

**MEVAS BANK LIMITED  
DIRECTORS' REPORT AND FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 31 DECEMBER 2009**

**MEVAS Bank Limited**  
**Report of the Directors**

The Directors submit their report together with the audited financial statements for the year ended 31 December 2009.

**Principal Activities**

The principal activities of MEVAS Bank Limited (the "Bank") are the provision of banking and related financial services. The principal activity of the subsidiary is shown in Note 24 to the financial statements.

**Results and Appropriations**

The results of the Bank for the year ended 31 December 2009 are set out in the income statement on page 4.

The Directors do not recommend the payment of a final dividend.

**Reserves**

Movements in reserves of the Bank during the year are set out in Note 33 to the financial statements.

**Fixed Assets**

Movements in the fixed assets of the Bank during the year are shown in Note 22 to the financial statements.

**Directors**

The Directors during the year and up to the date of this report are:

David Shou-Yeh Wong  
Chairman

\*John William Simpson

\*David Richard Hinde

\*Robert Tsai-To Sze

Hon-Hing Wong (Derek Wong)

Gary Pak-Ling Wang

Harold Tsu-Hing Wong (ceased to be the Chief Executive on 18 May 2009)

Frederic Suet-Chiu Lau

John Cheung-Wah Lam  
Alternate Chief Executive

Hoi-Leung Ho (appointed on 18 May 2009)  
Chief Executive

Po-Fung So (Francesca So) (appointed on 18 May 2009)

*\*Independent Non-executive Directors*

There being no provision in the Bank's Articles of Association for retirement by rotation, all Directors continue in office.

## MEVAS Bank Limited

### Report of the Directors

#### Directors' Interests

Pursuant to the Share Option Schemes (the "Schemes") as approved by the shareholders of Dah Sing Financial Holdings Limited ("DSFH") and Dah Sing Banking Group Limited ("DSBG"), the Bank's ultimate and immediate holding companies respectively, certain Directors of the Bank were granted options at a consideration of HK\$1 per option to subscribe for shares of DSFH or DSBG with a par value of HK\$2 and HK\$1 each respectively. The exercise price per share for the options varied by tranches of grant, which was determined in accordance with Rule 17.03(9) of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited being calculated as the higher of (i) the closing price of relevant shares traded on The Stock Exchange of Hong Kong Limited ("SEHK") on the date of grant; and (ii) the average closing price of relevant shares traded on the SEHK for the five trading days immediately preceding the date of the grant. The options can be exercised in varying amounts between the first and sixth anniversaries from the date of grant.

Details of the share options outstanding as at 31 December 2009 which have been granted under the Schemes are as follows:

Director	Number of shares in the options					Held at 31/12/2009	Exercise price HK\$	Exercise period		
	Held at 1/1/2009	Granted during 2009	Exercised during 2009	Lapsed / cancelled during 2009	Grant date (d/m/y)			From (d/m/y)	To (d/m/y)	
Number of DSBG share options										
Frederic Suet-Chiu Lau	250,000	-	-	-	250,000	14.40	25/8/2005	25/8/2006	25/8/2011	
Po-Fung So (Francesca So)	100,000	-	-	-	100,000	14.40	25/8/2005	25/8/2006	25/8/2011	
John Cheung-Wah Lam	250,000	-	-	-	250,000	14.32	30/12/2005	30/12/2006	30/12/2011	
Number of DSFH share options										
Hon-Hing Wong (Derek Wong)	1,000,000	-	-	-	1,000,000	51.71	25/8/2005	25/8/2006	25/8/2011	
Gary Pak-Ling Wang	400,000	-	-	-	400,000	51.71	25/8/2005	25/8/2006	25/8/2011	
Harold Tsu-Hing Wong	250,000	-	-	-	250,000	51.71	25/8/2005	25/8/2006	25/8/2011	
	100,000	-	-	-	100,000	61.93	28/9/2007	28/9/2008	28/9/2013	

Apart from the above, at no time during the year was the Bank, its subsidiary, its fellow subsidiaries or its holding companies a party to any arrangement to enable the Directors of the Bank nor their spouse or children under 18 years of age to acquire benefits by means of the acquisition of shares in, or debentures of, the Bank or any other body corporate.

The Directors do not have any service contracts with the Bank.

No contracts of significance in relation to the Bank's business to which the Bank, its subsidiary, its fellow subsidiaries or its holding companies was a party and in which a Director of the Bank had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year.

## **MEVAS Bank Limited**

### **Report of the Directors**

#### **Management Contracts**

Pursuant to a services agreement between the Bank and Dah Sing Bank, Limited (“DSB”), a fellow subsidiary, the Bank has outsourced the management and administration of most of its banking operations, credit risk management, information technology and other support services to DSB at a service fee agreed on an annual basis. This services agreement can be terminated by either party by giving the other party not less than 9 months’ written notice.

#### **Connected Transactions**

Details of transactions with related parties of the Group for the year ended 31 December 2009 have been set out in Note 30 and 36 to the financial statements.

#### **Statement of Compliance**

In preparing the financial statements for the year ended 31 December 2009, the Bank has fully complied with the requirements set out in the Banking (Disclosure) Rules issued by the Hong Kong Monetary Authority under section 60A of the Hong Kong Banking Ordinance. The Bank has fully complied with such disclosure requirements.

#### **Auditors**

The financial statements have been audited by PricewaterhouseCoopers who retire and, being eligible, offer themselves for re-appointment.

On behalf of the Board

**David Shou-Yeh Wong**  
*Chairman*

Hong Kong, 22 March 2010

**MEVAS Bank Limited**

**Income Statement**

**For the year ended 31 December 2009**

**(Expressed in thousands of Hong Kong dollars)**

	Note	2009	2008
Interest income		<b>108,094</b>	232,908
Interest expense		<b>(41,789)</b>	(146,476)
<b>Net interest income</b>	<b>6</b>	<b>66,305</b>	86,432
Fee and commission income		<b>20,559</b>	31,193
Fee and commission expense		<b>(1,594)</b>	(2,264)
<b>Net fee and commission income</b>	<b>7</b>	<b>18,965</b>	28,929
Net trading income	<b>8</b>	<b>1,100</b>	1,273
Other operating income	<b>9</b>	<b>4,822</b>	3,760
<b>Operating income</b>		<b>91,192</b>	120,394
Operating expenses	<b>10</b>	<b>(110,178)</b>	(94,195)
<b>Operating (loss) / profit before impairment losses</b>		<b>(18,986)</b>	26,199
Impairment losses on loans and advances	<b>13</b>	<b>(16,711)</b>	(14,730)
<b>Operating (loss) / profit before gains or losses on certain investments and fixed assets</b>		<b>(35,697)</b>	11,469
Net (loss) / gain on disposal of furniture and equipment		<b>(35)</b>	1
Net gain / (loss) from fair value adjustment on investment properties		<b>13,000</b>	(8,000)
Net (loss) / gain on disposal of available-for-sale securities		<b>(368)</b>	62
Net gain on disposal of personal loan portfolio	<b>14</b>	<b>3,100</b>	-
Net gain on transfer of credit card portfolio	<b>14</b>	<b>27,000</b>	-
<b>Profit before income tax</b>		<b>7,000</b>	3,532
Income tax credit / (expense)	<b>15</b>	<b>141</b>	(547)
<b>Profit attributable to shareholders of the Bank</b>		<b>7,141</b>	2,985
<b>Dividend</b>			
Interim dividend paid		<b>-</b>	30,000

The notes on pages 9 to 75 are an integral part of these financial statements.

**MEVAS Bank Limited**

**Statement of Comprehensive Income  
For the year ended 31 December 2009  
(Expressed in thousands of Hong Kong dollars)**

	<b>Note</b>	<b>2009</b>	2008
<b>Profit for the year</b>		<u>7,141</u>	<u>2,985</u>
<b>Other comprehensive income</b>			
Unrealised net gains on available-for-sale securities	<b>33</b>	<b>1,013</b>	650
Amounts transferred from / (to) profit or loss upon disposal of available-for-sale securities	<b>33</b>	<b>368</b>	(62)
Income tax relating to components of other comprehensive income	<b>33</b>	<u><b>(263)</b></u>	<u>(104)</u>
<b>Other comprehensive income for the year, net of tax</b>		<u><b>1,118</b></u>	<u>484</u>
<b>Total comprehensive income for the year</b>		<u><b>8,259</b></u>	<u>3,469</u>

The notes on pages 9 to 75 are an integral part of these financial statements.

**MEVAS Bank Limited****Statement of Financial Position****As at 31 December 2009****(Expressed in thousands of Hong Kong dollars)**

	Note	2009	2008
<b>ASSETS</b>			
Cash and balances with banks	16	1,713,137	4,327,407
Derivative financial instruments	17	8	2,717
Financial assets designated at fair value through profit or loss	18	-	82,721
Advances and other accounts	19,25	1,685,286	1,851,267
Available-for-sale securities	21	912,701	11,450
Furniture and equipment	22	6,666	8,384
Investment properties	23	76,000	63,000
Current income tax assets		4,751	2,607
Deferred income tax assets	29	-	1,847
<b>Total assets</b>		<b>4,398,549</b>	<b>6,351,400</b>
<b>LIABILITIES</b>			
Deposits from banks		18,574	14,088
Derivative financial instruments	17	77	2,733
Deposits from customers	26	3,614,060	5,747,294
Deposits from customers designated at fair value through profit or loss	27	-	82,721
Other accounts and accruals	28	335,959	83,363
Deferred income tax liabilities	29	419	-
<b>Total liabilities</b>		<b>3,969,089</b>	<b>5,930,199</b>
<b>EQUITY</b>			
Share capital	32	400,000	400,000
Reserves			
Retained earnings	33	27,814	20,673
Investment revaluation reserve	33	1,646	528
<b>Total equity</b>		<b>429,460</b>	<b>421,201</b>
<b>Total equity and liabilities</b>		<b>4,398,549</b>	<b>6,351,400</b>

Approved and authorised for issue by the Board of Directors on 22 March 2010.

**David Shou-Yeh Wong**  
*Director***Frederic Suet-Chiu Lau**  
*Director***Gary Pak-Ling Wang**  
*Director***Hoi-Leung Ho**  
*Chief Executive*

The notes on pages 9 to 75 are an integral part of these financial statements.

**MEVAS Bank Limited**

**Statement of Changes in Equity  
For the year ended 31 December 2009  
(Expressed in thousands of Hong Kong dollars)**

	<u>Attributable to the shareholders of the Bank</u>			<b>Total equity</b>
	<b>Share capital</b>	<b>Investment revaluation reserve</b>	<b>Retained earnings</b>	
<b>Balance at 1 January 2009</b>	<b>400,000</b>	<b>528</b>	<b>20,673</b>	<b>421,201</b>
Total comprehensive income for the year	-	1,118	7,141	8,259
<b>Balance at 31 December 2009</b>	<b>400,000</b>	<b>1,646</b>	<b>27,814</b>	<b>429,460</b>

  

	<u>Attributable to the shareholders of the Bank</u>			<b>Total equity</b>
	<b>Share capital</b>	<b>Investment revaluation reserve</b>	<b>Retained earnings</b>	
Balance at 1 January 2008	400,000	44	47,688	447,732
Total comprehensive income for the year	-	484	2,985	3,469
2008 interim dividend	-	-	(30,000)	(30,000)
<b>Balance at 31 December 2008</b>	<b>400,000</b>	<b>528</b>	<b>20,673</b>	<b>421,201</b>

The notes on pages 9 to 75 are an integral part of these financial statements.

**MEVAS Bank Limited****Statement of Cash Flows****For the year ended 31 December 2009****(Expressed in thousands of Hong Kong dollars)**

	<b>Note</b>	<b>2009</b>	<b>2008</b>
<b>Cash flows from operating activities</b>			
Cash absorbed by operations		<b>(2,614,046)</b>	(211,032)
Hong Kong profits tax paid		-	(10,823)
Net cash used in operating activities	<b>34(a)</b>	<u><b>(2,614,046)</b></u>	<u>(221,855)</u>
<b>Cash flows from investing activities</b>			
Purchase of investment properties		-	(71,000)
Purchase of furniture and equipment		<u><b>(224)</b></u>	<u>(656)</u>
Net cash used in investing activities		<u><b>(224)</b></u>	<u>(71,656)</u>
<b>Cash flows from financing activities</b>			
Dividend paid on ordinary shares		-	(30,000)
Net cash used in financing activities		<u>-</u>	<u>(30,000)</u>
<b>Net decrease in cash and cash equivalents</b>		<b>(2,614,270)</b>	(323,511)
Cash and cash equivalents at beginning of the year		<u><b>4,327,407</b></u>	<u>4,650,918</u>
<b>Cash and cash equivalents at end of the year</b>	<b>34(b)</b>	<u><b>1,713,137</b></u>	<u>4,327,407</u>

The notes on pages 9 to 75 are an integral part of these financial statements.

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

#### 1. General information

MEVAS Bank Limited (the "Bank") provides retail and commercial banking and related financial services in Hong Kong.

The Bank is a financial institution incorporated in Hong Kong. The address of its registered office is 36th Floor, Dah Sing Financial Centre, 108 Gloucester Road, Wanchai, Hong Kong.

The ultimate holding company is Dah Sing Financial Holdings Limited, a listed company incorporated in Hong Kong.

These financial statements are presented in thousands of units of Hong Kong dollars (HK\$'000), unless otherwise stated. These financial statements have been approved for issue by the Board of Directors on 22 March 2010.

#### 2. Summary of significant accounting policies

The principal accounting policies applied in the preparation of these financial statements are set out below. These policies have been consistently applied to all the reporting years presented, unless otherwise stated.

##### 2.1 Basis of preparation

Consolidated financial statements have not been prepared as the Bank is a wholly owned subsidiary of another body corporate, Dah Sing Banking Group Limited. The financial statements of the Bank have been prepared in accordance with Hong Kong Financial Reporting Standards ("HKFRSs" is a collective term which includes all applicable individual Hong Kong Financial Reporting Standards, Hong Kong Accounting Standards ("HKASs") and Interpretations) issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA"), accounting principles generally accepted in Hong Kong and the requirements of the Hong Kong Companies Ordinance.

These financial statements have been prepared under the historical cost convention, as modified by the revaluation of investment properties, available-for-sale financial assets, and financial assets and financial liabilities (including derivative instruments) at fair value through profit or loss.

The preparation of financial statements in conformity with HKFRSs requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Bank's accounting policies. Changes in assumptions may have a significant impact on the financial statements in the period the assumptions changed. Management believes that the underlying assumptions are appropriate and that the Bank's financial statements therefore present the financial position and results fairly. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements, are disclosed in Note 4.

(a) Standards, amendments and interpretations effective on or after 1 January 2009

Standard/ Interpretation	Content	Applicable for financial years beginning on/ after	Relevant to the Bank
HKFRS 2	Share-based payments - Vesting Conditions and Cancellations	1 January 2009	No
HKFRS 7	Improving Disclosures about Financial Instruments	1 January 2009	Yes
HKFRS 8	Operating Segments	1 January 2009	Yes
HKAS 1	Presentation of Financial Statements	1 January 2009	Yes
HKAS 23	Borrowing Costs	1 January 2009	No
HKAS 32 and HKAS 1	Puttable Financial Instruments and Obligations Arising on Liquidation	1 January 2009	No
HK (IFRIC) - Int 13	Customer Loyalty Programmes	1 July 2008	Yes

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

## 2. Summary of significant accounting policies (Continued)

### 2.1 Basis of preparation (Continued)

(a) Standards, amendments and interpretations effective on or after 1 January 2009 (Continued)

Standard/ Interpretation	Content	Applicable for financial years beginning on/ after	Relevant to the Bank
HK (IFRIC) - Int 15	Agreements for the Construction of Real Estate	1 January 2009	No
HK (IFRIC) - Int 16	Hedges of a Net Investment in a Foreign Operation	1 October 2008	No

#### HKFRS 2 Share-based Payments - Vesting Conditions and Cancellations

The HKICPA published an amendment to HKFRS 2 - Share-based Payments in March 2008. The changes pertain mainly to the definition of vesting conditions and the regulations for the cancellation of a plan by a party other than the company. These changes clarify that vesting conditions are solely service and performance conditions. As a result of the amended definition of vesting conditions, non-vesting conditions are now to be considered when estimating the fair value of the equity instrument granted. Furthermore, the Standard describes the posting type, if the vesting conditions and non-vesting conditions are not fulfilled. The application of HKFRS2 does not have an impact on the Bank's financial statements.

#### Amendment to HKFRS 7 Improving Disclosures about Financial Instruments

The HKICPA published amendments to the HKFRS 7 in March 2009. The amendments require enhanced disclosures about fair value measurements and liquidity risk. In particular, the amendment requires disclosure of fair value measurements by level of a fair value measurement hierarchy. The adoption of the amendment results in additional disclosures but does not have an impact on the financial position or the comprehensive income of the Bank.

#### HKFRS 8 Operating Segments

HKFRS 8 was issued in March 2007 and excluding early adoption would first be required to be applied to the Bank's accounting period beginning on 1 January 2009. The Standard replaces HKAS 14 Segment Reporting with its requirement to determine primary and secondary reporting segments. Under the requirements of the new Standard, the Bank's external segmental reporting will be based on the internal reporting to the Chief Executive and other members of the Executive Committee (in its function as the chief operating decision maker) which make decisions on the allocation of resources and assess the performance of the reportable segments. The application of HKFRS 8 does not have any material effects for the Bank but has an impact on segment disclosure and on the measurement bases within segments. The segment results have been changed accordingly.

#### HKAS 1 Presentation of Financial Statements

A revised version was issued in December 2007. It prohibits the presentation of items of income and expenses (that is, "non-owner changes in equity") in the statement of changes in equity, requiring "non-owner changes in equity" to be presented separately from owner changes in equity in a statement of comprehensive income. As a result, the Bank presents in the statement of changes in equity all owner changes in equity, whereas all non-owner changes in equity are presented in the statement of comprehensive income. Comparative information has been re-presented so that it also conforms with the revised Standard. According to the amendment of HKAS 1, each component of equity, including each item of other comprehensive income, should be reconciled between carrying amount at the beginning and the end of the period. Since the change in accounting policy only impacts presentation aspects, there is no impact on retained earnings.

#### HKAS 23 Borrowing Costs

A revised version was issued in June 2007. This eliminates the option of immediate recognition of borrowing costs as an expense regarding assets that require a substantial period of time to get ready for their intended use. The application of HKAS 23 Amendment does not have an impact on the results or items in the statement of financial position of the Bank.

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

## 2. Summary of significant accounting policies (Continued)

### 2.1 Basis of preparation (Continued)

(a) Standards, amendments and interpretations effective on or after 1 January 2009 (Continued)

#### HKAS 32 and HKAS 1 Puttable Financial Instruments and Obligations Arising on Liquidation

In June 2008, the HKICPA amended HKAS 32 by requiring some financial instruments that meet the definition of a financial liability to be classified as equity. Puttable financial instruments that represent a residual interest in the net assets of the entity are now classified as equity provided that specified conditions are met. Similar to those requirements is the exception to the definition of a financial liability for instruments that entitle the holder to a pro rata share of the net assets of an entity only on liquidation. The adoption of the amended HKAS 32 does not have an impact on the Bank's financial statements.

#### HK (IFRIC) - Int 13 Customer Loyalty Programmes

HK (IFRIC) - Int 13 clarifies that where goods or services are sold together with a customer loyalty incentive (for example, loyalty points or free products), the arrangement is a multiple element arrangement, and the consideration receivable from the customer is allocated between the components of the arrangement using fair values. HK (IFRIC) - Int 13 is relevant to the Bank's operation as the Bank operates some loyalty programmes.

#### HK (IFRIC) - Int 15 Agreements for the Construction of Real Estate

The Interpretation clarifies whether HKAS 18 "Revenue" or HKAS 11 "Construction contracts" should be applied to particular transactions. It is likely to result in HKAS 18 being applied to a wider range of transactions. This Interpretation does not have an impact on the Bank's financial statements.

#### HK (IFRIC) - Int 16 Hedges of a Net Investment in a Foreign Operation

This Interpretation clarifies the accounting treatment in respect of net investment hedging. This includes the fact that net investment hedging relates to differences in functional currency not presentation currency, and hedging instruments may be held anywhere in the Bank. This Interpretation does not have an impact on the Bank's financial statements.

(b) Standards and Interpretations issued but not yet effective

The following Standards and Interpretations have been issued and are mandatory for the Bank's accounting periods beginning on or after 1 July 2009 or later periods:

Standard/ Interpretation	Content	Applicable for financial years beginning on/ after	Relevant to the Bank	Early adopted by the Bank
HKFRS 1 and HKAS 27	Cost of an Investment in a Subsidiary, Jointly-Controlled Entity or Associate	1 July 2009	No	No
HKFRS 3	Business Combinations	1 July 2009	No	No
HKAS 27	Consolidated and Separate Financial Statements	1 July 2009	No	No
HKAS 39	Financial Instruments: Recognition and Measurements - Eligible Hedged Items	1 July 2009	No	No
HK (IFRIC) - Int 17	Distribution of Non-Cash Assets to Owners	1 July 2009	No	No
HK (IFRIC) - Int 18	Transfers of Assets from Customers	1 July 2009	No	No

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

## 2. Summary of significant accounting policies (Continued)

### 2.1 Basis of preparation (Continued)

(b) Standards and Interpretations issued but not yet effective (Continued)

Standard/ Interpretation	Content	Applicable for financial years beginning on/ after	Relevant to the Bank	Early adopted by the Bank
HKFRS 2	Group Cash-settled Share-based Payment Transaction	1 January 2010	No	No
HKAS 32	Classification of Rights Issue	1 February 2010	No	No
HK (IFRIC) - Int 19	Extinguishing Financial Liabilities with Equity Instruments	1 July 2010	No	No
HKAS 24	Related Party Disclosures	1 January 2011	Yes	No
HK (IFRIC) - Int 14	The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction	1 January 2011	No	No
HKFRS 9	Financial Instruments Part 1: Classification and Measurement	1 January 2013	Yes	No

#### HKFRS 1 and HKAS 27 Cost of an Investment in a Subsidiary, Jointly-Controlled Entity or Associate

The amended Standard allows first-time adopters to use a deemed cost of either fair value or the carrying amount under previous accounting practice to measure the initial cost of investments in subsidiaries, jointly controlled entities and associates in the separate financial statements. The amendment also removes the definition of the cost method from HKAS 27 and replaces it with a requirement to present dividends as income in the separate financial statements of the investor.

#### HKFRS 3 Business Combinations

The revised Standard continues to apply the acquisition method to business combinations, with some significant changes. For example, all payments to purchase a business are to be recorded at fair value at the acquisition date, with contingent payments classified as debt subsequently re-measured through the income statement. There is a choice on an acquisition-by-acquisition basis to measure the non-controlling interest in the acquiree either at fair value or at the non-controlling interest's proportionate share of the acquiree's net assets. All acquisition-related costs should be expensed.

