

NOTES TO THE ACCOUNTS

1. Principal activities

The Company is an investment holding company. Its subsidiaries are principally engaged in the provision of banking and related financial services in Hong Kong.

The Company was incorporated in Hong Kong on 12 September 2001. Its shares have been listed on the Main Board of the Stock Exchange since 25 July 2002.

2. Basis of preparation

The accounts have been prepared under the historical cost convention as modified by the revaluation of certain investments in securities, off-balance sheet instruments, premises and investment properties, and in accordance with accounting principles generally accepted in Hong Kong and comply with the Statements of Standard Accounting Practice (“SSAPs”) issued by the Hong Kong Society of Accountants (“HKSA”). In addition, these accounts comply fully with the requirements set out in the guideline on “Financial Disclosure by Locally Incorporated Authorized Institutions” under the Supervisory Policy Manual issued by the HKMA. These accounts also comply with the applicable disclosure provisions of the Listing Rules of the Stock Exchange.

Pursuant to the Group Reorganisation on 1 October 2001, accomplished by the Bank of China (Hong Kong) Limited (Merger) Ordinance and the Merger Agreements, the Company acquired the entire equity interests in BOCHK on 30 September 2001 and subsequently became the holding company of the Group. The Restructuring and Merger represents a business combination resulting from transactions among enterprises under the common control of BOC, the ultimate holding company of the Company. Under the principles of merger accounting prescribed in the SSAP 27, “Accounting for Group Reconstructions”, the accounts of the Group are prepared as if the group structure and capital structure as at 1 October 2001 had been in existence from the beginning of the period presented.

The accounts of the Company are for the period from 12 September 2001 (date of incorporation) to 31 December 2002. No accounts for the Company was prepared for the period from the date of incorporation to 31 December 2001 as the Company was not involved in any significant business transactions.

The accounting policies and methods of computation used in the preparation of the accounts are consistent with those used in the preparation of the Group’s financial information for the year ended 31 December 2001. In the current year, the Group adopted the following SSAPs issued by the HKSA which are effective for accounting periods commencing on or after 1 January 2002:

SSAP 1 (revised)	:	Presentation of financial statements
SSAP 11 (revised)	:	Foreign currency translation
SSAP 15 (revised)	:	Cash flow statements
SSAP 34 (revised)	:	Employee benefits

The adoption of these SSAPs has not had any significant impact on the accounts.

3. Principal accounting policies

(a) Basis of consolidation

The consolidated accounts include the accounts of the Company and its subsidiaries made up to 31 December. Subsidiaries are those entities in which the Group, directly and indirectly, controls the composition of the board of directors, controls more than half of the voting power or holds more than half of the issued share capital. The results of subsidiaries acquired or disposed of during the year are included in the consolidated profit and loss account from the effective date of acquisition or up to the effective date of disposal, as appropriate.

All significant intercompany transactions and balances within the Group are eliminated on consolidation.

The gain or loss on the disposal of a subsidiary represents the difference between: a) the proceeds of the sale and, b) the Group's share of its net assets together with any unamortised goodwill (or goodwill taken to reserves and which was not previously charged or recognised in the consolidated profit and loss account) and any related accumulated foreign currency translation difference.

Minority interests represent the interests of outside shareholders in the operating results and net assets of subsidiaries.

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

(b) Associates

An associate is a company, not being a subsidiary, in which an equity interest is held for the long term and significant influence is exercised in its management.

The consolidated profit and loss account includes the Group's share of the results of associates for the year. The consolidated balance sheet includes the Group's share of the net assets of the associates plus goodwill/negative goodwill (net of accumulated amortisation) on acquisition and net of any provision for impairment losses.

Unless the Group has incurred obligations or guaranteed obligations in respect of the associate, its share of further losses is discontinued when the share of losses of an associate equals or exceeds the carrying value of the investment in the associate.

(c) Revenue recognition

Interest income is recognised in the profit and loss account as it accrues, except in the case of doubtful debts, where interest is credited to a suspense account which is netted in the balance sheet against the relevant balances.

Fees and commission income are recognised in the period when earned unless they relate to transactions involving an interest rate risk or other risks which extend beyond the current period, in which case they are amortised over the period of the transaction.

Dividend income is recognised when the right to receive payment is established.

Rental income under operating leases is recognised on a straight-line basis over the period of the lease unless another systematic basis is more representative of the pattern in which the benefit derived from the leased asset is used.

3. Principal accounting policies (continued)

(d) Advances

Advances to customers, banks and other financial institutions are reported on the balance sheet at the principal amount outstanding net of provisions for bad and doubtful debts and suspended interest. Advances to banks and other financial institutions include placements with banks and other financial institutions of more than one year.

All advances are recognised when cash is advanced to the borrowers.

Assets acquired by repossession of collateral for realisation would continue to be reported as advances, except in the case of a loan restructuring where the asset acquired is part of the terms of a new loan agreement and the assets are recognised on the balance sheet under the relevant assets category. When the repossessed asset is realised, the sales proceeds are applied against the outstanding advance and any shortfall is written off to the profit and loss account.

(e) Provisions for bad and doubtful debts

The Group internally classifies loans and advances into categories reflecting the Group's assessment of the borrower's capacity to repay and on the degree of doubt about the collectibility of interest and / or principal.

Provisions are made against specific loans and advances as and when the directors have doubt on the ultimate recoverability of principal or interest in full. Based on the directors' assessment of the potential losses on those identified loans and advances on a case-by-case basis, specific provision is made to reduce the carrying value of the assets, taking into account available collateral to their expected net realisable value. Where it is not possible to reliably estimate the loss, the Group applies pre-determined provisioning levels to the unsecured portion of loans and advances based on the Group's loan classification procedures.

In addition, amounts have been set aside as a general provision for bad and doubtful debts. Specific and general provisions are deducted from "Advances and other accounts" and "Other assets" in the consolidated balance sheet.

When there is no realistic prospect of recovery, the outstanding debt is written off.

(f) Fixed assets

(i) Premises

Premises are stated at cost or valuation less accumulated impairment losses and accumulated depreciation calculated to write off the assets over their estimated useful lives on a straight-line basis as follows:

Leasehold land - Over the remaining period of lease

Buildings - Over the shorter of the remaining period of the lease and 15 to 50 years

3. Principal accounting policies (continued)

(f) Fixed assets (continued)

(i) Premises (continued)

Independent valuations were performed every five years prior to 2002 on individual properties on the basis of open market values. In the current year, the directors have assessed that the period between independent valuations should be changed from five years to three years. This change has no impact on the accounts of the Group. In the intervening years, the directors review the carrying value of individual properties and adjustment is made when they consider that there has been a material change. Increases in valuation are credited to the premises revaluation reserve. Decreases in valuation are first set off against increases on earlier valuations in respect of the same individual asset and thereafter are debited to the profit and loss account. Any subsequent increases are credited to the profit and loss account up to the amount previously debited, and then to the revaluation reserve. Upon disposal of premises, the relevant portion of the revaluation reserve realised in respect of previous valuations is released and transferred from the revaluation reserve to retained earnings.

The gain or loss on disposal of premises is the difference between the net sales proceeds and the carrying value of the relevant asset, and is recognised in the profit and loss account.

(ii) Investment properties

Investment properties are interests in land and buildings in respect of which construction work and development have been completed and which are held for their investment potential, any rental income being negotiated at arm's length.

Investment properties are valued annually and independent valuations are performed at intervals of not more than three years; in each of the intervening years, valuations are undertaken by professionally qualified persons appointed by the Group. The valuations are on an open market value basis. Changes in the value of investment properties are treated as movements in the investment properties revaluation reserve, unless the total of the reserve is insufficient to cover a deficit on a portfolio basis. In such cases, the amount by which the deficit exceeds the total amount in the investment properties revaluation reserve is charged to the profit and loss account. Where a deficit has previously been charged to the profit and loss account and a revaluation surplus subsequently arises, this surplus is credited to the profit and loss account to the extent of the deficit previously charged.

Investment properties held on leases with unexpired periods of 20 years or less are depreciated over the remaining terms of the leases.

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

(iii) Property under development

Property under development is carried at cost less impairment losses. Cost includes development and construction expenditure incurred, interest and other direct costs attributable to the development. On completion, the property is transferred to premises or investment properties.

3. Principal accounting policies (continued)

(f) Fixed assets (continued)

(iv) Equipment, fixtures and fittings

Equipment, fixtures and fittings are stated at cost less accumulated impairment losses and accumulated depreciation calculated on a straight-line basis to write off the assets over their estimated useful lives, which are generally between 3 and 15 years.

