# Knusford Berhad
(Company No. 380100-D)
(Incorporated in Malaysia)
# and its subsidiaries

# Notes to the financial statements

## 1. Summary of significant accounting policies

The following accounting policies are adopted by the Group and by the Company and are consistent with those adopted in previous years except for the adoption of the following:

(i) MASB 25, Income Taxes;

(ii) MASB 27, Borrowing Costs; and

(iii) MASB 29, Employee Benefits.

In addition to the new policies and extended disclosures where required by these new standards, the effects of the changes in the above accounting policies are disclosed in Note 27 to these financial statements.

### (a) Basis of accounting

The financial statements of the Group and of the Company are prepared on the historical cost basis except as disclosed in the notes to the financial statements and in compliance with the provisions of the Companies Act, 1965 and applicable approved accounting standards in Malaysia other than as disclosed in Note 1 (h).

### (b) Basis of consolidation

Subsidiaries are those enterprises controlled by the Company. Control exists when the Company has the power, directly or indirectly, to govern the financial and operating policies of an enterprise so as to obtain benefits from its activities. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control effectively commences until the date that control effectively ceases. Subsidiaries are consolidated using the acquisition method of accounting.

A subsidiary is excluded from consolidation when either control is intended to be temporary if the subsidiary is acquired and held exclusively with a view of its subsequent disposal in the near future and it has not previously been consolidated or it operates under severe long term restrictions which significantly impair its ability to transfer funds to the Company. Subsidiaries excluded on these grounds are accounted for as investments.

# 1. Summary of significant accounting policies

## (b) Basis of consolidation (continued)

Under the acquisition method of accounting, the results of subsidiaries acquired or disposed off during the year are included from the date of acquisition or up to the date of disposal. At the date of acquisition, the fair values of the subsidiaries' net assets are determined and these values are reflected in the Group financial statements. The difference between the acquisition cost and the fair values of the subsidiaries' net assets is reflected as goodwill or negative goodwill as appropriate.

Intra-group transactions and balances and the resulting unrealised profits are eliminated on consolidation. Unrealised losses resulting from intragroup transactions are also eliminated unless cost cannot be recovered.

## (c) Property, plant and equipment

Freehold land is stated at cost. All other property, plant and equipment are stated at cost less accumulated depreciation and accumulated impairment losses.

Property, plant and equipment retired from active use and held for disposal are stated at the carrying amount at the date when the asset is retired from active use, less impairment losses, if any.

***Depreciation***

Freehold land is not amortised. The straight line method is used to write off the cost of the assets over the term of their estimated useful lives at the following principal annual rates:

| | |
|---|---|
| Buildings | 2% |
| Equipment, furniture and fittings | 10% |
| Plant and machinery | 5%-20% |
| Motor vehicles | 20% |

## (d) Finance lease

Leases in which the Group assumes substantially all the risks and rewards of ownership are classified as finance leases. Assets acquired by way of finance leases are stated at an amount equal to the lower of their fair values and the present value of the minimum lease payments at the inception of the leases, less accumulated depreciation and impairment losses.

In calculating the present value of the minimum lease payments, the discount rate is the interest rate implicit in the lease, if this is practicable to determine; if not, the Group's incremental borrowing rate is used.

# 1. Summary of significant accounting policies

## (e) Investments

Long term investments in subsidiaries are stated at cost less impairment loss where applicable.

## (f) Land held for future development

Land held for future development comprising land and development costs are stated at cost. A proportionate amount of the land held for future development would be transferred to properties under development upon commencement of active development.

## (g) Negative goodwill

Negative goodwill represents the excess of the fair values of the net identifiable assets acquired over the cost of acquisition. Negative goodwill is stated at cost less accumulated amortisation.

Negative goodwill is amortised through the income statement of the Group over five (5) years from the date of initial recognition.

## (h) Inventories

Inventories are value at the lower of cost and net realisable value with first-in first-out being the main basis for cost. Cost of trading and rental inventories comprises purchase price plus associated costs.

