China Development Bank which advanced a subordinated loan of RMB2,000 million to the Company for the purpose of enhancing the Company's solvency position. The loan is unsecured, bears interest at 90% to 110% of the PBOC's five-year borrowing interest rate per annum and is repayable in November 2023.

34. NOTES TO THE CASH FLOW STATEMENT

(a) Major non-cash transactions

	7 July to 31 December 2003 *RMB million*
Net assets acquired upon the Reorganisation (note 1 to the financial statements)	
Investments in securities	2,331
Trading securities	11,896
Deposits with banks and other financial institutions with original maturity of more than 3 months	10,344
Cash and cash equivalents	17,797
Premiums receivables and agents' balances, net	2,874
Unearned premium reserves - reinsurers' share	7,162
Receivables from reinsurers	463
Reinsurance recoverable on unpaid losses	7,011
Prepayments and other receivables	2,388
Fixed assets	15,728
Construction in progress	791
Deferred acquisition costs	1,283
Other non-current assets	248
Unearned premium reserves	(33,112)
Loss and loss adjustment expenses reserves	(17,467)
Provision for premium deficiency	(1)
Policyholders' deposits	(8,021)
Payables to reinsurers	(2,309)
Accrued insurance protection	(340)
Tax payables	(44)
Other liabilities and accruals	(6,922)
Deferred tax liabilities	(405)
	11,695
Satisfied by:	
Shares issued	8,000
Share premium account	2,271
Other reserves	1,424
	11,695

34. NOTES TO THE CASH FLOW STATEMENT *(CONTINUED)*

(b) An analysis of the net inflow of cash and cash equivalents in respect of the net assets acquired upon the Reorganisation is as follow:

	7 July to 31 December 2003 *RMB million*
Cash and cash equivalents acquired	17,797
Net cash inflow in respect of the net assets acquired upon the Reorganisation	17,797

35. CONTINGENT LIABILITIES

(a) Pursuant to the Reorganisation, except for liabilities constituting or arising out of or relating to business undertaken by the Company after the Reorganisation, no other liabilities were assumed by the Company and the Company is not liable, whether severally or jointly and severally, for debts and obligations incurred prior to the Reorganisation. The ultimate holding company has also undertaken to indemnify the Company in respect of any loss or damage incurred in connection with or arising from the transfer of the assets and liabilities to the Company in the Reorganisation, any loss or damage suffered or incurred by the Company in relation to the novation of insurance contracts and reinsurance contracts from the ultimate holding company to the Company, and as a result of any breach by the ultimate holding company of any provision of the Reorganisation.

(b) Owing to the nature of insurance business, the Company is involved in legal proceedings in the ordinary course of business, including being the plaintiff or the defendant in litigation and arbitration. Such legal proceedings mostly involve claims on the Company's insurance policies. While the outcome of such contingencies, lawsuits or other proceedings cannot be determined at present, management believes that any resulting liabilities will not have a material adverse effect on the financial position or operating results of the Company.

36. SOLVENCY MARGIN

As at 31 December 2003, the solvency margin of the Company computed in accordance with the CIRC's regulations was as follows:

	31 December 2003	Pro forma 31 December 2002
	RMB million	*RMB million*
Solvency margin calculated pursuant to the CIRC's regulations	9,014	2,802
Statutory minimum requirement	(7,018)	(5,943)
Surplus/(deficit)	1,996	(3,141)

As at 31 December 2002, the Company's solvency margin was less than the minimum statutory level by approximately RMB3,141 million, and the Company has duly notified to the CIRC. On 4 July 2003, the Company obtained a waiver from the CIRC in relation to its compliance with the solvency margin requirement and regulatory benchmarks. Pursuant to the waiver, the CIRC agreed not to bring any retrospective action against the Company with respect to its non-compliance prior to its listing. In addition, the CIRC has also agreed to grant the Company a grace period of three years after its listing, within which period the CIRC will not take any regulatory action against the Company if the Company is unable to comply with its solvency margin requirement and more than 4 out of a total of 11 regulatory benchmarks. If a P&C insurance company incorporated in the PRC fails to meet more than 4 of the 11 regulatory benchmarks, it is required to explain the reasons for its non-compliance and may be subject to investigation by the CIRC regarding its solvency margin. As a result of the issue of H Shares during the year, the Company's solvency margin exceeded the minimum statutory level by RMB1,996 million as at 31 December 2003. The Company failed to meet less than 4 of the 11 regulatory benchmarks as at 31 December 2003.

37. OPERATING LEASE ARRANGEMENTS

(a) As lessor

The Company leases its land and buildings under operating lease arrangements, with leases negotiated for terms ranging from one to four years. The terms of the leases generally also require the tenants to provide for periodic rent adjustments according to the then prevailing market conditions.

At 31 December 2003, the Company had total future minimum lease receivables under non-cancellable operating leases with its tenants falling due as follows:

	31 December 2003	Pro forma 31 December 2002
	RMB million	*RMB million*
Within one year	21	9
In the second to fifth years, inclusive	49	7
	70	16

(b) As lessee

The Company leases certain of its land and buildings and motor vehicles under operating lease arrangements. Leases for properties are negotiated for terms ranging from one to twenty years, and those for motor vehicles for terms ranging between one to three years.