#### HKAS 27 Consolidated and Separate Financial Statements

The revised Standard requires the effects of all transactions with non-controlling interests to be recorded in equity if there is no change in control and these transactions will no longer result in goodwill or gains and losses. The Standard also specifies the accounting when control is lost. Any remaining interest in the entity is re-measured to fair value, and a gain or loss is recognised in profit or loss. The revised Standard will tend to produce higher volatility in equity and/or earnings in connection with the sale or acquisition of interests by the Bank.

#### HKAS 39 Financial Instruments: Recognition and Measurement - Eligible Hedged Items

The amendment was issued in November 2008. It provides guidance in two situations: On the designation of a one-sided risk in a hedged item HKAS 39 concludes that a purchased option designated in its entirety as the hedging instrument of a one-sided risk will not be perfectly effective. The designation of inflation as a hedged risk or portion is not permitted unless in particular situations. This is not expected to give rise to any changes to the Bank's financial statements.

## **MEVAS Bank Limited**

### **Notes to the Financial Statements**

(Expressed in thousands of Hong Kong dollars)

## **2. Summary of significant accounting policies (Continued)**

### **2.1 Basis of preparation (Continued)**

(b) Standards and Interpretations issued but not yet effective (Continued)

#### **HK (IFRIC) - Int 17 Distribution of Non-Cash Assets to Owners**

HK (IFRIC) - Int 17 was issued in December 2008. It addresses how the non-cash dividends distributed to the shareholders should be measured. A dividend obligation is recognised when dividend was authorised by the appropriate entity and is no longer at the discretion of the entity. This dividend obligation should be recognised at the fair value of the net assets to be distributed. The difference between the dividend paid and the amount carried forward of the net assets distributed should be recognised in profit and loss.

Additional disclosures are to be made if the net assets being held for distribution to owners meet the definition of a discontinued operation. The application of HK (IFRIC) 17 is not expected to have any impact on the financial statements of the Bank.

#### **HK (IFRIC) - Int 18 Transfer of Assets from Customers**

HK (IFRIC) - Int 18 was issued in February 2009. It clarifies how to account for transfer of items of property, plant and equipment by entities that receive such transfers from their customers. The Interpretation also applies to agreements in which an entity receives cash from a customer when that amount of cash must be used only to construct or acquire an item of property, plant and equipment and the entity must then use that item to provide the customer with ongoing access to supply of goods and/or services. The Bank is not expected to be impacted by applying HK (IFRIC) - Int 18.

#### **HKFRS 2 Group Cash-settled Share-based Payment Transaction**

The amended Standard addresses the accounting in the separate financial statements of a subsidiary when its suppliers/employees will receive cash payments from the parent that are linked to the price of the equity instruments of an entity in the group. The parent, and not the entity, has the obligation to deliver cash. The amendments state that the entity shall account for the transaction with its suppliers/employees as equity-settled, and recognise a corresponding increase in equity as a contribution from its parent. The subsidiary shall remeasure the cost of the transaction subsequently for any changes resulting from non-market vesting conditions. The adoption of these amendments is not expected to have any impact on the Bank's financial statements.

#### **HKAS 32 Classification of Rights Issue**

The amendment requires rights issues to be classified as equity if they are issued for a fixed amount of cash regardless of the currency in which the exercise price is denominated, provided they are offered on a pro rata basis to all owners of the same class of equity. The adoption of this amendment is not expected to have any impact on the Bank's financial statements.

#### **HK (IFRIC) - Int 19 Extinguishing Financial Liabilities with Equity Instruments**

The interpretation clarifies the accounting by the debtor when the debtor renegotiates the terms of its debt with the result that the liability is extinguished through issuing its own equity instruments to the creditor (i.e. a "debt for equity swap"). A gain or loss recognised in profit or loss is the difference between the fair value of the equity instruments issued and the carrying amount of the financial liability. The adoption of this interpretation is not expected to have any impact on the Bank's financial statements.

#### **HKAS 24 Related party disclosures**

The revised Standard introduces an exemption from all of the disclosure requirements of IAS/HKAS 24 for transactions among government-related entities and the government. The Standard also clarifies and simplifies the definition of a related party. The adoption of the revised Standard results in revised disclosures but does not have an impact on the financial position or the comprehensive income of the Bank.

## **MEVAS Bank Limited**

### **Notes to the Financial Statements**

(Expressed in thousands of Hong Kong dollars)

## **2. Summary of significant accounting policies (Continued)**

### **2.1 Basis of preparation (Continued)**

(b) Standards and Interpretations issued but not yet effective (Continued)

#### **HK (IFRIC) - Int 14 The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction**

The interpretation clarifies when refunds or reductions in future contributions for defined benefit type of employee benefits should be regarded as available and how a minimum funding requirement might affect the availability of reductions in future contributions or might give rise to a liability. The Bank does not operate any defined benefit type of employee benefits. This interpretation is not relevant to the Bank.

#### **HKFRS 9 Financial Instruments Part 1: Classification and Measurement**

HKFRS 9 was issued in November 2009 and replaces those parts of HKAS 39 relating to the classification and measurement of financial assets. Key features are as follows:

Financial assets are required to be classified into two measurement categories: those to be measured subsequently at fair value, and those to be measured subsequently at amortised cost. The decision is to be made at initial recognition. The classification depends on the entity's business model for managing its financial instruments and the contractual cash flow characteristics of the instruments.

An instrument is subsequently measured at amortised cost only if it is a debt instrument and both the objective of the entity's business model is to hold the asset to collect the contractual cash flows, and the asset's contractual cash flows represent only payments of principal and interest (that is, it has only "basic loan features"). All other debt instruments are to be measured at fair value through profit or loss.

All equity instruments are to be measured subsequently at fair value. Equity instruments that are held for trading will be measured at fair value through profit and loss. For all other equity instruments, an irrevocable election can be made at initial recognition, to recognise unrealised and realised fair value gains and losses through other comprehensive income rather than profit and loss. There is to be no recycling of fair value gains and losses to profit and loss. This election may be made on an instrument-by-instrument basis. Dividends are to be presented in profit and loss, as long as they represent a return on investment.

While adoption of HKFRS 9 is mandatory from 1 January 2013, earlier adoption is permitted.

The Bank is considering the implications of the Standard, the impact on the Bank and the timing of its adoption by the Bank.

(c) Improvements to HKFRS

"Improvements to HKFRS" contains numerous amendments to HKFRS which the HKICPA consider non-urgent but necessary. "Improvements to HKFRS" comprise amendments that result in accounting changes for presentation, recognition or measurement purposes as well as terminology or editorial amendments related to a variety of individual HKFRS. Most of the amendments are effective for annual periods beginning on or after 1 January 2009 or 1 January 2010 respectively, with earlier adoption permitted. No material changes to the Group's accounting policies are expected as a result of these amendments.

### **2.2 Consolidation**

Consolidated financial statements have not been prepared as the Bank is a wholly owned subsidiary of another body corporate, Dah Sing Banking Group Limited.

## **MEVAS Bank Limited**

### **Notes to the Financial Statements**

(Expressed in thousands of Hong Kong dollars)

## **2. Summary of significant accounting policies (Continued)**

### **2.3 Interest income and expenses**

Interest income and expense are recognised in the income statement for all instruments measured at amortised cost, available-for-sale securities and certain financial assets/liabilities designated at fair value through profit or loss using the effective interest method.

The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Bank estimates cash flows considering all contractual terms of the financial instrument (for example, prepayment options) but does not consider future credit losses. The calculation includes all fees and points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts.

Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income is recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

### **2.4 Fee and commission income and expense**

Fees and commissions are generally recognised on an accrual basis when the service has been provided. Loan syndication fees are recognised as revenue when the syndication has been completed and the Bank retained no part of the loan package for itself or retained a part at the same effective interest rate as the other participants. Wealth management, financial planning and custody services that are continuously provided over an extended period of time are recognised rateably over the period the service is provided.

### **2.5 Financial assets**

#### **2.5.1 Classification**

The Bank classifies its financial assets in the following categories: financial assets at fair value through profit or loss, loans and receivables and available-for-sale financial assets. The classification depends on the purpose for which the investments were acquired. Management determines the classification of its investments at initial recognition, except for subsequent reclassification meeting specified definition of relevant asset reclassification.

#### **(a) Financial assets at fair value through profit or loss**

This category has two sub-categories: financial assets held for trading, and those designated at fair value through profit or loss at inception. A financial asset is classified as held for trading if it is acquired principally for the purpose of selling in the short term or if so designated by management. Derivatives are also categorised as held for trading unless they are designated as hedges.

The Bank designates a financial asset upon initial recognition as designated at fair value through profit or loss (fair value option) if the following criteria are met:

- (i) It eliminates or significantly reduces a measurement or recognition inconsistency (sometimes referred to as "an accounting mis-match") that would otherwise arise from measuring the financial assets or recognising the gains and losses on them on different bases; or
- (ii) A group of financial assets is managed and its performance is evaluated on a fair value basis, in accordance with a documented risk management or investment strategy, and this is the basis on which information about the assets is provided internally to the key management personnel such as the Board of Directors and Chief Executive Officer; or
- (iii) Financial assets with embedded derivatives where the characteristics and risks of the embedded derivatives are not closely related to the host contracts.

## **MEVAS Bank Limited**

### **Notes to the Financial Statements**

(Expressed in thousands of Hong Kong dollars)

## **2. Summary of significant accounting policies (Continued)**

### **2.5 Financial assets (Continued)**

#### 2.5.1 Classification (Continued)

##### (a) Financial assets at fair value through profit or loss (Continued)

Financial assets for which the fair value option is applied are recognised in the statement of financial position as “Financial assets designated at fair value through profit or loss”.

##### (b) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than: (i) those that the Bank intends to sell immediately or in the short term, which are classified as held for trading, and those that the Bank upon initial recognition designates as at fair value through profit or loss; (ii) those that the Bank upon initial recognition designates as available-for-sale; or (iii) those for which the Bank may not recover substantially all of its initial investment, other than because of credit deterioration.

##### (c) Available-for-sale

Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories. Available-for-sale investments are those intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices.

#### 2.5.2 Recognition and measurement

Purchases and sales of financial assets are recognised on the trade date – the date on which the Bank commits to purchase or sell the asset.

Financial assets are initially recognised at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets carried at fair value through profit or loss are initially recognised at fair value, and transaction costs are expensed in the income statement. Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or the Bank has transferred substantially all the risks and rewards of ownership and the transfer qualifies for derecognition.

The bases for the determination of fair value of financial assets are set out in Note 3.5(a).

##### (a) Financial assets at fair value through profit or loss

Gains and losses arising from changes in fair value of financial assets held for trading and financial assets designated at fair value at inception are included directly in the income statement and are reported as part of “Net trading income”. Interest income and expense and dividend income and expenses derived from and incurred on financial assets at fair value through profit or loss are included in “Net interest income” and “Dividend income” respectively.

##### (b) Loans and receivables

Loans and receivables are carried at amortised cost less any impairment loss. For loans and receivables that are subject to fair value hedge arrangements, the hedged elements of the loans and receivables hedged are carried at fair value.

## **MEVAS Bank Limited**

### **Notes to the Financial Statements**

(Expressed in thousands of Hong Kong dollars)

## **2. Summary of significant accounting policies (Continued)**

### **2.5 Financial assets (Continued)**

#### 2.5.2 Recognition and measurement (Continued)

##### (c) Available-for-sale

Available-for-sale financial assets are initially recognised at fair value which is the cash given including any transaction costs. They are measured subsequently at fair value with gains and losses (except for impairment losses and foreign exchange gains and losses) recognised in equity and reported in the reconciliation from results of the year to total comprehensive income until the financial assets are derecognised.

If an available-for-sale financial asset is determined to be impaired the cumulative gain or loss previously recognised in equity and reported in the reconciliation from results of the year to total comprehensive income is recognised in the separate income statement.

Interest is calculated using the effective interest method. Foreign currency gains and losses on monetary assets classified as available-for-sale are recognised in the separate income statement. Dividends on available-for-sale equity instruments are recognised in the separate income statement under "Dividend income".

### **2.6 Impairment of financial assets**

#### (a) Assets carried at amortised cost

The Bank assesses at each end of the reporting period whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

The criteria that the Bank uses to determine that there is objective evidence of an impairment loss include:

- Delinquency in contractual payments of principal and interest;
- Cash flow difficulties experienced by the borrower (for example, high debt-to-equity ratio, low net income as a percentage of sales);
- Breach of loan covenants or conditions;
- Deterioration of the borrower's competitive position;
- Deterioration in the value of collateral; and
- Downgrading below investment grade level.

The Bank first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. If the Bank determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes that asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

The amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the income statement. If a loan has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract. As a practical expedient, the Bank may measure impairment on the basis of an instrument's fair value using an observable market price.

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

## 2. Summary of significant accounting policies (Continued)

### 2.6 Impairment of financial assets (Continued)

#### (a) Assets carried at amortised cost (Continued)

The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

For the purposes of a collective evaluation of impairment, financial assets are grouped on the basis of similar credit risk characteristics (i.e. on the basis of the Bank's grading process that considers asset type, collateral type, overdue status and other relevant factors). Those characteristics are relevant to the estimation of future cash flows for groups of such assets by being indicative of the debtors' ability to pay all amounts due according to the contractual terms of the assets are considered.

Future cash flows in a group of financial assets that are collectively evaluated for impairment are estimated on the basis of the contractual cash flows of the assets in the group and historical loss experience for assets with credit risk characteristics similar to those in the group. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not currently exist.

Estimates of changes in future cash flows for groups of assets should reflect and be directionally consistent with changes in related observable data from period to period (for example, changes in unemployment rates, property prices, payment status, or other factors indicative of changes in the probability of losses in the group and their magnitude). The methodology and assumptions used for estimating future cash flows are reviewed regularly by the Bank to reduce any differences between loss estimates and actual loss experience.

When a loan is uncollectable, it is written off against the related allowances for loan impairment. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off decrease the amount of the allowances for loan impairment in the income statement.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the previously recognised impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognised in the income statement.

#### (b) Assets classified as available-for-sale

The Bank assesses at each end of the reporting period whether there is objective evidence that a financial asset or a group of financial assets is impaired. In the case of equity investments classified as available-for-sale, a significant or prolonged decline in the fair value of the security below its cost is considered in determining whether the assets are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss measured as the difference between the acquisition cost (net of any principal repayment and amortisation) and the current fair value, less any impairment loss on that financial asset previously recognised in income statement, is removed from equity and recognised in the income statement. Impairment losses recognised in the income statement on equity instruments are not reversed through the income statement. If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in the income statement, the impairment loss is reversed through the income statement.

#### (c) Renegotiated loans

Loans that are either subject to collective impairment assessment or individually significant and whose terms have been renegotiated are no longer considered to be past due but are treated as new loans. In subsequent periods, the asset if past due again is considered to be and disclosed as past due loans.

## **MEVAS Bank Limited**

### **Notes to the Financial Statements**

(Expressed in thousands of Hong Kong dollars)

## **2. Summary of significant accounting policies (Continued)**

### **2.7 Financial liabilities**

Financial liabilities are classified into two categories: financial liabilities at fair value through profit or loss and other financial liabilities. All financial liabilities are classified at inception and recognised initially at fair value. The bases for the determination of fair value of financial liabilities are set out in Note 3.5(a).

#### **(a) Financial liabilities at fair value through profit or loss**

This category has two sub-categories: financial liabilities held for trading, and those designated at fair value through profit or loss at inception.

A financial liability is classified as held for trading if it is incurred principally for the purpose of repurchasing in the short term. It is carried at fair value and any gains and losses from changes in fair value are recognised in the income statement.

A financial liability is typically classified as fair value through profit or loss at inception if it meets the following criteria:

- (i) It eliminates or significantly reduces a measurement or recognition inconsistency (sometimes referred to as "an accounting mis-match") that would otherwise arise from measuring liabilities or recognising the gains and losses on them on different bases; or
- (ii) A group of financial liabilities is managed and its performance is evaluated on a fair value basis, in accordance with a documented risk management or investment strategy, and this is the basis on which information about the liabilities is provided internally to the key management personnel such as the Board of Directors and Chief Executive Officer; or
- (iii) Financial liabilities with embedded derivatives where the characteristics and risks of the embedded derivatives are not closely related to the host contracts.

Financial liabilities designated at fair value through profit or loss and deposits received from customers that are embedded with certain derivatives, are designated as such at inception. Financial liabilities designated at fair value through profit or loss are carried at fair value and any gains and losses from changes in fair value are recognised in the income statement.

#### **(b) Other financial liabilities**

Other financial liabilities are recognised initially at fair value net of transaction costs incurred and are subsequently carried at amortised cost. Any difference between proceeds net of transaction costs and the redemption value is recognised in the income statement over the period of the other financial liabilities using the effective interest method.

### **2.8 Derivative financial instruments**

Derivatives are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently re-measured at their fair value. The bases for the determination of fair value of derivative financial instruments are set out in Note 3.5(a). All derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative.

The best evidence of the fair value of a derivative at initial recognition is the transaction price (i.e. the fair value of the consideration given or received).

Changes in the fair value of derivative instrument are recognised immediately in the income statement under net trading income.

## **MEVAS Bank Limited**

### **Notes to the Financial Statements**

(Expressed in thousands of Hong Kong dollars)

## **2. Summary of significant accounting policies (Continued)**

### **2.9 Offsetting financial instruments**

Financial assets and liabilities are offset and the net amount reported in the statement of financial position when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

### **2.10 Repossessed assets**

Loans on which collateral assets have been repossessed are not derecognised and are carried in the statement of financial position with appropriate amounts of impairment allowances made.

### **2.11 Segment reporting**

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision maker. The chief operating decision maker is the person or group of persons that allocates resources to and assesses the performance of the operating segments of an entity. The Bank has determined the Bank's Executive Committee as its chief operating decision maker.

All transactions between business segments are conducted on an arm's length basis, with intra-segment revenues and costs being eliminated on consolidation. Income and expenses directly associated with each segment are included in determining operating segment performance.

Based on the requirements of HKFRS 8, the Group has the following segments: Personal banking, Commercial banking and Treasury.

### **2.12 Foreign currency translation**

#### **(a) Functional and presentation currency**

Items included in the financial statements of the Bank are measured using the currency of the primary economic environment in which the entity operates ("the functional currency"). The financial statements are presented in HK dollars, which is the Bank's presentation currency and functional currency.

#### **(b) Transactions and balances**

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement.

All foreign exchange gains and losses recognised in the income statement are presented net in the income statement within the corresponding item. Foreign exchange gains and losses on other comprehensive income items are presented in the statement of comprehensive income within the corresponding item.

In the case of changes in the fair value of foreign currency denominated monetary assets classified as available-for-sale, a distinction is made between translation differences resulting from changes in amortised cost of the assets and other changes in the carrying amount of the assets. Translation differences related to changes in the amortised cost are recognised in the income statement, and those related to changes in the carrying amount, except for impairment, are recognised in equity.

Translation differences on non-monetary items, such as investment in equity instruments held at fair value through profit or loss, are recognised in the income statement as part of the fair value gain or loss. Translation difference on certain other non-monetary items, such as equities classified as available-for-sale financial assets, are included in the fair value reserve in equity.

## **MEVAS Bank Limited**

### **Notes to the Financial Statements**

(Expressed in thousands of Hong Kong dollars)

## **2. Summary of significant accounting policies (Continued)**

### **2.13 Furniture and equipment**

All furniture and equipment are stated at historical cost less depreciation and impairment losses. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Bank and the cost of the item can be measured reliably. All other repairs and maintenance are expensed in the income statement during the financial period in which they are incurred.

Depreciation is calculated using the straight-line method to allocate their cost or revalued amounts to their residual values over their estimated useful lives, as follows:

- Furniture, fixtures and equipment                      Over the estimated useful lives generally between 5 and 10 years

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each end of the reporting period.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

### **2.14 Investment properties**

Property that is held for long-term rental yields or for capital appreciation or both, and that is not occupied by the Bank, is classified as investment property.

Investment property comprises land held under operating lease and buildings held under finance lease.

Land held under operating lease is classified and accounted for as investment property when the rest of the definition of investment property is met. The operating lease is accounted for as if it were a finance lease.

Investment property is measured initially at its cost, including related transaction costs.

After initial recognition, investment property is carried at fair value. Fair value is based on active market prices, adjusted, if necessary, for any difference in the nature, location or condition of the specific asset. If this information is not available, the Bank uses alternative valuation methods such as recent prices on less active markets or discounted cash flow projections. These valuations are performed in accordance with the guidance issued by the International Valuation Standards Committee. These valuations are reviewed annually by external valuers. Investment property that is being redeveloped for continuing use as investment property, or for which the market has become less active, continues to be measured at fair value.

The fair value of investment property reflects, among other things, rental income from current leases and assumptions about rental income from future leases in the light of current market conditions.

Subsequent expenditure is charged to the asset's carrying amount only when it is probable that future economic benefits associated with the item will flow to the Bank and the cost of the item can be measured reliably. All other repairs and maintenance costs are expensed in the income statement during the financial period in which they are incurred.

Changes in fair values are recognised in the income statement.

If an investment property becomes owner-occupied, it is reclassified as property, plant and equipment, and its fair value at the date of reclassification becomes its cost for accounting purposes.

## **MEVAS Bank Limited**

### **Notes to the Financial Statements**

(Expressed in thousands of Hong Kong dollars)

## **2. Summary of significant accounting policies (Continued)**

### **2.14 Investment properties (Continued)**

If an item of premises and other fixed assets becomes an investment property because its use has changed, any difference resulting between the carrying amount and the fair value of this item at the date of transfer is recognised in equity as a revaluation of premises and other fixed assets under HKAS 16. However, if a fair value gain reverses a previous impairment loss, the gain is recognised in the income statement.

### **2.15 Current and deferred income tax**

The tax expense for the period comprises current and deferred tax. Tax is recognised in the income statement, except to the extent that it relates to items recognised directly in equity. In this case, the tax is recognised in equity.

The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the end of the reporting period in the countries where the Bank's subsidiaries and associates operate and generate taxable income. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. It establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

Deferred income tax is recognised, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred income tax is determined using tax rates that have been enacted or substantially enacted by the end of the reporting period and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income tax assets are recognised only to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

Income tax payable on profits, based on the applicable tax law, is recognised as an expense in the period in which profits arise. The tax effects of income tax losses available for carry forward are recognised as an asset when it is probable that future taxable profits will be available against which these losses can be utilised.

Deferred income tax related to fair value re-measurement of available-for-sale investments, which is charged or credited directly to equity, is also credited or charged directly to equity and is subsequently recognised in the income statement together with the deferred gain or loss.