Inventories of machinery held for trading, which are also being rented out, are amortised at a rate of 5% per annum.

The policy of not capitalising machinery being rented out is not in compliance with MASB 10 on Leases. The standard requires assets held for operating leases to be recorded as property, plant and equipment of lessors. The Directors are of the view that the machinery are mainly held for trading and therefore it is inappropriate to account for the machinery as property, plant and equipment. The non-compliance has no material effect on the financial statements.

## (i) Properties under development

Properties under development comprising land and development costs are stated at cost plus attributable profit less foreseeable losses, net of progress billings. Development costs includes interest expense on loans and advances utilised to finance on-going development.

# 1. Summary of significant accounting policies

## (j) Trade and other receivables

Trade and other receivables are stated at cost less allowance for doubtful debts.

Known bad receivables are written off and specific allowance is made for any receivables considered to be doubtful of collection.

## (k) Employee benefits

***(i) Defined contribution plan***

Obligations for contributions to defined contribution plan are recognised as an expense in the income statement as incurred.

***(ii) Equity and equity-related compensation benefits***

The share option programme allows Group employees to acquire shares of the Company. When the options are exercised, equity is increased by the amount of the proceeds received.

## (l) Cash and cash equivalents

Cash and cash equivalents consist of cash on hand balances and deposits with banks and highly liquid investments which have an insignificant risk of change in value. For the purpose of the cash flow statement, cash and cash equivalents are presented net of pledged deposits.

## (m) Liabilities

Borrowings and trade and other payables are stated at cost.

## (n) Amount due from contract customers

Amount due from contract customers on construction contracts is stated at cost plus attributable profits less foreseeable losses and less progress billings. Cost includes all direct construction costs and other related costs. Where progress billings exceed the aggregate amount due from contract customers plus attributable profits less foreseeable losses, the net credit balance on all such contracts is shown in trade and other payables as amount due to contract customers.

# 1. Summary of significant accounting policies

## (o) Impairment

The carrying amounts of assets, other than inventories, assets arising from construction contracts, deferred tax assets and financial assets (other than investments in subsidiaries), are reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated. An impairment loss is recognised whenever the carrying amount of an asset or the cash-generating unit to which it belongs exceeds its recoverable amount. Impairment losses are recognised in the income statement.

The recoverable amount is the greater of the asset's net selling price and its value in use. In assessing value in use, estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount and it is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss has been recognised. The reversal is recognised in the income statement.

## (p) Foreign currency transactions

Transactions in foreign currencies are translated to Ringgit Malaysia at rates of exchange ruling at the date of the transactions. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated to Ringgit Malaysia at the foreign exchange rates ruling at that date. Foreign exchange differences arising on translation are recognised in the income statement.

The closing rate used in the translation of foreign currency monetary assets and liabilities is as follows:

| | |
|---|---|
| USD 1 | RM3.80 |

## (q) Capitalisation of borrowing costs

Borrowing costs incurred on capital work-in-progress, properties under development and gross amount due from contract customers are capitalised. Exchange differences arising from foreign currency borrowings, to the extent they are regarded as an adjustment to interest costs, are also capitalised. Capitalisation of borrowing costs will cease when the assets are ready for their intended use.

# 1. Summary of significant accounting policies

## (q) Capitalisation of borrowing costs (continued)

The capitalisation rate used to determine the amount of borrowing costs eligible for capitalisation is the weighted average of the borrowing costs applicable to the Group's borrowings that are outstanding during the year, other than borrowings made specifically for the purpose of financing a specific capital work-in-progress, property under development or gross amount due from contract customers, in which case the actual borrowing cost incurred on that borrowing less any investment income on the temporary investment of that borrowing will be capitalised.

Capitalisation of borrowing costs is suspended during extended periods in which active development is interrupted.