The gain or loss on disposal of equipment, fixtures and fittings is recognised in the profit and loss account.

(v) Impairment and gain or loss on sale

At each balance sheet date, both internal and external sources of information are considered to determine whether there is any indication that premises, equipment, fixtures and fittings are impaired. If any such indication exists, the recoverable amount of the asset is estimated and where relevant, an impairment loss is recognised to reduce the asset to its recoverable amount. Such impairment losses are recognised in the profit and loss account except where the asset is carried at valuation and the impairment loss does not exceed the revaluation surplus for that same asset, in which case it is treated as a revaluation decrease.

The gain or loss on disposal of fixed assets is the difference between the net sales proceeds and the carrying value of the relevant assets, and is recognised in the profit and loss account.

(g) Investments in securities

(i) Held-to-maturity securities

Held-to-maturity securities are dated debt securities which the Group has the expressed intention and ability to hold to maturity. These securities are stated at cost adjusted for the amortisation of premiums or discounts arising on acquisition over the periods to maturity, less provision for impairment in their value which is other than temporary. Provisions are made for the amount of the carrying value which the Group does not expect to recover and are recognised as an expense in the profit and loss account as they arise.

The amortisation of premiums and discounts arising on acquisition of dated debt securities is included as part of interest income in the profit and loss account. Gain or loss on realisation of held-to-maturity securities is accounted for in the profit and loss account as they arise.

(ii) Investment securities

Securities which are intended to be held on a continuing basis for an identified long-term purpose at the time of acquisition (for example, for strategic purposes), are stated in the balance sheet at cost less any provisions for impairment in value which is other than temporary.

The carrying value of investment securities are reviewed as at the balance sheet date in order to assess whether the fair value has declined below the carrying value. When such a decline has occurred, the carrying value is reduced to the fair value unless there is evidence that the decline is temporary. The amount of the reduction is recognised as an expense in the profit and loss account.

Fair value is the amount for which an asset can be exchanged, or a liability settled, between knowledgeable willing parties in an arm's length transaction.

3. Principal accounting policies (continued)

(g) Investments in securities (continued)

(iii) Other investments in securities

All other investments in securities (whether held for trading or otherwise) are stated in the balance sheet at fair value. Changes in fair value are recognised in the profit and loss account as they arise.

Provisions against the carrying value of held-to-maturity securities and investment securities are written back when the circumstances and events that led to the write-downs cease to exist and there is persuasive evidence that the new circumstances and events will persist for the foreseeable future. The amount written back is limited to the amount of the write-downs.

(h) Operating leases

Leases where substantially all the risks and rewards of ownership of assets remain with the lessor are accounted for as operating leases. Rentals applicable to such operating leases net of any incentives received from the lessor are charged to the profit and loss account on a straight-line basis over the lease term.

Where the Group is the lessor, the assets subject to the lease are included in fixed assets in the balance sheet. They are depreciated over their expected useful lives on a basis consistent with similar owned fixed assets. Rental income from operating leases is recognised on a straight-line basis over the lease term. Initial direct costs incurred specifically to earn revenue from an operating lease are recognised as an expense in the profit and loss account in the period in which they are incurred.

(i) Provisions

A provision is recognised when the Group has a present obligation, legal or constructive, as a result of a past event and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation.

A provision for restructuring costs is recognised when the above general recognition criteria are met and a detailed formal plan for the restructuring has been implemented, or has been announced and communicated to those affected by it in a sufficiently specific manner to raise a valid expectation that the restructuring will be carried out without long delay.

(j) Deferred taxation

Deferred taxation is provided at the current tax rate in respect of timing differences between profit as computed for taxation purposes and profit as stated in the profit and loss account to the extent that it is probable that a liability or an asset is expected to be payable or recoverable in the foreseeable future.

(k) Foreign currency translation

Transactions in foreign currencies are translated at exchange rates ruling at the transaction dates. Monetary assets and liabilities expressed in foreign currencies at the balance sheet date are translated at rates of exchange ruling at the balance sheet date. Exchange differences arising in these cases are dealt with in the profit and loss account.

3. Principal accounting policies (continued)

(k) Foreign currency translation (continued)

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

(l) Employee benefits

(i) Retirement benefit costs

The Group contributes to defined contribution retirement schemes under either recognised occupation retirement schemes (“ORSO schemes”) or mandatory provident fund (“MPF”) schemes which are available to all employees. Contributions to the schemes by the Group and employees are calculated as a percentage of employees’ basic salaries for the ORSO schemes and in accordance with the MPF rules for MPF schemes. The retirement benefit scheme costs are charged to the profit and loss account as incurred and represents contributions payable by the Group to the schemes. Forfeited contributions by those employees who leave the ORSO scheme prior to the full vesting of their contributions are used by the Group to reduce the existing level of contributions or to meet its expenses under the trust deed of the ORSO schemes.

The assets of the schemes are held separately from those of the Group in independently-administered funds.

(ii) Leave entitlements

Employee entitlements to annual leave and sick leave are recognised when they accrue to employees. A provision is made for the estimated liability for unused annual leave and the amount of sick leave expected to be paid as a result of services rendered by employees up to the balance sheet date.

Compensated absences other than annual leave and sick leave are non-accumulating; they lapse if the current period’s entitlement is not used in full and do not entitle employees to a cash payment for unused entitlement on leaving the Group. Such compensated absences are recognised when the absences occur.

(iii) Bonus plans

The expected cost of bonus payments are recognised as a liability when the Group has a present legal or constructive obligation as a result of services rendered by employees and a reliable estimate of the obligation can be made.

Liabilities for bonus plans are expected to be settled within 12 months and are measured at the amounts expected to be paid when they are settled.

(m) Off-balance sheet financial instruments

Off-balance sheet financial instruments arise from futures, forwards, swaps, options and other transactions undertaken by the Group in the foreign exchange, interest rate, equity and other markets. The accounting for these instruments is dependent upon whether the transactions are undertaken for trading purposes or to hedge risk. The Group designates a derivative as held for trading or hedging purposes when it enters into a derivative contract.

3. Principal accounting policies (continued)

(m) Off-balance sheet financial instruments (continued)

Transactions undertaken for trading purposes are marked to market at fair value. For exchange traded contracts, fair value is based on quoted market prices. For non-exchange traded contracts, fair value is based on dealers' quotes, pricing models or quoted prices for instruments with similar characteristics. The gain or loss arising from changes in fair value is recognised in the profit and loss account as "Net gain/(loss) from foreign exchange activities" or "Net gain/(loss) from other dealing activities".

Unrealised gains on transactions which are marked to market are included in "Other assets". Unrealised losses on transactions which are marked to market are included in "Other accounts and provisions".

Hedging derivative transactions are designated as such at inception and require that the hedging instrument, hedging objective, strategy and all relationships between hedging risk and items be fully documented. It must also be demonstrated that a derivative would be expected to be highly effective in accomplishing the objective of offsetting the risk being hedged throughout the contract period. Hedging instruments are valued on an equivalent basis to the assets, liabilities or net positions that they are hedging. Any profit or loss is recognised in the profit and loss account on the same basis as that arising from the related assets, liabilities or net positions.

If the derivative transaction no longer meets the criteria for a hedge, the derivative is deemed to be held for trading purposes and is accounted for as set out above.

Assets and liabilities arising from derivative transactions are netted off only when the Group has entered into master netting agreements or other legally enforceable arrangements, which assures beyond doubt, the Group's right to insist on settlement with the same counterparty on a net basis in all situations of default by the other party or parties including insolvency of any parties to the contract.

Derivative transactions are not offset unless the related settlement currencies are the same, or are denominated in freely convertible currencies for which quoted exchange rates are available in an active market.

(n) Contingent liabilities and contingent assets

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

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

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

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

3. Principal accounting policies (continued)

(o) Cash and cash equivalents

For the purposes of the consolidated cash flow statement, cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition including cash, balances with banks and other financial institutions, treasury bills, other eligible bills and certificates of deposit.

(p) Dividends

Dividends proposed or declared after the balance sheet date are disclosed as a post balance sheet event and are not recognised as a liability at the balance sheet date.