### **2.16 Employee benefits**

#### **(a) Pension obligations**

The Bank offers a mandatory provident fund scheme and a number of defined contribution plans, the assets of which are generally held in separate trustee-administered funds. These pension plans are funded by payments from employees and by the Bank.

The Bank's contributions to the mandatory provident fund schemes and defined contribution retirement schemes are expensed as incurred. Other than mandatory provident fund contribution, the Bank's contributions may be reduced by contributions forfeited by those employees who leave prior to vesting fully in the contributions.

#### **(b) Employee leave entitlements**

Employee entitlements to annual leave and long service leave are recognised when they accrue to employees. An accrual is made for the estimated liability for annual leave and long service leave as a result of services rendered by employees up to the end of the reporting period.

## **MEVAS Bank Limited**

### **Notes to the Financial Statements**

(Expressed in thousands of Hong Kong dollars)

## **2. Summary of significant accounting policies (Continued)**

### **2.16 Employee benefits (Continued)**

#### (c) Bonus plans

Liabilities for bonus plans due wholly within twelve months after the end of the reporting period are recognised when the Bank has a present or constructive obligation as a result of services rendered by employees and a reliable estimate of the obligation can be made.

### **2.17 Provisions**

Provisions for restructuring costs and legal claims are recognised when: the Bank has a present legal or constructive obligation as a result of past events; it is more likely than not that an outflow of resources will be required to settle the obligation; and the amount has been reliably estimated. Restructuring provisions comprise lease termination penalties and employee termination payments. Provisions are not recognised for future operating losses.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

### **2.18 Leases**

#### (a) Operating lease

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are expensed in the income statement on a straight-line basis over the period of the lease.

Where the Bank is a lessor under operating leases, assets leased out are included in fixed assets in the statement of financial position. They are depreciated over their expected useful lives on a basis consistent with similar owned fixed assets. Rental income (net of any incentives given to lessees) is recognised on a straight-line basis over the lease term.

#### (b) Finance lease

Leases of assets where the Bank has substantially retained all the risks and rewards of ownership are classified as finance leases. Finance leases are capitalised at the lease's commencement at the lower of the fair value of the leased property and the present value of the minimum lease payments. Each lease payment is allocated between the liability and finance charges so as to achieve a constant rate on the finance balance outstanding. The corresponding rental obligations, net of finance charges, are included as liabilities. The investment properties acquired under finance leases are carried at their fair value.

Where the Bank is a lessor under finance leases, the amounts due under the leases, net of unearned finance income, are recognised as a receivable and are included in "Advances and other accounts". Finance income implicit in rentals receivable is credited to the income statement over the lease period so as to produce a constant periodic rate of return on the net investment outstanding for each accounting period.

### **2.19 Fiduciary activities**

The Bank commonly acts as trustees and in other fiduciary capacities that result in the holding or placing of assets on behalf of individuals, trusts and other institutions. These assets are excluded from the Bank's financial statements, as they are not assets of the Bank.

## **MEVAS Bank Limited**

### **Notes to the Financial Statements**

(Expressed in thousands of Hong Kong dollars)

## **2. Summary of significant accounting policies (Continued)**

### **2.20 Share capital**

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new shares are shown in equity as a deduction, net of tax, from the proceeds.

Dividends on ordinary shares are recognised as a liability in the Bank's financial statements in the period in which they are approved by the Bank's shareholders.

### **2.21 Cash and cash equivalents**

For the purposes of the 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 and investment securities which are readily convertible to cash and are subject to an insignificant risk of changes in value.

### **2.22 Financial guarantee contracts**

Financial guarantee contracts are contracts that require the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payments when due, in accordance with the terms of a debt instrument. Such financial guarantees are given to banks, financial institutions and other bodies on behalf of customers to secure loans, overdrafts and other banking facilities, and to other parties in connection with the performance of customers under obligations related to contracts, advance payments made by other parties, tenders, retentions and the payment of import duties.

Financial guarantees are initially recognised in the financial statements at fair value on the date the guarantee was given. Subsequent to initial recognition, the Bank's liabilities under such guarantees are measured at the higher of the amount determined in accordance with HKAS 37 Provisions, Contingent Liabilities and Contingent Assets and the amount initially recognised less cumulative amortisation recognised. Any changes in the liability relating to financial guarantees are taken to the income statement.

### **2.23 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 Bank. It can also be a present obligation arising from past events that is not recognised because it is not probable that an 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 financial statements. 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 Bank.

A contingent asset is not recognised but is disclosed in the notes to the financial statements when an inflow of economic benefits is probable. When such inflow is virtually certain, an asset is recognised.

## **MEVAS Bank Limited**

### **Notes to the Financial Statements**

(Expressed in thousands of Hong Kong dollars)

#### **3. Financial risk management**

The Bank's activities expose it to a variety of financial risks and those activities involve the analysis, evaluation, acceptance and management of some degree of risk or combination of risks. Taking risk is core to the financial business, and the operational risks are an inevitable consequence of being in business. The Bank's aim is therefore to achieve an appropriate balance between risk and return and minimise potential adverse effects on the Bank's financial performance.

The Bank's risk management policies are designed to identify and analyse these risks, to set appropriate risk limits and controls, and to monitor the risks and adherence to limits by means of reliable and up-to-date information systems. The Bank regularly reviews its risk management policies and systems to reflect changes in markets, products and emerging best practice.

Risk management is carried out pursuant to the overall strategy and policies approved by the Board of Directors. The Executive Committee under the authority delegated by the Board oversees and guides the management of different risks which are more particularly managed and dealt with by the Group Risk and different functional committees. In addition, Internal Audit is responsible for the independent review of risk management and the control environment.

The most important types of risk are credit risk, liquidity risk, market risk and operational risk. Market risk includes currency risk, interest rate and other price risk.

##### **3.1 Strategy in using financial instruments**

The Bank accepts deposits from customers at both fixed and floating rates, and for various periods, and seeks to earn positive interest margins by investing these funds in high-quality assets. The Bank seeks to increase these margins by consolidating short-term funds and lending for longer periods at higher rates, while maintaining sufficient liquidity to meet all claims that might fall due.

The Bank also seeks to apply its interest margins through its lending to commercial and retail borrowers and to charge customers appropriate fees and commission, taking into consideration credit risk and market conditions. Such exposures involve not just on-balance sheet loans and advances, as the Bank also enters into guarantees and other commitments such as letters of credit, performance and other bonds.

Apart from specific hedging arrangements, foreign exchange and interest rate exposures are normally offset by entering into counterbalancing positions (including transactions with customers or market counterparties), or by the use of derivatives thereby controlling the variability in the net cash amounts required to liquidate market positions.

Pursuant to a services agreement entered into between the Bank and Dah Sing Bank, Limited ("DSB"), a fellow subsidiary, the management of risks of the Bank, including the management of different types of financial risks, is outsourced to DSB. The development of risk policies and control, ongoing risk monitoring and management review are carried out by DSB for the Bank with the participation of the Bank's Chief Executive.

## **MEVAS Bank Limited**

### **Notes to the Financial Statements**

(Expressed in thousands of Hong Kong dollars)

#### **3. Financial risk management (Continued)**

##### **3.2 Credit risk**

The Bank's main credit risk is that borrowers or counterparties may default on their payment obligations due to the Bank. These obligations arise from the Bank's lending and investment activities, and trading of financial instruments (including derivatives).

The Bank has a Credit Committee made up of certain Executive Directors and senior credit officers and chaired by the Dah Sing Banking Group Chief Executive. The Credit Committee has the responsibility for formulating and revising credit policies and procedures within the parameters of the Group Risk Policy and regulatory framework. Credit policies and procedures define the credit assessment and approval criteria and guidelines, use of scoring, review and monitoring process and the systems of loan classification and impairment.

The Bank manages all types of credit risk on a prudent basis, in accordance with the credit approval and review policies, by evaluating the credit-worthiness of different types of customers and counterparties based on assessment of business, financial, market and industry risks applicable to the types of loans, collateral and counterparty dealings including dealing in or use of derivative financial instruments. Credits are extended within the parameters set out in the credit policies and are approved by different levels of management based upon established guidelines. Credit exposures, limits and asset quality are regularly monitored and controlled by management, Credit Committee and Group Risk function of the immediate holding company. The Group's internal auditors conduct regular reviews and audits to ensure compliance with credit policies and procedures and regulatory guidelines.

The Bank's credit policies also establish policies and processes for the approval and review of new products and activities, together with details of the loan grading, or credit scoring, processes and impairment policies.

##### **3.2.1 Credit risk measurement**

###### **(a) Loans and advances**

In measuring credit risk of loans and advances to customers and to banks and other financial institutions at a counterparty level, the Bank reflects three components (i) the differentiation of credit risk of the client or counterparty on its contractual obligations; (ii) current exposures to the counterparty and its likely future development, from which the Bank derive the "exposure at default"; and (iii) the likely loss on the defaulted obligations after considering recovery and collateral realisation.

These credit risk measurements, which operate to control and monitor credit performance of individual and pools of borrowers through on-going credit review, loan classification, collection, credit risk mitigation including realisation of collateral, and provision of impairment on problem loans as required by the Bank's credit policies and procedures, and regulatory guidelines, are embedded in the Bank's daily operational management. Based on the Banking (Capital) Rules of the Hong Kong Banking Ordinance, the Bank is also required to assess expected loss of individual and portfolios of credits, and to set aside sufficient loan loss reserve against any expected loss. The operational measurements to also cover expected losses can be contrasted with impairment allowances required under HKAS 39, which are based on losses that have been incurred at the end of the reporting period (the "incurred loss model") rather than expected loss (Note 3.2.3).

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

#### 3. Financial risk management (Continued)

##### 3.2 Credit risk (Continued)

###### 3.2.1 Credit risk measurement (Continued)

###### (a) Loans and advances (Continued)

- (i) The Bank assesses the credit quality of individual counterparties using internal rating tools tailored to the various categories of counterparty. They have been developed internally and combine general analysis and judgements of credit officers, and are reviewed, where appropriate, by comparison with externally available data. Clients of the Bank are segmented into three broad rating classes. The Bank's rating scale, which is shown in Note 3.2.3, differentiates credit quality for each rating class. This means that, in principle, exposures migrate between classes as the assessment of credit quality and business environment changes. The rating tools are kept under review and upgraded as necessary. The Bank regularly reviews the performance of the rating and their predictive power with regard to default events.

The Bank uses both internal data and market information (e.g. credit rating migration, credit scoring) for internal credit risk assessment. Observed migration data per rating category vary year on year, especially over an economic cycle.

- (ii) Exposure at default is based on the amounts the Bank expects to be owed at the time of default. For example, for a loan, exposure at default is the face value. For a commitment, the Bank includes any amount already drawn plus the further amount that may have been drawn by the time of default, should it occur.
- (iii) Estimated credit loss or loss severity represents the Bank's expectation of the extent of loss on a claim should default occur. It is based on actual loss experience and typically varies by type of counterparty, type and seniority of claim and availability of collateral or other credit risk mitigation.

###### (b) Credit-related commitments

The primary purpose of these instruments is to ensure that funds are available to a customer as required. Guarantees and standby letters of credit - which represent irrevocable assurances that the Bank will make payments in the event that a customer cannot meet its obligations to third parties - carry the same credit risk as loans.

Commitments to extend credit represent unused portions of authorisations to extend credit in the form of loans, guarantees or letters of credit. With respect to credit risk on commitments to extend credit, the Bank is potentially exposed to loss in an amount equal to the total unused commitments. However, the likely amount of loss is less than the total unused commitments, as most commitments to extend credit are contingent upon customers maintaining specific credit standards. The Bank monitors the term to maturity of credit commitments because longer-term commitments generally have a greater degree of credit risk than shorter-term commitments.

###### (c) Debt securities

For debt securities, external ratings such as Standard & Poor's rating or their equivalents are used by Group Risk for managing the credit risk exposures. The investments in debt securities are made to gain a better credit quality, to diversify risk exposures and income streams, and to maintain a readily available source of funds to meet the funding and liquidity requirement of the Bank from time to time.

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

#### 3. Financial risk management (Continued)

##### 3.2 Credit risk (Continued)

###### 3.2.1 Credit risk measurement (Continued)

###### (d) Derivatives

The Bank uses the following derivative instruments for trading purposes:

- (i) Currency forwards represent commitments to purchase foreign and domestic currency, including undelivered spot transactions. Foreign currency and interest rate futures are contractual obligations to receive or pay a net amount based on changes in currency rates or interest rates or to buy or sell foreign currency or a financial instrument on a future date at a specified price, established in an organised financial market. The credit risk is negligible, as futures contracts are collateralised by cash or marketable securities, and changes in the futures contract value are settled daily with the exchange.
- (ii) Currency and interest rate swaps are commitments to exchange one set of cash flows for another. Swaps result in an economic exchange of currencies or interest rates (for example, fixed rate for floating rate) or a combination of all these (i.e., cross-currency interest rate swaps). No exchange of principal takes place, except for certain currency swaps. The Bank's credit risk represents the potential cost to replace the swap contracts if counterparties fail to perform their obligation. This risk is monitored on an ongoing basis with reference to the current fair value, a proportion of the notional amount of the contracts and the liquidity of the market. To control the level of credit risk taken, the Bank assesses counterparties using the same techniques as for its lending activities.
- (iii) Foreign currency and interest rate options are contractual agreements under which the seller (writer) grants the purchaser (holder) the right, but not the obligation, either to buy (a call option) or sell (a put option) at or by a set date or during a set period, a specific amount of a foreign currency or a financial instrument at a predetermined price. The seller receives a premium from the purchaser in consideration for the assumption of foreign exchange or interest rate risk. Options may be either exchange-traded or negotiated between the Bank and a customer. The Bank is exposed to credit risk on purchased options only, and only to the extent of their carrying amount, which is their fair value.

The Bank may be exposed to counterparty risk arising from its positions in derivative financial instruments, which is either "valuation risk" for the credit risk on receiving mark-to-market gains upon the default of a counterparty prior to scheduled settlement, or "settlement risk" for the possibility of not receiving the expected cash value of a derivative transaction or upon the expiry of a derivative contract on the settlement date.

## **MEVAS Bank Limited**

### **Notes to the Financial Statements**

(Expressed in thousands of Hong Kong dollars)

#### **3. Financial risk management (Continued)**

##### **3.2 Credit risk (Continued)**

###### 3.2.1 Credit risk measurement (Continued)

###### (d) Derivatives (Continued)

The notional amounts of certain types of financial instruments provide a basis for comparison with instruments recognised on the statement of financial position but do not necessarily indicate the amounts of future cash flows involved or the current fair value of the instruments and, therefore, do not indicate the Bank's exposure to credit or price risks. The derivative instruments become favourable (assets) or unfavourable (liabilities) as a result of fluctuations in market interest rates or foreign exchange rates relative to their terms. The aggregate contractual or notional amount of derivative financial instruments on hand, the extent to which instruments are favourable or unfavourable, and thus the aggregate fair values of derivative financial assets and liabilities, can fluctuate significantly from time to time.

The Bank maintains strict control limits on net open derivative positions (i.e., the difference between purchase and sale contracts), by both amount and term. At any one time, the amount subject to credit risk is limited to the current fair value of instruments that are favourable to the Bank (i.e., assets where their fair values are positive), which in relation to derivatives is only a small fraction of the contract, or notional values used to express the volume of instruments outstanding.

###### 3.2.2 Risk limit control and mitigation policies

The Bank manages, controls and limits concentrations of credit risk wherever they are identified - in particular, to individual counterparties and groups, and to industries and countries.

The Bank structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or groups of borrowers, and to geographical and industry segments. Such risks are monitored on a revolving basis and are subject to an annual or more frequent review, when considered necessary. Limits on the level of credit risk by product, industry sector and by country are approved by the Credit Committee and Group Risk.

The exposure to any one borrower or counterparty including banks and brokers is further restricted by sub-limits covering on- and off- balance sheet exposures, and daily delivery risk limits in relation to trading items such as forward foreign exchange contracts. Actual exposures against limits are monitored daily.

Exposures to credit risk is also managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations and by regular review and revision of these limits where appropriate.

To avoid concentration of risk, large exposures to individual customers or related groups are limited to a percentage of the capital base, and exposures to industry sectors and countries/regions are managed within approved limits to achieve a balanced portfolio.

###### (a) Loans and advances

In order to mitigate the credit risk and where appropriate, the Bank will obtain collateral to support the credit facility. To control credit risk exposure to counterparty arising from derivative positions, the Bank limits its derivative dealings with approved financial institutions, and uses established market practices on credit support and collateral settlement to reduce credit risk exposure to derivative counterparties. Overall credit risk limit for each financial institution counterparty, including valuation limit for derivatives, is approved by the Credit Committee with reference to the financial strength and credit rating of each counterparty. The acceptable types of collateral and their characteristics are established within the credit policies, as are the respective margins of finance.

Irrespective of whether collateral is taken, all credit decisions are based upon the customer's or counterparty's credit profile, cashflow position and ability to repay.

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

#### 3. Financial risk management (Continued)

##### 3.2 Credit risk (Continued)

###### 3.2.2 Risk limit control and mitigation policies (Continued)

###### (a) Loans and advances (Continued)

The Bank employs a range of policies and practices to mitigate credit risk. The most traditional of these is the taking of security for funds advanced, which is a common practice. The Bank implements guidelines on the acceptability of specific classes of collateral or credit risk mitigation. The principal collateral types for loans and advances are:

- Mortgages over residential properties;
- Charges over business assets such as premises, inventory and accounts receivable; and
- Charges over financial instruments such as debt securities and equities.

Longer-term finance and lending to corporate entities are generally secured; revolving individual credit facilities are generally unsecured. In addition, in order to minimise credit loss, the Bank will seek additional collateral from the counterparty as soon as impairment indicators are noticed on relevant individual loans and advances.

###### (b) Debt securities

Debt securities and treasury bills are generally unsecured, with the exception of asset-backed securities and similar instruments, which are secured by portfolios of financial instruments.

###### (c) Derivatives

Since all counterparties for derivatives trading are financial institutions, the risk is managed as part of the credit risk control and monitoring process in respect of financial institutions including credit controls such as setting individual limit for valuation risk, daily settlement limits and performing periodic credit assessment for each counterparty. Moreover, the Bank requires all derivative contract counterparties to enter into International Swaps and Derivatives Association ("ISDA") Agreement in order to follow the standardised market practice of close-out arrangement in the event of default, settlement procedure, valuation/pricing methods.

Collateral or other security is not usually obtained for credit risk exposures on these instruments, except where the Bank requires margin deposits from counterparties.

The Bank further restricts its exposure to credit losses by entering into master netting arrangements with counterparties with which it undertakes a significant volume of transactions. Master netting arrangements do not generally result in an offset of assets and liabilities in the statement of financial position, as transactions are usually settled on a gross basis. However, the credit risk associated with favourable contracts is reduced by a master netting arrangement to the extent that if an event of default occurs, all amounts with the counterparty are terminated and settled on a net basis.

The Bank's overall exposure to credit risk on derivative instruments subject to master netting arrangements can change substantially within a short period, as it is affected by each transaction subject to the arrangement.

###### 3.2.3 Impairment and provisioning policies

The internal rating system described in Note 3.2.1 focuses more on credit-quality assessment from the inception of the lending and investment activities. In contrast, impairment allowances are recognised for financial reporting purposes only for losses that have been incurred at the end of the reporting period based on objective evidence of impairment (see Note 2.6). Due to the different approaches applied, the amount of incurred credit losses provided for in the financial statements may be different from the amount determined from other loss estimation approach that is used for internal operational management and banking regulation purposes.

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

#### 3. Financial risk management (Continued)

##### 3.2 Credit risk (Continued)

###### 3.2.3 Impairment and provisioning policies (Continued)

The impairment allowance shown in the statement of financial position at year-end is derived from each of the three broad internal rating grades. However, the majority of the impairment allowance comes from the bottom two gradings. The table below shows the percentage of the Bank's on-balance sheet items relating to loans and advances and the associated impairment allowance covering on- and off-balance sheet amounts for each of these broad internal rating categories.

	2009		2008	
Grades	Loans and advances	Impairment allowance as a % of loan balance	Loans and advances	Impairment allowance as a % of loan balance
	%	%	%	%
1 – pass	98.4	0.1	99.4	0.3
2 - special mention	0.1	51.0	0.1	0.8
3 - sub-standard or below	1.5	20.2	0.5	70.2
	<u>100.0</u>		<u>100.0</u>	

Impairment allowance is determined after considering the value of collateral held for the loans.

As far as the commercial banking business of the Bank is concerned, the credit ratings are broadly categorised as follows.

Grade 1 "pass", which covers Grade 1 to 9 of the Bank's internal loan grading system, represents loans for which borrowers are current in meeting commitments and for which the full repayment of interest and principal is not in doubt.

Grade 2 "special mention", which covers Grade 10 of the Bank's internal loan grading system, represents loans with which borrowers are experiencing difficulties and which may lead to credit losses to the Bank if the deterioration in loan quality cannot be contained.

Grade 3 "sub-standard or below", which covers Grade 11 to 13 of the Bank's internal loan grading system, represents loans in which borrowers are displaying a definable weakness that is likely to jeopardise repayment; or collection in full is improbable and the Bank expects to sustain a loss of principal and/or interest, taking into account the fair value of collateral less cost to sell; or loans that are considered uncollectible after all collection options have been exhausted.

The internal rating tool assists management to determine whether objective evidence of impairment exists under HKAS 39, which is based on the following criteria set out by the Bank:

- Delinquency in contractual payments of principal or interest;
- Cash flow difficulties experienced by the borrower (e.g. equity to debt ratio, net income percentage of sales);
- Breach of loan covenants or conditions;
- Initiation of bankruptcy proceedings;
- Deterioration of the borrower's competitive position; and
- Deterioration in the value of collateral.

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

#### 3. Financial risk management (Continued)

##### 3.2 Credit risk (Continued)

###### 3.2.3 Impairment and provisioning policies (Continued)

The Bank's policy requires the review of individual financial assets that are above materiality thresholds at least annually or more regularly when individual circumstances require. Impairment allowances on individually assessed accounts are determined by an evaluation of the incurred loss at the end of the reporting period on a case-by-case basis, and are applied to all individually significant accounts. The assessment normally encompasses collateral held (including re-confirmation of its enforceability) and the anticipated receipts on liquidating collaterals for that individual account.

Collectively assessed impairment allowances are provided for: (i) portfolios of homogenous assets that are individually below materiality thresholds; and (ii) losses that have been incurred but have not yet been identified, by using the available historical experience, experienced judgement and statistical techniques.