## (r) Income tax

Tax on the profit or loss for the year comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax expense is the expected tax payable on the taxable income for the year, using tax rates enacted or substantially enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Temporary differences are not recognised for goodwill not deductible for tax purposes and the initial recognition of assets or liabilities that at the time of the transaction affects neither accounting nor taxable profit. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantially enacted at the balance sheet date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised.

## (s) Revenue

### *i) Goods sold and services rendered*

Revenue from the sale of goods are measured at the fair value of the consideration receivable and is recognised in the income statement when the significant risks and rewards of ownership have been transferred to the buyer.

Revenue from services rendered is recognised in the income statement in proportion to the stage of completion of the transaction at the balance sheet date. The stage of completion is assessed by reference to survey of works performed. Where the outcome of the transaction cannot be estimated reliably, revenue is recognised only to the extent of the expenses recognised that are recoverable.

# 1. Summary of significant accounting policies

## (s) Revenue (continued)

*ii) Rental of machinery*

Revenue from the rental of machinery is recognised in the income statement on an accrual basis in accordance with the substance of the rental agreements.

*iii) Construction contracts*

Revenue from fixed price construction contracts is recognised on the percentage of completion method, measured by reference to the proportion that contract costs incurred for contract work performed to date that reflect work performed bear to the total estimated contract costs.

When the outcome of a construction contract cannot be estimated reliably, revenue is recognised only to the extent of contract costs incurred that is probable to be recoverable and contract costs are recognised as an expense in the period in which they are incurred.

An expected loss on a contract is recognised immediately in the income statement.

*iv) Property development*

Profit from property development is recognised using the percentage of completion method. Where foreseeable losses are anticipated, full provision for these losses is made in the financial statements.

*v) Interest income*

Interest income is recognised in the income statement on a time proportion basis taking into account the principal outstanding and the rate applicable.

*vi) Dividend income*

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

## (t) Financing costs

All interest and other costs incurred in connection with borrowings other than that capitalised in accordance with Note 1(q), are expensed as incurred. The interest component of finance lease payments is recognised in the income statement so as to give a constant periodic rate of interest on the outstanding liability at the end of each accounting period.

## 2. Property, plant and equipment

| Group | Freehold land RM'000 | Buildings RM'000 | Equipment, furniture and fittings RM'000 | Plant and machinery RM'000 | Motor vehicles RM'000 | Total RM'000 |
|---|---|---|---|---|---|---|
| ***Cost*** | | | | | | |
| At 1 January 2003 | 5,173 | 2,822 | 1,410 | 30,545 | 6,090 | 46,040 |
| Additions | - | 30 | 189 | 21,881 | 1,128 | 23,228 |
| Disposals | - | - | - | (296) | (209) | (505) |
| Written off | - | - | - | - | (3) | (3) |
| Transfer to inventories | - | - | (4) | (441) | - | (445) |
| Acquisition of subsidiaries | - | - | 2 | - | - | 2 |
| At 31 December 2003 | 5,173 | 2,852 | 1,597 | 51,689 | 7,006 | 68,317 |
| ***Accumulated depreciation*** | | | | | | |
| At 1 January 2003 | - | 210 | 615 | 19,025 | 3,893 | 23,743 |
| Charge for the year | - | 43 | 143 | 3,710 | 803 | 4,699 |
| Disposals | - | - | - | (183) | (163) | (346) |
| Written off | - | - | - | - | (3) | (3) |
| Transfer to inventories | - | - | (2) | (428) | - | (430) |
| At 31 December 2003 | - | 253 | 756 | 22,124 | 4,530 | 27,663 |
| ***Net book value*** | | | | | | |
| At 31 December 2003 | 5,173 | 2,599 | 841 | 29,565 | 2,476 | 40,654 |
| At 31 December 2002 | 5,173 | 2,612 | 795 | 11,520 | 2,197 | 22,297 |
| Depreciation charge for the year ended 31 December 2002 | - | 43 | 120 | 3,242 | 744 | 4,149 |

## 2. Property, plant and equipment (continued)

Buildings which relate to shop lots costing approximately RM671,000 (2002 - RM671,000) have not been registered in the name of a subsidiary as the purchase consideration has not been settled.