At 31 December 2003, the Company had total future minimum lease payments under non-cancellable operating leases falling due as follows:

	31 December 2003	Pro forma 31 December 2002
	RMB million	*RMB million*
Within one year	296	72
In the second to fifth years, inclusive	681	141
After five years	54	64
	1,031	277

38. COMMITMENTS

In addition to the operating lease commitments detailed in note 37(b) above, the Company had the following capital commitments at the balance sheet date:

	31 December 2003	Pro forma 31 December 2002
	RMB million	*RMB million*
Contracted, but not provided for	**81**	539
Authorised, but not contracted for	**236**	22
	317	561

39. RELATED PARTY TRANSACTIONS

The Company conducts businesses with enterprises directly or indirectly owned or controlled by the PRC government ("state-owned enterprises"). Furthermore, the PRC government itself represents a significant customer of the Company both directly through its numerous authorities and indirectly through its numerous affiliates and other organisations. The Company considers that the sale of insurance products to the PRC government authorities and affiliates and other state-owned enterprises are in the ordinary and normal course of business in the PRC and has not disclosed such transactions as related party transactions.

In addition to the transactions and balances detailed elsewhere in these financial statements, the Company and PICC Holding Company, PICC Asset Management Company Limited and American International Group ("AIG"), a strategic shareholder of the Company, entered into a number of agreements during the period in connection with the Reorganisation. These agreements impact the results of the operations of the Company beginning from the respective dates. The terms of the principal agreements are summarised as follows:

		7 July to 31 December 2003
	Notes	*RMB million*
Property rental expenses to PICC Holding Company	(a)	106
Property rental income from PICC Holding Company	(a)	5
Motor vehicle rental expenses to PICC Holding Company	(b)	11
Motor vehicle rental income from PICC Holding Company	(b)	2
Management fee to PICC Asset Management Company Limited	(c)	4
Services fee income from PICC Holding Company	(d)	2
Special dividends to PICC Holding Company (note 12)		650

39. RELATED PARTY TRANSACTIONS *(CONTINUED)*

(a) The Company entered into a Property Leasing Agreement with PICC Holding Company on 9 October 2003 under which the Company rented certain properties from PICC Holding Company and PICC Holding Company rented certain properties from the Company. The rental charges in respect of these properties are based on market rates. The term of the Property Leasing Agreement is four years and it became effective on 7 July 2003.

(b) The Company entered into a Motor Vehicle Rental Agreement with PICC Holding Company on 9 October 2003 under which the Company rented certain motor vehicles from PICC Holding Company and PICC Holding Company rented certain motor vehicles from the Company. The rental charges for the motor vehicles are based on market rates. The term of the Motor Vehicle Rental Agreement is four years and it became effective on 7 July 2003.

(c) On 10 October 2003, the Company and PICC Asset Management Company Limited, a wholly-owned subsidiary of PICC Holding, entered into an asset management agreement which became effective on the same date. Pursuant to the asset management agreement, PICC Assets Management Company Limited provides investment management services in respect of certain cash assets of the Company. The Company pays an annual management fee to PICC Asset Management Company Limited, which is calculated based on the average daily net asset value of the assets under the management of PICC Asset Management Company Limited in a particular year and the applicable annual rate. The term of the asset management agreement is four years.

(d) The Company entered into an Information System Services Agreement with PICC Holding Company on 9 October 2003 pursuant to which the Company agreed to provide PICC Holding Company with certain information services, including (i) facilities leasing services and network services; (ii) software and application services; (iii) other computer-related facilities maintenance services; and (iv) other information system services agreed by both parties.

The services fee payable to the Company by PICC Holding Company are to be no less than market rates, and are determined with reference to the costs associated with the labour and the equipment required to provide the services and support pursuant to the Information System Services Agreement between the Company and PICC Holding Company. The term of the Information System Services Agreement is four years.

(e) The Company entered into a Technical Assistance and Co-operation Agreement with AIG on 29 September 2003, pursuant to which the Company and one of AIG's wholly-owned subsidiaries will co-operate in the development of accident and health insurance products and the Company will cede quota share reinsurance at fixed cession percentages. This obligation will be reflected in a separate reinsurance agreement, which will be entered in the Company's ordinary and usual course of business. The intention of the parties is for the co-operation to continue indefinitely. Either party may request to review the key terms of the co-operation six months prior to the 15th anniversary of the date of the Technical Assistance and Co-operation Agreement and every 15 years thereafter, and unless the parties disagree to these terms, the agreement automatically renews for a further 15 years. There was no reinsurance income from/expense to AIG for the period from 7 July to 31 December 2003.

39. RELATED PARTY TRANSACTIONS *(CONTINUED)*

Other than the above agreements, the Company also entered into a Trademark Licence Agreement with PICC Holding Company on 9 October 2003 under which the Company has been granted the right to use the trademark bearing the "PICC" logo. The use of the trademark is on a royalty-free basis. The term of the Trademark Licence Agreement is 10 years and the agreement automatically renews for a further 10 years after the expiry of each 10 year term.

The transactions mentioned in (a) to (d) above also constitute connected transactions under the Listing Rules. Such transactions were exempted from disclosure by press notices under a waiver obtained from the HKSE.

40. APPROVAL OF THE FINANCIAL STATEMENTS

The financial statements were approved and authorised for issue by the board of directors on 23 April 2004.