

**CHUNGHWA PICTURE TUBES, LTD.**  
**Financial Statements**  
**For The Years Ended**  
**December 31, 2004 And 2005**  
**With**  
**Report of Independent Auditors**

## **Report of Independent Auditors**

To the Board of Directors and Stockholders of  
Chunghwa Picture Tubes, Ltd.

We have audited the accompanying balance sheets of Chunghwa Picture Tubes, Ltd. (the “Company”) as of December 31, 2004 and 2005, and the related statements of operations, changes in stockholders' equity and cash flows for the years ended December 31, 2004 and 2005. These financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with “Rules Governing Auditing and Certification of Financial Statements by Certified Public Accountants” and auditing standards generally accepted in the Republic of China. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of Chunghwa Picture Tubes, Ltd. as of December 31, 2004 and 2005, and the results of its operations and its cash flows for the years ended December 31, 2004 and 2005, in conformity with the “Guidelines Governing the Preparation of Financial Report by Securities Issuers” and accounting principles generally accepted in the Republic of China.

As described in Note 3 to the financial statements, effective from January 1, 2005, the Company adopted the ROC Statement of Financial Accounting Standards No. 35 “Accounting for Assets Impairment” to account for the impairment of its assets.

We have also audited the consolidated financial statement of Chunghwa Picture Tubes, Ltd. as of and for the years ended December 31, 2004 and 2005 and an unqualified opinion was issued for 2004 and an unqualified opinion with explanatory language was issued in 2005, respectively.

Diwan, Ernst & Young  
Taipei, Taiwan  
Republic of China  
April 14, 2006

### Notice to Readers

The accompanying financial statements are intended only to present the financial position and results of operations and cash flows in accordance with accounting principles and practices generally accepted in the Republic of China and not those of any other jurisdictions. The standards, procedures and practices to audit such financial statements are those generally accepted and applied in the Republic of China.

CHUNGHWA PICTURE TUBES, LTD.  
BALANCE SHEETS  
DECEMBER 31, 2004 AND 2005  
(Expressed in Thousands of New Taiwan Dollars)

ASSETS	December 31	
	2004	2005
<b>CURRENT ASSETS:</b>		
Cash and cash equivalents (Notes 2, 4 and 11)	\$24,107,563	\$13,735,238
Marketable securities (Notes 2, 4 and 11)	1,115,499	363,000
Notes receivable, net (Notes 2, 4 and 11)	49,335	3,894
Accounts receivable, net		
Trade (Notes 2, 4 and 11)	8,842,167	15,917,914
Others (Notes 2, 4 and 11)	679,170	416,357
Due from affiliates, net		
Trade (Notes 2, 4, 5 and 11)	3,464,071	1,971,664
Others (Notes 2, 5 and 11)	17,783	757,215
Inventories, net (Notes 2 and 4)	6,176,535	9,817,329
Prepayments	73,880	88,520
Deferred tax assets, net (Notes 2 and 4)	27,444	-
Pledged time deposits-current (Notes 6 and 11)	2,005,742	382,350
Total Current Assets	<u>46,559,189</u>	<u>43,453,481</u>
<b>LONG-TERM INVESTMENTS: (Notes 2, 4 and 11)</b>		
Equity method	28,500,784	27,573,390
Cost method	917,698	696,875
Total Long-term Investment	<u>29,418,482</u>	<u>28,270,265</u>
<b>PROPERTY, PLANT AND EQUIPMENT :</b>		
(Notes 2, 4, 5 and 6)		
Land	3,039,102	3,336,335
Buildings	10,650,390	23,464,912
Machinery and equipment	48,265,787	90,043,163
Transportation equipment	319,100	320,795
Furniture and fixtures	568,642	720,901
Miscellaneous equipment	11,470,737	25,756,917
Revaluation increment	57,192	57,192
Total	<u>74,370,950</u>	<u>143,700,215</u>
Less: Accumulated depreciation	(29,410,376)	(43,627,794)
Add: Prepayments on equipments and		
Construction in progress	51,547,628	39,088,832
Property, plant and equipment, net	<u>96,508,202</u>	<u>139,161,253</u>
<b>INTANGIBLE ASSETS:</b>		
Deferred pension cost (Notes 2 and 4)	202,475	168,729
<b>OTHER ASSETS:</b>		
Refundable deposits (Note 11)	35,669	21,632
Deferred charges (Notes 2 and 4)	2,565,326	3,360,024
Prepayment for purchases-non-current (Note 4)	-	2,282,511
Pledged time deposits-non-current (Notes 6 and 11)	35,000	10,000
Others, net (Notes 2 and 4)	306,861	35,755
Total Other Assets	<u>2,942,856</u>	<u>5,709,922</u>
<b>TOTAL ASSETS</b>	<u><u>\$175,631,204</u></u>	<u><u>\$216,763,650</u></u>

The accompanying notes are an integral part of the financial statements.

CHUNGHWA PICTURE TUBES, LTD.  
BALANCE SHEETS (CONTINUED)  
DECEMBER 31, 2004 AND 2005  
(Expressed in Thousands of New Taiwan Dollars)

LIABILITIES AND STOCKHOLDERS' EQUITY	December 31	
	2004	2005
<b>CURRENT LIABILITIES:</b>		
Short-term bank loans (Notes 4 and 11)	\$7,898,870	\$3,128,438
Accounts payable (Note 11)		
Trade	8,003,573	12,570,827
Others	10,176,522	8,706,396
Due to affiliates (Notes 5 and 11)		
Trade	7,974,008	11,519,298
Others	1,631,821	634,976
Income tax payable (Notes 2 and 4)	-	55,959
Accrued expenses (Note 11)	2,192,875	3,020,371
Forward exchange contracts payable, net (Notes 2 and 11)	26,891	-
Current portion of bonds payable (Notes 2, 4 and 11)	7,092,242	-
Current portion of long-term bank loans (Notes 4, 5, 6 and 11)	6,737,987	7,019,604
Other current liabilities (Notes 5 and 11)	217,944	160,077
Total Current Liabilities	<u>51,952,733</u>	<u>46,815,946</u>
<b>LONG-TERM DEBT:</b>		
Bonds payable, net of current portion (Notes 2, 4 and 11)	6,825,967	7,211,149
Long-term bank loans, net of current portion (Notes 4, 5, 6 and 11)	18,717,716	65,153,303
Total Long-term Debt	<u>25,543,683</u>	<u>72,364,452</u>
<b>RESERVE FOR INCREMENT TAX ON LAND</b>		
REVALUATION (Notes 2 and 4)	26,793	26,793
<b>OTHER LIABILITIES:</b>		
Accrued pension liabilities (Notes 2 and 4)	1,511,990	1,681,231
Deferred tax liabilities, net (Notes 2 and 4)	543,767	777,478
Deferred credits (Notes 2, 4 and 5)	1,276,165	1,171,746
Total Other Liabilities	<u>3,331,922</u>	<u>3,630,455</u>
Total Liabilities	<u>80,855,131</u>	<u>122,837,646</u>
<b>STOCKHOLDERS' EQUITY:</b>		
Capital		
Common stock (Note 4)	68,564,159	82,126,048
Capital reserve (Notes 2 and 4)		
Additional paid-in capital	14,615,928	12,293,011
Premium on convertible bonds payable	3,927,694	4,028,677
Treasury stock	744	-
Reserve for assets revaluation	59,304	59,304
Long-term investments	515,955	594,015
Retained earnings (Notes 2 and 4)		
Legal reserve	93,996	1,125,768
Special reserve	845,962	3,125,641
Accumulated earnings (deficits)	10,317,715	(6,898,965)
Other items in stockholders' equity : (Notes 2 and 4)		
Unrealized losses on long-term investments	(2,398,311)	(2,711,230)
Cumulative translation adjustment	(566,572)	317,584
Excess of additional pension liability over unrecognized prior service cost	(160,758)	(133,849)
Treasury stock (Notes 2 and 4)	(1,039,743)	-
Total Stockholders' Equity	<u>94,776,073</u>	<u>93,926,004</u>
<b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>	<u><u>\$175,631,204</u></u>	<u><u>\$216,763,650</u></u>

The accompanying notes are an integral part of the financial statements.

CHUNGHWA PICTURE TUBES, LTD.  
STATEMENTS OF OPERATIONS  
FOR THE YEARS ENDED DECEMBER 31, 2004 AND 2005  
(Expressed in Thousands of New Taiwan Dollars Except Per Share Information)

	Years Ended December 31	
	2004	2005
OPERATING REVENUES:		
NET SALES (Notes 2, 4 and 5)	\$78,416,749	\$78,458,350
OPERATING COSTS:		
COST OF GOODS SOLD (Notes 4 and 5)	<u>(67,691,660)</u>	<u>(79,701,902)</u>
GROSS PROFIT (LOSS) INCLUDED UNREALIZED INTERCOMPANY PROFIT	10,725,089	(1,243,552)
REALIZED INTERCOMPANY GAIN, NET (Notes 2, 4 and 5)	148,683	165,907
UNREALIZED INTERCOMPANY GAIN, NET (Notes 2, 4 and 5)	<u>(87,088)</u>	<u>(68,721)</u>
NET GROSS PROFIT (LOSS)	<u>10,786,684</u>	<u>(1,146,366)</u>
OPERATING EXPENSES: (Notes 4 and 5)		
Selling and marketing	(790,293)	(988,811)
General and administrative	(1,326,807)	(1,452,047)
Research and development	<u>(3,066,961)</u>	<u>(3,472,022)</u>
Total	<u>(5,184,061)</u>	<u>(5,912,880)</u>
OPERATING INCOME (LOSS)	<u>5,602,623</u>	<u>(7,059,246)</u>
NON-OPERATING INCOME:		
Interest income (Note 11)	95,382	98,071
Investment income recognized by using equity method, net (Notes 2 and 4)	5,332,415	933,511
Gain on disposal of property, plant and equipment, net (Notes 2 and 5)	5,996	3,172
Gain on disposal of marketable securities, net (Note 2)	62,327	96,402
Gain on foreign currency exchange, net (Note 2)	221,577	-
Reversal of provision for loss on decline in market value of inventory, net (Notes 2 and 4)	-	113,000
Others (Note 5)	<u>277,090</u>	<u>546,489</u>
Total	<u>5,994,787</u>	<u>1,790,645</u>
NON-OPERATING EXPENSES:		
Interest expenses (Notes 2, 4 and 11)	(783,348)	(1,283,957)
Loss on foreign currency exchange, net (Note 2)	-	(736,395)
Loss on decline in market value and obsolescence of inventory, net (Notes 2 and 4)	(181,000)	-
Loss on disposal of other assets	(53,489)	-
Others	<u>(10,128)</u>	<u>(7,612)</u>
Total	<u>(1,027,965)</u>	<u>(2,027,964)</u>
INCOME (LOSS) BEFORE INCOME TAX	10,569,445	(7,296,565)
INCOME TAX EXPENSES (Notes 2 and 4)	<u>(247,562)</u>	<u>(55,736)</u>
NET INCOME (LOSS)	<u>\$10,321,883</u>	<u>\$(7,352,301)</u>
EARNINGS (LOSS) PER SHARE AVAILABLE TO COMMON		
STOCKHOLDERS (Notes 2 and 4)		
BASIC (in dollars)	<u>\$1.45</u>	<u>\$(0.94)</u>
DILUTED (in dollars)	<u>\$1.29</u>	<u>\$(0.94)</u>

The accompanying notes are an integral part of the financial statements.