###### 3.2.4 Maximum exposure to credit risk before collateral held or other credit enhancements

	2009	2008
Credit risk exposures relating to on-balance sheet assets are as follows:		
Cash and balances with banks	1,713,137	4,327,407
Derivative financial instruments	8	2,717
Financial assets designated at fair value through profit or loss	-	82,721
Loans and advances to customers		
Loans to individuals:		
- Credit cards	278,194	330,921
- Mortgages	687,656	778,211
- Others	54,180	226,272
Loans to corporate entities:		
- Term loans	330,028	509,917
Other assets	297,475	18,046
Investments in securities included in the loans and receivables category	43,779	-
Available-for-sale securities		
- Debt securities	900,244	325
	<u>4,304,701</u>	<u>6,276,537</u>
Credit risk exposures relating to off-balance sheet items are as follows:		
Financial guarantees and other credit related contingent liabilities	269	269
Loan commitments and other credit related commitments	2,301,892	2,443,558
	<u>2,302,161</u>	<u>2,443,827</u>
At 31 December	<u>6,606,862</u>	<u>8,720,364</u>

The above table represents a worse case scenario of credit risk exposure to the Bank at 31 December 2009 and 2008, without taking into account of any collateral held or other credit enhancements attached.

The results of credit performance of loan and advances to customers of the Bank can be further assessed with reference to the following:

- 4% of the loans and advances portfolio is categorised in the top three grades of the internal rating system (2008: 3%);
- Mortgage loans, which represent the biggest group in the portfolio, are backed by collateral;
- 98% of the loans and advances portfolio are considered to be neither past due nor individually impaired (2008: 98%).

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

#### 3. Financial risk management (Continued)

##### 3.2 Credit risk (Continued)

###### 3.2.5 Loans and advances

Loans and advances are summarised as follows:

	2009	2008
Loans and advances to customers		
Neither past due nor impaired	1,322,091	1,813,535
Past due but not impaired (Note 1)	26,896	30,004
Past due and collectively assessed as impaired	1,071	1,782
Gross	<u>1,350,058</u>	<u>1,845,321</u>
Less: allowance for collective impairment	<u>(6,026)</u>	<u>(12,100)</u>
Net	<u>1,344,032</u>	<u>1,833,221</u>
Impairment allowances made in respect of loans collectively assessed as impaired (Note 2)	<u>1,071</u>	<u>1,782</u>
Impaired loans and advances as a % of total loans and advances to customers	<u>0.08%</u>	<u>0.10%</u>

#### Note 1:

The Bank did not have any individually impaired loans and advances as at 31 December 2009 and 31 December 2008.

#### Note 2:

Collectively impaired loans and advances refer to those unsecured loans and advances assessed for impairment on a collectively basis and which have become overdue for more than 90 days as at the reporting date. The collective impairment allowance for these impaired loans, which is a part of the overall collective impairment allowances, is shown above.

The total collective impairment allowance for loans and advances is HK\$6,026,000 (2008: HK\$12,100,000). Further information on the impairment allowance for loans and advances to customers is provided in Note 19.

During the year ended 31 December 2009, the Bank's total loans and advances decreased by 27%. When entering into new markets or expanding business focus or allocation to different loan segments, the Bank undertakes proper risk assessment in accordance with credit policies and procedures, review and approval of new risk limits, financial and credit reviews with an emphasis on proper risk and return balance. In order to minimise the potential increase of credit risk exposure, the Bank focused more on the business with large corporate enterprises or banks with good credit rating or retail customers providing sufficient collateral.

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

#### 3. Financial risk management (Continued)

##### 3.2 Credit risk (Continued)

##### 3.2.5 Loans and advances (Continued)

##### (a) Loans and advances neither past due nor impaired

The credit quality of the portfolio of loans and advances that were neither past due nor impaired can be assessed with reference to the internal rating system adopted by the Bank.

##### At 31 December 2009

	Individual (retail customers)			Corporate entities	Total loans and advances to customers
	Credit cards	Mortgages	Others	Term loans	
Grades:					
1 - pass	273,088	670,488	48,473	330,028	1,322,077
2 - special mention	-	-	-	-	-
3 - sub-standard or below	14	-	-	-	14
<b>Total</b>	<b>273,102</b>	<b>670,488</b>	<b>48,473</b>	<b>330,028</b>	<b>1,322,091</b>

##### At 31 December 2008

	Individual (retail customers)			Corporate entities	Total loans and advances to customers
	Credit cards	Mortgages	Others	Term loans	
Grades:					
1 - pass	324,491	767,751	211,246	509,917	1,813,405
2 - special mention	-	-	-	-	-
3 - sub-standard or below	130	-	-	-	130
<b>Total</b>	<b>324,621</b>	<b>767,751</b>	<b>211,246</b>	<b>509,917</b>	<b>1,813,535</b>

Mortgage loans in the sub-standard or below class were assessed as not impaired after taking into consideration the value and recovery of collaterals.

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

#### 3. Financial risk management (Continued)

##### 3.2 Credit risk (Continued)

##### 3.2.5 Loans and advances (Continued)

##### (b) Past due loans and advances

#### At 31 December 2009

	Individual (retail customers)			Total
	Credit cards	Mortgages	Others	
Past due up to 1 month	2,105	14,702	4,220	21,027
Past due more than 1 month and up to 3 months	2,033	2,465	1,371	5,869
Past due more than 3 months and up to 6 months	954	-	117	1,071
Past due more than 6 months	-	-	-	-
<b>Total</b>	<b>5,092</b>	<b>17,167</b>	<b>5,708</b>	<b>27,967</b>
<b>Fair value of collaterals*</b>	<b>-</b>	<b>17,167</b>	<b>-</b>	<b>17,167</b>

#### At 31 December 2008

	Individual (retail customers)			Total
	Credit cards	Mortgages	Others	
Past due up to 1 month	2,957	7,894	12,536	23,387
Past due more than 1 month and up to 3 months	2,090	2,566	1,961	6,617
Past due more than 3 months and up to 6 months	1,253	-	529	1,782
Past due more than 6 months	-	-	-	-
<b>Total</b>	<b>6,300</b>	<b>10,460</b>	<b>15,026</b>	<b>31,786</b>
<b>Fair value of collaterals*</b>	<b>-</b>	<b>10,460</b>	<b>-</b>	<b>10,460</b>

\* Fair value of collateral is determined as the lower of the market value of collateral and outstanding loan balance.

As at 31 December 2009 and 2008, there were no loans and advances extended to corporate entities that were past due.

Upon initial recognition of loans and advances, the fair value of collateral is based on valuation techniques commonly used for the corresponding assets. In subsequent periods, the fair value is updated with reference to market price or indexes of similar assets.

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

### 3. Financial risk management (Continued)

#### 3.2 Credit risk (Continued)

##### 3.2.5 Loans and advances (Continued)

##### (c) Loans and advances overdue for more than 3 months

##### (i) Gross amount of overdue loans

	2009		2008	
	Gross amount of overdue loans	% of total advances to customers	Gross amount of overdue loans	% of total advances to customers
Gross advances to customers which have been overdue for:				
- six months or less but over three months	1,071	0.08	1,782	0.10
- one year or less but over six months	-	-	-	-
	<u>1,071</u>	<u>0.08</u>	<u>1,782</u>	<u>0.10</u>

##### (ii) Value of collateral held and impairment allowances against overdue loans and advances

##### At 31 December 2009

	Outstanding amount of loans and advances	Current market value of collateral	Covered portion by collateral	Portion not covered by collateral	Other credit risk mitigation	Impairment allowances - individual assessment
Overdue loans and advances to customers	<u>1,071</u>	<u>-</u>	<u>-</u>	<u>1,071</u>	<u>-</u>	<u>-</u>

##### At 31 December 2008

	Outstanding amount of loans and advances	Current market value of collateral	Covered portion by collateral	Portion not covered by collateral	Other credit risk mitigation	Impairment allowances - individual assessment
Overdue loans and advances to customers	<u>1,782</u>	<u>-</u>	<u>-</u>	<u>1,782</u>	<u>-</u>	<u>-</u>

##### (d) Rescheduled advances net of amounts included in advances overdue for more than 3 months

	2009	% of total advances to customers	2008	% of total advances to customers
Advances to Customers	<u>15,734</u>	<u>1.17</u>	<u>4,434</u>	<u>0.24</u>

##### 3.2.6 Repossessed collateral

As at 31 December 2009 and 31 December 2008, the Bank did not hold any repossessed collateral.

**MEVAS Bank Limited**

**Notes to the Financial Statements**

(Expressed in thousands of Hong Kong dollars)

**3. Financial risk management (Continued)**

**3.2 Credit risk (Continued)**

3.2.7 Debt securities

(a) Analysis by rating agency designation

The table below presents an analysis of debt securities by rating agency designation at 31 December 2009.

**At 31 December 2009**

	Designated at fair value	Available-for-sale investments	Loans and receivables	Total
AA- to AA+	-	899,919	-	899,919
Unrated	-	325	43,779	44,104
<b>Total</b>	<b>-</b>	<b>900,244</b>	<b>43,779</b>	<b>944,023</b>

At 31 December 2008

	Designated at fair value	Available-for-sale investments	Loans and receivables	Total
Rated but lower than A-	82,721	-	-	82,721
Unrated	-	325	-	325
<b>Total</b>	<b>82,721</b>	<b>325</b>	<b>-</b>	<b>83,046</b>

(b) Analysis by overdue period

Investment in securities classified as loans and receivables upon initial recognition in 2009 were overdue at the time of recognition, and as at 31 December 2009 as shown below. There were no overdue debt securities as at 31 December 2008.

	2009	2008
Investments in securities classified as loans and receivables upon initial recognition		
Overdue for		
- Over one year	<b>43,779</b>	-

The entire portfolio of investments in securities classified as loans and receivables upon initial recognition was recognised in the statement of financial position at a value after taking into account the above overdue status. The total carrying value at the time of initial recognition and as at 31 December 2009 was HK\$302,236,000 (Note 26).

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

#### 3. Financial risk management (Continued)

##### 3.2 Credit risk (Continued)

###### 3.2.8 Concentration of risks of financial assets with credit risk exposure

###### (a) Geographical sectors

Advances to customers by geographical area are classified according to the location of the counterparties after taking into account the transfer of risk. In general, risk transfer applies when an advance is guaranteed by a party located in an area which is different from that of the counterparty.

The following table analyses gross advances to customers and overdue loans by geographical area

	<b>As at 31 Dec 2009</b>	<b>As at 31 Dec 2008</b>
Gross advances to customers		
- Hong Kong	<b>1,154,964</b>	1,504,420
- China	<b>75,000</b>	75,000
- Macau	<b>82,215</b>	90,244
- Others	<b>37,879</b>	175,657
	<b>1,350,058</b>	1,845,321
Gross advances overdue for over 3 months		
- Hong Kong	<b>1,071</b>	1,782

The following table analyses the cross-border claims of the Bank in relation to loans and advances, investments in securities, and balances and placements with banks.

<b>As at 31 December 2009</b>	<b>Banks</b>	<b>Others</b>	<b>Total</b>
Asia Pacific excluding Hong Kong	<b>483,173</b>	<b>157,263</b>	<b>640,436</b>
North and South America	<b>1,019</b>	<b>47,127</b>	<b>48,146</b>
Caribbean	-	<b>37,895</b>	<b>37,895</b>
Europe	<b>903,934</b>	-	<b>903,934</b>
	<b>1,388,126</b>	<b>242,285</b>	<b>1,630,411</b>
<b>As at 31 December 2008</b>	<b>Banks</b>	<b>Others</b>	<b>Total</b>
Asia Pacific excluding Hong Kong	123,427	215,519	338,946
North and South America	557	2,007	2,564
Caribbean	-	127,416	127,416
Europe	349,560	-	349,560
	<b>473,544</b>	<b>344,942</b>	<b>818,486</b>

The above information of cross-border claims discloses exposures to foreign counterparties on which the ultimate risk lies, and is derived according to the location of the counterparties after taking into account any transfer of risk. In general, transfer of risk from one country to another is recognised if the claims against a counterparty are guaranteed by another party in a different country or if the claims are on an overseas branch of a bank whose head office is located in a different country. Only regions constituting 10% or more of the aggregate cross-border claims are disclosed.

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

#### 3. Financial risk management (Continued)

##### 3.2 Credit risk (Continued)

###### 3.2.8 Concentration of risks of financial assets with credit risk exposure (Continued)

###### (b) Industry sectors

Gross advances to customers by industry sector classified according to the usage of loans

	2009	2008
Loans for use in Hong Kong		
Industrial, commercial and financial		
- Property investment	74,479	81,270
- Financial concerns	66,450	30,303
- Stockbrokers	-	4,400
- Manufacturing	-	26,641
- Transport and transport equipment	44,429	89,454
- Recreational activities	8,088	-
	<u>193,446</u>	<u>232,068</u>
Individuals		
-Loans for the purchase of flats in Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	23,796	25,820
- Loans for the purchase of other residential properties	445,417	535,716
- Credit card advances (Note 1)	278,194	330,921
- Others	198,144	361,678
	<u>945,551</u>	<u>1,254,135</u>
Loans for use in Hong Kong	1,138,997	1,486,203
Loans for use outside Hong Kong (Note 2)	211,061	359,118
	<u>1,350,058</u>	<u>1,845,321</u>

###### Note 1:

Despite the Bank entered into a sale and purchase agreement with DSB on 31 December 2009 to transfer the economic benefits and risks in respect of the whole credit card portfolio owned by the Bank to DSB. The card customer relationship and account balances were not yet transferred as at 31 December 2009, and the outstanding balance of credit card advance receivable by the Bank is stated as part of the Bank's gross advances as at 31 December 2009.

###### Note 2:

Loans for use outside Hong Kong include loans extended to customers located in Hong Kong with the finance used outside Hong Kong.

## **MEVAS Bank Limited**

### **Notes to the Financial Statements**

(Expressed in thousands of Hong Kong dollars)

#### **3. Financial risk management (Continued)**

##### **3.3 Market risk**

Market risk is the risk of losses in assets, liabilities and off-balance sheet positions arising from movements in market rates and prices.

Market risk exposure for different types of transactions is managed within risk limits and guidelines approved by the Board, Executive Committee ("EXCO"), Asset and Liability Management Committee ("ALCO") and Treasury Risk Committee ("TRC"). The overall risk limits comprise sub-limits for each of the different risk categories which are interest rate and foreign exchange.

###### **3.3.1 Market risk arising from trading book**

The Bank has very limited foreign exchange exposures, as such exposures are normally offset against other transactions with the market. The Bank does not engage in trading of any on-balance sheet or off-balance sheet financial instruments. The Bank considers that its business and activities in the trading book do not give rise to any material market risk.

###### **3.3.2 Market risk arising from the banking book**

In the Bank's banking book, market risk is predominantly associated with positions in debt and equity securities.

###### **(a) Market risk measurement technique**

Within the risk management framework and policies established by the Board, EXCO and TRC, various management action triggers ("MATs") are established to provide early alert to management on the different levels of exposures of the Bank's banking book activities to foreign exchange risk, interest rate risk, and liquidity risk. Sensitivity analysis and stress testing covering shocks and shifts in interest rates on the Bank's on- and off- balance sheet positions, liquidity drift under institution-specific and general market crisis scenarios are regularly performed to gauge and forecast the market risk inherent in the Bank's banking book portfolios against these MATs.

###### **(b) Sensitivity analysis of non-trading portfolio**

###### **(i) Foreign exchange risk**

The Bank has limited net foreign exchange exposure as foreign exchange positions and foreign currency balances arising from customer transactions are normally matched against other customer transactions or transactions with the market. The net exposure positions, both by individual currency and in aggregate, are managed by the Treasury of the Bank on a daily basis within established foreign exchange limits.

Long-term foreign currency funding, to the extent that this is used to fund Hong Kong dollar assets, is normally matched using forward exchange forward contracts to reduce exposure to foreign exchange risk.

At 31 December 2009, if HK\$ had weakened by 1% against US\$ with all other variable held constant, there would be no impact on the profit after taxation for the year. In 2008, it would be HK\$59,000 lower mainly as a result of foreign exchange losses on translation of US\$ denominated financial liabilities compensated by foreign exchange gains on translation of US\$ denominated financial assets.

Conversely, if HK\$ had strengthened by 1% against US\$ with all other variables held constant, there would be no impact on the profit after taxation for the year (2008: HK\$59,000 higher).

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

#### 3. Financial risk management (Continued)

##### 3.3 Market risk (Continued)

###### 3.3.2 Market risk arising from the banking book (Continued)

###### (b) Sensitivity analysis of non-trading portfolio (Continued)

###### (ii) Interest rate risk

The Bank's interest rate risk mainly arises from the funding of fixed-rate loans and investments in fixed income securities by floating rate deposits. When interest rates rise or fall, the interest spread and net interest income will be affected as interest income generated by the existing fixed-rate loans or securities will not change. In addition to changes in earnings, the variations in market interest rates will also affect the economic values of the Bank's assets, liabilities and off-balance sheet positions, which can, in turn affect the net worth of the Bank. The Board sets limit on the level of mismatch of interest rate repricing that may be undertaken, which is monitored monthly by the Risk Management and Control Department.

The framework adopted by the Bank to measure interest rate risk exposures arising from its banking book positions is consistent with that set forth by the HKMA for reporting interest rate risk exposures. In this framework, deposits without a fixed maturity are assumed to be repayable and to reprice on the next working day whereas loan prepayments are not considered when allocating loan balances into respective interest repricing time bands.

At 31 December 2009, if HK\$ market interest rates had been 200 basis points higher and US\$ market interest rates had been 200 basis points higher with other variables held constant, profit after taxation over the next 12 months and economic value would have been HK\$8,000,000 higher (2008: HK\$11,000,000 higher) and HK\$1,000,000 higher (2008: HK\$3,000,000 higher) respectively.

The method and assumptions used in the above sensitivity analysis on foreign exchange and interest rate risk are on the same basis for both 2009 and 2008.

In addition to foreign exchange risk and interest rate risk, the Bank's investments in debt securities are also exposed to other price risks. Consequently, the value of such investments could change significantly depending on a variety of factors including liquidity risk, market sentiment and other events that might affect individual or portfolios of exposures.

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

#### 3. Financial risk management (Continued)

##### 3.3 Market risk (Continued)

###### 3.3.3 Currency risk

The table below summarises the Bank's financial assets and liabilities translated into equivalent HK dollar, categorised by currency.

	HKD	USD	Others	Total
<b>As at 31 December 2009</b>				
<b>Assets</b>				
Cash and balances with banks	762,960	538,280	411,897	1,713,137
Derivative financial instruments	8	-	-	8
Advances and other accounts	1,628,926	55,997	363	1,685,286
Available-for-sale securities	909,353	3,348	-	912,701
<b>Total financial assets</b>	<b>3,301,247</b>	<b>597,625</b>	<b>412,260</b>	<b>4,311,132</b>
<b>Liabilities</b>				
Deposits from banks	18,413	161	-	18,574
Derivative financial instruments	77	-	-	77
Deposits from customers	2,634,107	581,793	398,160	3,614,060
Other accounts and accruals	334,405	641	913	335,959
<b>Total financial liabilities</b>	<b>2,987,002</b>	<b>582,595</b>	<b>399,073</b>	<b>3,968,670</b>
<b>Net on-balance sheet positions</b>	<b>314,245</b>	<b>15,030</b>	<b>13,187</b>	<b>342,462</b>
<b>Off-balance sheet net notional positions *</b>	<b>12,065</b>	<b>(281)</b>	<b>(11,853)</b>	<b>(69)</b>
<b>Credit commitments</b>	<b>2,274,123</b>	<b>28,038</b>	<b>-</b>	<b>2,302,161</b>

\* Off-balance sheet net notional positions represent the net notional amounts of foreign currency derivative financial instruments which are principally used to reduce the Bank's exposure to currency movements.

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

#### 3. Financial risk management (Continued)

##### 3.3 Market risk (Continued)

###### 3.3.3 Currency risk (Continued)

	HKD	USD	Others	Total
As at 31 December 2008				
<b>Assets</b>				
Cash and balances with banks	2,883,446	1,043,996	399,965	4,327,407
Derivative financial instruments	2,709	8	-	2,717
Financial assets designated at fair value through profit or loss	74,274	8,447	-	82,721
Advances and other accounts	1,689,762	161,275	230	1,851,267
Available-for-sale securities	9,443	2,007	-	11,450
<b>Total financial assets</b>	<b>4,659,634</b>	<b>1,215,733</b>	<b>400,195</b>	<b>6,275,562</b>
<b>Liabilities</b>				
Deposits from banks	14,082	-	6	14,088
Derivative financial instruments	2,725	8	-	2,733
Deposits from customers	4,142,012	1,207,058	398,224	5,747,294
Deposits from customers designated at fair value through profit or loss	74,274	8,447	-	82,721
Other accounts and accruals	74,564	6,316	2,483	83,363
<b>Total financial liabilities</b>	<b>4,307,657</b>	<b>1,221,829</b>	<b>400,713</b>	<b>5,930,199</b>
<b>Net on-balance sheet positions</b>	<b>351,977</b>	<b>(6,096)</b>	<b>(518)</b>	<b>345,363</b>
<b>Off-balance sheet net notional positions *</b>	<b>(1,415)</b>	<b>1,938</b>	<b>(530)</b>	<b>(7)</b>
<b>Credit commitments</b>	<b>2,429,847</b>	<b>13,980</b>	<b>-</b>	<b>2,443,827</b>

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

### 3. Financial risk management (Continued)

#### 3.3 Market risk (Continued)

##### 3.3.4 Interest rate risk

The table below summarises the Bank's exposure to interest rate risks. Included in the table are the Bank's financial assets and liabilities at carrying amounts, categorised by the earlier of contractual repricing or maturity dates.

At 31 December 2009	3 months or less	Over 3 months to 1 year	Over 1 year to 5 years	Over 5 years	Non- interest bearing	Total
<b>Assets</b>						
Cash and balances with banks	1,589,040	-	-	-	124,097	1,713,137
Derivative financial instruments	-	-	-	-	8	8
Advances and other accounts	1,333,818	511	222	-	350,735	1,685,286
Available-for-sale securities	899,919	-	-	-	12,782	912,701
<b>Total financial assets</b>	<b>3,822,777</b>	<b>511</b>	<b>222</b>	<b>-</b>	<b>487,622</b>	<b>4,311,132</b>
<b>Liabilities</b>						
Deposits from banks	-	-	-	-	18,574	18,574
Derivative financial instruments	-	-	-	-	77	77
Deposits from customers	3,101,036	505,612	981	-	6,431	3,614,060
Other accounts and accruals	-	-	-	-	335,959	335,959
<b>Total financial liabilities</b>	<b>3,101,036</b>	<b>505,612</b>	<b>981</b>	<b>-</b>	<b>361,041</b>	<b>3,968,670</b>
<b>Total interest sensitivity gap (unadjusted)*</b>	<b>721,741</b>	<b>(505,101)</b>	<b>(759)</b>	<b>-</b>		
<b>Effect of interest rate derivative contracts</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>		
<b>Total interest sensitivity gap (adjusted)*</b>	<b>721,741</b>	<b>(505,101)</b>	<b>(759)</b>	<b>-</b>		

\* Unadjusted interest sensitivity gap is determined based on positions of on-balance sheet assets and liabilities. Adjusted interest sensitivity gap takes into account the effect of interest rate derivative contracts entered into by the Bank to mitigate interest rate risk.

