



# Notes to Financial Statements

31 December 2001

## 1. CORPORATE INFORMATION AND UPDATE

During the year, the Group was involved in the processing and sale of semi-finished and finished leather, the design, manufacture and sale of leather ware products, the sale of merchandise and the manufacture and sale of packaging materials.

On 22 December 2000, Guangdong Investment Limited ("GDI", and together with its subsidiaries referred to as the "GDI Group"), the Company's immediate holding company, completed the acquisition of an 81% equity interest in GH Water Supply (Holdings) Limited ("GH Water") (the "Acquisition") from GDH Limited, which is a wholly-owned subsidiary of 廣東粵港投資控股有限公司 (Guangdong Yue Gang Investment Holdings Company Limited) ("Yue Gang Investment"), a company established by the Guangdong Provincial Government in Mainland China. GH Water holds a 99% interest in Guangdong Yue Gang Water Supply Company Limited which owns the Dongshen Water Supply Project that generates revenue mainly from the provision and supply of natural water to Hong Kong. The acquisition formed part of the restructuring of Guangdong Enterprises (Holdings) Limited ("GDE", the then substantial shareholders of GDI) and its subsidiaries (the "GDE Group") (the "GDE Restructuring").

Upon GDI's completion of the Acquisition, GDI became a subsidiary of Yue Gang Investment and the GDI Group's Debt Restructuring, including the Group, was completed whereby, amongst other things, a Tannery Override Agreement dated 22 December 2000 (the "TOA") was entered into between the Company and its bank creditors and effected.

Pursuant to the TOA, inter alia, the Group was required to repay approximately HK\$108 million (2000: HK\$197 million), all of the Group's existing non-PRC bank debts as at 31 December 2001, by no later than 31 December 2003. The TOA operated by way of a formal standstill, but override provisions permit creditors to terminate the restructuring schemes and revert to the terms of the existing loan agreements upon the occurrence of events of default. Accordingly, the Group's bank borrowings as at 31 December 2001 and 2000 have been reclassified according to the repayment schedule as contained in the TOA.

Subsequent to the balance sheet date, on 31 January 2002, the Group repaid the existing non-PRC bank debts of HK\$108 million as at 31 December 2001 partially through using the Group's own resources of HK\$58 million while the balance of the repayment was financed by a new bank loan of HK\$50 million. Accordingly, the TOA was terminated and all the provisions prescribed in the TOA were released. Details of the arrangement of the new bank loan are further detailed in note 38(a) to the financial statements.

In the opinion of the Directors, the ultimate holding company of the Company as at 31 December 2001 is Yue Gang Investment.



## Notes to Financial Statements *(Cont'd)*

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### 2. IMPACT OF NEW AND REVISED STATEMENTS OF STANDARD ACCOUNTING PRACTICE ("SSAPs")

The following recently-issued and revised SSAPs and related Interpretations are effective for the first time for the current year's financial statements:

- SSAP 9 (Revised): "Events after the balance sheet date"
- SSAP 14 (Revised): "Leases"
- SSAP 26: "Segment reporting"
- SSAP 28: "Provisions, contingent liabilities and contingent assets"
- SSAP 29: "Intangible assets"
- SSAP 30: "Business combinations"
- SSAP 31: "Impairment of assets"
- SSAP 32: "Consolidated financial statements and accounting for investments in subsidiaries"
- Interpretation 12: "Business combinations – subsequent adjustment of fair values and goodwill initially reported"
- Interpretation 13: "Goodwill – continuing requirements for goodwill and negative goodwill previously eliminated against/credited to reserves"

These SSAPs prescribe new accounting measurement and disclosure practices. The major effects on the Group's accounting policies and on the amounts disclosed in these financial statements of adopting these SSAPs are summarised as follows:

SSAP 9 (Revised) prescribes which type of events occurring after the balance sheet date require adjustment to the financial statements, and which require disclosure, but no adjustment. Its principal impact is that the proposed final dividend which is not declared and approved until after the balance sheet date, is no longer recognised as a liability at the balance sheet date, but is disclosed as an allocation of retained earnings on a separate line within the capital and reserves section of the balance sheet. This has had no impact on the preparation of these financial statements.