CHUNGHWA PICTURE TUBES, LTD.  
STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY  
FOR THE YEARS ENDED DECEMBER 31, 2004 AND 2005  
(Expressed in Thousands of New Taiwan Dollars)

	CAPITAL RESERVE						RETAINED EARNINGS			UNREALIZED LOSSES ON LONG- TERM INVESTMENTS	CUMULATIVE TRANSLATION ADJUSTMENT	EXCESS OF ADDITIONAL PENSION LIABILITY OVER UNRECOGNIZED PRIOR SERVICE COST	TREASURY STOCK	TOTAL
	COMMON STOCK	ADDITIONAL PAID-IN CAPITAL	PREMIUM ON CONVERTIBLE BONDS PAYABLE	RESERVE FOR ASSETS REVALUATION	TREASURY STOCK	LONG-TERM INVESTMENTS	LEGAL RESERVE	SPECIAL RESERVE	ACCUMULATED EARNINGS (DEFICITS)					
Balance at January 1, 2004	\$58,908,629	\$7,218,664	\$2,324,653	\$59,304	\$744	\$515,955	\$-	\$-	\$939,958	\$(3,197,632)	\$1,076,055	\$(158,711)	\$(1,039,743)	\$66,647,876
Distribution of earnings in 2003 (Note 4)														
Legal reserve							93,996		(93,996)					-
Special reserve								845,962	(845,962)					-
Convertible bonds converted into common stock (Note 4)	2,613,000		1,603,041											4,216,041
Capital increase by cash in premium (Note 4)	7,000,000	7,383,016												14,383,016
Issuance of common stock - exercise of stock option (Notes 2 and 4)	42,530	14,248												56,778
Net income for 2004									10,321,883					10,321,883
Recovery gain on long-term investment (Notes 2 and 4)										238,115				238,115
Recovery gain on long-term investment for investee company, net of related tax effect (Notes 2 and 4)										561,206				561,206
Cumulative translation adjustment, net of related tax effect (Notes 2 and 4)											(1,642,627)			(1,642,627)
Adjustment of unappropriated earnings arising from changes in ownership percentage in investees									(4,168)					(4,168)
Excess of additional pension liabilities over unrecognized prior service cost (Note 4)												4,335		4,335
Excess of additional pension liabilities over unrecognized prior service cost in investees												(6,382)		(6,382)
Balance at December 31, 2004	68,564,159	14,615,928	3,927,694	59,304	744	515,955	93,996	845,962	10,317,715	(2,398,311)	(566,572)	(160,758)	(1,039,743)	94,776,073
Distribution of earnings in 2004 (Note 4)														
Legal reserve							1,031,772		(1,031,772)					-
Special reserve								2,279,679	(2,279,679)					-
Cash dividend									(4,086,049)					(4,086,049)
Employees' bonus-cash									(280,246)					(280,246)
Stock dividend	1,362,016								(1,362,016)					-
Employees' bonus-stock	420,380								(420,380)					-
Transfer of capital reserves to common stock (Note 4)	4,767,057	(4,767,057)												-
Convertible bonds converted into common stock (Note 4)	338,266		127,184											465,450
Capital increase by cash in premium (Note 4)	7,000,000	2,483,215												9,483,215
Issuance of common stock - exercise of stock option (Notes 2 and 4)	208,290	40,875												249,165
Retired treasury stock (Notes 2 and 4)	(534,120)	(79,950)	(26,201)		(744)				(398,728)				1,039,743	-
Net loss for 2005									(7,352,301)					(7,352,301)
Unrealized loss on long-term investment (Notes 2 and 4)										(220,823)				(220,823)
Unrealized loss on long-term investment of investee company, net of related tax effect (Notes 2 and 4)										(92,096)				(92,096)
Cumulative translation adjustment, net of related tax effect (Notes 2 and 4)											884,156			884,156
Proportional adjustments on reserve for assets revaluation in investees (Note 4)						77,821								77,821
Proportional adjustments on shares issued for conversion of convertible bonds in investees (Note 4)						239								239
Adjustment of unappropriated earnings arising from changes in ownership percentage in investees (Note 4)									(5,509)					(5,509)
Excess of additional pension liabilities over unrecognized prior service cost (Note 2)												30,025		30,025
Proportional adjustments on excess of additional pension liabilities over unrecognized prior service cost in investees (Note 4)												(3,116)		(3,116)
Balance at December 31, 2005	\$82,126,048	\$12,293,011	\$4,028,677	\$59,304	\$-	\$594,015	\$1,125,768	\$3,125,641	\$(6,898,965)	\$(2,711,230)	\$317,584	\$(133,849)	\$-	\$93,926,004

The accompanying notes are an integral part of the financial statements.

CHUNGHWA PICTURE TUBES, LTD.  
STATEMENTS OF CASH FLOWS  
FOR THE YEARS ENDED DECEMBER 31, 2004 AND 2005  
(Expressed in Thousands of New Taiwan Dollars)

	Years Ended December 31	
	2004	2005
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net income (loss)	\$10,321,883	\$(7,352,301)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Exchange rate effect (Note 2)	458,663	(21,983)
Depreciation (Notes 2 and 4)	9,207,712	14,284,411
Amortization (Notes 2 and 4)	724,056	997,896
Investment income recognized by using equity method, net (Notes 2 and 4)	(5,332,415)	(933,511)
Cash dividend received from long-term investee accounted for under equity method (Notes 2 and 4)	2,414,773	2,983,555
Unrealized (gain) loss on foreign currency exchange of long-term debt	(736,253)	1,287,369
Transfer of property, plant and equipment to expense	201,386	297,618
Gain on disposal of property, plant and equipment, net (Notes 2 and 4)	(5,996)	(3,172)
Loss on disposal of other assets, net	53,489	-
Loss (recovery) on decline in market value and obsolescence of inventory, net (Notes 2 and 4)	181,000	(113,000)
Forfeited interest on convertible bonds	1,863	5
Amortization of premium on bonds payable	(101,411)	(83,646)
Amortization of discount on commercial notes payable-long-term bank loans	-	9,658
Change in operating assets and liabilities:		
Decrease in notes receivable	80,684	45,441
Increase in accounts receivable-trade	(4,648,771)	(7,075,747)
Decrease in due from affiliates-trade	2,647,545	1,492,407
Decrease (increase) in accounts receivable-others	(343,425)	262,813
Increase in inventories	(1,991,616)	(3,527,794)
(Increase) decrease in prepayments	11,167	(14,640)
Increase in prepayment for purchases-non-current	-	(2,282,511)
(Increase) decrease in deferred tax assests	(27,444)	27,444
Increase in accounts payable	228,935	4,567,254
Increase in due to affiliates-trade	6,819,082	3,545,290
Increase (decrease) in forward exchange contract payable, net	26,891	(26,891)
Increase in income tax payable	-	55,959
Increase (decrease) in accrued expenses	(206,831)	866,902
Increase (decrease) in accounts payable-others	7,233,232	(1,470,126)
Decrease in deferred credits	(61,595)	(97,186)
Increase in accrued pension liabilities	248,997	387,335
Payments for pension	(149,026)	(193,729)
Increase in compensation interest payable	71,357	222,104
Increase (decrease) in deferred tax liabilities	275,005	(27,444)
Net cash provided by operating activities	<u>27,602,937</u>	<u>8,109,780</u>

The accompanying notes are an integral part of the financial statements.

CHUNGHWA PICTURE TUBES, LTD.  
STATEMENTS OF CASH FLOWS (CONTINUED)  
FOR THE YEARS ENDED DECEMBER 31, 2004 AND 2005  
(Expressed in Thousands of New Taiwan Dollars)

	Years Ended December 31	
	2004	2005
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
(Increase) decrease in pledged time deposits	(1,899,292)	1,648,392
(Increase) decrease in due from affiliates-others	5,813	(739,432)
(Increase) decrease in marketable securities, net	(297,886)	752,499
Increase in deferred charges	(1,723,296)	(1,792,594)
Proceeds from disposal of property, plant and equipment	8,826	28,178
Proceeds from disposal of other assets	70,373	-
Additions to property, plant and equipment	(54,330,106)	(56,996,213)
Decrease in refundable deposits	6,892	14,037
Net cash used in investing activities	<u>(58,158,676)</u>	<u>(57,085,133)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Issuance of bonds payable	14,885,985	-
Increase (decrease) in short-term bank loans	6,751,160	(4,770,432)
Increase (decrease) in due to affiliates-others	1,330,173	(996,845)
Redemption of bonds payable	(638,507)	(1,358,165)
Repayments of bonds payable	-	(5,580,383)
Increase in long-term bank loans	3,978,340	52,964,634
Repayments of long-term bank loans	(2,304,000)	(6,985,982)
Increase (decrease) in other current liabilities	100,344	(57,867)
Capital increase by cash in premium	14,383,016	9,483,215
Employees' bonus-cash	-	(280,246)
Cash dividends	-	(4,086,049)
Proceeds from exercise of stock options	56,778	249,165
Net cash provided by financing activities	<u>38,543,289</u>	<u>38,581,045</u>
EXCHANGE RATE EFFECT	<u>(458,663)</u>	<u>21,983</u>
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	7,528,887	(10,372,325)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	16,578,676	24,107,563
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u>\$24,107,563</u>	<u>\$13,735,238</u>
<b>SUPPLEMENT DISCLOSURES OF CASH FLOWS INFORMATION:</b>		
Interest expenses paid (excluding amount capitalized)	<u>\$752,200</u>	<u>\$1,106,725</u>
Income tax paid	<u>\$6,353</u>	<u>\$6,644</u>
<b>INVESTING AND FINANCING ACTIVITIES NOT AFFECTING CASH FLOWS:</b>		
Current portion of long-term debt (Note 4)	<u>\$13,830,229</u>	<u>\$7,019,604</u>
Property, plant and equipment transfer to other assets	<u>\$135,769</u>	<u>\$-</u>
Other assets transfer to property, plant and equipment	<u>\$-</u>	<u>\$271,106</u>
Conversion bonds converted into common stock	<u>\$4,216,041</u>	<u>\$465,450</u>

The accompanying notes are an integral part of the financial statements.

CHUNGHWA PICTURE TUBES, LTD.

NOTES TO FINANCIAL STATEMENTS

For The Years Ended December 31, 2004 and 2005

(Expressed in Thousands of New Taiwan Dollars Except Par Value, Shares or Stated Otherwise)

**1. ORGANIZATION AND OPERATIONS**

Chunghwa Picture Tubes, Ltd. (the "Company") was incorporated under the Company Law of the Republic of China (the "ROC") on May 4, 1971. The main activities of the Company include the design, manufacture, sale, installation, maintenance service, import, export and agency service of thin film transistor liquid crystal displays ("TFT-LCD"), color filter ("CF") and related materials, parts and components.

As of December 31, 2004 and 2005, the Company employed 7,718 and 8,777 employees, respectively.

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

*Generally Accepted Accounting Principles*

The financial statements have been prepared in accordance with "Guidelines Governing the Preparation of Financial Report by Securities Issuers" and accounting principles generally accepted in the Republic of China (collectively referred to as "ROC GAAP"). Certain amounts reported in previous year have been reclassified to conform to the 2005 presentation.

*Classification of Current and Noncurrent Assets and Liabilities*

Current assets are those expected to be converted to cash, sold or consumed within one year from the balance sheet date. Current liabilities are obligations due on demand within one year from the balance sheet date. Assets and liabilities that are not classified as current are noncurrent assets and liabilities.

*Foreign Currency Transactions and Translation*

The Company maintains its accounting records in New Taiwan dollars ("NT dollars" or "NT\$"). Transactions denominated in foreign currencies are recorded in NT dollars using the exchange rates in effect at the date of the transactions. Assets and liabilities denominated in foreign currencies are translated into NT dollars using the exchange rates in effect at the balance sheet date. The resulting foreign exchange gains or losses from settlement of such transactions or translations of assets and liabilities are included in statements of operations.

The New Taiwan dollar is performed using exchange rates in effect at the balance sheet date except for stockholders' equity, which is translated at historical exchange rates. Revenue and expense accounts are translated using average exchange rates during the year. Gains and losses resulting from such translations are recorded as cumulative translation adjustment, net of related tax effect, a separate component of

stockholders' equity.

#### Cash Equivalents

The Company classified all highly liquid investments that are readily convertible to cash with insignificant interest rate risk and an original maturity period of three months or less when purchased as cash equivalents.

#### Marketable Securities

Marketable securities are recorded at cost when acquired and are stated at the lower of aggregate cost or market value at the balance sheet date. The amount by which aggregate cost exceeds market value is reported as non-operating expenses in the statements of operations. Subsequent recoveries in market value are recognized as a gain to the extent that the market value does not exceed the original aggregate cost of the investment.

#### Allowance for Doubtful Accounts

The allowance for doubtful accounts is provided based on the aging analysis and results of the Company's evaluation of collectibility of the outstanding notes and accounts receivable.

Account receivable is derecognized while the risks and rewards of accounts receivable have been substantially transferred, including a surrender of control over the accounts receivable.

#### Inventories

Inventories are recorded at cost when acquired and are stated at the lower of aggregate cost or market value. Cost is determined using the weighted-average method. Market value of work-in-process and finished goods is determined on the basis of net realizable value. Market value of raw materials is determined on the basis of replacement cost.

#### Long-term Investments

Investments in which the Company owns 20% or more of the voting shares of investees, or under 20% but is able to exercise significant influence over the investee's operational decisions, are accounted for under the equity method. An impairment loss shall be recognized if the carrying amount of long-term investment using equity method may not be recoverable. Cash dividends received or receivable from equity investees are recorded as a reduction in investment.

When the Company subscribes to additional shares of an investee at a percentage different from its existing equity interest, the resulting difference between the carrying amount of the investment and the amount of the Company's proportionate share in the investee's net equity is recorded as an adjustment to capital reserve. If the capital reserve is not sufficient, then the excess will be charged against retained earnings.

If an equity investee records an addition in capital reserve, the Company will proportionately share the amount and increase its investments and capital reserve accordingly.

The equity method is not required when first and third quarter interim financial statements are prepared for a holding interest of between 20% and 50%.