4. Interest income

	2002 HK\$m	2001 HK\$m
Interest income from listed investments	1,341	766
Interest income from unlisted investments	3,621	5,666
Other interest income	16,501	31,875
	21,463	38,307

5. Other operating income

	2002 HK\$m	2001 HK\$m
Fees and commission income	3,649	3,585
Less: Fees and commission expenses	(701)	(889)
Net fees and commission income	2,948	2,696
Dividend income from investments in securities		
— listed investments	—	1
— unlisted investments	34	65
Net (loss)/gain from other investments in securities	(61)	108
Net gain from foreign exchange activities	824	816
Net gain from other dealing activities	14	8
Gross rental income from investment properties	279	257
Less: Outgoings in respect of investment properties	(87)	(80)
Others	221	151
	4,172	4,022

6. Operating expenses

	2002 HK\$m	2001 HK\$m
Staff costs (including directors' emoluments)		
— salaries and other costs	3,325	3,558
— pension cost	253	238
	3,578	3,796
Premises and equipment expenses (excluding depreciation)		
— rental of premises	245	297
— information technology and others	558	595
	803	892
Depreciation on owned fixed assets	632	460
Auditors' remuneration	18	23
Other operating expenses	994	676
	6,025	5,847

7. Charge for bad and doubtful debts

	2002 HK\$m	2001 HK\$m
Net charge for bad and doubtful debts		
Specific provisions		
— new provisions	4,519	10,649
— releases	(582)	(645)
— recoveries (note 23)	(904)	(530)
	3,033	9,474
General provisions	(178)	(2,062)
Net charge to profit and loss account (note 23)	2,855	7,412

8. Net loss from disposal/revaluation of fixed assets

	2002 HK\$m	2001 HK\$m
Net (loss)/gain on disposal of fixed assets	(55)	4
Net loss on revaluation of fixed assets	(977)	(1,241)
	(1,032)	(1,237)

9. (Provision)/write-back of provision for impairment on held-to-maturity securities and investment securities

	2002 HK\$'m	2001 HK\$'m
(Provision)/write-back of provision for impairment losses on held-to-maturity securities	(4)	23
(Provision)/write-back of provision for impairment losses on investment securities	(3)	1
	(7)	24

10. Taxation

Taxation in the profit and loss account represents:

	2002 HK\$'m	2001 HK\$'m
Hong Kong profits tax		
— current year taxation	1,505	877
— overprovision in prior years	(130)	(75)
Deferred tax liability	–	2
	1,375	804
Attributable share of estimated Hong Kong profits tax losses arising from investments in partnerships	(488)	(96)
	887	708
Investments in partnerships written off	365	77
Hong Kong profits tax	1,252	785
Overseas taxation	15	29
	1,267	814
Share of taxation attributable to associates	1	18
	1,268	832

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

10. Taxation (continued)

The Group has entered into a number of aircraft leasing and coupon strip transactions involving special purpose partnerships in which the Group is the majority general partner. The Group does not control the partnerships and consequently they are not consolidated in the Group's accounts. As at 31 December 2002, the Group's investments in such partnerships, which are included in "Other assets" in the consolidated balance sheet amounted to HK\$1,122 million (2001: HK\$876 million). The Group's investments in partnerships are amortised over the life of the partnership in proportion to the taxation benefits resulting from those investments. The total assets and liabilities of such partnerships are as follows:

	2002 HK\$m	2001 HK\$m
Assets	4,721	4,493
Liabilities	3,182	3,156

11. Profit attributable to shareholders

The profit of the Company for the period from 12 September 2001 (date of incorporation) to 31 December 2002 attributable to shareholders and dealt with in the accounts of the Company amounted to HK\$4,518 million.

12. Dividends

	2002 HK\$m	2001 HK\$m
Special dividend paid	1,935	–
Proposed final dividend	2,273	–
	4,208	–

At a meeting held on 18 June 2002, the Board declared a special dividend of HK\$0.183 per ordinary share (taking into account the share consolidation) amounting to HK\$1,935 million. On 28 June 2002, the shareholders of the Company approved the special dividend.

At a meeting held on 20 March 2003, the Board proposed to declare a final dividend of HK\$0.215 per ordinary share for the year ended 2002 amounting to HK\$2,273 million. This proposed dividend is not reflected as a dividend payable in these accounts, but will be reflected as an appropriation of retained earnings for the year ending 31 December 2003.

13. Earnings per share

The calculation of basic earnings per share is based on the consolidated profit attributable to shareholders for the year ended 31 December 2002 of approximately HK\$6,673,000,000 (2001: HK\$2,768,000,000) and on the ordinary shares in issue of 10,572,780,266 shares. The amount for 2001 has been restated after adjusting for the effect of the share consolidation as described in note 32 as if the share consolidation had occurred at the beginning of the year.

There was no dilution of earnings per share as no potential ordinary shares were in issue for the year ended 31 December 2002 (2001: Nil).

14. Retirement benefit costs

The Group operates certain defined contribution schemes which are ORSO schemes exempted under the Mandatory Provident Fund Schemes Ordinance (“MPF Schemes Ordinance”). Under the schemes, employees make monthly contributions to the ORSO schemes equal to 5% of their basic salaries, while the employer makes monthly contributions equal to 5% to 15% of the employees’ monthly basic salaries, depending on years of service. The employees are entitled to receive 100% of the employer’s contributions upon termination of employment after completing 20 years of service, or at a scale ranging from 20% to 95% for employees who have completed between 3 to 20 years of service, on conditions of retirement, early retirement, permanent incapacity and ill-health or termination of employment other than summary dismissal.

With the implementation of the MPF Schemes Ordinance on 1 December 2000, the Group also participates in the BOC-Prudential Easy Choice Mandatory Provident Fund Scheme (the “MPF Scheme”), of which the trustee is BOCI-Prudential Trustee and the investment manager is BOCI-Prudential Manager, which are related parties of the Company.

The Group’s total contributions made to the ORSO schemes for the year ended 31 December 2002 amounted to approximately HK\$242 million (2001: approximately HK\$234 million), after a deduction of forfeited contributions of approximately HK\$17 million (2001: approximately HK\$36 million). For the MPF Scheme, the Group contributed approximately HK\$7 million (2001: approximately HK\$4 million) for the year ended 31 December 2002.

15. Share option schemes

(a) 2002 Share Option Scheme and 2002 Sharesave Plan

The principal terms of the 2002 Share Option Scheme and the 2002 Sharesave Plan were approved and adopted by written resolutions of all the shareholders of the Company dated 10 July 2002.

The purpose of the 2002 Share Option Scheme is to provide the participants with the opportunity to acquire proprietary interests in the Company. The Board may, in its absolute discretion, offer to grant options under the 2002 Share Option Scheme to any person as the Board may select. The subscription price for the shares shall be determined on the date of grant by the Board as an amount per share calculated on the basis of established rules. An option may be exercised in whole or in part at any time after the date prescribed by the Board and from time to time as specified in the offer and on or before the termination date prescribed by the Board.

15. Share option schemes (continued)

(a) 2002 Share Option Scheme and 2002 Sharesave Plan (continued)

The purpose of the 2002 Sharesave Plan is to encourage broad-based employee ownership of the shares of the Company. The amount of the monthly contribution under the savings contract to be made in connection with an option shall be the amount which the relevant eligible employee is willing to contribute, which amount shall not be less than 1% and not more than 10% of the eligible employee's monthly salary as at the date of application or such other maximum or minimum amounts as permitted by the Board. When an option is exercised during an exercise period, it may be exercised in whole or in part.

In connection with the Company's listing on the Stock Exchange on 25 July 2002, it has undertaken to the Stock Exchange that it shall not, among other things, grant or offer or agree to grant options over any shares without the prior consent of the Stock Exchange for a period of 6 months from its listing, i.e. until 25 January 2003. Accordingly, no options have been granted by the Company pursuant to the 2002 Share Option Scheme or the 2002 Sharesave Plan for the year ended 31 December 2002. Details of the 2002 Share Option Scheme and 2002 Sharesave Plan are set out on page 41.

The two schemes have not commenced in current year.

(b) Pre-Listing Share Option Scheme

On 5 July 2002, several directors together with approximately 60 senior management personnel of the Group were granted options by BOC (BVI), the immediate holding company of the Company, pursuant to a Pre-Listing Share Option Scheme to purchase from BOC (BVI) an aggregate of 31,132,600 existing issued shares of the Company.

Details of the share options outstanding as at 31 December 2002 are as follows:

	Directors	Senior management	Total number of share options
At 1 January 2002	–	–	–
Add: Share options granted during the year	13,737,000	17,395,600	31,132,600
Less: Share options exercised during the year	–	–	–
Less: Share options lapsed during the year	–	(174,000)	(174,000)
At 31 December 2002	13,737,000	17,221,600	30,958,600

The options granted under this scheme can be exercised at HK\$8.50 per share in respect of the option price of HK\$1.00. None of these options may be exercised within one year from the date on which dealings in the shares commenced on the Stock Exchange. These options have a vesting period of four years (25% of the number of shares subject to such options will vest at the end of each year) from the date on which dealings in the shares commenced on the Stock Exchange with a valid exercise period of ten years. No offer to grant any options under the Pre-Listing Share Option Scheme will be made on or after the date on which dealings in the shares commenced on the Stock Exchange.