SSAP 14 (Revised) prescribes the basis for lessor and lessee accounting for finance and operating leases, and the required disclosures in respect thereof. Certain amendments have been made to the SSAP's previous accounting measurement treatments, which may be accounted for retrospectively or prospectively, in accordance with the requirements of the SSAP. This revised SSAP has been applied prospectively and its requirements have not had a material effect on the amounts previously recorded in the financial statements, therefore no prior year adjustment has been required. The disclosure changes under this SSAP have resulted in changes to the detailed information disclosed for operating leases, which are further detailed in note 32 to the financial statements.



## Notes to Financial Statements *(Cont'd)*

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### 2. IMPACT OF NEW AND REVISED STATEMENTS OF STANDARD ACCOUNTING PRACTICE ("SSAPs") (Cont'd)

SSAP 26 prescribes the principles to be applied for reporting financial information by segment. It requires that management assesses whether the Group's predominant risks or returns are based on business segments or geographical segments and determines one of these bases to be the primary segment information reporting format, with the other as the secondary segment information reporting format. The impact of this SSAP is the inclusion of significant additional segment reporting disclosures which are set out in note 4 to the financial statements.

SSAP 28 prescribes the recognition criteria and measurement bases to apply to provisions, contingent liabilities and contingent assets, together with the required disclosures in respect thereof. This SSAP has had no impact on previously reported amounts in these financial statements. However, provisions are now disclosed as a separate line item on the face of the balance sheet (see note 28 to the financial statements) and the disclosures in respect thereof have been revised to include the new required additional disclosures.

SSAP 29 prescribes the recognition and measurement criteria for intangible assets, together with the disclosure requirements. The adoption of this SSAP has resulted in no change to the previously adopted accounting treatment for intangible assets and the additional disclosures that it requires have not been significant for these financial statements. The SSAP does, however, require that impairment losses on intangible assets are aggregated with the accumulated amortisation (see note 13), whereas previously they were deducted from the cost of the relevant asset. This disclosure reclassification has had no effect on the net carrying amount of intangible assets in the balance sheet.

SSAP 30 prescribes the accounting treatment for business combinations, including the determination of the date of acquisition, the method for determining the fair values of the assets and liabilities acquired, and the treatment of goodwill or negative goodwill arising on acquisition. The SSAP requires the disclosure of goodwill in the non-current assets section of the consolidated balance sheet. It requires that goodwill is amortised to the consolidated profit and loss account over its estimated useful life. Interpretation 13 prescribes the application of SSAP 30 to goodwill arising from acquisitions in previous years which remains eliminated against consolidated reserves. The adoption of the SSAP and Interpretation has not resulted in a prior year adjustment, for the reasons detailed in note 14 to the financial statements. The required new additional disclosures are included in note 14 to the financial statements.



## **Notes to Financial Statements** *(Cont'd)*

31 December 2001

### **2. IMPACT OF NEW AND REVISED STATEMENTS OF STANDARD ACCOUNTING PRACTICE ("SSAPs") (Cont'd)**

SSAP 31 prescribes the recognition and measurement criteria for impairments of assets. The SSAP is required to be applied prospectively and therefore, has had no effect on amounts previously reported in prior year financial statements.

SSAP 32 prescribes the accounting treatment and disclosures for the preparation and presentation of consolidated financial statements, and has had no impact on the preparation of these financial statements.

In addition to the above new and revised SSAPs and related Interpretations, certain minor revisions to SSAP 17 "Property, plant and equipment" became effective for the first time for the current year's financial statements. The only significant effect of these revisions is that SSAP 17 requires that impairment losses on fixed assets are aggregated with accumulated depreciation in note 12 to the financial statements, whereas previously they were deducted from the cost of the relevant asset. This disclosure reclassification has had no effect on the net carrying amount of fixed assets in the balance sheet.

### **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 Companies Ordinance. They have been prepared under the historical cost convention, except for the periodic remeasurement of investment properties and leasehold land and buildings, as further explained below.

#### **Basis of consolidation**

The consolidated financial statements include the financial statements of the Company and its subsidiaries for the year ended 31 December 2001. The results of subsidiaries acquired or disposed of during the year are consolidated from or to their effective dates of acquisition or disposal, respectively. All significant intra-group transactions and balances within the Group are eliminated on consolidation.



## **Notes to Financial Statements** *(Cont'd)*

31 December 2001

### **3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Cont'd)**

#### **Subsidiaries**

A subsidiary is a company in which the Company, directly or indirectly, controls more than half of its voting power or issued share/registered capital or controls the composition of its board of directors.