Investments in which the Company owns less than 20% of the voting shares of investees are stated at cost except for investments in listed companies, which are stated at the lower of aggregate cost or market value, with unrealized loss and subsequent recovery, net of related tax effect, recorded as a separate component of stockholders' equity. However, permanent diminution in the value of an investee is recognized in the statements of operations. Cash dividends received from an investee accounted for under the cost method are recorded as non-operating income.

Stock dividends received are not treated as income. Instead, the number of shares held is increased. When long-term investments are sold, the costs of investments sold are determined using the weighted-average method.

#### Property, Plant and Equipment

Property, plant and equipment are stated at cost plus revaluation increment.

Major renewals and improvements are capitalized, while ordinary maintenances and repairs are expensed as incurred.

Gains or losses from sale or disposal of property, plant and equipment are recorded as non-operating income or expenses.

Depreciation is provided by using the straight-line method over the following estimated useful lives:

Buildings	5 – 60 years
Machinery and equipment	3 – 10 years
Transportation equipment	5 years
Furniture and fixtures	5 years
Miscellaneous equipment	5 – 10 years

Interest incurred on loans used to finance the construction of property, plant and equipment is capitalized and depreciated accordingly.

#### Impairment

Pursuant to SFAS No. 35, the Company assesses indicators for impairment for all its assets within the scope of SFAS No. 35 at each balance sheet date. If impairment indicators exist, the Company shall then compare the carrying amount with the recoverable amount of the assets or the cash-generating unit ("CGU") and write down the carrying amount to the recoverable amount where applicable. Recoverable amount is defined as the higher of fair values less costs to sell and the values in use.

For previously recognized losses, the Company shall assess, at each balance sheet date, whether there is any indication that the impairment loss may no longer exist or may have decreased. If there is any such indication, the Company has to recalculate the recoverable amount of the asset. If the recoverable amount increases as a result of the increase in the estimated service potential of the assets, the Company shall reverse the impairment loss to the extent that the carrying amount after the reversal would not exceed the carrying amount that would have been determined (net of amortization or depreciation) had no impairment loss been recognized for the assets in prior years.

Impairment loss / reversal is classified as non-operating losses / income.

#### Deferred Charges

Deferred charges, including technology license fees, computer software, shadow mask, bond issuance costs, expense of syndication loan application and other charges, are recorded at cost and amortized using the straight-line method over the following useful lives:

- Technology license fees - 5 years or the term of the technology cooperation contract
- Computer software and shadow mask- 3~5 years
- Bond issuance costs - the redemption period or over the period from issuance date to maturity date
- Expense of syndication loan application - the term of syndication loan
- Other charges - 3~5 years

#### Convertible Bonds

The excess of the stated redemption price of the convertible bonds over its par value is recognized as interest expense and interest payable using the interest method during the redemption period. If the bondholders do not exercise the redemption option by the expiry date, the Company should amortize the interest premium, which has been recognized as a liability, over the period from the option expiration to the maturity date of the bonds as a decrease of interest expense.

When the bondholders exercise their conversion rights, the carrying amount of the bonds and related interest payable is transferred to common stock and capital reserve (book value approach). However, if the conversion is an induced conversion, the amount that the market value of the securities given exceeds the market value of the securities, which should be issued according to the original conversion terms, should be recognized as an expense.

Convertible bonds are classified as current liability or long-term liability according to redemption clauses.

#### Deferred Credits

Unrealized intercompany gains and losses are eliminated under the equity method. Profit from sales of depreciable assets between the investee and the Company is amortized and recognized based on the assets' economic service lives. Profit from other types of intercompany transactions is recognized when realized. Unrealized intercompany gains and losses arising from transactions between investees accounted for under the equity method are eliminated in proportion to the multiplication of the Group's ownership percentages; while those arising from transactions between majority-owned subsidiaries are eliminated in proportion to

the Group's ownership percentage in the subsidiary that incurs a gain or loss.

#### Pension and Employee Retirement Plans

For employees under defined benefit pension plan, the net pension cost is computed based on an actuarial valuation in accordance with the provision of SFAS No. 18, which requires consideration of pension cost components such as employee service cost, interest cost, expected return on plan assets and amortization of net transition obligation. The unrecognized net transition obligation is amortized on the straight-line basis over the employees average remaining service period or 15 years.

For employees under defined contribution pension plan, the net pension cost is recorded based on the actual contribution made to the employees' individual pension account.

#### Treasury Stock

When treasury stock is purchased, it is recorded at cost of acquisition. When treasury stock is obtained through donation, it is recorded at market value. If the proceeds from the disposal of treasury stock exceed or less than the carrying value of treasury stock, the differences is credited to or charge against capital reserve from treasury stock transaction. If the capital reserve is not sufficient, then the excess is charged against retained earnings.

If treasury stock is retired, capital stock and additional paid-in capital are proportionately adjusted. If the carrying amount of treasury stock excess the total balance of par value of capital and additional paid-in capital, the excess is debited to capital reserve from treasury stock. If the balance of capital reserve from treasury stock is not sufficient to absorb such deficiency, the remaining is recorded as a reduction of retained earnings. If the carrying amount of treasury stock is less than the total balance of par value of capital and additional paid-in capital, the excess is credited to capital reserve from treasury stock.

Treasury stock is shown as a deduction to stockholders' equity.

#### Stock Compensation

In accordance with interpretations of ROC GAAP, the Company accounted for employee stock options using the intrinsic value method.

Under the intrinsic value method, deferred compensation for options granted to employees is equal to its intrinsic value determined as the difference between the exercise price of the option and the fair value of the underlying stock at the date of grant or amendment. The Company is required to disclose pro forma net income and earnings per share, if employee stock options that are amended or have options grant on or after January 1, 2004, assuming the fair value method had been used.

### Income Tax

The Company adopted an inter-period and intra-period income tax allocation method to recognize income tax. Tax effects on taxable temporary differences are recognized as deferred tax liabilities. Tax effects on deductible temporary differences, operating loss carryforwards and investment tax credits are recognized as deferred tax assets. Valuation allowance is provided based on the expected realization of the deferred tax assets. A deferred tax asset or liability should, according to the classification of its related asset or liability, be classified as current or non-current. However, if a deferred tax asset or liability is not directly related to an asset or liability, then the classification is based on the expected realization date of such deferred income tax asset or liability. The income tax expense or benefit for unrealized losses or gains that are not included in net income for the period, but are reported directly in the stockholders' equity section, should be adjusted directly in stockholders' equity.

Tax credits arising from purchases of machinery, equipment and technology, research and development expenditures, and employee training are recognized in the year that such purchases, expenditures and training occur.

Unappropriated earnings generated after 1997 are subject to a 10% retained earning tax (10% tax) in compliance with the Income Tax Law of R.O.C. The 10% tax is recorded as income tax expense at the time stockholders resolve that the Company's earnings shall be retained.

### Derivative Financial Instruments

Foreign currency forward exchange contracts:

Foreign currency forward exchange contracts entered into to manage currency risks are recorded at the spot rate at the date of inception. The premiums or discounts of the forward exchange contract are amortized over the life of the contract. Gains or losses on these contracts resulting from actual settlement are charged against or credited to statement of operations on the settlement date. At the balance sheet date, the receivables and payables of the foreign currency forward exchange contracts are offset and the resulting balances are recorded as either assets or liabilities. The difference between the spot rate at the date of inception and the spot rate at balance sheet date is reflected in the statement of operations.

Foreign currency option contracts:

Premiums and discounts on option contract are recorded at cost. The gains or losses arising from settlement of such options are recorded in the statement of operations on settlement date. The premiums paid or received for the call or put options are amortized using the straight-line method over the terms of contracts.

Effective from the quarter ended December 31, 2004, in accordance with interpretations of ROC GAAP, the carrying amount of outstanding call or put options at the balance sheet date is accounted for at their fair value and differences between carrying amount and fair value were included in the statement of operations.

Interest rate swap contracts:

No accounting entry is prepared for interest rate swap contracts at the contract date. Upon the settlement of the contract, the actual amount received or paid is credited to or charged against current year income.

Earnings Per Common Share

The Company presents basic earnings per share information. Basic earnings per share is equal to the net income attributable to common stock divided by the weighted-average number of common shares. When calculating diluted earnings per share, the numerator includes or adds back potential common stock dividends, interest and other conversion revenues (expenses). The denominator includes all potentially dilutive common shares.

The weighted-average outstanding shares shall be retroactively adjusted for capital increases arising from transfer of retained earnings, capital reserves and bonuses to employees.

Revenue Recognition

The Company recognizes revenue when the earnings process is complete, as evidenced by an agreement with the customer, transfer of title and acceptance, if applicable, as well as fixed pricing and probable collectibility. Allowance for sales discounts is accrued in the period the sales occur.

Use of Estimates

The preparation of the financial statements in conformity with ROC GAAP requires management to make estimates and assumptions that affect the amounts reported and disclosed in the financial statements and accompanying notes. Actual results could differ materially from those estimates.

**3. ACCOUNTING CHANGES**

Effective from January 1, 2005, the Company adopted ROC Statement of Financial Accounting Standards No. 35 “Accounting for Assets Impairment”. It requires that the Company should assess indicators for impairment for all its assets within the scope of ROC SFAS No. 35 at each balance sheet date. The adoption of ROC SFAS No. 35 did have no material effect on the Company’s financial statements.

**4. DETAILS OF SIGNIFICANT ACCOUNTS BALANCES**

(1) Cash and cash equivalents

	December 31	
	2004	2005
Cash:		
Cash on hand	\$2,701	\$2,769
Cash in banks-checking and savings account	22,601,988	13,732,469
Cash in banks-time deposits	500,969	-
Cash equivalents:		-

ROC Government bonds with resell agreements	1,001,905	-
Total	<u>\$24,107,563</u>	<u>\$13,735,238</u>

(2) Marketable securities

	December 31			
	2004		2005	
	Cost	Market value	Cost	Market value
Open-end mutual funds	<u>\$1,115,499</u>	<u>\$1,128,104</u>	<u>\$363,000</u>	<u>\$372,280</u>

The market value of open-end mutual funds is determined by their net asset value per unit at balance sheet date.

(3) Receivable, net

	December 31	
	2004	2005
Notes receivable	\$49,735	\$3,894
Less: Allowance for doubtful accounts	(400)	-
Net	<u>\$49,335</u>	<u>\$3,894</u>
Accounts receivable-trade	\$9,850,789	\$16,453,233
Less: Allowance for doubtful accounts	(351,000)	(535,319)
Allowance for sales discounts	(657,622)	-
Net	<u>\$8,842,167</u>	<u>\$15,917,914</u>
Due from affiliates-trade	\$3,510,071	\$1,990,164
Less: Allowance for doubtful accounts	(46,000)	(18,500)
Net	<u>\$3,464,071</u>	<u>\$1,971,664</u>

The Company entered into accounts receivable factoring agreements, without recourse, with China Trust Commercial bank and Citibank. Related information with respect to these agreements is as follows:

	December 31	
	2004	2005
Prepaid proceeds from factor	\$722,902	\$1,250,837
Due from factor (Note 1)	127,571	220,736
Amounts derecognized of accounts receivable	<u>\$850,473</u>	<u>\$1,471,573</u>
The range of interest rate of prepaid proceeds	<u>2.48%-4.59%</u>	<u>3.67%-5.13%</u>
Credit line	<u>\$5,000,000</u>	<u>\$6,971,600</u>
Promissory note (Note 2)	<u>\$5,000,000</u>	<u>\$500,000</u>

Note 1: The amount of due from factor was classified as “accounts receivable – others”.

Note 2: The promissory note is issued as the security of future commercial dispute.