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

### 3. Financial risk management (Continued)

#### 3.3 Market risk (Continued)

##### 3.3.4 Interest rate risk (Continued)

At 31 December 2008	3 months or less	Over 3 months to 1 year	Over 1 year to 5 years	Over 5 years	Non-interest bearing	Total
<b>Assets</b>						
Cash and balances with banks	4,244,313	-	-	-	83,094	4,327,407
Derivative financial instruments	-	-	-	-	2,717	2,717
Financial assets designated at fair value through profit or loss	40,423	42,298	-	-	-	82,721
Advances and other accounts	1,568,802	184,048	87,028	1,259	10,130	1,851,267
Available-for-sale securities	-	-	-	-	11,450	11,450
<b>Total financial assets</b>	<b>5,853,538</b>	<b>226,346</b>	<b>87,028</b>	<b>1,259</b>	<b>107,391</b>	<b>6,275,562</b>
<b>Liabilities</b>						
Deposits from banks	-	-	-	-	14,088	14,088
Derivative financial instruments	-	-	-	-	2,733	2,733
Deposits from customers	5,269,468	427,880	44,306	-	5,640	5,747,294
Deposits from customers designated at fair value through profit or loss	40,423	42,298	-	-	-	82,721
Other accounts and accruals	-	-	-	-	83,363	83,363
<b>Total financial liabilities</b>	<b>5,309,891</b>	<b>470,178</b>	<b>44,306</b>	<b>-</b>	<b>105,824</b>	<b>5,930,199</b>
<b>Total interest sensitivity gap (unadjusted)*</b>	<b>543,647</b>	<b>(243,832)</b>	<b>42,722</b>	<b>1,259</b>		
<b>Effect of interest rate derivative contracts</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>		
<b>Total interest sensitivity gap (adjusted)*</b>	<b>543,647</b>	<b>(243,832)</b>	<b>42,722</b>	<b>1,259</b>		

## **MEVAS Bank Limited**

### **Notes to the Financial Statements**

(Expressed in thousands of Hong Kong dollars)

#### **3. Financial risk management (Continued)**

##### **3.4 Liquidity risk**

Liquidity risk is the risk that the Bank is unable to meet its payment obligations associated with its financial liabilities when they fall due and to replace funds when they are withdrawn. The consequence may be the failure to meet obligations to repay depositors and fulfill commitments to lend.

###### **3.4.1 Liquidity risk management process**

The Bank manages its liquidity on a prudent basis to ensure that a sufficiently high liquidity ratio relative to the statutory minimum is maintained throughout the year. The average liquidity ratio of the Bank during the period was well above the 25% minimum ratio set by the Hong Kong Banking Ordinance.

Asset and Liability Management Committee ("ALCO") of the Bank's immediate holding company, Dah Sing Banking Group Limited, regularly reviews the Bank's current loan and deposit mix and changes, funding requirements and projections, and monitors the liquidity ratio and maturity mismatch on an ongoing basis. Appropriate limits on liquidity ratio and maturity mismatch are set and sufficient liquid assets are held to ensure that the Bank can meet all short-term funding requirements.

The Bank's funding comprises mainly deposits of customers. Short-term interbank deposits are taken on a limited basis and the Bank is a net lender to the interbank market.

Monitoring and reporting take the form of cash flow measurement and projections for the next day, week and month respectively, as these are key periods for liquidity management. The starting point for those projections is an analysis of the contractual maturity of the financial liabilities and the expected collection date of the financial assets.

ALCO also monitors unmatched medium-term assets, the level and type of undrawn lending commitments, the usage of overdraft facilities and the impact of contingent liabilities such as standby letters of credit and guarantees.

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

### 3. Financial risk management (Continued)

#### 3.4 Liquidity risk (Continued)

##### 3.4.2 Maturity analysis

The table below analyses the Bank's assets and liabilities into relevant maturity groupings based on the remaining period at end of the reporting period to the contractual maturity date or, where applicable, the earliest callable date.

At 31 December 2009

	Repayable on demand	Up to 1 month	3 months or less but over 1 month	Over 3 months to 1 year	Over 1 year to 5 years	Over 5 years	Indefinite	Total
<b>Assets</b>								
Cash and balances with banks	124,097	1,589,040	-	-	-	-	-	1,713,137
Derivative financial instruments	-	8	-	-	-	-	-	8
Advances and other accounts	311,201	282,560	49,356	131,119	382,574	489,747	38,729	1,685,286
Available-for-sale securities	-	149,996	749,923	-	-	-	12,782	912,701
Furniture and equipment	-	-	-	-	-	-	6,666	6,666
Investment properties	-	-	-	-	-	-	76,000	76,000
Current income tax assets	-	-	-	4,751	-	-	-	4,751
<b>Total assets</b>	<b>435,298</b>	<b>2,021,604</b>	<b>799,279</b>	<b>135,870</b>	<b>382,574</b>	<b>489,747</b>	<b>134,177</b>	<b>4,398,549</b>
<b>Liabilities</b>								
Deposit from banks	18,574	-	-	-	-	-	-	18,574
Derivative financial instruments	-	77	-	-	-	-	-	77
Deposits from customers	1,599,673	680,839	826,955	505,612	981	-	-	3,614,060
Other accounts and accruals	-	28,755	1,860	284,856	1,339	-	19,149	335,959
Deferred income tax liabilities	-	-	-	-	419	-	-	419
<b>Total liabilities</b>	<b>1,618,247</b>	<b>709,671</b>	<b>828,815</b>	<b>790,468</b>	<b>2,739</b>	<b>-</b>	<b>19,149</b>	<b>3,969,089</b>
<b>Net liquidity gap</b>	<b>(1,182,949)</b>	<b>1,311,933</b>	<b>(29,536)</b>	<b>(654,598)</b>	<b>379,835</b>	<b>489,747</b>	<b>115,028</b>	<b>429,460</b>

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

### 3. Financial risk management (Continued)

#### 3.4 Liquidity risk (Continued)

##### 3.4.2 Maturity analysis (Continued)

At 31 December 2008

	Repayable on demand	Up to 1 month	3 months or less but over 1 month	Over 3 months to 1 year	Over 1 year to 5 years	Over 5 years	Indefinite	Total
<b>Assets</b>								
Cash and balances with banks	83,094	4,244,313	-	-	-	-	-	4,327,407
Derivative financial instruments	-	2	1	2	2,712	-	-	2,717
Financial assets designated at fair value through profit or loss	-	30,487	9,935	42,299	-	-	-	82,721
Advances and other accounts	391,557	21,878	28,829	114,645	724,382	568,960	1,016	1,851,267
Available-for-sale securities	-	-	-	-	-	-	11,450	11,450
Furniture and equipment	-	-	-	-	-	-	8,384	8,384
Investment properties	-	-	-	-	-	-	63,000	63,000
Current income tax assets	-	-	-	2,607	-	-	-	2,607
Deferred income tax assets	-	-	-	-	1,847	-	-	1,847
<b>Total assets</b>	<b>474,651</b>	<b>4,296,680</b>	<b>38,765</b>	<b>159,553</b>	<b>728,941</b>	<b>568,960</b>	<b>83,850</b>	<b>6,351,400</b>
<b>Liabilities</b>								
Deposit from banks	14,088	-	-	-	-	-	-	14,088
Derivative financial instruments	-	9	1	2	2,721	-	-	2,733
Deposits from customers	1,022,636	2,408,532	1,889,600	426,075	451	-	-	5,747,294
Deposits from customers designated at fair value through profit or loss	-	30,487	9,935	42,299	-	-	-	82,721
Other accounts and accruals	-	30,709	6,997	32,896	1,401	-	11,360	83,363
<b>Total liabilities</b>	<b>1,036,724</b>	<b>2,469,737</b>	<b>1,906,533</b>	<b>501,272</b>	<b>4,573</b>	<b>-</b>	<b>11,360</b>	<b>5,930,199</b>
<b>Net liquidity gap</b>	<b>(562,073)</b>	<b>1,826,943</b>	<b>(1,867,768)</b>	<b>(341,719)</b>	<b>724,368</b>	<b>568,960</b>	<b>72,490</b>	<b>421,201</b>

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

### 3. Financial risk management (Continued)

#### 3.4 Liquidity risk (Continued)

##### 3.4.2 Maturity analysis (Continued)

In respect of certificates of deposit held for investment purposes and included in financial assets designated at fair value through profit or loss as at end of the reporting period, the applicable balance, analysed based on the remaining period at the end of the reporting period to contractual maturity, is shown as follows.

Repayable on demand	Up to 1 month	3 months or less but over 1 month	Over 3 months to 1 year	Over 1 year to 5 years	Over 5 years	Undated	Total
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##### As at 31 December 2009

Certificates of deposit held included in:

Financial assets designated at fair value through profit or loss	-	-	-	-	-	-	-
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##### As at 31 December 2008

Certificates of deposit held included in:

Financial assets designated at fair value through profit or loss	-	9,331	9,935	42,299	-	-	61,565
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The matching and controlled mismatching of the maturities and interest rates of assets and liabilities are fundamental to the management of the Bank. It is unusual for banks to be completely matched, as businesses transacted are often of uncertain term and of different types. An unmatched position potentially enhances profitability, but also increases the risk of losses.

The maturities of assets and liabilities and the ability to replace, at an acceptable cost, interest-bearing liabilities as they mature are important factors in assessing the liquidity of the Bank and its exposure to changes in interest rates and exchange rates.

The total outstanding contractual amount of commitments to extend credit does not necessarily represent future cash requirements, as many of these commitments will expire or terminate without being funded.

##### 3.4.3 Undiscounted cash flows by contractual maturities

The table below presents the cash flows payable by the Bank under non-derivative financial liabilities, derivative financial liabilities that will be settled on a net basis and derivative financial instruments that will be settled on gross basis by remaining contractual maturities at the end of the reporting period. The amounts disclosed in the table are the contractual undiscounted cash flows, whereas the Bank manages the inherent liquidity risk based on expected undiscounted cash inflows.

The Bank's derivatives that normally will be settled on a net basis include:

- Interest rate derivatives: interest rate swaps, over-the-counter (OTC) interest rate options; and
- Foreign exchange derivatives: OTC currency options.

The Bank's derivatives that will be settled on a gross basis include:

- Foreign exchange derivatives: currency forward.

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

### 3. Financial risk management (Continued)

#### 3.4 Liquidity risk (Continued)

##### 3.4.3 Undiscounted cash flows by contractual maturities (Continued)

As at 31 December 2009

	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
<b>Non-derivative cash flow</b>						
Liabilities						
Deposits from banks	18,574	-	-	-	-	18,574
Deposits from customers	2,281,768	829,821	508,991	1,035	-	3,621,615
Other liabilities	27,706	-	283,522	1,746	-	312,974
Total liabilities (contractual maturity dates)	2,328,048	829,821	792,513	2,781	-	3,953,163
<b>Derivative cash flow</b>						
Derivative financial instruments settled on gross basis						
Total outflow	25,515	-	-	-	-	25,515
Total inflow	(25,584)	-	-	-	-	(25,584)
	(69)	-	-	-	-	(69)

As at 31 December 2008

	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
<b>Non-derivative cash flow</b>						
Liabilities						
Deposits from banks	14,088	-	-	-	-	14,088
Deposits from customers	3,445,942	1,903,021	435,385	509	-	5,784,857
Deposits from customers designated at fair value through profit or loss	31,645	10,255	42,463	-	-	84,363
Other liabilities	18,212	-	30,000	1,394	-	49,606
Total liabilities (contractual maturity dates)	3,509,887	1,913,276	507,848	1,903	-	5,932,914
<b>Derivative cash flow</b>						
Derivative financial instruments settled on gross basis						
Total outflow	5,559	-	-	-	-	5,559
Total inflow	(5,552)	-	-	-	-	(5,552)
	7	-	-	-	-	7

Assets available to meet all of the liabilities and to cover outstanding loan commitments include cash, central bank balances, items in the course of collection and treasury bills; and loans and advances to customers. In the normal course of business, a proportion of customer loans contractually repayable within one year will be extended.

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

#### 3. Financial risk management (Continued)

##### 3.4 Liquidity risk (Continued)

###### 3.4.4 Off-balance sheet items

Included in the table below are the following items:

- Loan commitments by reference to the dates of the contractual amounts of the Bank's off-balance sheet financial instruments that commit it to extend credit to customers and other facilities;
- Financial guarantees based on the conditions existing at the reporting date as to what contractual payments are required; and
- The future minimum lease payments under non-cancellable operating leases in respect of operating lease commitments where the Bank is the lessee.

##### As at 31 December 2009

	No later than 1 year	1-5 years	Total
Loan commitments	2,301,892	-	2,301,892
Guarantees, acceptances and other financial facilities			
- Guarantees and standby letters of credit	269	-	269
Operating lease commitments	7,249	6,551	13,800
Total	<u>2,309,410</u>	<u>6,551</u>	<u>2,315,961</u>

##### As at 31 December 2008

	No later than 1 year	1-5 years	Total
Loan commitments	2,443,558	-	2,443,558
Guarantees, acceptances and other financial facilities			
- Guarantees and standby letters of credit	269	-	269
Operating lease commitments	7,178	2,946	10,124
Total	<u>2,451,005</u>	<u>2,946</u>	<u>2,453,951</u>

#### 3.5 Fair values of financial assets and liabilities

##### (a) Determination of fair value

For financial assets and liabilities traded in active markets, the determination of fair value is based on quoted market prices, dealer price quotations or broker quotes from Bloomberg and Reuters. The quoted market price used for financial assets held by the Bank is the current bid price; the appropriate quoted market price for financial liabilities is the current ask price.

A financial instrument is regarded as quoted in an active market if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency, and those prices represent actual and regularly occurring market transactions on an arm's length basis. If the above criteria are not met, the market is regarded as being inactive. Indications that a market is inactive are when there is a wide bid-offer spread or significant increase in bid-offer spread or there are few recent transactions.

The fair value of financial instruments that are not traded in an active market is determined by using valuation techniques. In these techniques, fair values are estimated from observable data in respect of similar financial instruments, using models to estimate the present value of expected future cash flows or other valuation techniques using inputs (for example LIBOR yield curve, FX rates, volatilities, comparable credit spreads, and counterparty spreads) existing at the end of the reporting period.

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

#### 3. Financial risk management (Continued)

##### 3.5 Fair values of financial assets and liabilities (Continued)

###### (a) Determination of fair value (Continued)

The Bank uses widely recognised valuation models including present value techniques and option pricing models for determining the fair values of non-standardised financial instruments of lower complexity such as options or interest rate swaps. For these financial instruments, inputs into models are generally market-observable. The fair value of interest-rate swaps is calculated as the present value of the estimated future cash flows. The fair value of foreign exchange forward contracts is generally based on current forward exchange rates.

The Bank uses external price quotes and its own credit risk spreads in determining the current value for its derivative liabilities and other liabilities for which it has elected the fair value option. When the Bank's credit spreads widen, the Bank recognises a gain on these liabilities because the value of the liabilities has decreased. When the Bank's credit spreads narrow, the Bank recognises a loss on these liabilities because the value of the liabilities has increased.

The output of a model is always an estimate or approximation of a value that cannot be determined with certainty, and valuation techniques employed may not fully reflect all factors relevant to the positions the Bank holds. Valuations are therefore adjusted, where appropriate, to allow for additional factors including model risks, liquidity risk and counterparty credit risk. Based on the established fair value model governance policies of the Bank, and the related controls and procedures applied, management believes that these valuation adjustments are necessary and appropriate to fairly state the values of financial instruments carried at fair value in the statement of financial position. Price data and parameters used in the measurement procedures applied are reviewed carefully and adjusted, if necessary, particularly in view of the current market developments.

During 2009 and 2008, there was no financial instrument measured at fair value using a valuation technique which is based on assumptions that are not supported by observable market prices for the same or similar instrument or not based on available observable market data.

###### (b) Fair value hierarchy

HKFRS 7 specifies a hierarchy of valuation techniques based on whether the inputs to those valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources; unobservable inputs reflect the Bank's market assumptions. These two types of inputs have created the following fair value hierarchy:

Level	Descriptions
1	Quoted prices (unadjusted) in active markets for identical assets or liabilities. This level includes listed equity securities and debt instruments on exchange (for example, London Stock Exchange, Frankfurt Stock Exchange, New York Stock Exchange) and exchanges traded derivatives like futures (for example, Nasdaq, S&P 500).
2	Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices). This level includes the majority of the over-the-counter derivative contracts, and issued structured debt. The sources of input parameters include LIBOR yield curve, or Bloomberg and Reuters for counterparty credit risk.
3	Inputs for the asset or liability that are not based on observable market data (unobservable inputs). This level includes equity investments and debt instruments with significant unobservable components.

The hierarchy requires the use of observable market data when available. The Bank considers relevant and observable market prices in its valuations where possible.

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

#### 3. Financial risk management (Continued)

##### 3.5 Fair values of financial assets and liabilities (Continued)

###### (b) Fair value hierarchy (Continued)

Assets and liabilities measured at fair value:

At 31 Dec 2009	Level 1	Level 2	Level 3	Total
Descriptions				
Financial assets at fair value through profit or loss				
Held for trading				
Derivatives	-	8	-	8
Available-for-sale financial assets				
Debt securities	-	900,244	-	900,244
Equity securities	109	12,348	-	12,457
Total assets measured at fair value	<u>109</u>	<u>912,600</u>	<u>-</u>	<u>912,709</u>
Total liabilities measured at fair value	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>

As at 31 December 2009, the Bank did not have any financial assets and liabilities in the Level 3 fair value hierarchy. There were no transfers of financial assets and liabilities into or out of the Level 3 fair value hierarchy.

###### (c) Financial instruments not measured at fair value

The table below summarises the carrying amounts and fair values of those financial assets and liabilities not presented in the Bank's statement of financial position at their fair value. For disclosure purposes, these fair values have been estimated by discounting the future contractual cash flows at the current market interest rate that is available to the Group for similar financial instruments, if applicable.

	Carrying value		Fair value	
	2009	2008	2009	2008
<b>Financial assets</b>				
Cash and balances with banks	<b>1,713,137</b>	4,327,407	<b>1,713,125</b>	4,328,071
Advances and other accounts	<b>1,685,286</b>	1,851,267	<b>1,685,293</b>	1,850,218
<b>Financial liabilities</b>				
Deposits from banks	<b>18,574</b>	14,088	<b>18,574</b>	14,088
Deposits from customers	<b>3,614,060</b>	5,747,294	<b>3,616,399</b>	5,763,211

###### (i) Placements with banks

The fair value of floating rate placements and overnight deposits is their carrying amount. The estimated fair value of fixed interest bearing deposits is based on discounted cash flows using prevailing money-market interest rates for debts with similar credit risk and remaining maturity.

###### (ii) Loans and advances to customers

The estimated fair value of loans and advances represents the discounted amount of estimated future cash flows expected to be received. Expected cash flows are discounted at current market rates to determine fair value.

###### (iii) Investment securities

The fair value of investment securities included in the loans and receivables is based on market prices or broker/dealer price quotations. Where this information is not available, fair value is estimated using quoted market prices for securities with similar credit, maturity and yield characteristics.

## **MEVAS Bank Limited**

### **Notes to the Financial Statements**

(Expressed in thousands of Hong Kong dollars)

#### **3. Financial risk management (Continued)**

##### **3.5 Fair values of financial assets and liabilities (Continued)**

(c) Financial instruments not measured at fair value (Continued)

(iv) Deposits from banks and customers

The estimated fair value of deposits with no stated maturity, which includes non-interest bearing deposits, is the amount repayable on demand. The estimated fair value of fixed interest-bearing deposits not quoted in an active market is based on discounted cash flows using interest rates for new debts with similar remaining maturity.

##### **3.6 Capital management**

The Bank's objectives when managing capital are:

- To comply with the capital requirements set by the banking regulator;
- To safeguard the Bank's ability to continue its business as a going concern;
- To maximise returns to shareholders and optimize the benefits to other stakeholders; and
- To maintain a strong capital base to support the development of its business.

Capital adequacy of and the use of regulatory capital by the Bank are monitored regularly by the Bank's management, employing techniques based on the guidelines developed by the Basel Committee, as implemented by the Hong Kong Monetary Authority ("HKMA"), for supervisory purposes. The required information is filed with the HKMA on a quarterly basis.

The HKMA requires the Bank to maintain a ratio of total regulatory capital to the risk-weighted asset (i.e. the capital adequacy ratio) at or above the internationally agreed minimum of 8%. The Bank's regulatory capital is divided into two tiers:

- Core capital: share capital, profit and loss, and reserves created by appropriations of retained earnings. The book value of goodwill and other intangible assets is deducted in arriving at core capital; and
- Supplementary capital: qualifying perpetual and term subordinated debts, collectively assessed impairment allowances, regulatory reserve, and fair value gains arising on revaluation of holdings of land and buildings and available-for-sale equities and debt securities.

Investment in subsidiaries, significant investments in non-subsidiary companies and shares, exposures to connected companies and investments in other banks' equity are deducted from core and supplementary capital to arrive at the regulatory capital.

Risk-weighted amount is the aggregate of the risk-weighted amounts for credit risk, market risk and operational risk, and covers both on-balance sheet and off-balance sheet exposures. On-balance sheet exposures are classified according to the obligor or the nature of each exposure and risk-weighted based on the credit assessment rating assigned by an external credit assessment institution recognised by the HKMA or other principles as set out in the Banking (Capital) Rules, taking into account the capital effects of credit risk mitigation. Off-balance sheet exposures are converted into credit-equivalent amounts by applying relevant credit conversion factors to each exposure, before being classified and risk-weighted as if they were on-balance sheet exposures.

##### **3.7 Fiduciary activities**

The Bank provides custody, trustee, wealth management and advisory services to third parties, which involve the Bank making allocation and purchase and sale decisions in relation to a variety of financial instruments. Those assets that are held in a fiduciary capacity are not included in the Bank's financial statements. These services could give rise to the risk that the Bank will be accused of mal-administration.