16. Directors' and senior management's emoluments

(a) Directors' emoluments

Details of the emoluments paid and payable to the directors of the Company in respect of their services rendered for managing the subsidiaries within the Group during the year are as follows:

	2002 HK\$'m	2001 HK\$'m
Fees	3	1
Other emoluments for executive directors		
— basic salaries and allowances	4	3
— discretionary bonuses	1	2
— others (including benefits in kind)	–	1
	8	7

Emoluments of the directors were within the following bands:

	Number of directors	
	2002	2001
Up to HK\$1,000,000	12	12
HK\$5,000,001 - HK\$5,500,000	1	1

The aggregate amount of emoluments paid to the Independent Non-executive Directors during the year was HK\$800,000 (2001: Nil).

During the year, options to purchase 13,737,000 shares (2001: Nil) of the Company at HK\$8.50 per share, which is the same as the offer price, were granted to the directors of the Company by the immediate holding company, BOC (BVI), under the Pre-Listing Share Option Scheme. The benefits arising from the granting of these share options are not included in the directors' emoluments disclosed above and have not been recognised in the profit and loss account.

16. Directors' and senior management's emoluments (continued)

(b) Five highest paid individuals

The five individuals whose emoluments were the highest in the Group for the year include 1 director (2001: 1) whose emoluments are reflected in the analysis presented above. The emoluments payable to the remaining 4 individuals (2001: 4) during the year are as follows:

	2002 HK\$m	2001 HK\$m
Basic salaries and allowances	9	6
Discretionary bonuses	1	3
Contributions to pensions schemes	1	1
	11	10

Emoluments of individuals were within the following bands:

	Number of individuals	
	2002	2001
HK\$2,000,001 - HK\$2,500,000	–	1
HK\$2,500,001 - HK\$3,000,000	2	3
HK\$3,000,001 - HK\$3,500,000	2	–

During the year, no directors waived any emoluments and no emoluments have been paid by the Group to the directors or any of the 5 highest paid individuals as an inducement to join or upon joining the Group or as compensation for loss of office.

17. Cash and short-term funds

	2002 HK\$m	2001 HK\$m
Cash	2,637	3,240
Balances with banks and other financial institutions	2,370	56,658
Money at call and short notice maturing within one month	95,997	117,446
Treasury bills (including Exchange Fund Bills)	14,071	18,911
	115,075	196,255
An analysis of treasury bills held is as follows:		
Unlisted, held-to-maturity, at amortised cost:	10,933	12,932
Unlisted, other investments in securities, at fair value:	3,138	5,979
	14,071	18,911

18. Certificates of deposit held

	2002 HK\$m	2001 HK\$m
Held-to-maturity, at amortised cost		
– Unlisted	8,342	9,130
Other investments in securities, at fair value:		
– Unlisted	9,186	10,344
	17,528	19,474

19. Held-to-maturity securities

	2002 HK\$m	2001 HK\$m
Listed, at amortised cost	35,219	16,438
Less: Provision for impairment in value	(12)	—
	35,207	16,438
Unlisted, at amortised cost	59,049	34,592
Less: Provision for impairment in value	(29)	(42)
	59,020	34,550
Total	94,227	50,988
Listed, at amortised cost less provision		
– in Hong Kong	2,946	2,239
– outside Hong Kong	32,261	14,199
	35,207	16,438
Market value of listed securities	36,073	15,905
Held-to-maturity securities are analysed by issuers as follows:		
– Central governments and central banks	3,620	3,470
– Public sector entities	17,028	17,722
– Banks and other financial institutions	64,457	24,454
– Corporate entities	9,122	5,342
	94,227	50,988

20. Investment securities

	2002 HK\$'m	2001 HK\$'m
Equity securities		
– Listed in Hong Kong, at cost	16	16
Less: Provision for impairment in value	(15)	(12)
	1	4
– Listed outside Hong Kong, at cost	1	1
	2	5
– Unlisted, at cost	44	39
Total	46	44
Market value of listed equity securities	4	5
Investment securities are analysed by issuers as follows:		
– Banks and other financial institutions	1	22
– Corporate entities	45	18
– Others	–	4
	46	44

21. Other investments in securities

	2002 HK\$m	2001 HK\$m
At fair value:		
Debt securities		
— Listed in Hong Kong	1,313	294
— Listed outside Hong Kong	20,818	4,812
	22,131	5,106
— Unlisted	42,078	50,973
	64,209	56,079
Equity securities		
— Listed in Hong Kong	121	28
— Unlisted	30	62
	151	90
Total	64,360	56,169
Other investments in securities are analysed by issuers as follows:		
— Central governments and central banks	3,069	1,495
— Public sector entities	4,914	24,557
— Banks and other financial institutions	46,662	28,876
— Corporate entities	9,715	1,241
	64,360	56,169

22. Advances and other accounts

	2002 HK\$m	2001 HK\$m
Advances to customers	321,034	323,038
Accrued interest	2,006	2,180
	323,040	325,218
Provision for bad and doubtful debts		
— General	(6,363)	(6,538)
— Specific	(8,650)	(10,576)
	(15,013)	(17,114)
	308,027	308,104
Advances to banks and other financial institutions	305	4
	308,332	308,108

Non-performing loans are analysed as follows:

	2002 HK\$m	2001 HK\$m
Non-performing loans	25,659	35,512
Specific provisions made in respect of such advances	8,637	10,322
As a percentage of total advances to customers	7.99%	10.99%
Amount of interest in suspense	408	610

NPLs are defined as loans and advances to customers on which interest is being placed in suspense or on which interest accrual has ceased. Specific provisions were made after taking into account the value of collateral in respect of such advances.

There were no advances to banks and other financial institutions on which interest has been placed in suspense or on which interest accrual has ceased as at 31 December 2002 (2001: Nil), nor were there any specific provisions made.

On 26 June 2002, BOCHK disposed of loans with a gross book value of HK\$11,401 million net of specific provisions of HK\$2,679 million to BOC Cayman without recourse (note 42(a)). As at 31 December 2001, the outstanding balance of NPLs which were disposed of in 2002 amounted to HK\$7,269 million and specific provisions made in respect of such NPLs amounted to HK\$2,538 million. Had the disposal taken place as at 31 December 2001, the NPLs as a percentage of total advances to customers would have been 9.06%.

23. Provisions for bad and doubtful debts

	2002			
	Specific HK\$m	General HK\$m	Total HK\$m	Suspended interest HK\$m
At 1 January 2002	10,621	6,541	17,162	610
Charge/(credit) to profit and loss account (note 7)	3,033	(178)	2,855	–
Amounts written off	(3,229)	–	(3,229)	(37)
Recoveries of advances written off in previous years (note 7)	904	–	904	–
Amounts written off on disposal (note)	(2,679)	–	(2,679)	–
Interest suspended during the year	–	–	–	296
Suspended interest recovered	–	–	–	(461)
At 31 December 2002	8,650	6,363	15,013	408
Deducted from:				
– advances to customers	8,650	6,363	15,013	
	2001			
	Specific HK\$m	General HK\$m	Total HK\$m	Suspended interest HK\$m
At 1 January 2001	11,031	8,624	19,655	763
Charge/(credit) to profit and loss account (note 7)	9,474	(2,062)	7,412	(13)
Amounts written off	(10,414)	(21)	(10,435)	(173)
Recoveries of advances written off in previous years (note 7)	530	–	530	–
Interest suspended during the year	–	–	–	339
Suspended interest recovered	–	–	–	(306)
At 31 December 2001	10,621	6,541	17,162	610
Deducted from:				
– other assets	45	3	48	
– advances to customers	10,576	6,538	17,114	
	10,621	6,541	17,162	

Note:

On 26 June 2002, BOCHK disposed of loans with a gross book value of HK\$11,401 million net of specific provisions of HK\$2,679 million to BOC Cayman without recourse (note 42(a)).

24. Investments in subsidiaries

	2002 HK\$m
Unlisted shares, at cost	52,864

The particulars of all direct and indirect subsidiaries of the Company are set out in Appendix I of the Annual Report, "Subsidiaries of the Company". The following is a list of principal subsidiaries as at 31 December 2002.