(4) Inventories, net

	December 31	
	2004	2005
Raw materials and supplies	\$3,360,413	\$3,210,444
Work in process	1,561,279	2,134,778
Finished goods	1,545,843	4,650,107
Total	6,467,535	9,995,329
Less: Allowance for decline in market value and obsolescence	(291,000)	(178,000)
Net	<u>\$6,176,535</u>	<u>\$9,817,329</u>
Insurance coverage	<u>\$4,170,000</u>	<u>\$6,608,000</u>

(5) Long-term investments

Investee	December 31, 2004	Percentage of ownership or voting rights	December 31, 2005	Percentage of ownership or voting rights
<u>Equity method:</u>				
<u>Unlisted Company</u>				
Chunghwa P.T. (Bermuda) Ltd.	\$26,134,636	100.00	\$25,030,541	100.00
Chunghwa P.T.(Labuan) Ltd.	970,390	41.03	1,060,032	41.03
Shang Chih Investment Co., Ltd.	47,348	25.00	33,835	25.00
Grand Cathay Optronics Co., Ltd.	20,000	100.00	20,000	100.00
Toppa Chunghwa Electronics Co., Ltd.	908,521	30.00	922,516	30.00
Subtotal	<u>28,080,895</u>		<u>27,066,924</u>	
<u>Listed Company</u>				
Forward Electronics Co., Ltd.	419,889	23.16	506,466	22.78
Subtotal	<u>28,500,784</u>		<u>27,573,390</u>	
<u>Lower of aggregate cost or market value:</u>				
<u>Listed Company</u>				
Tatung Co., Ltd.	1,531,059	1.88	1,531,059	1.88
Less: Allowance for loss on decline in market value of long-term investments	(613,361)		(834,184)	
Net	<u>917,698</u>		<u>696,875</u>	
Total	<u>\$29,418,482</u>		<u>\$28,270,265</u>	

On November 14, 2005, the Board of Directors of the Company resolved to invest Xiamen Overseas Chinese Electronic Co., Ltd. via Chunghwa Picture Tubes, (Wujiang) Ltd., or CPT (Wujiang) (a

subsidiary of Chunghwa P.T (Bermuda) Ltd.). Hence, CPT (Wujiang) signed a share transfer contract with the major shareholder of Xiamen Overseas Chinese Electronic Co., Ltd. on December 29, 2005. CPT (Wujiang) will hold 32.64% shares, total amount of 311 million RMB. However, as of December 31, 2005, the transfer still waits for the approvals from the government of P.R.C.

(6) Property, plant and equipment

- a. The Company, in accordance with related regulations of ROC, revalued its property, plant and equipment in 1978, 1979, and 1981. As a result, a total of \$88,005 was added to total assets and \$59,304 (net of reserve for incremental tax on land revaluation of \$28,701) was credited to capital reserve. As of December 31, 2005, the revalued assets amounted to \$57,192.
- b. The insurance coverage over property, plant and equipment as of December 31, 2004 and 2005 amounted to \$86,807,751 and \$167,718,135, respectively.
- c. Interest expense (before deducting capitalized amounts of \$25,380 and \$797,727 in 2004 and 2005, respectively) for the years ended December 31, 2004 and 2005 were \$808,728 and \$2,081,681, respectively. The interest rates of capitalized interest for the years ended December 31, 2004 and 2005 ranged from 0.41% to 5.75 % and 0.41% to 6.30%, respectively.

(7) Deferred charges

	December 31	
	2004	2005
Technology license fees	\$1,205,273	\$992,663
Expense of syndication loan application	185,916	204,980
Bond issuance cost	211,878	61,051
Shadow mask	912,424	1,824,855
Others	49,835	276,475
Total	\$2,565,326	\$3,360,024

(8) Other assets-others

As of December 31, 2005, due to legal restriction of ROC, the Company had not been able to register as the legal owner of certain farmlands (0.347118 hectares; \$35,755 in the amount) purchased by the Company. Accordingly, such lands were temporarily held in trust by third parties. However, in order to protect the Company's interest, the Company has kept control of the sellers' chop, land purchase agreement and the title deeds.

(9) Short-term bank loans

Items	December 31	
	2004	2005

Unsecured loans	\$-	\$1,880,000
Usance L/C loan	7,898,870	1,248,438
Total	<u>\$7,898,870</u>	<u>\$3,128,438</u>
Interest rates	<u>0.41%~5.75%</u>	<u>0.41%~6.10%</u>

(10) Bonds payable

	December 31	
	2004	2005
Convertible Bonds, issued in 2002 and due 2007 at 0.25%	\$1,198,483	\$-
Add: Compensation interest payable	88,089	-
Subtotal	<u>1,286,572</u>	-
Credit Enhanced Zero Coupon Convertible Bonds, issued in 2004 and due 2005	5,719,207	\$-
Add: Premium	86,463	-
Subtotal	<u>5,805,670</u>	-
Credit Enhanced Zero Coupon Convertible Bonds, issued in 2004 and due 2007	6,814,279	7,015,610
Add: Compensation interest payable	11,688	195,539
Subtotal	<u>6,825,967</u>	<u>7,211,149</u>
Less: Current portion of bonds payable	<u>(7,092,242)</u>	-
Bonds payable, net of current portion	<u>\$6,825,967</u>	<u>\$7,211,149</u>

The significant terms of the Convertible Bonds are as follows:

	Convertible Bonds, issued in 2002 and due 2007 at 0.25%	Credit Enhanced Zero Coupon Convertible Bonds, issued in 2004 and due 2005	Credit Enhanced Zero Coupon Convertible Bonds, issued in 2004 and due 2007
· Amount	US\$143.75 million	US\$230 million	US\$213.5 million
· Issue price	100%	103%	100%
· Period	5 years (2002.11.19 to 2007.11.19)	22 months (2004.1.13 to 2005.11.13)	30 months (2004.12.8 to 2007.6.8)
· Place of trading	Luxembourg Stock Exchange	Luxembourg Stock Exchange	Singapore Stock Exchange
· Coupon rate	0.25%	-	-

· Conversion period	Bondholders may convert the bonds to the Company's common shares during a period 30 days after the issuance and 30 days before the maturity. The number of common shares received by the bondholders is determined by dividing the principal amount over conversion price. No cash payment will be made for fractional shares. (The exchange rate is fixed at NT\$34.57 = US\$1)	Bondholders may convert the bonds to the Company's common shares during a period 30 days after the issuance and 30 days before the maturity. The number of common shares received by the bondholders is determined by dividing the principal amount over conversion price. No cash payment will be made for fractional shares. (The exchange rate is fixed at NT\$33.83 = US\$1)	Bondholders may convert the bonds to the Company's common shares during a period 30 days after the issuance and 30 days before the maturity. The number of common shares received by the bondholders is determined by dividing the principal amount over conversion price. No cash payment will be made for fractional shares. (The exchange rate is fixed at NT\$32.371 = US\$1)
		Credit Enhanced Zero	Credit Enhanced Zero
	<u>Convertible Bonds, issued in 2002 and due 2007 at 0.25%</u>	<u>Coupon Convertible Bonds, issued in 2004 and due 2005</u>	<u>Coupon Convertible Bonds, issued in 2004 and due 2007</u>
· Conversion price and adjustment	The conversion price is \$15.53 per share and will be adjusted if number of the Company's common stock changes after the issuance of the bonds.	The conversion price is \$16.46 per share and will be adjusted if number of the Company's common stock changes after the issuance of the bonds.	The conversion price is \$20.25 per share and will be adjusted if number of the Company's common stock changes after the issuance of the bonds. As of December 31, 2005, the conversion price was \$17.91 per share.
· Company's redemption rights	① After 2 years of the issuance of the bonds, the Company may redeem the bonds at 100% of the unpaid principal amount outstanding if the closing price of the Company's common stock on TSE is equal to 125% or above of the conversion price in effect on each trading day for a period of 20 consecutive trading days, or the bonds not yet converted or bought back amounted to US\$5,000 thousand or below.	① After six months of the issuance of the bonds, the Company may redeem the bonds at 100% of the unpaid principal amount outstanding if the closing price of the Company's common stock on TSE is equal to 120% or above of the conversion price in effect on each trading day for a period of 20 consecutive trading days, or the bonds not yet converted or bought back amounted to less than 10% of the aggregate principal amount originally issued.	① After 1 year of the issuance of the bonds, the Company may redeem the bonds at 100% of the unpaid principal amount outstanding if the closing price of the Company's common stock on TSE is equal to 125% or above of the conversion price in effect on each trading day for a period of 20 consecutive trading days, or the bonds not yet converted or bought back amounted to less than 10% of the aggregate principal amount originally issued.

	<p>② The Company may redeem the bonds at 100% of the unpaid principal amount outstanding if there is a change in legislation, resulting in an increase in tax liabilities of the Company.</p> <p>③ The bonds will mature on November 19, 2007 at 117.59% of their principal amount.</p>	<p>② The Company may redeem the bonds at 100% of the unpaid principal amount outstanding if there is a change in legislation, resulting in an increase in tax liabilities of the Company.</p> <p>③ The bonds will mature on November 13, 2005 at 100% of their principal amount .</p>	<p>② The Company may redeem the bonds at 100% of the unpaid principal amount outstanding if there is a change in legislation, resulting in an increase in tax liabilities of the Company.</p> <p>③ The bonds will mature on June 8, 2007 at 105.36% of their principal amount.</p>
	Convertible Bonds, issued in 2002 and due 2007 at 0.25%	Credit Enhanced Zero Coupon Convertible Bonds, issued in 2004 and due 2005	Credit Enhanced Zero Coupon Convertible Bonds, issued in 2004 and due 2007
· Bondholders' option rights	<p>① On January 19, 2004 and the third anniversary of the bonds, the bondholders have the right to require the Company to redeem the bonds at a price equal to 103.84% and 110.19% of the principal amount, respectively.</p> <p>② The bondholders may demand the Company to redeem the bonds if trading of the Company's shares is restricted on the TSE.</p>	<p>① On the first anniversary of the bonds, the bondholders have the right to require the Company to redeem the bonds at a price equal to 100% of the principal amount.</p> <p>② The bondholders may demand the Company to redeem the bonds if trading of the Company's shares is restricted on the TSE.</p>	None.
· Converting status	All bonds have been redeemed on the call options.	All bonds have been repaid on matured.	None.

During the credit enhanced zero coupon convertible bonds repayment period, the financial statements of the Company are required to maintain financial ratios such as current ratio, debt to equity ratio, time interest tangible assets ratio and others as specified in the agreements of bonds payable on annual consolidated basis and semi-annual unconsolidated basis.

As of December 31, 2005, the Company breached one or more of financial covenants as specified in the agreements of bonds payable. The committed bank of bonds payable could request the Company to deposit the sums which were not less than 25% principal amount of the Bonds into account or the sinking account. The Company believes that the Company will be able to obtain waivers and avoid deposit to the sinking account after taking necessary action to remedy the violation.

The Board of Directors resolved to issue overseas zero coupon convertible bonds totaling USD 300 million (revised). As of the date of this report, the ROC Securities Future Bureau (“SFB”) is still reviewing the Company’s application.

(11) Long-term bank loans

	December 31	
	2004	2005
Unsecured loan	\$300,000	\$240,000
Secured syndicate loan	25,155,703	67,108,666
Secured – usance L/C loan	-	1,889,584
Subtotal	<u>25,455,703</u>	<u>69,238,250</u>
Commercial notes payable	-	3,000,000
Less: Unamortized discount of commercial notes payable	-	(65,343)
Subtotal	<u>-</u>	<u>2,934,657</u>
Less: current portion	<u>(6,737,987)</u>	<u>(7,019,604)</u>
Net	<u>\$18,717,716</u>	<u>\$65,153,303</u>
Interest rates	<u>1.79%-3.62%</u>	<u>0.60%~6.30%</u>

- a. Certain of the Company’s syndicate loan agreements require the financial statements of the Company to maintain (1) a current ratio higher than 100%; (2) debt to equity ratio under 125% or 150%; (3) interest coverage over 1.15 or 1.2; and (4) tangible equity more than \$35 billion, \$40 billion, \$60 billion or \$65 billion on annual consolidated basis and semi-annual unconsolidated basis.

As of December 31, 2005, the Company breached one or more of financial covenants which prescribed in the agreements of syndicate loan. The Bank of syndicate loan could prevent the Company from drawing down available funds under the Company’s existing credit facilities. However, the Company believes that the Company will be able to obtain waivers after taking necessary action to remedy the violation.

- b. The long-term bank loans are to be repaid in NT\$ or foreign currency quarterly, or semiannually, or upon maturity before November 2012.
- c. The L/C facility and commercial paper payable is revolving within the credit limit of the syndicate loan. The Company classified the L/C loan and commercial paper payable as long-term bank loans

because the term of the syndicate loan is over 12 months and the Company intends to refinance the syndicate loan.

- d. Certain of the long-term bank loans were jointly guaranteed by the President of the Company. In addition, these loans are secured by the mortgage of the Company's building, machinery and equipment (included prepayment on equipment).

(12) Accrued pension liability and deferred pension cost

- a. Details of pension expense for the years ended December 31, 2004 and 2005 are as follows:

	<u>2004</u>	<u>2005</u>
Defined benefit pension plan	\$248,997	\$299,258
Defined contribution pension plan	-	88,077
Total	<u>\$248,997</u>	<u>\$387,335</u>

- b. Effective from October 1996, as required by the ROC Labor Standard Law, the Company makes monthly contributions to a pension fund at a pre-determined percentage of salaries paid. The pension fund is administered by the employee committee and deposited, in the committee's name, with Central Trust of China, a ROC government entity.

The Labor Pension Act of R.O.C. ("the Act"), which adopts a defined contribution scheme, takes effect from July 1, 2005. In accordance with the Act, employees of the Company may elect to be subject to either the Act, and maintain their seniority before the enforcement of the Act, or the pension mechanism of the Labor Standards Law. For employees subject to the Act, the Company shall make monthly contributions to the employees' individual pension accounts on a basis at 6% of the employees' monthly wages.