## **MEVAS Bank Limited**

### **Notes to the Financial Statements**

(Expressed in thousands of Hong Kong dollars)

#### **4. Critical accounting estimates, and judgements in applying accounting policies**

##### **4.1 Critical accounting estimates and assumptions**

The Bank makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Changes in estimates and assumptions may have a significant impact on the results of the Bank in the periods when changes are made. The application and selection of different estimates and assumptions, and their subsequent changes, could affect the Bank's profit and net asset value in the future. The Bank, based on its high-level assessment of the sensitivity impacts on the reported assets and liabilities of the Bank arising from the changes in critical accounting estimates and assumptions, believes that the estimates and assumptions adopted are appropriate and reasonable, and the financial results and positions presented in the Bank's financial statements are fair and reasonable in all material respects.

##### **(a) Impairment allowances on loans and advances**

The Bank reviews its loan portfolios to assess impairment at least on a quarterly basis. In determining whether an impairment loss should be recorded in the income statement, the Bank makes judgments as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans before the decrease can be identified with an individual loan in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or economic conditions that correlate with defaults on assets in the group. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when estimating its future cash flows of recoverable amounts. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

##### **(b) Fair value of financial instruments**

A majority of the Bank's investments in debt securities carried at fair value are valued based on observable market quotations. As a consequence of the difficulties in financial markets, the Bank has witnessed observable declines in market liquidity and the range of market quotations for certain securities have widened. The Bank applies judgment in selecting the most appropriate quotation for valuation purposes based on its assessment of the range of observable quotations, recent observable transactions, the reliability and quality of the pricing source, and the value of securities of a similar nature.

#### **4.2 Critical judgments in applying accounting policies**

##### **(a) Distinction between investment properties and owner-occupied properties**

The Bank determines whether a property qualifies as an investment property. In making its judgment, the Bank considers whether the property generates cash flows largely independently of the other assets held by an entity. Owner-occupied properties generate cash flows that are attributable not only to property but also to other assets used in the production or supply process.

Some properties comprise a portion that is held to earn rentals or for capital appreciation and another portion that is held to supply services or for administrative purposes. If these portions can be sold separately (or leased out separately under a finance lease), the Bank accounts for the portions separately. If the portions cannot be sold separately, the property is accounted for as investment property only if an insignificant portion is held to supply services or for administrative purposes. Judgment is applied in determining whether ancillary services are so significant that a property does not qualify as investment property. The Bank considers each property separately in making its judgment.

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

#### 4. Critical accounting estimates, and judgements in applying accounting policies (Continued)

##### 4.2 Critical judgments in applying accounting policies (Continued)

###### (b) Assessment of claims and contingencies

Judgment is needed to determine if provision for compensation to certain customers who had bought structured investments distributed (but not originated or arranged) by the Bank need to be recorded in accordance with the requirements of HKAS 37 "Provisions, Contingent Liabilities and Contingent Assets". In making this judgment, the Bank evaluates the information relating to each or similar cases, and the likelihood and estimated amount of outflow of resources which may be incurred to settle the obligation after considering factors such as recent settlement experiences and advice from legal counsel.

###### (c) Initial recognition of Lehman Brothers minibonds and private placement notes acquired pursuant to repurchase scheme and settlement arrangements agreed with customers

On 22 July and 23 December 2009, the Bank agreed with the Securities and Futures Commission, and the HKMA to make an offer to eligible customers to repurchase, respectively, their holdings in all outstanding Lehman Brothers minibonds ("Minibonds") and principal protected notes ("PPN") subscribed through the Bank ("the Repurchase Schemes").

In determining the charge to the income statement in respect of the Minibonds and PPN, the Bank took into account the estimated aggregate amount paid and payable under the Repurchase Schemes and the voluntary offer, the provision made prior to the date of the Repurchase Schemes and the estimated amount recoverable from the Minibonds and PPN.

The amount recoverable from the Minibonds and PPN is uncertain and dependent on a number of factors including resolution of certain legal matters, which may result in a wide range of recovery outcomes. The Bank has made an assessment of the amount recoverable under such uncertainties. The final amount of recovery could be different from the assessment made by the Bank, and may result in future charge or credit to be recognised in the income statement in the period when legal clarifications or realisation of assets take place.

## **MEVAS Bank Limited**

### **Notes to the Financial Statements**

(Expressed in thousands of Hong Kong dollars)

#### **5. Operating segment reporting**

In prior years, the Bank has determined the segment information on the basis of business segments, which are distinguishable business divisions of the Bank that provide products and services to customers base or dealing with the market that are different to those of other business segments (e.g. personal banking, commercial banking, treasury & others).

In the 2009 financial year, segment reporting by the Bank was prepared for the first time in accordance with HKFRS 8 "Operating Segments". Information reported to the chief operating decision maker ("CODM") which includes the Chief Executive and other executive committee members, for the purposes of resource allocation and assessment of performance, is determined on the basis of personal banking, commercial banking and treasury.

Considering the customer groups, products and services of local businesses, the economic environment, and regulations, we group the operating segments of the Bank into the following reportable segments:

- Personal banking business includes the acceptance of deposits from individual customers and the extension of residential mortgage lending, personal loans, overdraft and credit card services, the provision of insurance sales and investment services.
- Commercial banking business includes the provision of finance to commercial, industrial and institutional customers.
- Treasury activities are mainly the provision of centralized cash managements for deposit taking and lending.
- Others include results of operations and corporate investments not directly identified under other business divisions.

For the purpose of segment reporting, revenue derived from customers, products and services directly identifiable with individual segments are reported directly under respective segments, while revenue and funding cost arising from inter-segment funding operation and funding resources are allocated to segments by way of transfer pricing mechanism with reference to market interest rates. Transactions within segments are priced based on similar terms offered to or transacted with external parties. Inter-segment income or expenses are eliminated on consolidation.

All direct costs incurred by different segments are grouped under respective segments. Indirect costs and support functions' costs are allocated to various segments and products based on effort and time spent as well as segments' operating income depending on the nature of costs incurred. Costs related to corporate activities that cannot be reasonably allocated to segments, products and support functions are grouped under Others as corporate overhead.

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

#### 5. Operating segment reporting (continued)

For the year ended 31 December 2009

	Personal Banking	Commercial Banking	Treasury	Others	Total
Net interest income	52,743	6,957	6,148	457	66,305
Non-interest income	18,331	641	1,100	4,815	24,887
Total operating income	71,074	7,598	7,248	5,272	91,192
Operating expenses	(108,884)	(328)	(966)	-	(110,178)
Operating (loss)/profit before impairment losses	(37,810)	7,270	6,282	5,272	(18,986)
Loan impairment losses	(17,041)	330	-	-	(16,711)
Operating (loss)/profit before gains or losses on certain investment and fixed assets	(54,851)	7,600	6,282	5,272	(35,697)
Net gain on disposal of furniture and equipment and fair value adjustment on investment properties	-	-	-	12,965	12,965
Net loss on disposal of investment in securities	(368)	-	-	-	(368)
Net gain on disposal of personal loan portfolio	3,100	-	-	-	3,100
Net gain on transfer of credit card portfolio	27,000	-	-	-	27,000
(Loss)/profit before income tax	(25,119)	7,600	6,282	18,237	7,000
Income tax credit/(expense)	5,053	(1,276)	(1,117)	(2,519)	141
(Loss)/profit after income tax	(20,066)	6,324	5,165	15,718	7,141
As at 31 December 2009					
Segment assets	1,077,751	330,028	2,599,122	391,648	4,398,549
Segment liabilities	3,886,582	-	18,651	63,856	3,969,089

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

#### 5. Operating segment reporting (continued)

For the year ended 31 December 2008 (Restated)

	Personal Banking	Commercial Banking	Treasury	Others	Total
Net interest income	58,669	10,678	10,404	6,681	86,432
Non-interest income	29,052	530	1,273	3,107	33,962
Total operating income	87,721	11,208	11,677	9,788	120,394
Operating expenses	(92,882)	(452)	(861)	-	(94,195)
Operating (loss)/profit before impairment losses	(5,161)	10,756	10,816	9,788	26,199
Loan impairment losses	(14,155)	(575)	-	-	(14,730)
Operating (loss)/profit before gains or losses on certain investment and fixed assets	(19,316)	10,181	10,816	9,788	11,469
Net loss on disposal of furniture and equipment and fair value adjustment on investment properties	-	-	-	(7,999)	(7,999)
Net (loss)/gain on disposal of investment in securities	(321)	-	-	383	62
(Loss)/profit before income tax	(19,637)	10,181	10,816	2,172	3,532
Income tax credit/(expense)	3,172	(1,638)	(1,717)	(364)	(547)
(Loss)/profit after income tax	(16,465)	8,543	9,099	1,808	2,985
As at 31 December 2008					
Segment assets	1,431,417	509,917	4,316,832	93,234	6,351,400
Segment liabilities	5,830,015	-	16,821	83,363	5,930,199

**MEVAS Bank Limited****Notes to the Financial Statements**

(Expressed in thousands of Hong Kong dollars)

**6. Net interest income**

	2009	2008
<b>Interest income</b>		
Cash and balances with banks	22,107	109,765
Investments in unlisted securities	750	6,739
Advances to customers	85,101	115,469
Others	136	935
	<u>108,094</u>	<u>232,908</u>
<b>Interest expense</b>		
Deposits from banks / Deposits from customers	<u>41,789</u>	146,476
<b>Included within interest income</b>		
Interest income on financial assets not at fair value through profit or loss	<u>107,344</u>	<u>226,169</u>
<b>Included within interest expense</b>		
Interest expense on financial liabilities not at fair value through profit or loss	<u>40,762</u>	<u>139,002</u>

**7. Net fee and commission income**

	2009	2008
<b>Fee and commission income</b>		
Fee and commission income from financial assets and liabilities not at fair value through profit or loss		
- Credit related fees and commissions	3,336	3,872
- Credit card	12,768	14,129
Other fee and commission income		
- Securities brokerage and investment services	1,149	6,517
- Insurance distribution and others	2,080	2,798
- Retail investment funds and fiduciary services	263	1,947
- Other fees	963	1,930
	<u>20,559</u>	<u>31,193</u>
<b>Fee and commission expense</b>		
Handling fees and commission	1,061	1,487
Other fees paid	533	777
	<u>1,594</u>	<u>2,264</u>

**8. Net trading income**

	2009	2008
Net gain arising from dealing in foreign currencies	<u>1,100</u>	<u>1,273</u>

**9. Other operating income**

	2009	2008
Dividend income from investments in available-for-sale securities		
- Unlisted investments	1,215	1,057
Initial fair value recognition of available-for-sale securities	-	484
Gross rental income from investment properties	3,600	2,050
Others	7	169
	<u>4,822</u>	<u>3,760</u>

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

#### 10. Operating expenses

	2009	2008
Employee compensation and benefit expenses (including directors' remuneration) (Note 11)	10,750	9,285
Management fee paid to a fellow subsidiary, Dah Sing Bank, Limited	15,005	15,908
Premises and equipment expense, excluding depreciation		
- Rental of premises	9,838	9,632
- Others	2,548	1,994
Depreciation (Note 22)	1,840	1,598
Advertising costs	5,893	9,498
Auditors' remuneration	521	573
Others (Note)	63,783	45,707
	<u>110,178</u>	<u>94,195</u>

Note:

A substantial portion of other operating expenses included in "Others" in 2009 and 2008 was expenses incurred on Lehman Brothers related products in relation to the Repurchase Schemes (Note 4.2 (c)) and the voluntary offers based on the Bank's judgment as at 31 December 2008, and subsequently settlements with customers pursuant to a voluntary repurchase scheme announced in July 2009 (together with another 14 banks in Hong Kong) on the repurchase of Lehman Brothers minibonds, followed by another voluntary repurchase scheme announced by the Bank in December 2009 on certain principal protected notes issued by Lehman Brothers, and further assessment for position as at 31 December 2009.

#### 11. Employee compensation and benefit expenses

	2009	2008
Salaries and other staff costs	10,361	8,906
Pension costs - defined contribution plans	389	379
	<u>10,750</u>	<u>9,285</u>

Employee benefit expenses included directors' emoluments (Note 12).

#### 12. Directors' emoluments

	2009	2008
Salaries, housing, benefits in kind and other allowances	1,010	488
Pensions	48	45
	<u>1,058</u>	<u>533</u>

#### 13. Impairment losses on loans and advances

	2009	2008
Net charge of impairment losses on loans and advances		
- Collectively assessed	16,711	14,730
Of which		
- new allowances (including any amount directly written off in the year)	28,080	21,066
- releases	(6,116)	-
- recoveries	(5,253)	(6,336)
Net charge to income statement	<u>16,711</u>	<u>14,730</u>

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

#### 14. Net gain on disposal/transfer of loan portfolios

	2009	2008
Premium on disposal of personal loan portfolio	3,100	-
Premium on transfer of credit card portfolio	27,000	-
	<u>30,100</u>	<u>-</u>

During the year, personal loans (net of impairment allowances made) amounting to HK\$103 million were sold to Dah Sing Bank, Limited ("DSB"), a fellow subsidiary, at a premium of HK\$3.1 million to the Bank.

On 31 December 2009 the Bank entered into an agreement with DSB to transfer the economic benefits and risks in respect of the Bank's credit card portfolio. An amount of HK\$27 million is recognised as an income in the income statement since the benefits of the credit card portfolio (e.g. market share, customer relationships and Mevas brand use right) have been passed to DSB since the date of the agreement. The title to all rights and obligations in respect of the credit card portfolio, however, will be transferred on a later date in 2010. Therefore, the Bank continues to recognise the outstanding balance of credit card receivable in its loan book as of 31 December 2009.

There is a contractual obligation of the Bank to pass the cash flows of the credit card portfolio to DSB. This payable is reported under "Other accounts and accruals" in Note 28. The consideration receivable from DSB is reported under "Other assets" in Note 25.

#### 15. Income tax (credit) / expense

Hong Kong profits tax has been provided at the rate of 16.5% (2008: 16.5%) on the estimated assessable profit for the year.

	2009	2008
Current income tax	(2,144)	2,294
Deferred income tax		
- Impact of change of Hong Kong tax rate	-	12
- Origination and reversal of temporary differences	2,003	(1,759)
<b>Income tax (credit) / expense</b>	<u>(141)</u>	<u>547</u>

The tax on the Bank's profit before income tax differs from the theoretical amount that would arise using the tax rate applicable to profits of the Bank as follows:

	2009	2008
Profit before income tax	<u>7,000</u>	<u>3,532</u>
Calculated at a taxation rate of 16.5% (2008: 16.5%)	1,155	583
Tax effects of:		
Income not subject to taxation	(2,349)	(255)
Expenses not deductible for tax purposes	1,053	207
Remeasurement of deferred tax – change of Hong Kong tax rate	-	12
<b>Income tax (credit) / expense</b>	<u>(141)</u>	<u>547</u>

#### 16. Cash and balances with banks

	2009	2008
Cash and balances with banks	124,097	83,094
Money at call and short notice	1,589,040	4,244,313
	<u>1,713,137</u>	<u>4,327,407</u>

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

#### 17. Derivative financial instruments

The notional principal amounts of outstanding derivative contracts and their fair values as of 31 December 2009 were as follows:

	Contract/ notional amount	Fair values	
		Assets	Liabilities
<b>Derivatives held for trading</b>			
a) <i>Foreign exchange derivatives</i>			
Currency forwards	25,523	8	(77)
b) <i>Interest rate derivatives</i>			
Interest rate swaps	-	-	-
Interest rate options	-	-	-
<b>Total recognised derivative financial assets/(liabilities)</b>	<b>25,523</b>	<b>8</b>	<b>(77)</b>

The notional principal amounts of outstanding derivative contracts and their fair values as of 31 December 2008 were as follows:

	Contract/ notional amount	Fair values	
		Assets	Liabilities
Derivatives held for trading			
a) <i>Foreign exchange derivatives</i>			
Currency forwards	5,701	2	(9)
b) <i>Interest rate derivatives</i>			
Interest rate swaps	91,320	1,338	(1,347)
Interest rate options	91,320	1,377	(1,377)
<b>Total recognised derivative financial assets/(liabilities)</b>	<b>188,341</b>	<b>2,717</b>	<b>(2,733)</b>

The effect of valid bilateral netting agreements had been taken into account in disclosing the fair value of derivatives.

The credit risk weighted amounts of the above off-balance sheet exposures calculated under Basel II basis and without taking into account the effect of bilateral netting arrangements that the Bank entered into, are as follows:

	2009	2008
Derivatives		
Interest rate swaps	-	1,000
Interest rate options	-	1,596
	-	2,596

The above positions taken in financial instruments arose from the execution of trade orders from customers or transactions taken to hedge these positions and funding management of the Bank.

The contract amounts of these instruments indicate the volume of transactions outstanding as at the end of the reporting period, they do not represent the amounts at risk.

The credit risk weighted amounts are the amounts that have been calculated with reference to the Banking (Capital) Rules issued by the HKMA. The amounts calculated are dependent upon the status of the counterparty and the maturity characteristics of each type of contract.

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

#### 18. Financial assets designated at fair value through profit or loss

	2009	2008
Debt securities designated at fair value through profit or loss:		
- unlisted	-	82,721
Included within debt securities are:		
- Certificates of deposit held	-	61,565
- Other debt securities	-	21,156
	-	82,721

Financial assets designated at fair value through profit or loss were securities issued by Dah Sing Bank, Limited (Note 27).

#### 19. Advances and other accounts

##### (a) Analysis of advances to customers

	2009	2008
Loans and advances to individuals		
- Credit cards	278,194	330,921
- Mortgages	687,656	778,211
- Others	54,180	226,272
Loans and advances to corporate entities		
- Term loans	330,028	509,917
Gross advances to customers	1,350,058	1,845,321
Less: Impairment allowances		
- Collectively assessed	(6,026)	(12,100)
Other assets (Note 25)	297,475	18,046
Investments in securities included in the loans and receivables category (Note 20)	43,779	-
Advances and other accounts	1,685,286	1,851,267

**MEVAS Bank Limited**

**Notes to the Financial Statements**

(Expressed in thousands of Hong Kong dollars)

**19. Advances and other accounts (Continued)**

(b) Reconciliation of allowance account for losses on loans and advances to customers

	Impairment allowance - Collective assessment				Total
	Individual (retail customers)			Corporate entities	
	Credit cards	Mortgages	Others	Term loans	
<b>Movement in impairment allowances on loans and advances</b>					
Balance at 1 January 2008	6,157	289	2,160	-	8,606
Impairment losses charged / (reversed)	8,579	(259)	5,835	575	14,730
Loans written off as uncollectible	(11,542)	-	(6,030)	-	(17,572)
Recoveries of advances written off in previous years	1,338	-	4,998	-	6,336
<b>Balance at 31 December 2008</b>	<b>4,532</b>	<b>30</b>	<b>6,963</b>	<b>575</b>	<b>12,100</b>
<b>Balance at 1 January 2009</b>	<b>4,532</b>	<b>30</b>	<b>6,963</b>	<b>575</b>	<b>12,100</b>
Impairment losses charged / (reversed)	14,528	(21)	2,534	(330)	16,711
Loans written off as uncollectible	(17,144)	-	(9,787)	-	(26,931)
Recoveries of advances written off in previous years	1,399	-	3,854	-	5,253
Transfer of impairment losses upon disposal of personal loans and advance under cash cards	-	-	(1,107)	-	(1,107)
<b>Balance at 31 December 2009</b>	<b>3,315</b>	<b>9</b>	<b>2,457</b>	<b>245</b>	<b>6,026</b>

Loans and advances of the Bank are assessed for impairment on a collective basis. The Bank did not have any individually assessed impairment allowances as at 31 December 2009 and 2008.

**20. Investments in securities included in the loans and receivables category**

	2009	2008
Investments in securities classified as loan and receivables upon initial recognition	<b>43,779</b>	-

Investments in securities classified as loans and receivables upon initial recognition represented investments acquired from settlement arrangements with customers. They are unlisted and issued by corporate entities.

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

#### 21. Available-for-sale securities

	2009	2008
Debt securities:		
- unlisted	<u>900,244</u>	<u>325</u>
Equity securities:		
- listed in Hong Kong	109	118
- unlisted	<u>12,348</u>	<u>11,007</u>
	<u>12,457</u>	<u>11,125</u>
Total available-for-sale securities	<u>912,701</u>	<u>11,450</u>
Available-for-sale securities are analysed by categories of issuers as follows:		
- Central governments and central banks	899,919	-
- Corporate entities	12,707	11,375
- Others	75	75
	<u>912,701</u>	<u>11,450</u>

#### 22. Furniture and equipment

At 1 January 2008		
Cost		16,656
Accumulated depreciation		<u>(6,016)</u>
Net book amount		<u>10,640</u>
Year ended 31 December 2008		
Opening net book amount		10,640
Additions		656
Disposals		(1,314)
Depreciation charge (Note 10)		<u>(1,598)</u>
Closing net book amount		<u>8,384</u>
At 31 December 2008		
Cost		15,565
Accumulated depreciation		<u>(7,181)</u>
Net book amount		<u>8,384</u>
<b>Year ended 31 December 2009</b>		
Opening net book amount		8,384
Additions		224
Disposals		(102)
Depreciation charge (Note 10)		<u>(1,840)</u>
Closing net book amount		<u>6,666</u>
At 31 December 2009		
Cost		15,544
Accumulated depreciation		<u>(8,878)</u>
Net book amount		<u>6,666</u>

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

#### 23. Investment properties

	2009	2008
At 1 January	63,000	-
Additions	-	71,000
Fair value gains/(losses) on revaluation	13,000	(8,000)
At 31 December	<u>76,000</u>	<u>63,000</u>

The investment properties were last revalued at 31 December 2009. Valuations were made on the basis of open market value by independent, professionally qualified valuer Savills (Valuation and Professional Services) Limited.

The net book value of investment properties comprises:

	2009	2008
Leaseholds		
Held in Hong Kong on medium-term lease (between 10-50 years)	<u>76,000</u>	<u>63,000</u>

#### 24. Investment in a subsidiary

	2009	2008
Investments, at cost		
Unlisted shares	50	50
Amount due to a subsidiary	<u>(50)</u>	<u>(50)</u>
	<u>-</u>	<u>-</u>

The wholly-owned subsidiary at 31 December 2009 and 2008 is as follows:

Name of company	Principal activity	Place of incorporation	Particulars of issued ordinary shares
MEVAS (Nominees) Limited	Nominee services	Hong Kong	500 ordinary shares of HK\$100 each

#### 25. Other assets

	2009	2008
Accrued income	2,758	11,828
Receivable from DSB for the transfer of the credit card portfolio	272,522	-
Accounts receivable and prepayments	20,533	3,702
Others	1,662	2,516
	<u>297,475</u>	<u>18,046</u>

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

#### 26. Deposits from customers

	2009	2008
Demand deposits and current account	1,346,436	909,120
Savings deposits	253,237	113,516
Time, call and notice deposits	<u>2,014,387</u>	<u>4,724,658</u>
	<u>3,614,060</u>	<u>5,747,294</u>

#### 27. Deposits from customers designated at fair value through profit or loss

	2009	2008
Structured deposits	-	30,487
Other deposits from customers designated at fair value through profit or loss	<u>-</u>	<u>52,234</u>
	<u>-</u>	<u>82,721</u>

During 2008 and 2009, the Bank did not designate on initial recognition any deposits from customers at fair value through profit or loss.