The Company's interests in subsidiaries are stated at cost less any impairment losses.

#### **Associates**

An associate is a company, not being a subsidiary or a jointly-controlled entity, in which the Group has a long term interest of generally not less than 20% of the equity voting rights and over which it is in a position to exercise significant influence.

The Group's share of the post-acquisition results and reserves of associates is included in the consolidated profit and loss account and consolidated reserves, respectively. The Group's interests in associates are stated in the consolidated balance sheet at the Group's share of net assets under the equity method of accounting, less any impairment losses.

Goodwill arising from the acquisition of associates, which was not previously eliminated against reserves, is included as part of the Group's interests in associates.

#### **Joint venture companies**

A joint venture company is a company set up by contractual arrangement, whereby the Group and other parties undertake an economic activity. The joint venture company operates as a separate entity in which the Group and the other parties have an interest.

The joint venture agreement between the venturers stipulates the capital contributions of the joint venture parties, the duration of the joint venture and the basis on which the assets are to be realised upon its dissolution. The profits and losses from the joint venture company's operations and any distributions of surplus assets are shared by the venturers, either in proportion to their respective capital contributions, or in accordance with the terms of the joint venture agreement.



## Notes to Financial Statements *(Cont'd)*

31 December 2001

### 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

#### Joint venture companies (Cont'd)

A joint venture company is treated as

- (a) a subsidiary, if the Company has unilateral control over the joint venture company; or
- (b) an associate, if the Company does not have unilateral or joint control, but holds generally not less than 20% of the joint venture company's registered capital and is in a position to exercise significant influence over the joint venture company.

#### Goodwill

Goodwill arising on the acquisition of subsidiaries represents the excess of the cost of the acquisition over the Group's share of the fair values of the identifiable assets and liabilities acquired as at the date of acquisition.

Goodwill arising on acquisition is recognised in the consolidated balance sheet as an asset and amortised on the straight-line basis over its estimated useful life. In the case of associates, any unamortised goodwill is included in the carrying amount thereof, rather than as a separately identified asset on the consolidated balance sheet.

In prior years, goodwill arising on acquisitions was eliminated against consolidated reserves in the year of acquisition. The Group has adopted the transitional provision of SSAP 30 that permits goodwill on acquisitions which occurred prior to 1 January 2001, to remain eliminated against consolidated reserves. Goodwill on subsequent acquisitions is treated according to the new accounting policy above.

On disposal of subsidiaries, the gain or loss on disposal is calculated by reference to the net assets at the date of disposal. Any attributable goodwill previously eliminated against consolidated reserves at the time of acquisition is written back and included in the calculation of the gain or loss on disposal.

The goodwill remaining eliminated against consolidated reserves, is reviewed annually and written down for impairment when it is considered necessary. A previously recognised impairment loss for goodwill is not reversed unless the impairment loss was caused by a specific external event of an exceptional nature that was not expected to recur, and subsequent external events have occurred which have reversed the effect of that event.



## Notes to Financial Statements *(Cont'd)*

31 December 2001

### 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

#### 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.

#### Impairment of assets

An assessment is made at each balance sheet date of whether there is any indication of impairment of any asset, or whether there is any indication that an impairment loss previously recognised for an asset in prior years may no longer exist or may have decreased. If any such indication exists, the asset's recoverable amount is estimated. An asset's recoverable amount is calculated as the higher of the asset's value in use or its net selling price.

An impairment loss is recognised only if the carrying amount of an asset exceeds its recoverable amount. An impairment loss is charged to the profit and loss account in the period in which it arises, unless the asset is carried at a revalued amount, when the impairment loss is accounted for in accordance with the relevant accounting policy for that revalued asset.

A previously recognised impairment loss is reversed only if there has been a change in the estimates used to determine the recoverable amount of an asset, however not to an amount higher than the carrying amount that would have been determined (net of any depreciation/amortisation), had no impairment loss been recognised for the asset in prior years.

A reversal of an impairment loss is credited to the profit and loss account in the period in which it arises, unless the asset is carried at a revalued amount, when the reversal of the impairment loss is accounted for in accordance with the relevant accounting policy for that revalued asset.

#### Fixed assets and depreciation

Fixed assets, other than construction in progress and investment properties, 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





## Notes to Financial Statements (Cont'd)

31 December 2001

### 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

#### Fixed assets and depreciation (Cont'd)

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 leasehold land and buildings are dealt with as movements in the property 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 earnings as a movement in reserves.