Name	Place of incorporation & establishment	Particulars of issued share capital	Interest held	Principal activities
Bank of China (Hong Kong) Limited	Hong Kong	43,042,840,858 ordinary shares of HK\$1 each	*100%	Banking business
Nanyang Commercial Bank, Limited	Hong Kong	6,000,000 ordinary shares of HK\$100 each	100%	Banking business
Chiyu Banking Corporation Limited	Hong Kong	3,000,000 ordinary shares of HK\$100 each	70.49%	Banking business
BOC Credit Card (International) Limited	Hong Kong	1,000,000 ordinary shares of HK\$100 each	100%	Credit card services
Po Sang Futures Limited	Hong Kong	250,000 ordinary shares of HK\$100 each	100%	Commodities brokerage

* Shares held directly by the Company

25. Investments in associates

	2002 HK\$m	2001 HK\$m
Share of net assets	186	368
Less: Provision for impairment in value	(22)	(22)
	164	346
Loans to associates (note)	346	68
Amounts due from associates	–	2
Less: Provision for loans to associates	(27)	–
	483	416

Note:

As at 31 December 2002, loans to associates are all on commercial terms and carry interest at the prevailing market interest rates.

25. Investments in associates (continued)

The following is a list of the principal associates as at 31 December 2002, all of which are corporate entities.

Name	Place of incorporation & establishment	Particulars of issued share capital	Group's equity interest held indirectly	Principal activities
CCIC Finance Limited	Hong Kong	100,000 ordinary shares of HK\$1,000 each	30%	Provision of financial advisory services
Charleston Investments Company Limited	Hong Kong	100,000 ordinary shares of HK\$10 each	40%	Property investment
CJM Insurance Brokers Limited	Hong Kong	6,000,000 ordinary shares of HK\$1 each	33%	Insurance broker
Joint Electronic Teller Services Limited	Hong Kong	100,238 ordinary shares of HK\$100 each	19.96%	Operation of a private interbank message switching network in respect of ATM services
Kincheng-Tokyo Finance Company Limited	Hong Kong	1,000,000 ordinary shares of HK\$100 each	50%	Deposit taking company
Trilease International Limited	Hong Kong	30,000,000 ordinary shares of HK\$1 each	40%	Provision of leasing finance
Wealthy Full Enterprises Limited	Hong Kong	10,000 ordinary shares of HK\$1 each	35%	Property investment
Zhejiang Commercial Bank Limited	PRC	Registered capital	25%	Banking and related financial services

26. Fixed assets

	2002				Total HK\$'m
	Premises HK\$'m	Investment properties HK\$'m	Property under development HK\$'m	Equipment, fixtures and fittings HK\$'m	
Cost or valuation					
At 1 January 2002	15,539	4,881	39	3,418	23,877
Additions	1	2	–	431	434
Acquisitions of subsidiaries	597	315	–	5	917
Disposals	(699)	(36)	–	(330)	(1,065)
Revaluation	(1,211)	(219)	–	–	(1,430)
Reclassification	(782)	782	–	–	–
At 31 December 2002	13,445	5,725	39	3,524	22,733
Accumulated depreciation					
At 1 January 2002	214	–	7	2,607	2,828
Depreciation for the year	401	–	–	231	632
Acquisitions of subsidiaries	–	–	–	4	4
Disposals	(127)	–	–	(330)	(457)
Write-back on revaluation	(486)	–	–	–	(486)
At 31 December 2002	2	–	7	2,512	2,521
Net book value					
At 31 December 2002	13,443	5,725	32	1,012	20,212
At 31 December 2001	15,325	4,881	32	811	21,049
The analysis of cost or valuation of the above assets is as follows:					
At 31 December 2002					
At cost	–	–	39	3,524	3,563
At valuation	13,445	5,725	–	–	19,170
	13,445	5,725	39	3,524	22,733
At 31 December 2001					
At cost	–	–	39	3,418	3,457
At valuation	15,539	4,881	–	–	20,420
	15,539	4,881	39	3,418	23,877

26. Fixed assets (continued)

The carrying value of premises is analysed based on the remaining terms of the leases as follows:

	2002 HK\$m	2001 HK\$m
Held in Hong Kong		
On long term lease (over 50 years)	8,217	10,394
On medium term lease (10-50 years)	4,942	4,616
On short term lease (less than 10 years)	3	3
Held outside Hong Kong		
On long term lease (over 50 years)	53	94
On medium term lease (10-50 years)	222	217
On short term lease (less than 10 years)	6	1
	13,443	15,325

The carrying value of investment properties is analysed based on the remaining terms of the leases as follows:

	2002 HK\$m	2001 HK\$m
Held in Hong Kong		
On long term lease (over 50 years)	4,666	4,038
On medium term lease (10-50 years)	929	690
Held outside Hong Kong		
On long term lease (over 50 years)	37	5
On medium term lease (10-50 years)	93	148
	5,725	4,881

26. Fixed assets (continued)

Investment properties were revalued at 31 December 2002 on the basis of their open market value by an independent firm of chartered surveyors, Chesterton Petty Limited.

As at 31 December 2002, the premises are included in the balance sheet at directors' valuation, having regard to the independent professional valuations carried out on majority of the premises.

As a result of the above-mentioned revaluation, increases and decreases in value of the Group's premises and investment properties were recognised in the Group's property revaluation reserves and the profit and loss account respectively as follows:

	Premises HK\$m	Investment properties HK\$m
Increase/(Decrease) in valuation credited /(debited) to property revaluation reserves	46	(13)
Decrease in valuation charged to profit and loss account	(771)	(206)
	(725)	(219)

As at 31 December 2002, the net book value of premises that would have been included in the Group's balance sheet had the assets been carried at cost less accumulated depreciation and impairment losses were HK\$7,448 million (2001: HK\$7,924 million).

27. Hong Kong SAR currency notes in circulation

The Hong Kong SAR currency notes in circulation are secured by deposit of funds in respect of which the Hong Kong SAR Government certificates of indebtedness are held.

28. Deposits from customers

	2002 HK\$m	2001 HK\$m
Demand deposits and current accounts	21,476	18,639
Savings deposits	204,363	184,288
Time, call and notice deposits	375,138	403,501
	600,977	606,428

29. Assets pledged as security

	2002 HK\$m	2001 HK\$m
Secured liabilities	3,198	1,813
Assets pledged as security		
— securities pledged as collateral	3,400	1,883

Secured liabilities and assets pledged as security relate to short positions in Exchange Fund Bills and Notes (“EFBNs”) which are collateralised by long positions in EFBNs.

30. Other accounts and provisions

	2002 HK\$m	2001 HK\$m
Interest payable	1,167	1,615
Current taxation (note (a))	544	59
Deferred taxation	11	8
Restructuring provision (note (b))	649	666
Accruals and other payables	15,019	18,323
	17,390	20,671

(a) Current taxation

	2002 HK\$m	2001 HK\$m
Hong Kong profits tax	531	42
Overseas taxation	13	17
	544	59

30. Other accounts and provisions (continued)

(b) Restructuring provision

	2002 HK\$m	2001 HK\$m
At 1 January	666	–
Charge to profit and loss account	–	937
Utilised during the year	(17)	(271)
At 31 December	649	666

The restructuring provision was made in relation to the Restructuring and Merger of the Group. The amounts not being utilised at 31 December 2002 mainly represents the stamp duty payable which arose from restructuring activities of the Group.

31. Deferred taxation

The deferred tax liability mainly represents the taxation effect of accelerated depreciation allowances. The potential deferred tax asset arising from the general provision for bad and doubtful debts amounted to HK\$1,018 million as at 31 December 2002 (2001: HK\$1,046 million) has not been recognised in the Group's balance sheet.

32. Share capital

	2002 HK\$m	2001 HK\$m
Authorised: 20,000,000,000 ordinary shares of HK\$5.00 each	100,000	100,000
Issued and fully paid: 10,572,780,266 ordinary shares of HK\$5.00 each	52,864	52,864

Pursuant to written resolutions of all the shareholders of the Company passed on 10 July 2002, the authorised and issued share capital of the Company, comprising 100,000,000,000 and 52,863,901,330 ordinary shares of HK\$1.00 each, respectively, was consolidated and divided into 20,000,000,000 shares and 10,572,780,266 shares of HK\$5.00 each, respectively.

