**1. GROUP REORGANISATION**

The Company was incorporated in the Cayman Islands as an exempted company with limited liability under the Companies Law (2000 Revision) of the Cayman Islands on 25 September 2000. Pursuant to a reorganisation scheme to rationalise the structure of the Group on 28 November 2000 (the "Reorganisation") in preparation for the public listing of the Company's shares on The Stock Exchange of Hong Kong Limited (the "Stock Exchange"), the Company became the holding company of the companies now comprising the Group. This was accomplished by acquiring the entire issued share capital of Global Success Properties Limited ("GSPL"), the then holding company of the subsidiaries listed in note 16 to the financial statements, in consideration for the allotment and issue of Company's shares, credited as fully paid, to the former shareholders of GSPL. Further details of the Reorganisation are set out in note 24 to the financial statements and in the Company's prospectus dated 5 December 2000.

**2. BASIS OF PRESENTATION**

The Reorganisation involved companies under common control. The consolidated financial statements have been prepared using the merger basis of accounting in accordance with Statement of Standard Accounting Practice ("SSAP") No. 2.127 "Accounting for Group Reconstructions" as a result of the Reorganisation. Under this basis, the Company has been treated as the holding company of its subsidiaries for the financial years presented rather than from the date of its acquisition of the subsidiaries. Accordingly, the consolidated results of the Group for the years ended 31 December 1999 and 2000 include the results of the Company and its subsidiaries with effect from 1 January 1999 or since their respective dates of incorporation or establishment, where this is a shorter period. The comparative consolidated balance sheet as at 31 December 1999 has been prepared on the basis that the existing Group had been in place at that date.

In the opinion of the directors, the consolidated financial statements prepared on the above basis present more fairly the results and the state of affairs of the Group as a whole.

All significant intercompany transactions and balances within the Group have been eliminated in the preparation of the consolidated financial statements.

Comparative amounts have not been presented for the Company because the Company did not exist at 31 December 1999.

**3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Basis of preparation**

These financial statements have been prepared in accordance with SSAPs, 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, modified with respect to the periodic remeasurement of certain fixed assets and investment properties, as further explained below.

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

**Subsidiaries**

A subsidiary is a company in which the Company, directly or indirectly, controls more than 50% of its voting power or controls the composition of its board of directors.

Interests in subsidiaries are stated at cost unless, in the opinion of the directors, there have been permanent diminutions in values, when they are written down to values determined by the directors.

**Investment properties**

Investment properties are interests in land and buildings in respect of which construction work and development have been completed and which are intended to be held on a long term basis for their investment potential, any rental income being negotiated at arm's length. Such properties are not depreciated except where the unexpired term of the lease is 20 years or less, in which case depreciation is provided on the carrying amount over the remaining term of the lease, and are stated at their open market values on the basis of annual professional valuations.

Changes in the values of the investment properties are dealt with as movements in the investment properties revaluation reserve. If the total of this reserve is insufficient to cover a deficit, on a portfolio 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.

Upon the disposal of an investment property, the relevant portion of the investment property revaluation reserve realised in respect of previous valuations is released to the profit and loss account.

**Fixed assets and depreciation**

Fixed assets are stated at cost or valuation less accumulated depreciation.

The original 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 the 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 the fixed asset, the expenditure is capitalised as an additional cost of that asset.

Changes in the values of fixed assets, other than investment properties, are dealt with as movements in the assets revaluation reserve. If the 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. A subsequent revaluation increase is recognised as income to the extent that it reverses a revaluation deficit of the same asset previously charged to the profit and loss account. On disposal of a revalued asset, the relevant portion of the assets revaluation reserve realised in respect of previous valuations is transferred to retained profits as a movement in reserves.

### 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

**Fixed assets and depreciation (continued)**

Depreciation is calculated on the straight-line basis to write off the cost or valuation of each asset over its estimated useful life. The principal annual rates used for this purpose are as follows:

| | |
|---|---|
| Medium term leasehold land and buildings | Over the lease terms |
| Leasehold improvements | 5% or over the lease terms, whichever is shorter |
| Plant and machinery | 10% |
| Furniture, fixtures and computer equipment | 20% - 30% |
| Motor vehicles | 20% |

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

All of the Group's fixed assets prior to the listing of the Company's shares on the Stock Exchange were stated at cost less accumulated depreciation. The financial effect involved in the remeasurement of certain of the Group's fixed assets on a valuation basis principally involving the incorporation of a surplus on revaluation in the amount of HK$11,001,000, which is recognised in the asets revaluation reserve. Further datails of the change in accounting policy for the remeasurement of the Group's fixed assets are set out in note 14 below.

**Inventories**

Inventories are stated at the lower of cost and net realisable value. Cost is determined on the first-in, first-out basis and, in the case of work in progress and finished goods, comprises direct materials, direct labour and an appropriate proportion of manufacturing overheads. Net realisable value is based on estimated selling prices less any estimated costs to be incurred to completion and disposal.

**Deferred tax**

Deferred tax is provided, using the liability method, on all significant timing differences in the recognition of revenue and expenses for tax and for financial reporting purposes, to the extent it is probable that the liability will crystallise in the foreseeable future. A deferred tax asset is not recognised unless its realisation is assured beyond reasonable doubt.

**Revenue recognition**

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

(a) from the sales of goods, when the significant risks and rewards of ownership have been transferred to the buyer, provided that the Group maintains neither managerial involvement to the degree usually associated with ownership, nor effective control over the goods sold;

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

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

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

**Operating leases**

Leases where substantially all the rewards and risks of ownership of assets remain with the lessor are accounted for as operating leases. The rentals applicable to such operating leases are charged to the profit and loss account on the straight-line basis over the lease terms.