- c. Details of net periodic pension cost of the defined benefit pension plan for the years ended December 31, 2004 and 2005 are as follows:

	<u>2004</u>	<u>2005</u>
Employee service cost	\$158,087	\$177,080
Interest cost	54,642	79,752
Expected return on plan assets	(8,088)	(13,139)
Amortization of net transition obligation	33,746	33,746
Amortization of actuarial gain or loss	10,610	21,819
Total	<u>\$248,997</u>	<u>\$299,258</u>

- d. The reconciliation statements of reporting funded status of the defined benefit pension plan as of December 31, 2004 and 2005 are as follows:

	<u>December 31</u>	
	<u>2004</u>	<u>2005</u>
Pension obligation		
Vested	\$216,800	\$187,890

Non-Vested	1,915,577	2,061,026
Accumulated benefit obligation	2,132,377	2,248,916
Additional benefits based on future salaries	526,017	263,601
Projected benefit obligation	2,658,394	2,512,517
Fair value of plan assets	(437,950)	(454,510)
Funded status	2,220,444	2,058,007
Unamortized net transition obligation	(202,475)	(168,729)
Unrealized loss on pension assets	(680,394)	(387,951)
Deferred pension cost	202,475	168,729
Excess of additional pension liability over unrecognized prior service cost	154,376	124,350
Accrued pension liability	1,694,426	1,794,406
Less: current portion	(182,436)	(113,175)
Long-term portion-net of current portion	<u>\$1,511,990</u>	<u>\$1,681,231</u>

The major actuarial assumptions are as follows:

	December 31	
	2004	2005
Discount rate	2.50%	3.00%
Rate of increase in future compensation levels	0.50%	1.00%
Expected long-term rate of return on plan assets	2.50%	3.00%

- e. For the years ended December 31, 2004 and 2005, vested benefits amounted to \$232,052 and \$202,791, respectively.

(13) Deferred credits

- a. As of December 31, 2004 and 2005, the balances of deferred credits were as follows:

	Transaction item			Total
	Inventory	Fixed asset	Stock	
Balance at January 1, 2004	\$363,164	\$42,622	\$942,055	\$1,347,841
Increase (decrease) in unrealized gain (loss)	87,088	(2,589)	-	84,499
Amortized and realized	(148,683)	(7,492)	-	(156,175)
Balance at December 31, 2004	301,569	32,541	942,055	1,276,165
Increase in unrealized gain	68,721	-	-	68,721
Amortized and realized	(165,907)	(7,233)	-	(173,140)
Balance at December 31, 2005	<u>\$204,383</u>	<u>\$25,308</u>	<u>\$924,055</u>	<u>\$1,171,746</u>

- b. The unrealized gain of \$942,055 resulted from the stock transaction between the company and its subsidiaries. The gain was deemed unrealized as its subsidiaries have not disposed the stock.

(14) Capital

- a. The authorized and issued capital of the Company at January 1, 2004 was \$85,000,000 and \$58,908,629 (including 600 million shares reserved for future exercise of stock options), divided into 8,500,000,000 shares and 5,890,862,904 shares, respectively, each at a par value of \$10.
- b. On December 15, 2003, the Board of Directors resolved to increase the capital by 700,000,000 shares by a local offering at a premium price of \$20.6 per share. The effective date of the issuance was May 6, 2004.
- c. On June 16, 2004, the Company's stockholders resolved to increase the authorized capital to \$99,700,000, divided into 9,970,000,000 shares (including 600 million shares reserved for future exercise of stock options), each at par value of \$10. In addition, it was resolved that no earnings of 2003 could be distributed except for appropriations of legal reserve and special reserve.
- d. For the year ended December 31, 2004, the Company issued 261,299,988 shares and 4,253,000 shares for the conversion of the Company's convertible bonds and stock options exercise, respectively. Total outstanding common stock after conversion and exercise was \$68,564,159.
- e. On December 22, 2004, the Board of Directors resolved to increase the capital by issuing GDSs for up to 700,000,000 shares. On June 21, 2005, the Company completed the offering of 28,000,000 unit of GDSs (each unit representing 25 common shares) in Luxembourg stock Exchange.
- f. On May 18, 2005, the Company's stockholders resolved to increase the authorized capital to \$125,000,000 (including 700 million shares reserved for future exercise of stock options), divided into 12,500,000,000 shares, each at par value of \$10. The Board of Directors of the Company also resolved to increase the capital by \$12,000,000 by a local right issue or issuing Global Depository Shares (GDSs). In addition, the stockholders of the Company also resolved to issue new shares by capitalizing retained earnings of \$1,362,016, employee's bonus of \$420,380 and additional paid-in capital of \$4,767,057.
- g. In August, 2005, the Company decided to retire all treasury stock 53,412,000 shares, (\$1,039,743 in the amount) each at a par value of \$10. The Company adjusted decrease proportionately capital stock \$534,120 and paid-in capital \$106,151. The deficiency \$399,472 was recorded as a reduction of capital reserve from treasury stock \$744 first and the remaining amount to decrease retained earning \$398,728. After the retiring, total outstanding common stock was \$81,579,492.
- h. As of December 31, 2005, the Company issued 33,826,625 shares and 20,829,000 shares for the conversion of the Company's convertible bonds and stock options exercise, respectively. Total outstanding common stock after conversion and exercise was \$82,126,048.

(15) Stock compensation

The Company has two stock option plans (2002 plan and 2004 plan). These stock options provide for the granting of options to qualified employees of the Company or any of its domestic or foreign subsidiaries for the purchase of the Company's common shares at the market price of the grant date. Stock options expire in five years from the date granted and vest over service periods that range from two to four years. The Company is authorized to grant options for up to 400,000 thousand shares and 233,982 thousand shares under the 2002 plan and 2004 plan, respectively.

- a. A summary of the Company's stock option activity and the related information for the years ended December 31, 2004 and 2005 is shown below:

	2004			
	2002 plan		2004 plan	
	Options (in thousand shares)	Weighted-Average Exercise Price (in dollars)	Options (in thousand shares)	Weighted-Average Exercise Price (in dollars)
Outstanding, beginning of period	218,041	\$12.45	-	\$-
Granted	-	-	186,170	16.11
Exercised	(4,253)	13.35	-	-
Forfeited	(15,721)	12.35	(7,125)	16.69
Outstanding, end of period	<u>198,067</u>	12.44	<u>179,045</u>	16.09

  

	2005			
	2002 plan		2004 plan	
	Options (in thousand shares)	Weighted-Average Exercise Price (in dollars)	Options (in thousand shares)	Weighted-Average Exercise Price (in dollars)
Outstanding, beginning of period	198,067	\$12.44	179,045	\$16.09
Granted	-	-	46,430	12.30
Exercised	(20,829)	11.96	-	-
Forfeited	(9,725)	11.59	(15,905)	14.53
Outstanding, end of period	<u>167,513</u>	11.03	<u>209,570</u>	13.47

- b. Information with respect to the outstanding options of the Company's as of December 31, 2004 and 2005 is as follows:

2004	
Outstanding options at balance sheet date	Options Exercise

	Date of Approval	Range of Exercise Price (in dollars)	Options (in thousand shares)	Weighted-Average Remaining Contractual Life (in years)	Weighted-Average Exercise Price (in dollars)	Number of Exercisable Options (in thousand shares)	Weighted-Average Exercise Price (in dollars)
2002 plan	May 14, 2002	\$11.90-\$13.35	198,067	1.75	\$12.44	37,098	\$13.35
2004 plan	April 29, 2004	\$14.55-\$17.10	179,045	3.40	16.09	-	-
2005							
				Outstanding options at balance sheet date		Options Exercise	
	Date of Approval	Range of Exercise Price (in dollars)	Options (in thousand shares)	Weighted-Average Remaining Contractual Life (in years)	Weighted-Average Exercise Price (in dollars)	Number of Exercisable Options (in thousand shares)	Weighted-Average Exercise Price (in dollars)
2002 plan	May 14, 2002	\$10.50-\$11.80	167,513	0.74	\$11.03	100,970	\$11.16
2004 plan	April 29, 2004	\$10.80-\$15.00	209,570	2.55	13.47	-	-

- c. Pro forma net income (loss) and earnings per share are disclosed below as if the Company had accounted for its employee stock options under the fair value method.

	2004 (Note)	2005
Net income (loss) as reported (in thousands)	\$10,321,883	\$(7,352,301)
Pro forma net income (loss) (in thousands)	\$10,107,849	\$(7,730,884)
Basic earnings (loss) per share as reported (in dollars)	\$1.45	\$(0.94)
Pro forma basic earnings (loss) per share (in dollars)	\$1.43	\$(0.99)
Diluted earnings (loss) per share as reported (in dollars)	\$1.29	\$(0.94)
Pro forma diluted earnings (loss) per share (in dollars)	\$1.26	\$(0.99)

(Note: All shares have been adjusted retroactively)

The fair value of these options is calculated at the date of grant using the Black-Scholes option pricing model with the following weighted-average assumptions for the years ended December 31, 2004 and 2005, respectively:

2004	2005
------	------

Dividend yield:	-	3.84%
Expected volatility:	49.41%	37.86%
Risk-free interest rate:	1.00%	1.00%
Expected life:	5 years	5 years

Compensation cost recognized for the years ended December 31, 2004 and 2005 was nil, respectively. Had the Company used the fair value method to account for its stock options, compensation cost for the years ended December 31, 2004 and 2005 would have been \$214,034 and \$378,583, respectively.

(16) Capital Reserve

According to the ROC Company Law, additional paid-in capital and capital reserve can only be used for offsetting accumulated deficits or distribution of stock dividends. The Company cannot use additional paid-in capital or capital reserve to offset accumulated deficits unless the legal reserve is insufficient for offsetting such deficits.

(17) Legal Reserve

According to the ROC Company Law the Company must retain at least 10% of its annual earnings as legal reserve until such reserve equals the amount of capital. Once the legal reserve equals one-half of the paid-in capital, 50% of the reserve may be transferred to common stock. The legal reserve can be used to offset deficits.

(18) Special reserve

In accordance with the ROC Securities Future Bureau (SFB) regulations, a special reserve must be provided for unrealized losses on long-term investments, excess of additional pension liability over unrecognized prior service cost and cumulative translation adjustment that are accounted for as deductions to stockholders' equity. Once the aforementioned deductions to stockholders' equity are reversed, the related reserve can be reversed to distributable earnings.

(19) Distributions of earnings

Pursuant to the Company's Articles of Incorporation, current year's earnings before tax, if any, shall be distributed in the following order:

- (a) payment of all taxes;
- (b) offset of prior years' operation losses;
- (c) set aside 10% of the remaining amount after deducting (a) and (b) as legal reserve;
- (d) set aside special reserve in accordance with regulation prescribed by the ROC's SFB or reverse special reserve previously provided; and

(e) after deduction of items (a), (b), (c) and (d) from current year's earnings, the remaining is allocated as follows: 5%-10% as employees' bonus, and 90%-95% as distributable earnings.

The Company is engaged in high-tech industry and the cycle of high-tech industry is experiencing the stage of growth. In order to expand scale and improve its strength to compete with other major companies in the world, the Company adopts a policy of residual dividends. The Company shall base its budget on capital expenditures and the demands of the fund, taking into account the balance of retained earnings, to determine dividends or bonuses provided; however, cash dividends shall not be less than 100% of the sum of the on stock dividend and cash dividend.

The appropriations of earnings of 2003 and 2004 were approved in stockholders' meeting on June 16, 2004 and May 18, 2005, respectively. The appropriations of earnings and dividend per share were as follows:

	For fiscal year 2003		For fiscal year 2004	
	Appropriation of earnings	Dividend per share	Appropriation of earnings	Dividend per share
Legal reserve	\$93,996	\$-	\$1,031,772	\$-
Special reserve	845,962	-	2,279,679	-
Common stock-in cash	-	-	4,086,049	0.60
Common stock-in stock	-	-	1,362,016	0.20
Bonus to employees -in stock	-	-	420,380	-
Bonus to employees -in cash	-	-	280,246	-

If the above bonus paid to employees-in stock had been paid entirely in cash and charged against earnings for 2004, the basic and diluted earnings per share (before adjusted retroactively) would have decreased from \$1.58 to \$1.48 and \$1.39 to \$1.30. Formula for the calculation of the EPS is as follows:

$$\frac{\text{Net income of 2004} - \text{Employee cash bonus} - \text{Employee stock bonus} - \text{Directors and supervisors' bonus}}{\text{Average weighted number of shares of 2004}}$$

On July 1, 2005, the Board of Directors resolved to change the above type and monetary amount of dividend distribution for 2004 due to adjust from issuance of GDSs, conversion of convertible bonds and exercising of stock option plans as follows:

	(Unit: per share in dollars)	
	Original	After change
Cash dividend	\$0.60	\$0.5407
Stock dividend	0.20	0.1802

The information relating to earnings distribution (or makeup of accumulated deficits) is accessible on the website of "Market observation post system" (<http://newmops.tse.com.tw>) of TSE.