33. Reserves

	2002 HK\$m	2001 HK\$m
Premises revaluation reserve	113	141
Investment properties revaluation reserve	–	18
Translation reserve	(2)	(2)
Retained earnings/(Accumulated losses)	3,966	(851)
	4,077	(694)

34. Notes to consolidated cash flow statement

(a) Reconciliation of operating profit after provisions to operating cash outflow before taxation

	2002 HK\$m	2001 HK\$m
Operating profit after provisions	9,234	5,750
Depreciation	632	460
Charge for bad and doubtful debts	2,855	7,412
Advances written off net of recoveries	(2,325)	(9,905)
Change in money at call and short notice with original maturity over three months	11,620	(9,507)
Change in treasury bills with original maturity over three months	9,904	(12,464)
Change in placements with banks and other financial institutions with original maturity over three months	3,494	(10,212)
Change in trade bills	(210)	157
Change in certificates of deposit held with original maturity over three months	989	331
Change in held-to-maturity securities	(43,243)	(2,639)
Change in other investments in securities	(8,191)	(22,288)
Change in advances and other accounts	(9,524)	19,914
Change in other assets	1,357	824
Change in deposits and balances of banks and other financial institutions repayable over three months	(5,204)	(13,801)
Change in deposits from customers	(5,451)	(18,298)
Change in other accounts and provisions	(3,830)	10,045
Exchange differences	–	(4)
Operating cash outflow before taxation	(37,893)	(54,225)

34. Notes to consolidated cash flow statement (continued)**(b) Analysis of changes in financing**

	2002		
	Share capital HK\$m	Certificates of deposit issued HK\$m	Minority interests HK\$m
At 1 January 2002	52,864	5,000	1,066
Cash outflow upon redemption	–	(5,000)	–
Minority interests share of profits	–	–	127
Dividends paid to minority shareholders	–	–	(79)
At 31 December 2002	52,864	–	1,114

	2001		
	Share capital HK\$m	Certificates of deposit issued HK\$m	Minority interests HK\$m
At 1 January 2001	52,864	9,000	1,532
Cash outflow upon redemption	–	(4,000)	–
Minority interests share of profits	–	–	133
Minority interests share of revaluation reserve	–	–	49
Dividends paid to minority shareholders	–	–	(638)
Released on disposal of subsidiaries	–	–	(10)
At 31 December 2001	52,864	5,000	1,066

(c) Analysis of the balances of cash and cash equivalents

	2002 HK\$m	2001 HK\$m
Cash and balances with banks and other financial institutions	5,007	59,898
Money at call and short notice with original maturity within three months	77,354	87,183
Treasury bills with original maturity within three months	8,258	3,194
Placements with banks and other financial institutions with original maturity within three months	19,723	16,843
Certificates of deposit held with original maturity within three months	234	1,191
Deposits and balances of banks and other financial institutions with original maturity within three months	(27,511)	(47,645)
	83,065	120,664

34. Notes to consolidated cash flow statement (continued)

(d) Acquisition of subsidiaries

	2002 HK\$'m	2001 HK\$'m
Net assets acquired:		
— Fixed assets	913	13
— Other assets	41	–
— Cash and bank balances	124	61
— Other accounts and provisions	(64)	(37)
	1,014	37
Satisfied by:		
— Cash consideration	1,014	37
Analysis of net (outflow)/inflow of cash and cash equivalents in respect of the acquisition of subsidiaries		
— Cash consideration	(1,014)	(37)
— Cash and bank balances	124	61
	(890)	24

(e) Significant non-cash transaction

As at 31 December 2002, the Group no longer exercised significant influence on Hong Kong Note Printing Limited amounted to HK\$31 million as at 31 December 2001 and such amount has therefore been reclassified from investments in associates to investment securities.

35. Maturity profile

The maturity profile of assets and liabilities analysed by the remaining period as at 31 December to the contractual maturity dates is as follows:

	2002						Total HK\$m
	Repayable on demand HK\$m	3 months or less HK\$m	1 year or less but over 3 months HK\$m	5 years or less but over 1 year HK\$m	Over 5 years HK\$m	Undated HK\$m	
Assets							
Treasury bills	–	12,567	1,504	–	–	–	14,071
Cash and other short-term funds	5,007	95,997	–	–	–	–	101,004
Placements with banks and other financial institutions	21	72,411	7,727	–	–	–	80,159
Certificates of deposit held	–	1,921	6,589	8,824	194	–	17,528
Debt securities included in:							
– held-to-maturity securities	–	11,565	12,798	65,763	4,064	78	94,268
– other investments in securities	–	15,919	6,068	39,178	3,044	–	64,209
Advances to customers	26,979	17,172	25,702	124,813	100,533	25,835	321,034
Advances to banks and other financial institutions	–	1	1	303	–	–	305
Liabilities							
Deposits and balances of banks and other financial institutions	4,164	25,403	390	–	–	–	29,957
Deposits from customers	228,103	350,232	22,215	427	–	–	600,977

35. Maturity profile (continued)

	2001						Total HK\$m
	Repayable on demand HK\$m	3 months or less HK\$m	1 year or less but over 3 months HK\$m	5 years or less but over 1 year HK\$m	Over 5 years HK\$m	Undated HK\$m	
Assets							
Treasury bills	–	12,721	6,190	–	–	–	18,911
Cash and other short-term funds	59,898	117,446	–	–	–	–	177,344
Placements with banks and other financial institutions	–	53,700	27,073	–	–	–	80,773
Certificates of deposit held	–	4,768	6,768	7,789	149	–	19,474
Debt securities included in:							
– held-to-maturity securities	2	8,641	12,853	24,675	4,859	–	51,030
– other investments in securities	–	27,021	5,885	22,130	1,043	–	56,079
Advances to customers	29,161	19,787	22,809	111,542	103,796	35,943	323,038
Advances to banks and other financial institutions	–	–	–	4	–	–	4
Liabilities							
Deposits and balances of banks and other financial institutions	5,154	48,477	1,664	–	–	–	55,295
Deposits from customers	205,835	367,024	32,473	1,096	–	–	606,428
Certificates of deposit issued	–	–	5,000	–	–	–	5,000

The above maturity classifications have been prepared in accordance with the guideline on “Financial Disclosure by Locally Incorporated Authorized Institutions” under the Supervisory Policy Manual issued by the HKMA. In accordance with the guideline, the Group has reported assets such as advances and debt securities which have been overdue for not more than one month as “Repayable on demand” and assets which are non-performing or which are overdue for more than one month as “Undated”. In the case of an asset which is repayable by different payments or instalments, only that portion of the asset which is actually overdue is reported as overdue. Any part of the asset which is not due is reported according to the residual maturity unless the repayment of the asset is in doubt in which case the amount is reported as “Undated”. The above assets are stated before deduction of provisions, if any.

The analysis of other investments in securities by remaining period to maturity is disclosed in order to comply with the guideline on “Financial Disclosure by Locally Incorporated Authorized Institutions” under the Supervisory Policy Manual issued by the HKMA. The disclosure does not imply that the securities will be held to maturity.

36. Off-balance sheet exposures

(a) Contingent liabilities and commitments

The following is a summary of the contractual amounts of each significant class of contingent liabilities and commitments:

	2002 HK\$m	2001 HK\$m
Direct credit substitutes	3,839	1,967
Transaction-related contingencies	2,286	2,273
Trade-related contingencies	16,409	16,391
Other commitments with an original maturity of:		
— under 1 year or which are unconditionally cancellable	75,844	84,497
— 1 year and over	64,402	43,879
Others	—	88
	162,780	149,095

(b) Derivatives

The following is a summary of the notional amounts of each significant type of derivative:

	2002			2001		
	Trading HK\$m	Hedging HK\$m	Total HK\$m	Trading HK\$m	Hedging HK\$m	Total HK\$m
Exchange rate contracts						
Spot	13,697	—	13,697	18,766	—	18,766
Forward and futures contracts	224	—	224	3,224	—	3,224
Swaps	179,544	6,082	185,626	124,585	4,688	129,273
Foreign exchange option contracts:						
— Currency options purchased	622	—	622	2,195	—	2,195
— Currency options written	28,633	—	28,633	19,850	—	19,850
	222,720	6,082	228,802	168,620	4,688	173,308
Interest rate contracts						
Interest rate swaps	228	20,055	20,283	60	10,088	10,148
Forward rate agreements	—	—	—	1,280	—	1,280
	228	20,055	20,283	1,340	10,088	11,428
Bullion contracts	779	—	779	545	—	545
Equity contracts						
— Equity options purchased	975	—	975	—	—	—
— Equity options written	873	—	873	—	—	—
	1,848	—	1,848	—	—	—
Total	225,575	26,137	251,712	170,505	14,776	185,281

36. Off-balance sheet exposures (continued)

(b) Derivatives (continued)

The replacement costs and credit risk weighted amounts of the above off-balance sheet exposures which do not take into account the effects of bilateral netting arrangements are as follows:

	2002	2001	2002	2001
	Credit risk weighted amount HK\$m	HK\$m	Replacement cost HK\$m	HK\$m
Contingent liabilities and commitments	45,936	29,490	N/A	N/A
Derivatives:				
– Exchange rate contracts	596	407	870	457
– Interest rate contracts	60	37	120	99
– Bullion contracts	5	5	13	6
– Equity contracts	33	–	17	–
	694	449	1,020	562
Total	46,630	29,939	1,020	562

The contract or notional amounts of these instruments indicate the volume of transactions outstanding as at 31 December 2002 and 31 December 2001; they do not represent the amounts at risk.