At at 31 December 2008, the amount that the Bank would be contractually required to pay at maturity to the holders of these deposits is HK\$99,000 higher than the above carrying amount. However, there is no such difference in 2009, as the Bank holds no such deposits.

#### 28. Other accounts and accruals

	2009	2008
Accruals	6,634	25,163
Payable to DSB for the transfer of the credit card portfolio	272,522	-
Others	<u>56,803</u>	<u>58,200</u>
	<u>335,959</u>	<u>83,363</u>

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

#### 29. Deferred income tax

Deferred income tax assets and liabilities are netted when there is a legally enforceable right to offset current income tax assets against current income tax liabilities and when the deferred income taxes relate to the same fiscal authority. The netted amounts are as follows:

	2009	2008
Deferred income tax assets:		
- Deferred income tax assets to be recovered after more than 12 months	994	2,821
Deferred income tax liabilities:		
- Deferred income tax liabilities to be settled after more than 12 months	(1,413)	(974)
	<u>(419)</u>	<u>1,847</u>

The gross movement on the deferred income tax account is as follows:

	2009	2008
<b>At 1 January</b>	1,847	204
Tax (charged) / credited to the income statement (Note 15)	(2,003)	1,747
Tax charged to equity	(263)	(104)
<b>At 31 December</b>	<u>(419)</u>	<u>1,847</u>

The movement in deferred income tax assets and liabilities during the year, without taking into consideration the offsetting of balances within the same tax jurisdiction, is as follows:

#### Deferred income tax assets:

	Provisions
At 1 January 2008	1,506
Credited to income statement	<u>1,315</u>
<b>At 31 December 2008 and at 1 January 2009</b>	<b>2,821</b>
Charged to income statement	<u>(1,827)</u>
<b>At 31 December 2009</b>	<b><u>994</u></b>

**MEVAS Bank Limited****Notes to the Financial Statements**

(Expressed in thousands of Hong Kong dollars)

**29. Deferred income tax (Continued)****Deferred income tax liabilities:**

	<b>Accelerated tax depreciation</b>	<b>Investment revaluation</b>	<b>Total</b>
At 1 January 2008	1,302	-	1,302
Credited to income statement	(432)	-	(432)
Charged to equity	-	104	104
	<hr/>	<hr/>	<hr/>
<b>At 31 December 2008 and at 1 January 2009</b>	<b>870</b>	<b>104</b>	<b>974</b>
Charged to income statement	176	-	176
Charged to equity	-	263	263
	<hr/>	<hr/>	<hr/>
<b>At 31 December 2009</b>	<b>1,046</b>	<b>367</b>	<b>1,413</b>

**30. Balances with fellow subsidiaries**

Included in the following statement of financial position captions are balances with fellow subsidiaries detailed as follows:

	<b>2009</b>	2008
Cash and balances with banks	<b>250,622</b>	3,781,352
Financial assets designated at fair value through profit or loss	-	82,721
Advances and other accounts	<b>290,628</b>	5,940
Derivative financial instruments	<b>8</b>	1,344
	<hr/>	<hr/>
	<b>541,258</b>	<b>3,871,357</b>
	<hr/>	<hr/>
Deposits from banks	<b>161</b>	5
Deposits from customers	<b>202</b>	2,161
Other accounts and accruals	<b>3,002</b>	700
Derivative financial instruments	<b>77</b>	1,378
	<hr/>	<hr/>
	<b>3,442</b>	<b>4,244</b>
	<hr/>	<hr/>

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

#### 31. Contingent liabilities and commitments

##### (a) Credit commitments

The contract and credit risk weighted amounts of the Bank's off-balance sheet financial instruments that commit it to extend credit to customers are as follows:

	<b>Contract amount</b>	
	<b>2009</b>	<b>2008</b>
Direct credit substitutes	<b>269</b>	269
Commitments that are unconditionally cancellable without prior notice	<b>2,144,338</b>	2,265,225
Other commitments with an original maturity of: - under 1 year	<b>157,554</b>	178,333
	<b>2,302,161</b>	2,443,827

  

	<b>Credit risk weighted amount</b>	
	<b>2009</b>	<b>2008</b>
Contingent liabilities and commitments	<b>26,665</b>	29,478

##### (b) Operating lease commitments

Where the Bank is the lessee, the future minimum lease payments under non-cancellable building operating leases are as follows:

	<b>2009</b>	<b>2008</b>
No later than 1 year	<b>7,249</b>	7,178
Later than 1 year and no later than 5 years	<b>6,551</b>	2,946
	<b>13,800</b>	10,124

Where the Bank is the lessor, the future minimum lease payments under non-cancellable building operating leases are as follows:

	<b>2009</b>	<b>2008</b>
No later than 1 year	<b>3,600</b>	3,600
Later than 1 year and no later than 5 years	<b>1,551</b>	5,151
	<b>5,151</b>	8,751

#### 32. Share capital

	<b>2009</b>	<b>2008</b>
Authorised, issued and fully paid: 40,000,000 ordinary shares of HK\$10 each	<b>400,000</b>	400,000

**MEVAS Bank Limited****Notes to the Financial Statements**

(Expressed in thousands of Hong Kong dollars)

**33. Reserves**

	<b>Investment revaluation reserve</b>	<b>Retained earnings</b>	<b>Total</b>
At 1 January 2008	44	47,688	47,732
Fair value gains on available-for-sale securities	650	-	650
Disposal of available-for-sale securities	(62)	-	(62)
Deferred income tax liabilities recognised on movements in investment revaluation reserve	(104)	-	(104)
Profit for the year	-	2,985	2,985
2008 interim dividend	-	(30,000)	(30,000)
<b>At 31 December 2008 and at 1 January 2009</b>	<b>528</b>	<b>20,673</b>	<b>21,201</b>
Fair value gains on available-for-sale securities	<b>1,013</b>	-	<b>1,013</b>
Disposal of available-for-sale securities	<b>368</b>	-	<b>368</b>
Deferred income tax liabilities recognised on movements in investment revaluation reserve	<b>(263)</b>	-	<b>(263)</b>
Profit for the year	-	<b>7,141</b>	<b>7,141</b>
<b>At 31 December 2009</b>	<b>1,646</b>	<b>27,814</b>	<b>29,460</b>

Note: At 31 December 2009, a regulatory reserve amounting to HK\$18,343,000 (2008: HK\$12,714,000) has been earmarked in the retained earnings of the Bank. The regulatory reserve is maintained to satisfy the provisions of the Banking Ordinance for prudential supervision purposes. Movements in the regulatory reserve are made directly through retained earnings and in consultation with the HKMA.

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

#### 34. Notes to the statement of cash flows

(a) Reconciliation of profit before income tax to net cash flow (used in)/ from operating activities

	2009	2008
Operating (loss)/profit before gains or losses on certain investments and fixed assets	(35,697)	11,469
Net gain on disposal of available-for-sale securities	3,100	-
Net gain on transfer of credit card portfolio	27,000	-
Net interest income	(66,305)	(86,432)
Interest received	117,164	236,868
Interest paid	(59,929)	(144,510)
Impairment losses on loans and advances	16,711	14,730
Advances written off net of recoveries	(22,785)	(11,236)
Depreciation	1,840	1,598
	<u>(18,901)</u>	<u>22,487</u>
Operating (losses) / profits before changes in operating assets and liabilities		
Change in financial assets designated at fair value through profit or loss	82,721	163,228
Change in advances and other accounts	162,986	229,483
Change in available-for-sale securities	(900,238)	1,237
Change in deposits from banks	4,486	(23,002)
Change in derivative financial instruments	53	(1,161)
Change in deposits from customers	(2,133,234)	(367,193)
Change in deposits from customers designated at fair value through profit or loss	(82,721)	(262,450)
Change in other accounts and accruals	270,802	26,339
	<u>(2,614,046)</u>	<u>(211,032)</u>
Cash absorbed by operating activities		

(b) For the purposes of the statement of cash flows, cash and cash equivalents comprise the following balances with maturity of three months or less from the date of acquisition.

	2009	2008
Cash and balances with banks	124,097	83,094
Money at call and short notice	1,589,040	4,244,313
	<u>1,713,137</u>	<u>4,327,407</u>

#### 35. Loans to officers

Particulars of loans made to officers and disclosed pursuant to section 161B of the Hong Kong Companies Ordinance are as follows:

	<b>Balance outstanding at 31 December</b>	
	2009	2008
Aggregate amount outstanding in respect of principal and interest	<u>2</u>	<u>3</u>
	<b>Maximum balance during the year</b>	
	2009	2008
Aggregate amount outstanding in respect of principal and interest	<u>8</u>	<u>3</u>

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

#### 36. Related-party transactions

The Bank's immediate holding company is Dah Sing Banking Group Limited and the ultimate holding company is Dah Sing Financial Holdings Limited. Both holding companies are incorporated and listed in Hong Kong.

During 2009 and 2008, the Bank entered into various transactions with its fellow subsidiaries on normal commercial terms. These transactions include interbank placements and deposit taking, marketing and distribution of life and general insurance products and the provision of other banking services.

Details of the significant related party transactions are as follows:

(a) Transactions and balances with fellow subsidiaries

Various treasury, operational, administrative and other functions of the Bank are provided by DSB, a fellow subsidiary of the Bank. In addition, the property acquired from DSB in 2008 as shown in Note 23 has been leased back to DSB at market rate.

DSB is engaged by the Bank to perform loan administration and operation support and processing in respect of its participation in syndicated loans.

(i) Income and expense

	Fellow subsidiaries	
	2009	2008
Interest expense incurred	(6)	(44)
Interest income earned	16,584	115,649
Commission income	964	1,023
Service fee incurred	(15,005)	(15,908)
Rental income	3,600	2,050

(ii) Inter-company balances

Inter-company balances with fellow subsidiaries are shown under Note 30.

(iii) Derivative financial instruments - Outstanding notional principal at year-end

	Fellow subsidiaries	
	2009	2008
Foreign exchange forward contracts	25,514	4,686
Interest rate contracts	-	91,320

(iv) Transfer of personal loans and credit card advances of the Bank to DSB at a gain. These transactions and the key financial impacts are set out under Note 14.

## MEVAS Bank Limited

### Notes to the Financial Statements

(Expressed in thousands of Hong Kong dollars)

#### 36. Related-party transactions (Continued)

(b) Key management personnel

(i) Material transactions and balances with directors and key management personnel

During the year, the Bank had banking transactions with the directors and key management personnel of the Bank and its holding companies, including deposit taking, loans, credit card facilities and investment services. These transactions were provided in the ordinary course of business and on the same terms offered to other employees.

Income and expenses arising from the transactions with key management personnel are immaterial and the loans and deposits balances with them as at 31 December are shown below.

	2009	2008
Loans and advances	2	3
Deposits	<u>520</u>	<u>1,014</u>

(ii) Remuneration of key management personnel

Key management personnel of the Bank comprise only executive directors and information on their remuneration is described in Note 12 to the financial statements.

(c) Related companies

The Bank has no loans and advances balances and deposits balances with related companies controlled or significantly influenced by Bank's shareholders and directors as at 31 December 2009 and 31 December 2008.

## MEVAS Bank Limited

### Supplementary Financial Information

(Expressed in thousands of Hong Kong dollars)

The following information relates to the Bank and is disclosed as part of the accompanying information to the financial statements and does not form part of the audited financial statements.

#### 1. Capital adequacy ratios

	As at 31 Dec 2009	As at 31 Dec 2008
Capital adequacy ratio		
- Core	23.9%	16.0%
- Overall	25.2%	17.0%

The capital adequacy ratio of the Bank is computed on Basel II basis with reference to the Banking (Capital) Rules. This capital adequacy ratio takes into account operational risk.

The Bank has been exempted by the Hong Kong Monetary Authority ("HKMA") to maintain capital against market risk as it met all the relevant criteria specified in the Banking (Capital) Rules.

The capital base after deductions used in the calculation of the above capital adequacy ratio as at 31 December and reported to the HKMA is analysed as follows:

	As at 31 Dec 2009	As at 31 Dec 2008
Core capital:		
Paid up ordinary share capital	400,000	400,000
Reserves	10,330	34,974
Profit and loss account	(5,859)	(27,015)
Less: net deferred tax assets	-	(1,847)
	404,471	406,112
Less: 50% of total amount of deductible items	(150)	(150)
Core capital	404,321	405,962
Supplementary capital:		
Reserves attributable to fair value gains on revaluation of holdings of available-for-sale equities and debt securities	741	237
Regulatory reserve	18,343	12,714
Collective impairment allowances for impaired assets	6,026	12,100
	25,110	25,051
Eligible amount of supplementary capital	21,941	25,051
Less: 50% of total amount of deductible items	(150)	(150)
Supplementary capital	21,791	24,901
Total capital base	426,112	430,863

In calculating its capital adequacy ratio, the Bank has deducted the cost of investment in the subsidiary, MEVAS Nominees Limited, which is a "regulated financial entity" as defined by the Banking (Capital) Rules, from its capital base.

Consolidated financial statements have not been prepared as the Bank is a wholly owned subsidiary of another body corporate, Dah Sing Banking Group Limited.

## MEVAS Bank Limited

### Supplementary Financial Information

(Expressed in thousands of Hong Kong dollars)

#### 2. Liquidity ratio

	2009	2008
Liquidity ratio	<u>106.8%</u>	<u>105.2%</u>

The liquidity ratio is calculated as the simple average of each calendar month's average liquidity ratio of the Bank for the twelve months of the financial year. The liquidity ratio is computed with reference to the methods set out in the Fourth Schedule of the Hong Kong Banking Ordinance.

#### 3. Currency concentrations

The following sets out the Bank's net foreign exchange position in USD and other individual currency that constitute more than 10% of the total net position in all foreign currencies as at 31 December 2009 and the corresponding comparative balances.

	As at 31 December 2009			
	USD	CNY	AUD	NZD
Equivalent in HK\$'000				
Spot assets	597,399	56,658	146,211	147,719
Spot liabilities	(584,378)	(55,165)	(140,942)	(145,567)
Forward purchases	6,204	-	408	46
Forward sales	(6,486)	-	(5,679)	(2,473)
<b>Net long / (short) position</b>	<b><u>12,739</u></b>	<b><u>1,493</u></b>	<b><u>(2)</u></b>	<b><u>(275)</u></b>
	As at 31 December 2008			
	USD	CNY	AUD	NZD
Equivalent in HK\$'000				
Spot assets	1,215,557	56,135	123,958	131,840
Spot liabilities	(1,222,321)	(54,473)	(124,642)	(132,758)
Forward purchases	2,682	-	175	319
Forward sales	(744)	(1,023)	(142)	(136)
<b>Net (short) / long position</b>	<b><u>(4,826)</u></b>	<b><u>639</u></b>	<b><u>(651)</u></b>	<b><u>(735)</u></b>

## MEVAS Bank Limited

### Supplementary Financial Information

(Expressed in thousands of Hong Kong dollars)

#### 4. Loans and advances to customers

- (a) Gross advances to customers by industry sector classified according to the usage of loans and analysed by percentage covered by collateral

	As at 31 Dec 2009		As at 31 Dec 2008	
	Outstanding balance	% of gross advances covered by collateral	Outstanding balance	% of gross advances covered by collateral
Loans for use in Hong Kong				
Industrial, commercial and financial				
- Property investment	74,479	100.0	81,270	100.0
- Financial concerns	66,450	-	30,303	-
- Stockbrokers	-	-	4,400	-
- Manufacturing	-	-	26,641	-
- Transport and transport equipment	44,429	100.0	89,454	58.2
- Recreational activities	8,088	-	-	-
	<b>193,446</b>	<b>61.5</b>	<b>232,068</b>	<b>57.4</b>
Individuals				
- Loans for the purchase of flats in Home Ownership Scheme, Private Sector Participation Scheme and Tenants Purchase Scheme	23,796	100.0	25,820	99.9
- Loans for the purchase of other residential properties	445,417	100.0	535,716	99.8
- Credit card advances (Note 1)	278,194	-	330,921	-
- Others	198,144	73.1	361,678	37.9
	<b>945,551</b>	<b>64.9</b>	<b>1,254,135</b>	<b>55.6</b>
Loans for use in Hong Kong	<b>1,138,997</b>	<b>64.3</b>	<b>1,486,203</b>	<b>55.9</b>
Loans for use outside Hong Kong (Note 2)	<b>211,061</b>	<b>38.9</b>	<b>359,118</b>	<b>35.9</b>
	<b>1,350,058</b>	<b>60.4</b>	<b>1,845,321</b>	<b>52.0</b>

#### Note 1:

While the Bank had entered into a sale and purchase agreement with DSB on 31 December 2009 to transfer the economic benefits and risks in respect of the whole credit card portfolio owned by the Bank to DSB, the card customer relationship and account balances were not yet transferred as at 31 December 2009, and the outstanding balance of credit card advance receivable by the Bank is stated as part of the Bank's gross advances as at 31 December 2009.

#### Note 2:

Loans for use outside Hong Kong include loans extended to customers located in Hong Kong with the finance used outside Hong Kong.

**MEVAS Bank Limited****Supplementary Financial Information**

(Expressed in thousands of Hong Kong dollars)

**4. Loans and advances to customers (Continued)**

- (a) Gross advances to customers by industry sector classified according to the usage of loans and analysed by percentage covered by collateral (Continued)

For each industry sector reported above with loan balance constituting 10% or more of the total balance of advances to customers, the attributable amount of overdue loans and collectively assessed loan impairment allowances are as follows:

	<b>As at 31 Dec 2009</b>		
	<b>Outstanding balance</b>	<b>Gross advances overdue for over 3 months</b>	<b>Collectively assessed impairment allowances</b>
Loans for use in Hong Kong			
Individuals			
- Loans for the purchase of other residential properties	445,417	-	6
- Credit card advances	278,194	954	3,315
		<b>As at 31 Dec 2008</b>	
	<b>Outstanding balance</b>	<b>Gross advances overdue for over 3 months</b>	<b>Collectively assessed impairment allowances</b>
Loans for use in Hong Kong			
Individuals			
- Loans for the purchase of other residential properties	535,716	-	21
- Credit card advances	330,921	1,253	4,532

**MEVAS Bank Limited**

**Supplementary Financial Information**

(Expressed in thousands of Hong Kong dollars)

**4. Loans and advances to customers (Continued)**

- (a) Gross advances to customers by industry sector classified according to the usage of loans and analysed by percentage covered by collateral (Continued)

The amount of new allowances charged to income statement and advances written off during the year were disclosed in the tables below.

	<b>2009</b>		
	<b>(Allowances written back) / New provisions</b>	<b>Loans written off as uncollectible</b>	<b>Recoveries of advances written off in previous years</b>
<b>Loans for use in Hong Kong</b>			
Individuals			
- Loans for the purchase of other residential properties	(15)	-	-
- Credit card advances	<u>14,528</u>	<u>(17,144)</u>	<u>1,399</u>
	<u>14,513</u>	<u>(17,144)</u>	<u>1,399</u>
	<b>2008</b>		
	<b>(Allowances written back) / New provision</b>	<b>Loans written off as uncollectible</b>	<b>Recoveries of advances written off in previous years</b>
<b>Loans for use in Hong Kong</b>			
Individuals			
- Loans for the purchase of other residential properties	(198)	-	-
- Credit card advances	<u>8,579</u>	<u>(11,542)</u>	<u>1,338</u>
	<u>8,381</u>	<u>(11,542)</u>	<u>1,338</u>

**MEVAS Bank Limited**

**Supplementary Financial Information**

(Expressed in thousands of Hong Kong dollars)

**4. Loans and advances to customers (Continued)**

(b) Non-bank Mainland exposures

<b>As at 31 Dec 2009</b>			
Type of counterparties	<b>On-balance sheet exposure</b>	<b>Off-balance sheet exposure</b>	<b>Total</b>
Mainland entities	187,481	-	187,481
Companies and individuals outside Mainland where the credits are granted for use in the Mainland	<u>14,684</u>	<u>-</u>	<u>14,684</u>
<b>As at 31 Dec 2008</b>			
Type of counterparties	<b>On-balance sheet exposure</b>	<b>Off-balance sheet exposure</b>	<b>Total</b>
Mainland entities	217,274	-	217,274
Companies and individuals outside Mainland where the credits are granted for use in the Mainland	<u>104,186</u>	<u>-</u>	<u>104,186</u>

Note: The balances of exposures reported above include gross advances and other balances of claims on the customers.

(c) Analysis of gross advances to customers and overdue loans by geographical area

	<b>As at 31 Dec 2009</b>	<b>As at 31 Dec 2008</b>
Gross advances to customers		
- Hong Kong	1,154,964	1,504,420
- China	75,000	75,000
- Macau	82,215	90,244
- Others	<u>37,879</u>	<u>175,657</u>
	<u>1,350,058</u>	<u>1,845,321</u>
Gross advances overdue for over 3 months		
- Hong Kong	<u>1,071</u>	<u>1,782</u>

Advances to customers by geographical area are classified according to the location of the counterparties after taking into account the transfer of risk. In general, risk transfer applies when an advance is guaranteed by a party located in an area which is different from that of the counterparty.

## MEVAS Bank Limited

### Supplementary Financial Information

(Expressed in thousands of Hong Kong dollars)

#### 5. Capital charge for credit, market and operational risks

The capital adequacy ratio of the Bank as at 31 December 2009 disclosed in Note 1 above is computed on Basel II basis with reference to the methods set out in the Banking (Capital) Rules.

The capital charge for each class of exposures are summarised as follows.

(a) Capital charge for credit risk

	2009	2008
Sovereign exposures	-	-
Public Sector Entity exposures	660	574
Multilateral Development Bank exposures	-	-
Bank exposures	31,682	72,296
Securities firm exposures	-	-
Corporate exposures	26,329	42,112
Collective investment schemes exposures	-	-
Cash items	-	-
Regulatory retail exposures	21,264	34,973
Residential mortgage loans	22,527	24,522
Other exposures which are not past due exposures	8,399	7,273
Past due exposures	5,382	216
Total capital charge for on-balance sheet exposures	<u>116,243</u>	<u>181,966</u>
Direct credit substitutes	21	21
Other commitments	2,112	2,337
Exchange rate contracts	-	-
Interest rate contracts	-	208
Total capital charge for off-balance sheet exposures	<u>2,133</u>	<u>2,566</u>
Total capital charge for credit risk	<u>118,376</u>	<u>184,532</u>

This disclosure is made by multiplying the Bank's risk-weighted amount derived from the relevant calculation approach by 8%, not the Bank's actual "regulatory capital".