(20) Treasury stock

- a. The Company repurchased its own shares from open market. The purpose and ending balances of treasury stock were as follows:

Purpose	Number of Shares Repurchased			
	Beginning	Addition	Disposal	Ending
<u>2004</u> In thousands of share				
Future issuance to employees as bonuses	53,412	-	-	53,412
<u>2005</u>				
Future issuance to employees as bonuses	53,412	-	53,412	-

- b. Pursuant to the resolution of the Board of Directors meeting of the Company in 2000 and 2002, the Company has repurchased its common stock totalling 104,463 thousand shares (\$2,197,987 in the amount), of which 51,051 thousand shares (\$1,158,244 in the amount) have been transferred to employees. The remaining treasury stock 53,412 thousand shares (\$1,039,743 in the amount) were all retired on August 31, 2005, resulting in a reduction of capital stock amounting to \$534,120.

(21) Operating revenue

	2004	2005
TFT-LCD (larger size)	\$73,370,037	\$73,987,901
TFT-LCD (smaller / medium size)	296,028	2,580,694
Others	4,750,684	1,889,755
Total	\$78,416,749	\$78,458,350

(22) Personnel, depreciation and amortization expenses

	2004			2005		
	Operating cost	Operating expenses	Total	Operating cost	Operating expenses	Total
Personnel expenses:						
Salaries	\$4,094,487	\$776,254	\$4,870,741	\$4,672,740	\$883,460	\$5,556,200
Staff labor/health insurance	229,258	38,336	267,594	294,967	50,943	345,910
Pension	205,113	43,884	248,997	333,209	54,126	387,335
Depreciation	9,019,410	188,302	9,207,712	13,928,941	355,470	14,284,411

Amortization	9,262	714,794	724,056	70,211	927,685	997,896
--------------	-------	---------	---------	--------	---------	---------

(23) Income tax

- a. The ROC income tax authorities have assessed the income tax returns of the Company through 2003 except for 2001.
- b. There is no taxation charge on the profit of the Company and certain operating subsidiaries due to the following:
- ① The Company is entitled to an income tax exemption for a period of five consecutive years for the income generated by sales of its TFT-LCD.

The following are details of the Company's effective tax exemption periods:

Tax exemption products	Tax exemption period
TFT-LCD	2002~2006
TFT-LCD	2004~2008

- ② The Company obtained the approval letter for claiming tax exemption in respect of setting its headquarters in Taiwan.
- c. The provision for income tax expenses consists of the following:

	2004	2005
Income tax-current	\$-	\$-
Income tax-deferred		
Net change in deferred income tax assets (liabilities):		
Investment tax credits	423,239	2,632,162
Operating loss carryforwards	(25,686)	1,973,196
Temporary differences	319,431	(13,169)
Valuation allowances	(964,546)	(4,592,189)
Prior year adjustment	-	(55,736)
Income tax expenses	<u>\$(247,562)</u>	<u>\$(55,736)</u>

- d. Significant components of the Company's deferred tax assets and liabilities at fiscal year-ends are as follows:

Components	December 31	
	2004	2005
Deferred tax assets:		
Allowance for bad debts	\$65,488	\$92,337

Employees' welfare fund	520	-
Deferred pension expense	263,443	306,775
Unrealized loss on foreign currency exchange, net	27,444	254,261
Unrealized loss on decline in market value and obsolescence of inventory	72,750	44,500
Unrealized intercompany losses	83,528	57,422
Unrealized loss on long-term investments of overseas investee company	594,984	625,683
Investment tax credits	5,652,815	8,284,977
Operating loss carryforwards	1,576,859	3,550,055
Compensation interest payable	133,965	45,017
Allowance for sales discounts	164,405	-
Cumulative translation adjustment	187,995	-
Others	7,750	5,812
Valuation allowance	(6,845,824)	(11,438,013)
	<u>\$1,986,122</u>	<u>\$1,828,826</u>

Deferred tax liabilities:

Overseas investment income accounted for under the equity method	\$(2,502,445)	\$(2,502,445)
Cumulative translation adjustment	-	(103,859)
	<u>\$(2,502,445)</u>	<u>\$(2,606,304)</u>

	December 31	
	2004	2005
e. Deferred tax assets-current	\$2,770,128	\$1,098,368
Valuation allowance-current	(2,742,684)	(1,098,368)
Deferred tax assets-net-current	<u>\$27,444</u>	<u>-</u>

	December 31	
	2004	2005
f. Deferred tax assets-non-current	\$6,061,818	\$12,168,471
Valuation allowance-non-current	(4,103,140)	(10,339,645)
Deferred tax assets-net-non-current	1,958,678	1,828,826
Deferred tax liabilities-non-current	(2,502,445)	(2,606,304)
Net deferred tax liabilities-non-current	<u>\$(543,767)</u>	<u>\$(777,478)</u>

g. Details of unused investment tax credits and tax operating loss carryforwards are as follows:

Regulation of ROC	Tax credit item	tax credit	Unused tax credit	Expiration year
-------------------	-----------------	------------	----------------------	--------------------

Statute for Upgrading Industries	Investment tax credit in production equipment	\$4,351,764	\$4,351,764	2009
		136,267	136,267	2008
		1,496,593	1,496,593	2007
		198,558	198,558	2006
		<u>\$6,183,182</u>	<u>\$6,183,182</u>	
Statute for Upgrading Industries	Investment tax credit in research and development expenditure, employee training expenditure	\$441,814	\$441,814	2009
		620,032	620,032	2008
		531,237	531,237	2007
		508,712	508,712	2006
		<u>\$2,101,795</u>	<u>\$2,101,795</u>	
Income tax Law	Tax loss carryforwards	\$1,997,837	\$1,997,837	2010
		142,471	142,471	2008
		94,509	94,509	2007
		1,315,238	1,315,238	2006
		<u>\$3,550,055</u>	<u>\$3,550,055</u>	

h. The integrated income tax information of the Company is as follows:

	December 31	
	2004	2005
Imputation credit account (ICA)	\$3,353	\$3,638

The actual or expected creditable ratios for earnings distribution to ROC resident stockholders in 2004 and 2005 are 0.03% and nil, respectively.

i. Unappropriated earnings as of December 31, 2004 and 2005 are as follows:

	December 31	
	2004	2005
Unappropriated earnings (accumulated deficits)	\$10,317,715	\$(6,898,965)

(24) Earnings (loss) per common share

The following table sets forth the computation of the Company's basic and diluted earnings (loss) per common share:

	Amount	
	2004	2005
Numerator:		
Net income (loss) available to common stockholders	\$10,321,883	\$(7,352,301)
Net income available to common stockholders and diluted potential common shares	\$10,325,111	
	Shares (Unit:thousands)	
	2004	2005
Denominator:		
Denominator for basic income per share-weighted average share (in thousands)	7,084,035	7,807,278
Denominator for diluted income per share-weighted average share (in thousands)	8,000,972	
	Amount	
	2004	2005
Basic earnings (loss) per common share (in dollars)	\$1.45	\$(0.94)
Diluted earnings per common share (in dollars)	\$1.29	

(Note: All shares have been adjusted retroactively)

The Company did not present diluted earning per common share for the year ended December 31, 2005 as it reported loss from continuing operations for the same period.

(25) Technical cooperation agreement

<u>Contracting party</u>	<u>The term of the contract</u>	<u>The content of repayment</u>
<u>Technology Agreement</u>		
<u>TFT-LCD</u>		
Hitachi	January 2003   December 2010	1. The Company is required to pay licensing fees on installment basis for using the technologies. 2. The Company is required to pay royalty fees based on a pre-determined percentage of net sales of the related products for continuing use of exclusive technology.
Advanced Display Inc. (ADI)	April 1997   July 2006	1. The Company is required to pay licensing fees on installment basis for using the technologies. 2. The Company is required to pay royalty fees based on a pre-determined percentage of net sales of the related products for continuing use of exclusive technology. 3. ADI has the right to purchase no more than 15% of the total products from the Company at 90% of the average selling price. The Company bears the shipping costs of the products to locations designated by ADI.
Sharp Corporation	January 2002   December 2006	1. The Company is required to pay licensing fees (one time payment) for using the technologies. 2. The Company is required to pay royalty fees based on a pre-determined percentage of net sales of the related products for continuing use of exclusive technology.
Semiconductor Energy Laboratory Co., Ltd. (SEL)	January 2004   December 2008	1. The Company is required to pay licensing fees on installment basis for using the technologies. 2. The Company is required to pay royalty fees based on a pre-determined percentage of net sales of the related products for continuing use of exclusive technology.
Industrial Technology Research Institute (ITRI)	May 2002   May 2009	The Company is required to pay licensing fees on installment basis for using the technologies.
Mitsubishi Electric Corporation and Advanced Display Inc.	November 2002	The Company is required to pay licensing fees on installment basis for using the technologies.
Hewlett - Packard Development Company, L.P. (HP)	February 2004	The Company is required to pay licensing fees on installment basis for using the technologies.
<u>Purchase Agreement</u>		
Corning Display Technologies Taiwan Co., Ltd ("Corning	April 2005 	1. Corning Taiwan will guarantee to supply materials of TFT-LCD to the Company for 6 generation fabrication.

Taiwan”)

March 2011 2. The Company is required to make prepayments on installment basis to Corning Taiwan to deductible from subsequent purchase.

## 5. RELATED PARTY TRANSACTIONS

(1) Name and relationship:

<u>Name of related party</u>	<u>Relationship with the Company</u>
Tatung Co., Ltd.	The Company's major stockholder and represented on the Company's board of directors
Forward Electronics Co., Ltd.	An investee accounted for under the equity method
Toppan Chunghwa Electronics Co., Ltd.	An investee accounted for under the equity method
Tatung Chungai Precious Metals Co., Ltd.	Subsidiary of Tatung Co., Ltd.
Tatung Atherton Co.	Subsidiary of Tatung Co., Ltd.
Taiwan Telecommunication Industry Co., Ltd.	Subsidiary of Tatung Co., Ltd.
Tatung Fine Chemical Co., Ltd.	Subsidiary of Tatung Co., Ltd.
Shang Chih International Express Co., Ltd.	Subsidiary of Tatung Co., Ltd.
Tatung-Fanuc Robotics Company	Subsidiary of Tatung Co., Ltd.
Tatung Co. of Japan, Inc.	Subsidiary of Tatung Co., Ltd.
Tatung (U.K.) Ltd.	Subsidiary of Tatung Co., Ltd.
Tatung (Thailand) Co., Ltd.	Subsidiary of Tatung Co., Ltd.
Tatung Co. of America, Inc.	Subsidiary of Tatung Co., Ltd.
Tatung Consumer Products (Taiwan) Co., Ltd.	Subsidiary of Tatung Co., Ltd.
Tatung Electronics (Singapore) Pte Ltd.	Subsidiary of Tatung Co., Ltd.
Tatung System Technology Inc.	Subsidiary of Tatung Co., Ltd.
Toes Opto-Mechatronics Co.	Subsidiary of Tatung Co., Ltd.
Tatung OTIS Elevator Co., Ltd.	An investee of Tatung Co., Ltd. accounted for under the equity method
Kuender Company Co., Ltd.	An investee of Tatung Co., Ltd. accounted for under the equity method
Tatung Okuma Co., Ltd.	An investee of Tatung Co., Ltd. accounted for under the equity method
Tatung Telecom Corporation	An investee of Tatung Co., Ltd. accounted for under the equity method
TIS Net Technology Inc.	Subsidiary of subsidiary of Tatung Co., Ltd.
Tatung Information Technology (Jiang Su) Co., Ltd.	Subsidiary of subsidiary of Tatung Co., Ltd.
Chunghwa P.T. (Bermuda) Ltd.	A subsidiary of the Company
Chunghwa P.T. (Labuan) Ltd.	A subsidiary of the Company's subsidiary
Chunghwa P.T. (Malaysia) Sdn. Bhd.	A subsidiary of the Company's subsidiary
Chunghwa P.T. (U.K.) Ltd.	A subsidiary of the Company's subsidiary
CPTF Optronics Co., Ltd.	A subsidiary of the Company's subsidiary
Chunghwa P.T. (Wujiang) Ltd.	A subsidiary of the Company's subsidiary
Dalemont Investment Ltd.	A subsidiary of the Company's subsidiary
Daliant Investment Ltd.	A subsidiary of the Company's subsidiary
Bangalor Investment Ltd.	A subsidiary of the Company's subsidiary
Bensaline Investment Ltd.	A subsidiary of the Company's subsidiary
Chunghwa P.T. Display Technology (Fujian) Ltd.	A subsidiary of the Company's subsidiary
Chunghwa P.T. Display technology (Shen-Zhen) Ltd.	A subsidiary of the Company's subsidiary
CPT TPV Optical Co., Ltd.	A subsidiary of the Company's subsidiary
CPTF Visual Display (Fuzhou) Ltd.	A subsidiary of CPTF Optronics Co., Ltd.
Chunghwa P.T. (Kampar) Sdn. Bhd.	A subsidiary of Chunghwa P.T. (Malaysia) Sdn. Bhd.
Makolin Electronics (M) Sdn. Bhd.	The Company's affiliated company accounted for under the equity method
Fujian Fujia Electronics Co., Ltd.	The Company's affiliated company accounted for under the equity method
Jean Co., Ltd.	Chairman is one of the immediate family members of the Company's chairman