The credit risk weighted amounts are the amounts which have been calculated in accordance with the Third Schedule of the Banking Ordinance and guidelines issued by the HKMA. The amounts calculated are dependent upon the status of the counterparty and the maturity characteristics of each type of contract.

Replacement cost is the cost of replacing all contracts which have a positive value when marked to market (should the counterparty default on its obligations) and is obtained by marking contracts to market. Replacement cost is a close approximation of the credit risk for these contracts at the balance sheet dates.

37. Capital commitments

The Group has the following outstanding capital commitments not provided for in the accounts:

	2002 HK\$m	2001 HK\$m
Authorised and contracted for but not recorded	303	74
Authorised and not contracted for	–	25
	303	99

The above capital commitments mainly relate to the purchases of computer equipment and software.

38. Operating lease commitments

The Group as lessee

The Group has commitments to make the following future minimum lease payments under non-cancellable operating leases:

	2002 HK\$'m	2001 HK\$'m
Land and buildings		
– not later than one year	164	333
– later than one year but not later than five years	175	150
– later than five years	9	–
	348	483

The Group as lessor

The Group has contracted with tenants for the following future minimum lease receivables:

	2002 HK\$'m	2001 HK\$'m
Land and buildings		
– not later than one year	198	241
– later than one year but not later than five years	226	291
– later than five years	2	–
	426	532

39. Litigation

The Group is currently being served a number of claims and counterclaims by various independent parties. These claims and counterclaims are in relation to the normal commercial activities of the Group.

No material provision was made against these claims and counterclaims because the directors believe the Group has meritorious defences against the claimants or the amounts involved in these claims are not expected to be material.

40. Segmental reporting

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

Segment revenue, expenses, results, assets and liabilities include items directly attributable to a segment and those that can be allocated on a reasonable basis to that segment. The allocation of revenue reflects the benefits of capital and other funding resources allocated to the business or geographical segments by way of internal capital allocations and fund transfer mechanisms.

40. Segmental reporting (continued)

(a) By class of business

	2002					
	Commercial banking HK\$'m	Treasury HK\$'m	Unallocated HK\$'m	Subtotal HK\$'m	Eliminations HK\$'m	Consolidated HK\$'m
Net interest income	10,876	2,375	691	13,942	–	13,942
Other operating income	3,110	745	861	4,716	(544)	4,172
Operating income	13,986	3,120	1,552	18,658	(544)	18,114
Operating expenses	(4,504)	(174)	(1,891)	(6,569)	544	(6,025)
Operating profit/(loss) before provisions	9,482	2,946	(339)	12,089	–	12,089
Charge for bad and doubtful debts	(2,855)	–	–	(2,855)	–	(2,855)
Operating profit/(loss) after provisions	6,627	2,946	(339)	9,234	–	9,234
Net loss from disposal/ revaluation of fixed assets	–	–	(1,032)	(1,032)	–	(1,032)
Provision for impairment on held-to-maturity securities and investment securities	–	(4)	(3)	(7)	–	(7)
Provision for impairment on investments in associates	–	–	(27)	(27)	–	(27)
Share of operating losses of associates	–	–	(100)	(100)	–	(100)
Profit/(loss) before taxation	6,627	2,942	(1,501)	8,068	–	8,068
ASSETS						
Segment assets	313,429	400,100	21,173	734,702	–	734,702
Investments in associates	–	–	483	483	–	483
Unallocated corporate assets	–	–	304	304	–	304
	313,429	400,100	21,960	735,489	–	735,489
LIABILITIES						
Segment liabilities	612,240	62,431	2,469	677,140	–	677,140
Unallocated corporate liabilities	–	–	294	294	–	294
	612,240	62,431	2,763	677,434	–	677,434
OTHER INFORMATION						
Additions of fixed assets	–	–	1,351	1,351	–	1,351
Depreciation	–	–	632	632	–	632
Amortisation of premium/discount of held-to-maturity securities	–	1,089	–	1,089	–	1,089
Non-cash expenses other than depreciation/amortisation	2,855	–	–	2,855	–	2,855

40. Segmental reporting (continued)

(a) By class of business (continued)

	2001					
	Commercial banking HK\$m	Treasury HK\$m	Unallocated HK\$m	Subtotal HK\$m	Eliminations HK\$m	Consolidated HK\$m
Net interest income	10,758	3,238	991	14,987	–	14,987
Other operating income	2,925	888	724	4,537	(515)	4,022
Operating income	13,683	4,126	1,715	19,524	(515)	19,009
Operating expenses	(4,811)	(335)	(1,216)	(6,362)	515	(5,847)
Operating profit before provisions	8,872	3,791	499	13,162	–	13,162
Charge for bad and doubtful debts	(7,412)	–	–	(7,412)	–	(7,412)
Operating profit after provisions	1,460	3,791	499	5,750	–	5,750
Restructuring costs	–	–	(937)	(937)	–	(937)
Net loss from disposal/ revaluation of fixed assets	–	–	(1,237)	(1,237)	–	(1,237)
Net gain from disposal of held-to-maturity securities and investment securities	–	–	20	20	–	20
Write-back of provision for impairment on held-to-maturity securities and investment securities	–	23	1	24	–	24
Net gain on disposal of subsidiaries	–	–	12	12	–	12
Provision for impairment on investments in associates/gain on disposal of associates	–	–	20	20	–	20
Share of operating profits of associates	–	–	81	81	–	81
Profit/(loss) before taxation	1,460	3,814	(1,541)	3,733	–	3,733
ASSETS						
Segment assets	312,158	430,990	21,938	765,086	–	765,086
Investments in associates	–	–	416	416	–	416
Unallocated corporate assets	–	–	638	638	–	638
	312,158	430,990	22,992	766,140	–	766,140
LIABILITIES						
Segment liabilities	616,875	93,444	2,357	712,676	–	712,676
Unallocated corporate liabilities	–	–	228	228	–	228
	616,875	93,444	2,585	712,904	–	712,904
OTHER INFORMATION						
Additions of fixed assets	–	–	1,463	1,463	–	1,463
Depreciation	–	–	460	460	–	460
Amortisation of premium/discount of held-to-maturity securities	–	734	–	734	–	734
Non-cash expenses other than depreciation/amortisation	7,412	–	–	7,412	–	7,412

40. Segmental reporting (continued)

(a) By class of business (continued)

Commercial banking business includes acceptance of deposits, mortgage lending, credit card advances, remittance, provision of securities brokerage and insurance agency services, commercial lending, trade finance and overdraft facilities.

Treasury activities include money market, foreign exchange dealing and capital market activities. Treasury manages funding of the Group. Treasury provides funding to all other business segments and receives funds from commercial banking's deposit taking activities. These inter-segment funding transactions are priced either at market bid/offer rates as appropriate or at an internal funding rate as determined by the average funding requirements of other business segments and the average one-month inter-bank rates of the relevant financial year. In addition, the gains and losses on the foreign exchange activities of the Group are included under "Treasury". The profit and loss information presented in this note has been prepared using inter-segment charging/income transactions. The segmental assets and liabilities have not been adjusted to reflect the effect of inter-segment borrowing and lending (i.e. segmental profit and loss information is not comparable to segmental assets and liabilities information).

Unallocated items mainly comprise fixed assets of the Group, investment securities, investments in associates and other items which cannot be reasonably allocated to a specific business segment. The interest benefit of the capital of the Group is also included as unallocated within net interest income. Rental expenses are allocated to business segments based on a fixed rate per square footage occupied.

Operating expenses of a functional unit are allocated to the relevant business segment which is the predominant user of the services provided by the unit. Operating expenses of other shared services which cannot be allocated to a specific business segment are included under "Unallocated".

(b) By geographical area

No geographical reporting is provided as over 90% of the Group's revenues are derived from Hong Kong and over 90% of the Group's assets are originated from business decisions and operations based in Hong Kong.

41. Loans to directors and officers

Particulars of advances made to directors and officers of the Group pursuant to section 161B(4C) of the Hong Kong Companies Ordinance are as follows:

	2002 HK\$m	2001 HK\$m
Aggregate amount of relevant loans outstanding at year end	99	14
Maximum aggregate amount of relevant loans outstanding during the year	137	20

42. Significant related party transactions

Related parties are those parties which have 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 other entities.