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:

Leasehold land held under long and medium term leases	Over the lease terms
Buildings	2% – 10%
Leasehold improvements	4% – 20%
Plant and machinery	10% – 12.5%
Electronic equipment	20%
Motor vehicles	15% – 20%
Furniture, fixtures and equipment	15% – 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 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.





## Notes to Financial Statements *(Cont'd)*

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### 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

#### 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, based on their existing use, on the basis of annual professional valuations performed at the end of each financial year. Changes in the values of investment properties are dealt with as movements in the property 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.

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

#### Trademarks

Trademarks are stated at their acquisition costs less accumulated amortisation and any impairment losses. Amortisation is calculated on a straight-line basis to write off their costs over a period of five years.

Expenditure incurred for the renewal of trademarks is charged to the profit and loss account in the period in which it is incurred.

#### Leased assets

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



## **Notes to Financial Statements** *(Cont'd)*

31 December 2001

### **3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Cont'd)**

#### **Inventories**

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

#### **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 assets similar in nature to cash, which are not restricted as to use.

#### **Provisions**

A provision is recognised when a present obligation (legal or constructive) has arisen as a result of a past event and it is probable that a future outflow of resources will be required to settle the obligation, provided that a reliable estimate can be made of the amount of the obligation.

When the effect of discounting is material, the amount recognised for a provision is the present value at the balance sheet date of the future expenditures expected to be required to settle the obligation. The increase in the discounted present value amount arising from the passage of time is included in finance costs in the profit and loss account.

Provisions for compensation payments are made based on respective employment contracts and joint venture agreement.

#### **Deferred tax**

Deferred tax is provided, using the liability method, on all significant timing differences to the extent it is probable that the liability will crystallise in the foreseeable future. A deferred tax asset is not recognised until its realisation is assured beyond reasonable doubt.



## Notes to Financial Statements *(Cont'd)*

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### 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

#### 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 date 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 subsidiaries and associates operating in Mainland China and overseas 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 translation reserve.

#### Retirement benefits scheme

The Group operates a defined contribution Mandatory Provident Fund retirement benefits scheme (the "MPF Scheme") under the Mandatory Provident Fund Schemes Ordinance, for those employees who are eligible to participate in the Scheme. The MPF Scheme has operated since 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 MPF Scheme. The assets of the MPF 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 MPF 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 MPF Scheme.

Prior to the MPF Scheme becoming effective, the Group operated a defined contributions retirement benefits scheme (the "prior scheme") for those employees who were eligible to participate in this scheme. This prior scheme operated in a similar way to the MPF scheme, except that when an employee left the prior scheme before his/her interest in the Group's employer contributions vested fully, the ongoing contributions payable to the Group were reduced by the relevant amount of the forfeited employer's contributions. With effect from 1 December 2000, the prior scheme was terminated.

The employees of the Group's subsidiaries which operate in Mainland China are required to participate in central pension schemes ("CPSs") operated by respective local municipal government. These subsidiaries are required to contribute certain percentage of their covered payroll to the CPSs to fund their benefits. The only obligation of the Group with respect to the CPSs is to pay the ongoing required contributions under the CPSs. Contributions under the CPSs are charged to the profit and loss account as they become payable in accordance with the rules of the CPSs.



## Notes to Financial Statements *(Cont'd)*

31 December 2001

### 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

#### Dividends

Final dividends proposed by the directors are classified as a separate allocation of retained earnings within capital and reserves in 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 dividends are simultaneously proposed and declared, because the Company's memorandum and articles of association grant the directors the authority to declare interim dividends. Consequently, interim dividends are recognised immediately as a liability when they are proposed and declared.

In previous years, the Company recognised its proposed final dividend to shareholders, which was declared and approved after the balance sheet date, as a liability in its balance sheet. The Company also recognised the proposed final dividends of subsidiaries, which were declared and approved after the balance sheet date, as income in its profit and loss account for the year.

#### 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 sale of goods, properties, fixed assets and investments (collectively as "goods and investments"), 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 and investments sold;
- (b) rental and royalty income, on a time proportion basis over the lease/contract terms;
- (c) interest income, on a time proportion basis taking into account the principal outstanding and the effective interest rate applicable; and
- (d) dividends and investment income, when the right to receive payment/benefits has been established.