Motor vehicles with an aggregate net book value of RM435,000 (2002 - RM255,000) have not been registered in the name of the subsidiaries.

*Assets under finance lease*

Included in the property, plant and equipment of the Group are assets acquired under finance lease arrangements with an aggregate net book value as follows:

| | Group | |
|---|---|---|
| | **2003** | **2002** |
| | **RM'000** | **RM'000** |
| Motor vehicles | 1,403 | 1,192 |
| Plant and machinery | 18,763 | 2,879 |
| | 20,166 | 4,071 |

*Security*

Certain freehold land and buildings with an aggregate net book value amounting to RM4,689,000 (2002 - RM4,712,000) of a subsidiary are charged to secure banking facilities of the subsidiary.

## 3. Investments in subsidiaries

| | Company | |
|---|---|---|
| | **2003** | **2002** |
| | **RM'000** | **RM'000** |
| Unquoted shares, at cost | 65,892 | 57,892 |

Details of the subsidiaries are shown in Note 22.

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## 4. Properties under development

| | Group 2003 RM'000 | Group 2002 RM'000 |
|---|---|---|
| Land and development costs | 56,712 | 21,333 |
| Attributable profits | 1,535 | - |
| | 58,247 | 21,333 |
| Less: Progress billings | (9,843) | - |
| | 48,404 | 21,333 |
| Less: Non-current portion | (32,874) | (21,333) |
| Current portion | 15,530 | - |

Additions to development costs during the period include rental of equipment of RM380,000 (2002 - Nil).

The portion of properties under development in respect of which significant development work has been undertaken and which is expected to be completed within the normal operating cycle of two to three years is considered as a current asset.

*Security*

The properties under development amounting to RM32,410,000 (2002 - Nil) are charged to secure banking facilities of a subsidiary.

## 5. Deferred tax

The amounts, determined after appropriate offsetting, are as follows:

| | Group 2003 RM'000 | Group 2002 RM'000 |
|---|---|---|
| Deferred tax liabilities | 2,934 | - |
| Deferred tax assets | (687) | (841) |
| | 2,247 | (841) |

Deferred tax liabilities and assets are offset above where there is a legally enforceable right to set off current tax assets against current tax liabilities and where the deferred taxes relate to the same taxation authority.

## 5. Deferred tax (continued)

The recognised deferred tax assets and liabilities (before offsetting) are as follows:

| | Group | |
|---|---|---|
| | 2003 RM'000 | 2002 RM'000 |
| Properties under development | 2,870 | - |
| Property, plant and equipment | | |
| - capital allowances | 672 | - |
| Provisions | (420) | - |
| Unabsorbed capital allowances | (132) | - |
| Other items | (56) | - |
| Deferred tax liabilities | 2,934 | - |
| Property, plant and equipment | | |
| - capital allowances | 53 | (15) |
| Provisions | (740) | (826) |
| Deferred tax assets | (687) | (841) |

No deferred tax asset has been recognised for the following items:

| | Group | |
|---|---|---|
| | 2003 RM'000 | 2002 RM'000 |
| Deductible temporary differences | 6,720 | 5,801 |
| Taxable temporary differences | (2,721) | (619) |
| Unabsorbed capital allowances | 3,443 | 960 |
| Unutilised tax losses | 1,596 | 128 |
| | 9,038 | 6,270 |
| Tax effect at 28% | 2,531 | 1,756 |

The deductible temporary differences mainly relate to the accumulated amortisation on rental inventories. Deferred tax assets have not been recognised in respect of these items because under the Group's current accounting practice, the temporary differences are not reversed upon the disposals of the rental inventories.

The unutilised tax losses, unabsorbed capital allowances and temporary differences do not expire under current tax legislation. Deferred tax assets have not been recognised in respect of these items because it is not probable that future taxable profit will be available against which the Group can utilise the benefits.