During the year, the Group entered into various transactions with related parties including the ultimate holding company, the associates of the Group and entities, directly or indirectly, controlled or significantly influenced by the ultimate holding company.

(a) Sale of certain assets to related parties

Sale of loans to BOC Cayman in 2002

Pursuant to a sale and purchase agreement entered into on 26 June 2002 between BOCHK and BOC acting through its Grand Cayman Branch, BOCHK disposed of all of its beneficial interest in certain loans with a gross book value of HK\$11,401 million net of specific provisions of HK\$2,679 million for a consideration of HK\$8,722 million. Included in the loans disposed were loans granted to related parties with a gross book value of HK\$5,693 million and specific provisions of HK\$749 million. The consideration received in respect of these loans amounted to HK\$4,944 million. The gross and net book value of these loans included in the balance sheet as at 31 December 2001 amounted to HK\$5,418 million and HK\$4,635 million, respectively.

The sale and purchase agreement provides that BOCHK sells and BOC acquires, on and from the transaction date, without recourse the beneficial interests of BOCHK in the loans together with certain related security.

Sale of properties to BOC Insurance

On 2 December 2002, BOCHK entered into a sale and purchase agreement with BOC Insurance, an indirect owned subsidiary of BOC. Pursuant to the said agreement, BOCHK agreed to sell and BOC Insurance agreed to purchase the property known as Sin Hua Bank Centre situated at 134-136 Des Voeux Road Central at a consideration of HK\$193 million. Following completion of the said disposal, BOCHK will lease back part of the subject property from BOC Insurance at a monthly rental of HK\$400,000 per month (exclusive of rates and management fees) to continue with the operation of its Gilman Street Branch. Completion is expected to take place on or before 2 April 2003.

Service and administration of loans sold to related parties

Pursuant to servicing agreements entered into on 6 July 2002 between BOCHK, Nanyang, BOC and Zhong Gang, BOCHK and Nanyang undertake to service and administer the loans and the related securities which were transferred to Zhong Gang in 1999 and BOC Cayman in June 2002 at a fee to be agreed among the parties from time to time. In 2002, the relevant service fees amounted to approximately HK\$7 million.

(b) Purchase of certain assets from related parties

Acquisition of subsidiaries

During the year, BOCHK acquired a 100% interest in two companies, namely Sin Chiao and Perento from a fellow subsidiary, Kawell, at a total consideration of approximately HK\$1 billion. The primary business of the two companies is the holding of properties mainly used by BOCHK as bank premises. The acquisition discharged certain inter-company debts due from a fellow subsidiary to BOCHK. The transactions were conducted on normal commercial terms.

42. Significant related party transactions (continued)

(c) Advances to third parties guaranteed by related parties

As at 31 December 2002, BOC and a fellow subsidiary provided guarantees for loans in favour of the Group amounted to HK\$1,982 million (2001: HK\$1,900 million) to certain third parties. The fellow subsidiary held equity interests of not more than 20% in these third parties.

(d) Summary of transactions entered into during the ordinary course of business with the related parties

The aggregate income and expenses arising from related party transactions with BOC, fellow subsidiaries, and associates are summarised as follows:

	Note	2002 HK\$m	2001 HK\$m
Profit and loss items:			
Interest income	(i)	491	4,349
Interest expense	(ii)	(247)	(2,795)
Insurance commission received (net)	(iii)	98	39
Administrative services fees received	(iv)	24	14
Rental and license fees received	(iv)	28	25
Funds selling commission received	(vi)	103	29
Correspondent banking fee sharing	(vii)	9	8
Credit card commission paid (net)	(v)	(47)	(21)
Securities brokerage commission paid (net)	(v)	(82)	(119)
Rental fees paid	(v)	(35)	(61)
Property management and letting agency fees paid	(v)	(18)	(13)
Charge for bad and doubtful debts		(15)	(403)

	Note	2002 HK\$m	2001 HK\$m
Balance sheet items:			
Cash and short-term funds	(i)	15,041	69,458
Placements with banks and other financial institutions	(i)	17,539	13,400
Advances	(i), (viii)	867	6,531
Other investments in securities	(i)	234	234
Other assets	(ix)	5	106
Deposits from and balances of banks and other financial institutions	(ii)	20,304	48,386
Deposits from customers	(ii)	4,409	3,958
Other accounts and provisions	(ix)	5	–

42. Significant related party transactions (continued)

(d) Summary of transactions entered into during the ordinary course of business with the related parties (continued)

Notes:

(i) Interest income

In the ordinary course of business, the Group enters into various transactions with BOC, fellow subsidiaries and associates including deposit of cash and short-term funds, placement of interbank deposits, investments in its securities and provision of loans. The transactions were conducted in the normal course of business at prices and terms which are no more favourable than those charged to and contracted with other third party customers of the Group.

(ii) Interest expense

In the ordinary course of business, the Group accepts interbank deposits and current, fixed, savings and other deposits from BOC, fellow subsidiaries and associates on normal commercial terms with reference to prevailing market rates.

(iii) Insurance commission received (net)

In the ordinary course of business, the Group provides insurance agency services to and purchases general and life insurance policies from fellow subsidiaries on normal commercial terms with reference to prevailing market rates.

(iv) Administrative services fees, rental and license fees received

In the ordinary course of business, the Group provides various administrative services including internal audit, technology, human resources support and training to, and receives office premises rental and license fees from BOC, fellow subsidiaries and associates on normal commercial terms.

(v) Commission, property management, letting agency fee and rental fees paid

In the ordinary course of business, the Group pays commission fees for credit card administrative and promotional services, securities brokerage services, property management and letting agency fees to BOC and fellow subsidiaries. The Group also pays rental fees to BOC and its associates. These transactions have been entered into in the ordinary course of business and on normal commercial terms.

(vi) Funds selling commission received

In the ordinary course of business, the Group also engages in promoting and selling fund products of a fellow subsidiary to customers of the Group as their intermediary on normal commercial terms.

(vii) Correspondent banking fee sharing

In the ordinary course of business, the Group provides services to its customers include advising on and collecting letters of credit issued by BOC and remittances. BOC also provides similar services to its customers including advising on and collecting letters of credit issued by the Group and remittances. The Group shares the fees paid by customers of BOC and of the Group accordingly.

(viii) Advances to related parties

In the ordinary course of business, the Group extends loans and credit facilities to BOC, fellow subsidiaries, and associates on normal commercial terms with reference to prevailing market rates. The revenue from such transactions would include interest income on the amount drawn as well as arrangement and commitment fees.

(ix) Other assets and other accounts and provisions

Included within "Other assets" and "Other accounts and provisions" are receivables from and payables to BOC and fellow subsidiaries. The receivables and payables arose from transactions carried out in the normal course of business.

(e) Off-balance sheets items

Contingent liabilities and commitments

In the ordinary course of business, the Group provides guarantees for the obligations of BOC and fellow subsidiaries on normal commercial terms. Such guarantees as at 31 December 2002 amounted to HK\$185 million (2001: HK\$297 million).

42. Significant related party transactions (continued)

(e) Off-balance sheets items (continued)

Derivatives

In the ordinary course of business, the Group enters into foreign exchange contracts and interest rate contracts with BOC and fellow subsidiaries. The aggregate notional amount of such derivative transactions amounted to HK\$12,722 million as at 31 December 2002 (2001: HK\$10,655 million). These transactions are executed on normal commercial terms with reference to prevailing market rates.

(f) Balances with group companies and associates

Included in the following balance sheet captions are balances with the ultimate holding company:

	2002 HK\$m	2001 HK\$m
Cash and short-term funds	15,031	69,197
Placements with banks and other financial institutions	17,533	13,053
Advances	4	37
Other investments in securities	234	234
Other assets	–	106
Deposits from and balances of banks and other financial institutions	19,107	48,004

Included in the following balance sheet captions are balances with fellow subsidiaries and associates of the ultimate holding company:

	2002 HK\$m	2001 HK\$m
Cash and short-term funds	10	191
Placements with banks and other financial institutions	6	347
Advances	517	5,717
Other assets	5	–
Deposits from and balances of banks and other financial institutions	1,195	379
Deposits from customers	4,352	3,936
Other accounts and provisions	5	–

There were no material balances with associates of the Group as at 31 December 2002.

(g) Key management personnel

Other than the advances to key management personnel of approximately HK\$99 million, no material transaction was conducted with key management personnel of BOCHK and its holding companies and parties related to them.

43. Ultimate holding company

The ultimate holding company is BOC, a state-owned commercial bank established under the laws of PRC.

44. Approval of accounts

The accounts were approved and authorised for issue by the Board of Directors on 20 March 2003.