Jeffrey Investment Ltd.  
K-tronics, Inc.  
Jean (M) Sdn. Bhd., Malaysia  
Tatung University  
Lin, Cheng-Hon

Subsidiary of Jean Co., Ltd.  
Subsidiary of subsidiary of Jean Co., Ltd.  
Subsidiary of Jean Co., Ltd.  
The major stockholder of Tatung Co., Ltd.  
Chairman of Board of Directors and President of the Company

(2) Significant transactions with related parties:

a. Operating revenue

Name of Related Party	2004		2005	
	Amount	%	Amount	%
Chunghwa P.T. (Labuan) Ltd.	\$2,932,953	3.74	\$2,547,602	3.25
Tatung Information Technology (Jiang Su) Co., Ltd.	8,668,768	11.05	2,950,756	3.76
Jeffrey Investment Ltd.	1,627,984	2.08	2,159,896	2.75
K-tronics, Inc.	6,045,243	7.71	2,307,603	2.94
Others	735,170	0.94	746,742	0.95
Total	<u>\$20,010,118</u>	<u>25.52</u>	<u>\$10,712,599</u>	<u>13.65</u>

There are no significant differences between prices to related parties and prices to ordinary customers. The comparison of collection terms between related parties and ordinary customers is as follows:

Region	2004		2005	
	Related party	Ordinary customers	Related party	Ordinary customers
Overseas	O/A 90-120 days	Cash payment with 30 to 65 days L/C with 30 to 60 days At sight payment	O/A 90-120 days	Cash payment with 30 to 65 days L/C with 30 to 60 days At sight payment
ROC Domestic	O/A 90-120 days	Cash payment with 30 to 60 days At sight payment	O/A 60-120 days	Cash payment with 30 to 60 days At sight payment

b. Purchases

Name of Related Party	2004		2005	
	Amount	%	Amount	%
Chunghwa P.T. (Labuan) Ltd.	\$21,629,451	39.78	\$22,898,475	37.26
Others	131,410	0.24	190,920	0.31
Total	<u>\$21,760,861</u>	<u>40.02</u>	<u>\$23,089,395</u>	<u>37.57</u>

There are no significant differences between purchase prices from related parties and purchase prices from ordinary suppliers. The comparison of terms of payment between related parties and

ordinary suppliers is summarized as follows:

<u>Region</u>	2004		2005	
	<u>Related party</u>	<u>Ordinary suppliers</u>	<u>Related party</u>	<u>Ordinary suppliers</u>
Overseas	T/T 30 to 180 days	L/C, T/T 30 to 180 days	T/T 30 to 360 days	T/T 30 to 360 days L/C 30 to 180 day
ROC Domestic	30 to 60 days after QC	30 to 150 days after QC	30 to 60 days after QC	30 to 180 days after QC

c. Fixed asset addition

<u>Name of Related Party</u>	2004		2005	
	<u>Amount</u>	<u>%</u>	<u>Amount</u>	<u>%</u>
Tatung Co., Ltd.	\$509,098	0.94	\$277,430	0.49
Tatung System Technology Inc.	75,053	0.14	154,910	0.27
Toes Opto-Mechatronics Co.	-	-	326,770	0.57
Others	86,630	0.15	109,240	0.19
Total	<u>\$670,781</u>	<u>1.23</u>	<u>\$868,350</u>	<u>1.52</u>

d. Expenditures

<u>Name of Related Party</u>	2004		2005	
	<u>Amount</u>	<u>%</u>	<u>Amount</u>	<u>%</u>
Toppan Chunghwa Electronics Co., Ltd.	\$14,910	0.08	\$1,464	0.01
Chunghwa P.T. (Labuan) Ltd.	35,055	0.18	144,391	0.55
Tatung Co., Ltd.	51,340	0.26	31,930	0.12
Tatung Co. of Japan, Inc.	8,095	0.04	6,024	0.02
Tatung System Technology Inc.	12,129	0.06	8,437	0.03
Others	8,704	0.05	11,363	0.04
Total	<u>\$130,233</u>	<u>0.67</u>	<u>\$203,609</u>	<u>0.77</u>

(1) The above expenditure incurred in connection with the purchase of materials, products or services from related parties.

(2) The Company purchased certain raw material, components and equipments from Japan through Tatung Co. of Japan, Inc., which charges the Company commissions for such services. The total raw material and equipments purchased through Tatung Co. of Japan, Inc. amounted to \$7,508,679 and \$5,291,615 for the years ended on December 31, 2004 and 2005, respectively.

The commission charged, included in the aforementioned purchase amount, amounted to \$8,095 and \$6,024 for the corresponding periods, respectively.

e. Fixed asset disposal

Name of Related Party	2004			2005		
	Selling price	Carrying amount	Gain (Loss) on sale of fixed asset	Selling price	Carrying amount	Loss on sale of fixed asset
Chunghwa P.T. (Labuan) Ltd.	\$4,167	\$6,779	\$(2,612)	\$27,203	\$27,447	\$(244)
Chunghwa P.T. (Malaysia) Sdn. Bhd.	913	913	-	-	-	-
Chunghwa P.T. (Kampar) Sdn. Bhd.	718	695	23	-	-	-
Tatung Co., Ltd.	790	790	-	-	-	-
Total	<u>\$6,588</u>	<u>\$9,177</u>	<u>\$(2,589)</u>	<u>\$27,203</u>	<u>\$27,447</u>	<u>\$(244)</u>

f. Non-operating income-others

Name of Related Party	2004		2005	
	Amount	%	Amount	%
Chunghwa P.T. (Malaysia) Sdn. Bhd.	\$2,479	0.89	\$2,584	0.47
Chunghwa P.T. (Labuan) Ltd.	2,883	1.04	3,756	0.69
Chunghwa P.T. (Kampar) Sdn. Bhd.	1,793	0.65	434	0.08
Tatung Co., Ltd.	2,768	1.00	1,985	0.36
Others	136	0.05	322	0.06
Total	<u>\$10,059</u>	<u>3.63</u>	<u>\$9,081</u>	<u>1.66</u>

g. Due from affiliates-trade, net

Name of Related Party	December 31			
	2004		2005	
	Amount	%	Amount	%
Tatung Co., Ltd.	\$79,886	2.28	\$108,117	5.43
Chunghwa P.T. (Labuan) Ltd.	344,639	9.82	108,545	5.45
Tatung Information Technology (Jiang Su) Co., Ltd.	1,912,107	54.47	963,395	48.41
Jeffrey Investment Ltd.	1,032,211	29.41	355,563	17.87
K-tronics, Inc.	78,236	2.23	413,856	20.80
Others	62,992	1.79	40,688	2.04
Total	<u>3,510,071</u>	<u>100.00</u>	<u>1,990,164</u>	<u>100.00</u>
Less: Allowance for doubtful accounts	<u>(46,000)</u>		<u>(18,500)</u>	
Net	<u>\$3,464,071</u>		<u>\$1,971,664</u>	

h. Due from affiliates - others

Name of Related Party	December 31			
	2004		2005	
	Amount	%	Amount	%
Chunghwa P.T. (Bermuda) Ltd.	\$8,393	47.20	\$751,104	99.19
Toppan Chunghwa Electronics Co., Ltd.	4,291	24.13	5,863	0.77
Chunghwa P.T. (Labuan) Ltd.	4,211	23.68	200	0.03
Others	888	4.99	48	0.01

Total	\$17,783	100.00	\$757,215	100.00
-------	----------	--------	-----------	--------

i. Due to affiliates - trade

Name of Related Party	December 31			
	2004		2005	
	Amount	%	Amount	%
Tatung Co. of Japan, Inc.	\$4,161,731	52.19	\$2,338,628	20.30
Chunghwa P.T. (Labuan) Ltd.	3,749,282	47.02	9,051,851	78.58
Others	62,995	0.79	128,819	1.12
Total	\$7,974,008	100.00	\$11,519,298	100.00

j. Due to affiliates - others

Name of Related Party	December 31			
	2004		2005	
	Amount	%	Amount	%
Tatung Co., Ltd.	\$253,248	15.52	\$97,644	15.38
Tatung Co. of Japan, Inc.	1,205,647	73.88	310,753	48.94
Chunghwa P.T. (Labuan) Ltd.	7,952	0.49	86,863	13.68
Others	164,974	10.11	139,716	22.00
Total	\$1,631,821	100.00	\$634,976	100.00

k. Other current liabilities

Name of Related Party	December 31			
	2004		2005	
	Amount	%	Amount	%
Chunghwa P.T. (Labuan) Ltd.	\$2,213	1.02	\$29	0.02
Jean Co., Ltd.	3,552	1.63	2,740	1.71
Others	2,011	0.92	213	0.13
Total	\$7,776	3.57	\$2,982	1.86

l. Deferred credits

Name of Related Party	December 31			
	2004		2005	
	Amount	%	Amount	%
Chunghwa P.T. (Malaysia) Sdn. Bhd.	\$99,849	7.82	\$48,172	4.11
Chunghwa P.T. (Labuan) Ltd.	227,648	17.84	175,560	14.98
Chunghwa P.T. (Bermuda) Ltd. and Dalemont Investment Ltd. etc.	942,055	73.82	942,055	80.40
Chunghwa P.T. (Kampar) Sdn. Bhd.	6,613	0.52	5,959	0.51
Total	\$1,276,165	100.00	\$1,171,746	100.00

m. Guarantees

The amount of guarantees that the Company provided for related parties as of December 31, 2004 and 2005 is as follows:

(Unit: in thousand dollars)

Name of Related Party	December 31		Purpose
	2004	2005	
Chunghwa P.T. (Bermuda) Ltd.	USD82,000	USD78,000	Working Capital
CPTF Optronics Co., Ltd.	USD16,900	-	Working Capital
Chunghwa P.T. (Labuan) Ltd.	USD45,000	-	Working Capital
Toppan Chunghwa Electronics Co., Ltd.	NTD330,000	NTD330,000	Working Capital
Chunghwa P.T. (Wujiang) Ltd.	USD10,000	-	Working Capital

- n. The Company leased portions of its plants to Toppan Chunghwa Electronics Co., Ltd. Those generated rental revenue of \$16,979 and \$18,890 for the years ended December 31, 2004 and 2005, respectively. The related receivables (recorded in due from affiliates-others) were \$4,291 and \$5,863 as of December 31, 2004 and 2005, respectively. In addition, the Company charged Toppan Chunghwa Electronics Co., Ltd. management fees of \$31,685 and \$46,367 for the years ended December 31, 2004 and 2005, respectively, which were recorded as a deduction of expenditure.
- o. In order to integrate education-industry for research and development, the Company contributed a donation of about two hundreds of million to Tatung University in 2004.
- p. The Company received royalty fees from Chunghwa Picture Tubes (Bermuda) Ltd. amounted to \$212,410 in 2005. The related receivables (recorded in due from affiliates-others) were \$107,210 as of December 31, 2005.