## 6. Inventories

| | Group | |
|---|---|---|
| | 2003 | 2002 |
| | RM'000 | RM'000 |
| Trading and rental inventories, at cost | 32,057 | 30,127 |
| Less: Accumulated amortisation | (6,720) | (5,801) |
| | 25,337 | 24,326 |

Inventories of machinery held for trading, which are also rented out, net of amortisation at year end were RM15,246,000 (2002 - RM17,756,000).

## 7. Trade and other receivables

| | Group | | Company | |
|---|---|---|---|---|
| | 2003 | 2002 | 2003 | 2002 |
| | RM'000 | RM'000 | RM'000 | RM'000 |
| Trade receivables | 47,439 | 54,477 | - | - |
| Other receivables, deposits and prepayments | 5,815 | 4,137 | 5 | 85 |
| Amount due from contract customers | 118 | - | - | - |
| Subsidiaries | - | - | 38,436 | 12,491 |
| | 53,372 | 58,614 | 38,441 | 12,576 |

***Amount due from contract customers***

| | Group | |
|---|---|---|
| | 2003 | 2002 |
| | RM'000 | RM'000 |
| Aggregate costs incurred to date | 2,379 | - |
| Add: Attributable profits | 96 | - |
| | 2,475 | - |
| Less: Progress billings | (2,357) | - |
| | 118 | - |

Included in the trade receivables of the Group are amounts due from companies deemed related to Directors as defined in Note 24 amounting to RM4,281,000 (2002 - RM1,096,000).

The amounts due from subsidiaries comprise advances that are unsecured, interest free and have no fixed terms of repayment.

## 8. Cash and cash equivalents

| | Group | | Company | |
|---|---|---|---|---|
| | 2003 RM'000 | 2002 RM'000 | 2003 RM'000 | 2002 RM'000 |
| Cash and bank balances | 13,613 | 4,271 | 131 | 67 |
| Deposits with licensed banks | 32,221 | 30,388 | 24,078 | 18,403 |
| | 45,834 | 34,659 | 24,209 | 18,470 |

Deposits with licensed banks amounting to RM6,261,000 (2002 - RM6,132,000) and RM3,311,000 (2002 - RM3,223,000) of the Group and the Company respectively are pledged to banks to secure bank borrowings and facilities granted to subsidiaries.

Included in the Group's cash and bank balances is an amount of RM1,822,000 (2002 - Nil), the utilisation of which is subject to the Housing Development (Housing Development Account) Regulations 2002.

## 9. Trade and other payables

| | Group | | Company | |
|---|---|---|---|---|
| | 2003 RM'000 | 2002 RM'000 | 2003 RM'000 | 2002 RM'000 |
| Trade payables | 27,684 | 29,475 | - | - |
| Directors | 1,050 | 1,218 | 70 | 70 |
| Other payables and accrued expenses | 10,621 | 2,907 | 8,139 | 66 |
| | 39,355 | 33,600 | 8,209 | 136 |

Included in trade payables of the Group are amounts due to companies deemed related to Directors as defined in Note 24 amounting to RM5,806,000 (2002 - RM6,467,000).

The amounts due to Directors comprise advances that are unsecured, interest free and have no fixed terms of repayment.

Included in other payables and accrued expenses of the Group is an amount due to a third party (former holding company of D-Hill Sdn. Bhd.) of RM5,250,000 (2002 - Nil) which comprises advances that are unsecured, interest free and have no fixed terms of repayment.

## 10. Borrowings

| | Group 2003 RM'000 | Group 2002 RM'000 |
|---|---|---|
| Current | | |
| Finance lease liabilities | 2,733 | 1,874 |
| Revolving credit - secured | 1,000 | 1,000 |
| | 3,733 | 2,874 |
| Non-current | | |
| Finance lease liabilities | 10,444 | 1,143 |

***Terms and debt repayment schedule***

Finance lease liabilities are subject to fixed interest rates ranging from 4.00% to 9.31% (2002 - 4.00% to 9.31%) per annum.

