

# Report of the Auditors



## To the members

### Paliburg Holdings Limited

(Incorporated in Bermuda with limited liability)

We have audited the financial statements on pages 68 to 147 which have been prepared in accordance with accounting principles generally accepted in Hong Kong.

### Respective responsibilities of Directors and auditors

The Company's Directors are responsible for the preparation of financial statements which give a true and fair view. In preparing financial statements which give a true and fair view, it is fundamental that appropriate accounting policies are selected and applied consistently. It is our responsibility to form an independent opinion, based on our audit, on those statements and to report our opinion to you.

### Basis of opinion

We conducted our audit in accordance with Statements of Auditing Standards issued by the Hong Kong Society of Accountants. An audit includes an examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the Directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Company's and the Group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance as to whether the financial statements are free from material misstatement. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements. We believe that our audit provides a reasonable basis for our opinion.

### Fundamental uncertainty - Provisions against investments in two investee companies

In forming our opinion, we have considered the adequacy of the disclosures made in note 20 to the financial statements concerning the outcome of the negotiations with the relevant government authorities in the People's Republic of China in respect of the resumption of a land site beneficially and collectively held by two investee companies (the "Investee Companies") during 2000. The carrying value of the Group's investments in the Investee Companies amounted to HK\$118.9 million (2000 - HK\$298.9 million) as at 31st December, 2001 which is included in long term investments under non-current assets. As further explained in note 20 to the financial statements, the Directors are currently unable to determine with reasonable certainty the outcome of the negotiations for the reversion of the land site to the Investee Companies. Accordingly, it is not possible to determine at this stage as to whether any further provision against the Group's investments in the Investee Companies is necessary. We consider that appropriate disclosures have been made and our opinion is not qualified in this respect.



Fundamental uncertainty - Provision against a receivable

In forming our opinion, we have considered the adequacy of the disclosures made in note 25 to the financial statements concerning the outcome in respect of a receivable of approximately HK\$400.1 million as at 31st December, 2001 included in debtors, deposits and prepayments under current assets of Regal Hotels International Holdings Limited ("RHIHL"), a principal listed subsidiary company of the Group, and its subsidiary companies (the "RHIHL Group"). The receivable comprised (i) deferred consideration of US\$45.0 million (approximately HK\$351.0 million) which arose in connection with the RHIHL Group's disposal of its hotel interests in the United States of America in December 1999 (the "Disposal"); and (ii) interest aggregating HK\$49.1 million accrued thereon at 7% per annum (collectively, the "Consideration Receivable") which was due to be paid by the purchaser (the "Purchaser") on 17th December, 2001. As more fully explained in note 25 to the financial statements, the Purchaser alleges that the aggregate amount of certain indemnity claims, relating to litigation cases underlying the third party claims covered by indemnifications given by the RHIHL Group under the Disposal agreement, exceeds the deferred consideration, and has withheld payment to the RHIHL Group of the Consideration Receivable. The directors of RHIHL are currently unable to determine with reasonable certainty the time required for the resolution of the underlying legal claims, the legal or settlement costs that may be involved and the timing of the receipt of the Consideration Receivable. Accordingly, the directors of RHIHL are currently unable to determine whether a provision, if any, is required against the Consideration Receivable. We consider that appropriate disclosures have been made and our opinion is not qualified in this respect.

Fundamental uncertainties relating to the going concern basis

In forming our opinion, we have considered the adequacy of the disclosures made in note 3 to the financial statements which explain the circumstances giving rise to the fundamental uncertainties relating to:

- i. the outcome of completion of the proposed settlement with the bondholders of two outstanding bonds of the Group;
- ii. the outcome of finalisation of the proposed bilateral facilities arrangement with the financial creditors of the Group to replace its existing informal standstill arrangement;
- iii. the outcome of the proposed restructuring of a syndicated loan of HK\$3,822.1 million (the "Syndicated Loan") and a construction loan of HK\$1,079.5 million (collectively, the "Regal Loans") as at 31st December, 2001, of the RHIHL Group;
- iv. the successful recovery of the RHIHL Group's Consideration Receivable;
- v. the outcome of the proposed fund-raising arrangement of the RHIHL Group through equity issues; and
- vi. the continued successful implementation of assets disposal programmes of the Group and the RHIHL Group.



For the reasons detailed in note 3 to the financial statements, notwithstanding the non-compliance of certain loan covenants specified under the relevant loan agreements of the Regal Loans, the RHIHL Group has classified the Regal Loans as current or non-current liabilities as at 31st December, 2001 in accordance with their original maturity dates, on the basis that (i) the agents of the Regal Loans have not served and the directors of RHIHL do not expect that they will serve notice to the RHIHL Group to declare the Regal Loans immediately due and repayable; and (ii) the lenders of the Syndicated Loan have not exercised and the directors of RHIHL do not expect that they will exercise their respective individual put options to require the RHIHL Group to prepay their respective participations in the remaining outstanding indebtedness by serving a notice to the RHIHL Group, during the forthcoming year. The Directors of the Company have also adopted such classification for the Group for the same reasons. Were such notices and put options to be served and fully exercised, liabilities of HK\$4,349.5 million classified as non-current as at 31st December, 2001 have to be reclassified as current and the liability position and the continuance of the RHIHL Group would be adversely affected.

The financial statements have been prepared on a going concern basis, the validity of which depends upon the successful outcome of implementation of the measures noted above. The financial statements do not include any adjustments that would result from the failure of implementation of such measures. If the going concern basis were not to be appropriate, adjustments would have to be made to restate the values of the Group's assets to their recoverable amounts, to provide for any further liabilities, in addition to those described in the preceding paragraph, which might arise and to reclassify non-current assets and liabilities as current assets and liabilities, respectively.

We consider that appropriate disclosures have been made but the inherent uncertainties surrounding the circumstances under which the Group might successfully continue to adopt the going concern basis are so extreme that we have disclaimed our opinion.

#### **Disclaimer of opinion**

On account of the foregoing fundamental uncertainties relating to the appropriateness of the going concern basis, we are unable to form an opinion as to whether the financial statements give a true and fair view of the state of affairs of the Company and of the Group as at 31st December, 2001 and of the loss and cash flows of the Group for the year then ended and as to whether the financial statements have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

#### **Ernst & Young**

Certified Public Accountants

Hong Kong  
19th April, 2002