(b) Operational risk capital charge

The Bank uses the Basic Indicator Approach for calculating operational risk.

	2009	2008
Capital charge for operational risk	<u>17,306</u>	<u>17,910</u>

## MEVAS Bank Limited

### Supplementary Financial Information

(Expressed in thousands of Hong Kong dollars)

#### 6. Corporate governance

Corporate governance is concerned with how companies are managed and controlled, and in particular the role and operation of the Board of Directors in sustaining sound business integrity and practices, and effective accountability.

##### (a) Statement of Compliance

The Bank has fully complied with the requirements set out in the Supervisory Policy Manual entitled "Corporate Governance of Locally Incorporated Authorized Institutions" issued by the HKMA.

##### (b) The Board

As at 31 December 2009, the Board comprised an executive Chairman, six executive directors including the Chief Executive, and four non-executive directors. The Board meets at least quarterly. Its principal roles include the formulation and approval of corporate and business strategy, review of operations and financial performance, approval of key policies and annual business plan, and ensuring the maintenance of sound risk management and regulatory compliance.

Executive directors are appointed to the Board based on their experience, specialist skill and knowledge of different businesses of the Bank. Non-executive directors bring to the Board their knowledge and experience of other markets and industries, guide executive management's strategy development and policy implementation, and provide valuable external perspectives in the Board's deliberations.

##### (c) Board and Specialised Committees

###### (i) Audit Committee

The Banking Group Audit Committee, established by the Board of Dah Sing Banking Group Limited ("DSBG" or the "Group"), has the authority to review all matters related to the financial statements and disclosures, audit work performed by internal and external auditors, internal control systems, and the effectiveness of risk management and compliance for the whole Group including the Bank. The Committee reports to the Board of DSBG and of the Bank its observations and comments on any issue that needs to be brought to the attention of the Board, and makes recommendation to the Board regarding financial statements and results announcements.

Three independent non-executive directors of DSBG comprise the Group Audit Committee, which meets at least three times a year with the Group's and the Bank's senior management, the head of internal audit and the external auditors. The Chairman of the Committee is an independent non-executive director with a very high level of financial and audit experience.

The head of internal audit of the Group reports functionally to the Audit Committee. External auditors have direct access to the Committee for expressing their views and comments on any matter or concern relating to the Group or the Bank.

###### (ii) Executive Committee

The Executive Committee is chaired by the Chairman of the Group. Members include the Chief Executive of the Bank and the Alternate Chief Executives of the Bank, the Group's Finance Director, and Head of Group Risk. It is responsible for developing and setting the strategy and objectives of the Bank. It provides direction and guidance to business divisions, reviews business performance, ensures effective internal control systems, allocates resources, prioritises business initiatives and investment, and is delegated with the authority of the Board to exercise the authority and power of the Board on matters relating to the normal course of business of the Bank.

The Executive Committee can call upon other directors or members of senior management for advice or participation in its discussion as it deems appropriate.

## MEVAS Bank Limited

### Supplementary Financial Information

(Expressed in thousands of Hong Kong dollars)

#### 6. Corporate governance (Continued)

##### (c) Board and Specialised Committees (Continued)

##### (iii) Asset and Liability Management Committee

The Banking Group Asset and Liability Management Committee (“ALCO”) is accountable to the Banking Group Executive Committee, and oversees the overall management of the statement of financial position, liquidity, funding, interest rate risk and market risk of the Group and of the Bank. It is responsible for formulating business plans affecting lending business, loan mix, treasury investments, deposit taking and capital management. It also plays a key role in the overall risk governance and management of the Group and the Bank.

ALCO meets every week and its regular tasks include the review of key business emphasis and development, loan and deposit changes, funding requirement, liquidity, surplus funds investments, capital market dealing, and review of market changes and competition. ALCO also conducts a regular monthly review of overall statement of financial position and business performance, including trend analysis and actual positions against limits and targets.

ALCO is chaired by the Group Chief Executive. Members of the Committee include all executive directors of the Bank, heads of most business divisions, risk management and financial control.

##### (iv) Credit Committee

The Group’s Joint Retail Credit Committee consists of the relevant executive directors, Head of Group Risk, senior business, credit and risk officers of the Group which include the Chief Executive of the Bank, and is chaired by the Chief Executive of the Group. The Committee has the responsibility for formulating and revising credit policies and procedures for the Bank, approving credits which exceed individual credit officer’s credit authority, and reviewing credit performance and loan provisioning. Credit policies and procedures define the credit extension criteria and guidelines, credit approval, review and monitoring process and the systems of loan classification and provisioning.

The Bank’s commercial banking activities (mainly in the form of syndicated lending) are conducted, controlled and monitored in accordance with the commercial banking credit policy and procedure of Dah Sing Bank, Limited (“DSB”). The Bank has outsourced the credit administration, credit review and control of its commercial lending portfolio to DSB and its commercial banking credit committee.

##### (v) Compliance Committee

The Banking Group Compliance Committee is responsible for overseeing and guiding the development, maintenance and enhancement of compliance system, policies and practices to ensure compliance with all statutory requirements and regulatory guidelines. The Committee serves to uphold a high level of awareness and accountability for compliance requirements. The Banking Group has adopted an ongoing compliance control and monitoring process within business and support functions to enhance compliance control.

Members of the Compliance Committee include the Group Chief Executive, the Head of Legal and Compliance, a number of executive directors and senior operation and risk control executives of the Group. Minutes of the Committee meetings and regular reports are submitted to the Banking Group Audit Committee.

## **MEVAS Bank Limited**

### **Supplementary Financial Information**

(Expressed in thousands of Hong Kong dollars)

#### **6. Corporate governance (Continued)**

(c) Board and Specialised Committees (Continued)

(vi) IT Steering Committee

The Group IT Steering Committee is responsible for providing IT strategic direction, ensuring sound and robust IT infrastructure and processes to support the Group's businesses. It is also responsible for ensuring that IT risk control, information security and operations continuity are managed effectively, and for overseeing the Group's IT resources allocation, project justification and prioritisation.

The Committee is chaired by the Group Chief Executive and includes most division heads of the Group, including the Chief Executive of the Bank, as its members.

(vii) Human Resources Committee

The Group Human Resources Committee is responsible for setting the overall human resources direction of the Group and guiding the development of people strategy, policy and practices. It is responsible for overseeing corporate culture development, planning and implementation, remuneration programs and changes, staff development plans, employee relations projects and human resources systems.

The Committee is chaired by the Group Chief Executive. Members comprise the Chairman of the Group and a number of division heads.

#### **7. Risk management**

The Bank recognises the changing nature of risk and manages it through a well-developed management structure.

Risk management is focused on the five major areas of risk – credit risk, market risk, interest rate risk, liquidity risk and operational risk. Credit risk occurs mainly in the Bank's credit portfolios comprising primarily retail secured and unsecured lending.

Market risk arises mainly in Treasury and is associated principally with the Bank's on-balance sheet positions in the trading book, and off-balance sheet trading positions including position taken to hedge elements of the trading book.

Interest rate risk means the risk to the Bank's financial condition resulting from adverse movements in interest rates.

Liquidity risk arises across the Bank's statement of financial position.

Operational risk is the risk of loss (direct or indirect) resulting from inadequate or failed internal processes, people and systems or from external events.

## **MEVAS Bank Limited**

### **Supplementary Financial Information**

(Expressed in thousands of Hong Kong dollars)

#### **7. Risk management (Continued)**

Apart from the description of financial risk management disclosed in Note 3 to the financial statements, the other risk management aspects are disclosed below:

(a) The risk management structure of the Bank

The Board of Directors has the broad overall responsibility for the management of all types of risk. The responsibilities of the Board in relation to risk control are:

- the approval of the overall strategy and policies to ensure that credit and other risks are properly managed at both the transaction and portfolio levels;
- the management of risk, both financial and non-financial, conducted through operational and administrative control systems including the operation of the Group Audit Committee; review of key results (against forecasts), operational statistics and policy compliance; and
- financial performance by analysis against approved budgets and analysis of variations in key non-financial measures.

The Executive Committee has been delegated the authority to oversee and guide the management of different risks which are more particularly managed and dealt with by Group Risk Division and different functional committees.

(b) Group risk function

The independent Group Risk function is responsible for ensuring that policies and mandates are established for the Group as a whole. Group Risk Division monitors and reports Group risk positions to the Board via the Executive Committee, sets standards for financial risks and data integrity and ensures that the financial risks are fully considered in the product planning and pricing process. Group Risk Division reviews and approves all credit and risk exposure policies for the Bank including the approval of exposures to new markets, economic sectors, organisations, credit products and financial instruments which expose the Bank to credit and related risks. In determining credit and risk policies, Group Risk Division takes into account the guidelines established by the HKMA, business direction and risk adjusted performance of each business. The Group Risk director is a member of the Group's Joint Retail Credit Committee and an executive director of the Bank.

The Bank's risk management expertise continues to advance the overall quality of the Bank's lending portfolios, and enables the Bank to meet the changing regulatory requirements and enter into credit exposures with the confidence that it understands the associated risks and rewards.

The Bank is continuing to evolve its risk management capabilities under the aegis of the Head of Group Risk Division, increasing the focus of its risk strategy on risk and reward and returns on capital. The Bank uses a range of risk measurement and analytical tools in its management of the various risks which it faces in its day-to-day businesses and these are continually being enhanced and upgraded to reflect the ever-changing business needs and the requirements of the regulators.

## MEVAS Bank Limited

### Supplementary Financial Information

(Expressed in thousands of Hong Kong dollars)

#### 7. Risk management (Continued)

(c) Credit risk

(i) Credit risk exposures

Standard & Poor's Ratings Services ("Standard & Poor's"), Moody's Investors Services ("Moody's") and Fitch Ratings are the external credit assessment institutions ("ECAIs") that the Bank uses for the assessment of its credit risk exposures to banks, sovereigns, public sector entities, and collective investment schemes as well as securitisation exposures and exposures to corporates that do not qualify as regulatory retail exposures.

The process the Bank uses to map ECAI issuer ratings to exposures booked in its banking book follows the process prescribed in Part 4 of the Banking (Capital) Rules.

2009 Class of exposures	Exposures after recognised credit risk mitigation		Risk-weighted amounts				Total exposure covered by recognised collateral	Total exposure covered by recognised guarantees or recognised credit derivative contracts
	Total Exposures (Note 1)	Rated (Note 2)	Unrated (Note 3)	Rated (Note 2)	Unrated (Note 3)	Total risk- weighted amounts		
<b>A. On-balance sheet</b>								
1. Sovereign	904,510	904,510	-	-	-	-	-	-
2. Public Sector Entity	8,088	41,247	-	8,249	-	8,249	-	-
3. Bank	1,980,094	1,980,094	-	396,019	-	396,019	-	-
4. Corporate	329,109	-	329,109	-	329,109	329,109	-	-
5. Cash items	18,073	-	18,073	-	-	-	-	-
6. Regulatory retail	354,400	-	354,400	-	265,800	265,800	-	-
7. Residential mortgage loans	660,202	-	627,043	-	281,587	281,587	-	33,159
8. Other exposures which are not past due exposures	104,991	-	104,991	-	104,991	104,991	-	-
9. Past due exposures	44,850	-	44,850	-	67,275	67,275	-	-
<b>B. Off-balance sheet</b>								
1. Off-balance sheet exposures other than OTC derivative transactions or credit derivative contracts	31,780	6,382	25,398	1,276	25,389	26,665	-	-
2. OTC derivative transactions	-	-	-	-	-	-	-	-
3. Credit derivative contracts	-	-	-	-	-	-	-	-
Exposures deducted from capital base	300							

## MEVAS Bank Limited

### Supplementary Financial Information (Expressed in thousands of Hong Kong dollars)

#### 7. Risk management (Continued)

##### (c) Credit risk (Continued)

##### (i) Credit risk exposures (Continued)

2008 Class of exposures	Exposures after recognised credit risk mitigation			Risk-weighted amounts			Total exposure covered by recognised collateral	Total exposure covered by recognised guarantees or recognised credit derivative contracts
	Total Exposures (Note 1)	Rated (Note 2)	Unrated (Note 3)	Rated (Note 2)	Unrated (Note 3)	Total risk- weighted amounts		
A. On-balance sheet								
1. Sovereign	2,817	2,817	-	-	-	-	-	-
2. Public Sector Entity	-	35,860	-	7,172	-	-	-	-
3. Bank	4,393,468	4,393,468	-	903,702	-	903,702	-	-
4. Corporate	526,402	-	526,402	-	526,402	526,402	-	-
5. Cash items	19,701	-	21,013	-	-	-	-	-
6. Regulatory retail	584,190	-	582,878	-	437,159	437,159	1,312	-
7. Residential mortgage loans	739,393	-	703,533	-	306,524	306,524	-	35,860
8. Other exposures which are not past due exposures	90,911	-	90,911	-	90,911	90,911	-	-
9. Past due exposures	1,803	-	1,803	-	2,705	2,705	-	-
B. Off-balance sheet								
1. Off-balance sheet exposures other than OTC derivative transactions or credit derivative contracts	35,936	8,000	27,936	1,600	27,878	29,478	-	-
2. OTC derivative transactions	3,377	1,561	1,816	780	1,816	2,596	-	-
3. Credit derivative contracts	-	-	-	-	-	-	-	-
Exposures deducted from capital base	2,147							

#### Note

- (1) principal amount or credit equivalent amount, as applicable, net of individually assessed impairment allowances
- (2) including exposures with ECAI issue-specific rating and exposures which have an inferred rating (i.e. exposures which do not have an issue-specific rating but whose risk-weights are determined under the Capital Rules by reference to an ECAI issuer rating assigned to the obligor of the exposure or to an ECAI issue rating of any other exposures of the obligor).
- (3) exposures which do not have ECAI issue-specific rating, nor inferred rating.

## MEVAS Bank Limited

### Supplementary Financial Information

(Expressed in thousands of Hong Kong dollars)

#### 7. Risk management (Continued)

(c) Credit risk (Continued)

(ii) Counterparty credit risk exposures

The Bank exercises strict control limits in tenor and outstanding amounts on net open positions arising from over-the-counter ("OTC") derivative transactions booked in its banking book. The credit risk exposures associated with these contracts are predominantly their fair values (i.e. the positive marked-to-market values favourable to the Bank). These credit risk exposures together with potential exposures from market movements are managed as part of the overall lending limits allowed to counterparties. Collateral or other security is generally not obtained for such credit risk exposures.

Settlement risk arises in situations where a payment in cash or a delivery of securities or equities is made in expectation of a corresponding receipt in cash, securities or equities. To mitigate settlement risk, daily settlement limits are established for each counterparty on the aggregate of all settlements on any day. The Bank will also enter into netting arrangements and make settlement on the basis of delivery against payment as appropriate.

The following table summarises the Bank's main credit exposures arising from OTC derivative transactions.

	2009	2008
<b>OTC derivative transactions:</b>		
Gross total positive fair value	-	2,719
Credit equivalent amounts	-	3,377
	<u>          </u>	<u>          </u>
Risk weighted amounts	-	2,596
	<u>          </u>	<u>          </u>

An analysis of the credit equivalent amounts or net credit exposures, and the risk-weighted amount is summarised as follows.

	2009	2008
<b>OTC derivative transactions:</b>		
Notional amounts:		
- Banks	-	45,660
- Others	-	91,320
	<u>          </u>	<u>          </u>
	-	136,980
Credit equivalent amounts:		
- Banks	-	1,561
- Others	-	1,816
	<u>          </u>	<u>          </u>
	-	3,377
Risk-weighted amounts:		
- Banks	-	780
- Others	-	1,816
	<u>          </u>	<u>          </u>
	-	2,596
	<u>          </u>	<u>          </u>

## MEVAS Bank Limited

### Supplementary Financial Information

(Expressed in thousands of Hong Kong dollars)

#### 7. Risk management (Continued)

(c) Credit risk (Continued)

(iii) Credit risk mitigation

The credit risk mitigation techniques used by the Bank are generally those recognised by the Banking (Capital) Rules for reduced capital weighting. Common types of collateral obtained are cash deposits and real estate properties. For certain types of advances to customers, the Bank also places reliance on guarantees issued by governments, public sector entities and corporates with acceptable credit rating.

The value of all real estate properties taken as collateral is appraised prior to the inception of the loans. For property collateral supporting problem accounts, their open market values are appraised at least every six months. For property collateral that has been repossessed, the Bank's policy is to arrange for realisation as soon as practicable.

(d) Market risk

The Bank is exposed to various types of market risk. Details of the risk management policies and procedures adopted are set out in Note 3.3 to the financial statements.

(e) Equity exposures in banking book

The Bank distinguishes its equity holdings between those taken for strategic reasons and those taken for capital appreciation purposes at inception of the acquisition. Equity holdings identified for capital appreciation purpose is evaluated based on rigorous investment analysis and is subject to internal guidelines on stock selection, marketability, valuation, position limit, management action trigger, and various other control guidelines specified in the Treasury Policy Manual. Equity holdings are valued on the basis of bid market prices.

	2009	2008
Realised (loss)/gains from sales and redemption	<b>(368)</b>	546
Unrealised revaluation gains		
- Amount included in reserves but not through income statement	<b>1,709</b>	528
- Amount deducted from supplementary capital	<b>769</b>	237

(f) Interest rate risk exposures in banking book

	Currency		Total
	HK\$	US\$	
<b>2009</b>			
Interest rate risk shock +200 basis points			
- Increase in earnings	<b>8,000</b>	-	<b>8,000</b>
<b>2008</b>			
Interest rate risk shock +200 basis points			
- Increase in earnings	10,000	1,000	11,000

## **MEVAS Bank Limited**

### **Supplementary Financial Information**

(Expressed in thousands of Hong Kong dollars)

#### **7. Risk management (Continued)**

##### **(g) Operational risk**

The Bank manages its operational risk through a management structure comprising members of senior management and operational risk officers from each business and support function, and operating through a set of operational risk policies, risk tool-kits, operational risk incident reporting and tracking system, and control self assessment and key risk indicator tools. Together with a well established internal control systems, operational risk in most situations can be adequately identified, assessed, monitored and mitigated. To allow the operational risk framework to be clearly communicated to all levels within the Bank, awareness and training programs are conducted from time to time.

To minimise the impact on the Bank's business in the event of system failure or disasters, back-up sites and operational recovery policies and plans have been established and tested for all critical business and operations functions.

Operational risk framework is also supported by periodic independent reviews of internal control systems by external and internal auditors. Reporting and assessment of the performance of operational risk management are monitored by the Group Risk and reported to the Group's Risk Management Committee.

##### **(h) Reputation risk**

Reputation risk is the risk arising from the potential that negative publicity regarding the Bank's business practices, operational errors or operating performance, whether true or not, could cause customer concerns or negative view, decline in the customer base or market share, or lead to costly litigation or revenue reductions.

The Bank manages reputation risk through upholding a high standard of corporate governance and management oversight, maintenance of effective policies and procedures with emphasis on internal control, risk management and compliance; proper staff training and supervision; proper handling of customer complaints or dissatisfaction; and adherence to sound business practices. Standards are set and policies and procedures are established by the Bank in all areas, which operate to reduce vulnerability to reputation risk.

##### **(i) Strategic risk**

Strategic risk generally refers to the corporate risk that may bring significant immediate or future negative impact on the financial and market positions of the Bank because of poor strategic decisions, unacceptable financial performance, improper implementation of strategies and lack of effective response to the market changes.

The Board of Directors, assisted by senior management, is directly responsible for the management of strategic risk. Directors formulate the strategic goals and key direction of the Bank, ensure business strategies are developed to achieve these goals, oversee the strategic development and implementation to secure compatibility with the Bank's strategic goals, review business performance, deploy proper resources to achieve the Bank's objectives, and authorise management to take appropriate actions to mitigate risks.

## **MEVAS Bank Limited**

### **Supplementary Financial Information**

(Expressed in thousands of Hong Kong dollars)

#### **7. Risk management (Continued)**

##### **(j) Implementation of the Basel II Capital Accord**

The revised capital adequacy framework known as Basel II has come into force for all locally incorporated authorized institutions in Hong Kong from January 2007. To implement Basel II, the HKMA published the final Banking (Capital) Rules and Banking (Disclosure) Rules at the end of 2006.

Basel II is structured around three "Pillars". Pillar 1 sets out the minimum capital requirements for a bank's operational risk, in addition to revising the "Basel I" treatment of credit risk and market risk. Pillar 2 requires that banks should have in place sound internal processes to assess the adequacy of their capital, based on a thorough assessment of their risks including those risks not covered under Pillar 1, and that supervisors should carry out supervisory review of this process. Pillar 3 complements Pillar 1 and Pillar 2 through enhanced market transparency and market discipline by requiring banks to make public disclosure of information on their risk profiles, capital adequacy and risk management.

Starting January 2007, the Bank adopts the standardised approach for credit risk, and the basic indicator approach for operational risk. These are the default approaches as specified in the Banking (Capital) Rules. Accordingly, the Bank has overhauled its systems and controls in order to meet the standards required for these approaches.

##### **(k) The role of Internal Audit**

The Banking Group's Internal Audit Division is an independent, objective assurance and consulting unit which is designed to focus on enhancing and sustaining sound internal control in all business and operational units of the Banking Group including the Bank. The Division reports functionally to the Banking Group Audit Committee, which is chaired by an Independent Non-Executive Director. The Division conducts a wide variety of internal control activities such as compliance audits and operations and systems reviews to ensure the integrity, efficiency and effectiveness of the systems of control of the Bank.

**Independent Auditor's Report**  
**To the shareholders of MEVAS Bank Limited**  
(incorporated in Hong Kong with limited liability)

We have audited the financial statements of MEVAS Bank Limited (the "Bank") set out on pages 4 to 75 which comprise the statement of financial position as at 31 December 2009, and the income statement, the statement of comprehensive income, the statement of changes in equity and the statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory notes.

**Directors' responsibility for the financial statements**

The directors of the Bank are responsible for the preparation and the true and fair presentation of these financial statements in accordance with Hong Kong Financial Reporting Standards issued by the Hong Kong Institute of Certified Public Accountants, and the Hong Kong Companies Ordinance. This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and the true and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

**Auditor's responsibility**

Our responsibility is to express an opinion on these financial statements based on our audit and to report our opinion solely to you, as a body, in accordance with section 141 of the Hong Kong Companies Ordinance and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

We conducted our audit in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance as to whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and true and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

**Opinion**

In our opinion, the financial statements give a true and fair view of the state of affairs of the Bank as at 31 December 2009 and of its profit and cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards and have been properly prepared in accordance with the Hong Kong Companies Ordinance.

**PricewaterhouseCoopers**  
Certified Public Accountants

Hong Kong, 22 March 2010