## 6. ASSETS PLEDGED OR MORTGAGED

As of December 31, 2004 and 2005, the following assets were mortgaged to several banks, customs and government agencies as collateral for bank loans, credit facilities and other purposes:

Accounts	Creditors	Carrying amount	
		December 31	
		2004	2005
Building	Chiao Tung Bank	\$2,012,125	\$2,423,714
Machinery and equipment	Chiao Tung Bank	15,991,060	11,564,800
Building	Bank of Taiwan	1,498,253	1,451,222
Machinery and equipment & prepayment on equipment	Bank of Taiwan	9,256,676	58,285,260
Machinery and equipment & prepayment on equipment	China Trust Commercial Bank	-	13,090,677
Prepayments on equipment	Taiwan Cooperative Bank	-	9,044,320
Pledged time deposit	Bank of Taiwan		200,000
Pledged time deposit	General office of the customs-Keelung, ROC	12,679	12,778
Pledged time deposit	General office of the customs-Taipei, ROC	171,255	144,875
Pledged time deposit	Hua Nan Commercial Bank	3,850	-
Pledged time deposit	Chiao Tung Bank	1,542,885	-

Pledged time deposit	Bank of Taiwan	310,073	34,697
		<u>\$30,798,856</u>	<u>\$96,252,343</u>

## 7. COMMITMENTS AND CONTINGENCIES

- A. The Company's unused letters of credit were approximately USD 21,074 thousand, JPY 3,285,015 thousand, CHF 790 thousand and EUR 256 thousand as of December 31, 2005.
- B. Besides the guarantees disclosed in Note 5 (2) m, the Company issued promissory notes as of December 31, 2005 as follows:

Item	Amount (in thousands)	
Notes for bank loans	NTD	56,865,850
	USD	298,000
Guarantee notes for account receivable factoring	NTD	500,000

- C. The Company signed several construction contracts for the expansion of its factory space. As of December 31, 2005, these construction contracts have amounted to \$117,928,650 with \$29,127,977 remaining unpaid.

## 8. SIGNIFICANT DISASTER LOSS

NONE.

## 9. SIGNIFICANT SUBSEQUENT EVENTS

NONE.

## 10. SEGMENT INFORMATION

### (1) Industrial information

The related information for 2004 and 2005 is as follows:

#### 2004

	TFT-LCD	Other	Total
Total revenues	<u>\$73,707,863</u>	<u>\$4,708,886</u>	<u>\$78,416,749</u>
Gross profit (loss)	<u>\$11,979,005</u>	<u>\$(1,253,916)</u>	<u>\$10,725,089</u>
Unrealized intercompany profit			61,595
R&D			(3,066,961)
SG&A			(2,117,100)
Interest income			95,382
Investment income recognized by using equity method, net			5,332,415
Other income			566,990
Interest expenses			(783,348)
Other expenses			(244,617)
Income before income tax			<u>\$10,569,445</u>
Identifiable assets:			
Property, plant and equipment, net	<u>\$86,153,482</u>	<u>\$7,258,426</u>	<u>\$93,411,908</u>
Inventory, net	<u>\$5,704,005</u>	<u>\$472,530</u>	<u>\$6,176,535</u>

Depreciation expenses	\$7,911,058	\$1,296,654	\$9,207,712
Capital expenditure	\$53,732,260	\$597,846	\$54,330,106

2005

	TFT-LCD	Other	Total
Total revenues	\$76,664,775	\$1,793,575	\$78,458,350
Gross profit (loss)	786,551	(2,030,103)	(1,243,552)
Unrealized intercompany loss			97,186
R&D			(3,472,022)
SG&A			(2,440,858)
Interest income			98,071
Investment income recognized by using equity method, net			933,511
Other income			759,063
Interest expenses			(1,283,957)
Other expenses			(744,007)
Income before income tax			\$(7,296,565)
Identifiable assets:			
Property, plant and equipment, net	\$131,420,314	\$4,347,412	\$135,767,726
Inventory, net	\$9,702,441	\$114,888	\$9,817,329
Depreciation expenses	\$12,359,556	\$1,924,855	\$14,284,411
Capital expenditure	\$56,733,034	\$263,179	\$56,996,213

(2) Regional information

NONE.

(3) Export sales

Export sales by region for 2004 and 2005 are as follows:

	2004	2005
EUROPE	\$124,844	\$710,737
AMERICA	1,356,450	921,306
SOUTHEAST ASIA	71,235,856	73,977,242
OTHERS	612,278	359,379
Total	\$73,329,428	\$75,968,664

(4) Major customers (individual customer accounting for at least 10% of net operating revenue):

Customer Name	2004		2005	
	Sales	Percentage	Sales	Percentage
A Co., Ltd.	11,037,632	14.08%	\$7,060,555	9.00%

B Co., Ltd.	8,668,768	11.05%	2,950,756	3.76%
C Co., Ltd.	9,054,990	11.55%	4,763,857	6.07%

## 11. Derivative

A. The relevant information of the derivative financial instruments is as follows:

- (1) Types of derivative financial instruments, purpose of holding the derivative financial instruments and the strategy for achieving the purpose:

The purpose for holding foreign currency forward exchange contracts and foreign currency option contracts is to manage the exchange rate fluctuation risks (hedging against accounts payable denominated in Japanese Yen or accounts receivable denominated in US dollars). Interest rate swap (“IRS”) contracts are entered into to hedge interest rate fluctuation risk. The Company’s hedging strategy is to mitigate most of its market price risk. Derivative financial instruments selected for hedging purposes are highly negatively correlated with the fluctuation in the fair value of the hedged items. Derivatives are evaluated periodically.

- (2) Details of contract amount or notional amount:

- ① The Company’s outstanding foreign currency forward exchange contracts and foreign currency options as of December 31, 2004 and 2005 were as follows:

	December 31	
	2004	2005
Financial instruments	Contract amount or notional amount (in thousands)	Contract amount or notional amount (in thousands)
a. Foreign currency forward exchange contracts:		
Buy USD Sell JPY	USD 28,000	-
b. European style foreign currency options:		
<u>BUY</u>		
NTD Call / USD Put	USD 10,000	USD 10,000
JPY Call / USD Put	USD 175,000	USD 46,000
USD Call / JPY Put	USD 13,000	-
<u>Sell</u>		
JPY Call / USD Put	USD 173,500	USD 521,500
USD Call / JPY Put	USD 885,100	-
USD Call / GBP Put	GBP 8,000	-
USD Call / NTD Put	USD 20,000	USD 10,000
GBP Call / USD Put	GBP 8,000	-

- ② The Company's outstanding IRS contracts as of December 31, 2004 and 2005 were as follows:

Maturity period	Notional Amounts	Payable on Fixed Interest Rate	Receivables on Floating Interest Rate	Fair Value
December 31, 2005				
2009.4-2010.3	\$19,600,000	0.77%-1.67%	1.166%-1.428%	\$(335,811)
2009.4~2009.6	\$11,000,000	0.90%-1.65%	0.96%-1.077%	\$(44,112)

(3) Transaction risk:

- ① Credit risk relating to derivative financial instruments:

Credit risk represents the risk of loss that would be recognized at reporting date if counterparties failed to perform. The Company entered into the above derivative contracts with major international foreign banks or reputable local banks. The likelihood of default by the counterparties is considered remote.

- ② Market price risk relating to derivative instruments:

Foreign currency forward exchange contracts and foreign currency option contracts:

Market price risk represents the accounting loss that would be recognized at the reporting date for the derivative financial instruments due to the changes in foreign exchange rates. As the Company's derivative financial instruments are for hedging purposes, the gains or losses due to changes in foreign exchange rates will be offset by the hedged items. As a result, market price risk is considered minimal.

Interest rate swap contracts:

The IRS contracts are used to hedge interest rate fluctuation on its liabilities with floating interest rates. Since the interest receivables and payables are settled at net amounts on the settlement date, the market risk is immaterial.

- ③ Liquidity risk, cash flow risk and the uncertainty of future cash needs:

Foreign currency forward exchange contracts and foreign currency option contracts:

Liquidity risk is the risk of being unable to settle the derivative contracts on schedule. The Company's working capital is sufficient for the cash demand upon the settlement of contracts. As such, there is no significant liquidity risk for the related cash flows.

Furthermore, the exchange rates of the foreign currency forward exchange contracts and foreign currency option contracts are fixed at the inception, so there are no significant cash flow risk.

Interest rate swap contracts:

There is no significant liquidity risk or cash flow risk involved in the interest rate swap contract as the Company has taken into consideration the future cost of capital before entering into such contract.

(4) Presentation of derivative instruments in the financial statements:

① Foreign currency forward exchange contracts:

Receivable and payable resulting from the forward exchange contracts that are not settled at reporting date are netted off. The net amount is recorded as other current assets or other current liabilities.

Details of foreign currency forward exchange contracts as of December 31, 2004 and 2005 were as follows:

	December 31	
	2004	2005
Foreign currency forward exchange contracts-receivable	\$893,676	\$-
Foreign currency forward exchange contracts-payable	(917,162)	-
Unamortized premium	(3,405)	-
Foreign currency forward exchange contracts payable, net	\$(26,891)	\$-

② Foreign currency option contracts:

The unrealized foreign currency loss for these contracts for the years ended December 31, 2004 and 2005 was \$81,182 and \$266,368, respectively.

③ Interest rate swap contracts:

Interest revenues and expenses on these interest rate swap contracts for the years ended December 31, 2004 and 2005 were \$1,104, \$35,896 and \$16,027, \$22,194, respectively.

Accounting policy : Please see Note 2.

B. Fair value of financial instruments:

Non-derivative	December 31, 2004	
	Carrying amount	Fair value
<u>Financial assets:</u>		
Cash and cash equivalents	\$24,107,563	\$24,107,563
Marketable securities	1,115,499	1,128,104

Receivables, net (including accounts receivable-others)	13,052,526	13,052,526
Long-term investments, net	29,418,482	29,356,608
Refundable deposits	35,669	35,669
Pledged time deposits	2,040,742	2,040,742

	December 31, 2004	
	Carrying amount	Fair value
<u>Non-derivative</u>		
<u>Financial liabilities:</u>		
Short-term bank loans	\$7,898,870	\$7,898,870
Payables (including accounts payable-others)	29,897,617	29,897,617
Other current liabilities	217,944	217,944
Bonds payable (including current portion)	13,918,209	14,416,588
Long-term bank loans (including current portion)	25,455,703	25,455,703
<u>Derivatives</u>		
<u>Financial liabilities:</u>		
Foreign currency forward exchange contracts-payable, net	\$(26,891)	\$(26,891)
Foreign currency options contracts, net	(81,182)	(81,182)
Interest rate swap contracts	-	(44,112)

	December 31, 2005	
	Carrying amount	Fair value
<u>Non-derivative</u>		
<u>Financial assets:</u>		
Cash and cash equivalents	\$13,735,238	\$13,735,238
Marketable securities	363,000	372,280
Receivables, net (including accounts receivable-others)	19,067,044	19,067,044
Long-term investments, net	28,270,265	28,173,859
Refundable deposits	21,632	21,632
Pledged time deposits	392,350	392,350
<u>Financial liabilities:</u>		
Short-term bank loans	\$3,128,438	\$3,128,438
Payables (including accounts receivable-others)	36,185,500	36,185,500
Other current liabilities	160,077	160,077
Bonds payable (including current portion)	7,211,149	6,931,423
Long-term bank loans (including current portion)	72,172,907	72,172,907
<u>Derivatives</u>		
<u>Financial liabilities:</u>		
Foreign currency options contracts, net	\$(266,368)	\$(1,081,034)
Interest rate swap contracts	-	(335,811)

The methods and assumptions used to measure the fair value of financial instruments are as follows:

The carrying amounts of cash and cash equivalents, receivables (including accounts receivable-others),

refundable deposits, pledged time deposits, short-term bank loans, payables (including accounts receivable-others) and other current liabilities approximate fair values because of short maturity of these instruments.

Marketable securities and long-term investments are measured based on quoted market prices for these instruments. If market prices are unavailable, fair values are measured based on carrying amount in net assets or other information.

The fair values of long-term bank loans due within one year approximate carrying amount as the long-term bank loans bear interest at variable rates. The fair values of the non-current portion of bank loans are determined based on the sum of the carrying value of the bank loans and accrued interest payable. The fair values of bonds payable are determined based on market price provided by bank.

The fair value of derivative financial instruments represents the estimated net receivable or payable amount if those contracts are terminated at the balance sheet date.

## 12. **Other**

- (1) L.G. Philips LCD. Co., Ltd. (LPL) filed suit for patent infringement against the Company in 2002. The suit alleges that certain TFT-LCD products currently utilized by the Company infringe six patents registered by LPL in Taiwan and U.S. In September, 2005, the U.S. Federal District Court in Los Angeles grant CPT's motion for summary judgments stating that LPL lacks standing to sue on four out of six of the patents in suit. The court's ruling was LPL's lack of ownership in the patents which were rightfully the intellectual property of Digital Equipment Corporation ("DEC") pursuant to the terms of a 1996 joint development agreement entered into between LPL and DEC. The Company acquired the worldwide ownership rights in these DEC technologies earlier in 2004 from Hewlett-Packard, DEC's success in interest. However, the ultimate outcome of the lawsuit is still in process. The Company believes that the suit will not have a material effect on the Company's result of operations or financial position.
- (2) Guardian Industries Corp. filed a complaint for patent infringement relating to a wide-view film application used in the manufacturing of TFT-LCD products against the Company. As of the date of this report, due to the nature of the litigation, the Company cannot predict the ultimate outcome of the lawsuit. The Company believes that the suit will not have a material effect on the Company's results of operations or financial position.