**Research and development costs**

All research costs are charged to the profit and loss account as incurred.

Expenditure incurred on projects to develop new products is capitalised and deferred only when the projects are clearly defined; the expenditure is separately identifiable and can be measured reliably; there is reasonable certainty that the projects are technically feasible; and the products have commercial value. Product development expenditure which does not meet these criteria is expensed when incurred.

Deferred development costs are amortised, using the straight-line method, over the expected useful lives of the products, subject to a maximum period of five years, commencing in the year when the products are put into commercial production.

**Pension costs**

The Group operates a defined contribution Mandatory Provident Fund retirement benefits scheme (the “Hong Kong Scheme”) under the Mandatory Provident Fund Schemes Ordinance, for all of those employees who are eligible to participate in the Hong Kong Scheme. The Hong Kong Scheme became effective from 1 December 2000. Contributions are made based on a percentage of the employees' basic salaries and are charged to the profit and loss account as they become payable in accordance with the rules of the Hong Kong Scheme. The assets of the Hong Kong Scheme are held separately from those of the Group in an independently administered fund. The Group's employer contributions vest fully with the employees when contributed into the Hong Kong Scheme, except for the Group's employer voluntary contributions, which are refunded to the Group when the employee leaves employment prior to the contributions vesting fully, in accordance with the rules of the Hong Kong Scheme.

Before the Hong Kong Scheme became effective, the Group operated a defined contribution retirement benefits scheme for those employees who were eligible to participate in the scheme. This scheme operated in a similar way to the Mandatory Provident Fund retirement benefits scheme, except that when an employee left the scheme prior to his/her interest in the Group's employee contributions vesting fully, the ongoing contributions payable by the Group were reduced by the relevant amount of forfeited contributions. This scheme was terminated with effect from 1 December 2000.

Pursuant to the relevant regulations of the PRC government, a subsidiary of the Company operating in the PRC participates in a local municipal government retirement benefits scheme (the “PRC Scheme”), whereby the subsidiary is required to make contributions, as calculated under the rules specified by the relevant PRC local government authorities, to the PRC Scheme to fund their retirement benefits. The local municipal government undertakes to assume the retirement benefits obligations of all existing and future retired employees of the subsidiary. The only obligation of the Group with respect to the PRC Scheme is to pay the ongoing required contributions under the PRC Scheme mentioned above. Contributions under the PRC Scheme are charged to the profit and loss account as incurred. There are no provisions under the PRC Scheme whereby forfeited contributions may be used to reduce future contributions.

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

**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 financing 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.

**Foreign currencies**

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

On consolidation, the financial statements of overseas subsidiaries are translated into Hong Kong dollars at the applicable rates of exchange ruling at the balance sheet date. The resulting translation differences are included in the exchange fluctuation reserve.

**Trade receivables**

Trade receivables, which generally have credit terms of 30-90 days, are recognised and carried at the original invoice amount. An estimate for doubtful debts is made and deducted when collection of the full amount is no longer probable. Bad debts are written-off as incurred.

**Cash equivalents**

For the purpose of the consolidated cash flow statement, cash equivalents represent short term highly liquid investments which are readily convertible into known amounts of cash and which were within three months of maturity when acquired, less advances from banks repayable within three months from the date of the advance. For the purpose of balance sheet classification, cash equivalents represent cash, bank balances and deposits, which are not restricted as to use.

4. **CORPORATE INFORMATION**

The principal activity of the Company is investment holding. The principal activities of the Company's subsidiaries are set out in note 16 below. There were no changes in the nature of the subsidiaries' principal activities during the year.

5. **RELATED PARTY TRANSACTIONS**

During the year, the Group had the following transactions with related parties in addition to those disclosed elsewhere in the financial statements:

(i) Mr. Lau Jin Wei, Jim ("Mr. Lau") and Mr. Choi Woon Man ("Mr. Choi"), directors of the Company, executed personal guarantees for banking facilities granted to the Group at nil consideration;

(ii) A property located in Hong Kong and owned by Mr. Choi was pledged to secure certain banking facilities granted to the Group at nil consideration;

**5. RELATED PARTY TRANSACTIONS (continued)**

(iii) On 3rd April, 2000, a trademark transfer agreement was entered into between the Group and Shanghai Excellent Match Cosmetics Co. Ltd. ("SEMC"), a company controlled by Ms. Wong Wai Kwan, Connie, a director of the Company, under which five registered trademarks owned by SEMC were to be transferred to the Group at a consideration of RMB1.00 (approximately HK$0.93). The registration of the transfer of the above trademarks to the Group was completed on 28 September 2000; and

(iv) The Group made advances to Mr. Lau, further details of which are set out in note 21. The balance was fully settled in November 2000, before the public listing of the Company's shares on the Stock Exchange.

Upon the listing of the Company's shares on 18 December 2000, the personal guarantees and security provided by Mr. Lau and Mr. Choi, as detailed in (i) and (ii) above, were released and replaced by corporate guarantees of the Company and the pledge of the Company's bank deposits as set out in note 23.

**6. TURNOVER AND REVENUE**

Turnover represents the net invoiced value of goods sold, after allowances for returns and trade discounts. All significant intra-group transactions have been eliminated on consolidation.

An analysis of turnover and revenue is as follows:

| | 2000<br>HK$'000 | 1999<br>HK$'000 |
|---|---|---|
| Turnover-sales of goods | 188,734 | 106,547 |
| Other revenue: | | |
| Interest income | 576 | 2 |
| Rental income | 1,529 | 1,248 |
| Sales of raw materials | 1,108 | - |
| Gain on disposal of fixed assets | 12 | - |
| | 3,225 | 1,250 |
| Total revenue | 191,959 | 107,797 |