Revolving credit of a subsidiary is subject to interest at 0.5% (2002 - 0.5%) per annum above the Kuala Lumpur Interbank Offer Rates and is secured by bank guarantee.

Finance lease liabilities are payable as follows:

| *Group* | Payments 2003 RM'000 | Interest 2003 RM'000 | Principal 2003 RM'000 | Payments 2002 RM'000 | Interest 2002 RM'000 | Principal 2002 RM'000 |
|---|---|---|---|---|---|---|
| Less than one year | 3,829 | 1,096 | 2,733 | 2,092 | 218 | 1,874 |
| Between one and five years | 9,311 | 2,591 | 6,720 | 1,295 | 152 | 1,143 |
| More than five years | 4,067 | 343 | 3,724 | - | - | - |
| | 17,207 | 4,030 | 13,177 | 3,387 | 370 | 3,017 |

## 11. Share capital

| | Group and Company 2003 RM'000 | Group and Company 2002 RM'000 |
|---|---|---|
| Ordinary shares of RM1.00 each | | |
| Authorised | 200,000 | 200,000 |
| Issued and fully paid | | |
| Opening balance | 74,042 | 74,042 |
| Shares issued under share option scheme | 1,275 | - |
| Shares issued under private placement exercise | 22,212 | - |
| | 97,529 | 74,042 |

## 12. Reserves

| | Group | | Company | |
|---|---|---|---|---|
| | 2003 | 2002 | 2003 | 2002 |
| | RM'000 | RM'000 | RM'000 | RM'000 |
| Non-distributable | | | | |
| Share premium | 22,168 | 14,105 | 22,168 | 14,105 |
| Distributable | | | | |
| Retained profits | 36,154 | 25,933 | 566 | 627 |
| | 58,322 | 40,038 | 22,734 | 14,732 |

Subject to agreement by the Inland Revenue Board, the Company has sufficient Section 108 tax credit to frank all of its retained profits at 31 December 2003 if paid out as dividends.

## 13. Negative goodwill

| | Group | |
|---|---|---|
| | 2003 | 2002 |
| | RM'000 | RM'000 |
| At cost | | |
| At 1 January/At 31 December | 34,475 | 34,475 |
| Accumulated amortisation | | |
| At 1 January | 20,685 | 13,790 |
| Current year amortisation | 6,895 | 6,895 |
| At 31 December | 27,580 | 20,685 |
| | 6,895 | 13,790 |

The negative goodwill was derived from the acquisition of the subsidiaries in 2000 where the fair values of the subsidiaries were higher than the cost of investment.

## 14. Employee benefits

| | Group | | Company | |
|---|---|---|---|---|
| | 2003 | 2002 | 2003 | 2002 |
| | RM'000 | RM'000 | RM'000 | RM'000 |
| Expenses recognised in the income statement under defined contribution plan | 973 | 805 | 36 | 10 |

# 14. Employee benefits (continued)

***Equity compensation benefits***

***Share option plan***

The Group offers vested share options over ordinary shares to eligible employees. Movements in the number of share options held by employees are as follows:

| | |
|---|---|
| Details of share options granted during the year: | |
| Expiry date | 22/4/2008 |
| Exercise price per ordinary share (RM) | 1.25 |
| Aggregate proceeds if shares are issued (RM'000) | 12,031 |
| | |
| Details of share options exercised during the year: | |
| Expiry date | 22/4/2008 |
| Exercise price per ordinary share (RM) | 1.25 |
| Aggregate issue proceeds (RM'000) | 1,594 |
| Fair value at date of issue (RM'000) | 2,440 |

Terms of the options outstanding at 31 December 2003:

| Expiry date | Exercise price | Number |
|---|---|---|
| 22 April 2008 | RM1.25 | 8,350,000 |

The Group received proceeds of RM1,594,000 in respect of the 1,275,000 options exercised during the year: RM1,275,000 was credited to share capital and RM319,000 was credited to share premium.