

**INVENTEC APPLIANCES CORPORATION**  
**FINANCIAL STATEMENTS**  
**SEPTEMBER 30, 2005 AND 2004**  
**AND**  
**INDEPENDENT AUDITORS' REVIEW REPORT**

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Inventec Appliances Corporation

Financial Statements

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## Independent Auditors' Review Report

To the Board of Directors  
Inventec Appliances Corporation:

We have reviewed the accompanying balance sheets of Inventec Appliances Corporation as of September 30, 2005 and 2004, and the related statements of income, and cash flows for the nine-month periods then ended. These financial statements are the responsibility of the management of Inventec Appliances Corporation. Our responsibility is to issue a report on these financial statements based on our reviews.

Except as described in the following paragraph, we reviewed these financial statements in accordance with Statements of Auditing Standard No. 36 "Review of Financial Statements." A review is limited primarily to inquiries of company personnel and applying analytical procedures to financial data and thus provides less assurance than an audit. It is substantially less in scope than an audit conducted in accordance with generally accepted auditing standards. We did not perform an audit and, accordingly, we do not express an audit opinion.

As described in Note 4.d, Inventec Appliances Corporation had long-term equity investments of \$4,267,842 thousand and \$3,142,209 thousand, as of September 30, 2005 and 2004, respectively. Investment income for the nine-month periods ended September 30, 2005 and 2004, of \$839,980 thousand and \$662,403 thousand, respectively, were recognized under the equity method based upon the financial statements prepared by the investee companies and not reviewed in compliance with the review procedures mentioned in the preceding paragraph.

Based on our review, except for the effects of any adjustments that might have emerged had the financial statements of investee companies been reviewed by independent auditors, we are not aware of any material modifications that should be made to the accompanying financial statements for them to be in conformity with generally accepted accounting principles of the Republic of China.

Taipei, Taiwan, R.O.C.  
October 19, 2005

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### Note to Readers

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

Reviewed only, not audited in accordance with generally accepted auditing standards

INVENTEC APPLIANCES CORPORATION

Balance Sheets

September 30, 2005 and 2004

(New Taiwan Dollars in Thousands, Except for Share Data)

	2005		2004	
	Amount	%	Amount	%
<b>ASSETS</b>				
<b>Current assets</b>				
Cash (Note 4)(a))	\$ 1,465,935	7	3,640,603	16
Notes receivable-other customers	312	-	3,041	-
Accounts receivable, net of allowance for doubtful accounts (Notes 2) and 4)(b))				
-Other customers	9,099,762	43	10,510,575	47
-Related parties	1,617,705	8	1,893,176	10
Other financial assets - current	325,626	1	115,581	1
Inventories, less allowance for inventory obsolescence (Notes 2 and 4)(c))	2,736,222	13	1,499,509	7
Other current assets	136,939	1	46,704	-
Deferred income tax assets - current (Notes 2) and 4)(g))	57,264	-	77,437	-
	<u>15,439,765</u>	<u>73</u>	<u>17,786,626</u>	<u>81</u>
<b>Long-term equity investments (Notes 2) and 4)(d))</b>				
Accounted for under the equity method	4,267,842	20	3,142,209	14
Accounted for under the cost method	97,050	-	50,000	-
Prepayments for long-term investments	8,000	-	44,850	-
	<u>4,372,892</u>	<u>20</u>	<u>3,237,059</u>	<u>14</u>
<b>Other financial assets - non-current</b>				
	<u>5,686</u>	<u>-</u>	<u>4,870</u>	<u>-</u>
<b>Property, plant, and equipment (Notes 2) and 4)(e))</b>				
Land	279,855	1	279,855	1
Buildings	284,958	2	284,958	1
Machinery	593,004	3	537,276	3
Mold and tools	30,206	-	30,206	-
Transportation equipment	662	-	662	-
Furniture and office facilities	45,485	-	46,985	-
Other equipment	186,965	1	162,242	1
	<u>1,421,135</u>	<u>7</u>	<u>1,342,184</u>	<u>6</u>
Less: accumulated depreciation	(525,273)	(2)	(394,736)	(2)
Prepayment for equipment	10,719	-	998	-
	<u>906,581</u>	<u>5</u>	<u>948,446</u>	<u>4</u>
<b>Intangible assets</b>				
Deferred pension cost (Notes 2))	61,052	-	15,269	-
<b>Other assets</b>				
Deferred income tax assets - non-current (Notes 2) and 4)(g))	53,717	-	165,697	1
Others	484,116	2	52,497	-
	<u>537,833</u>	<u>2</u>	<u>218,194</u>	<u>1</u>
<b>TOTAL ASSETS</b>	<b>\$ 21,323,809</b>	<b>100</b>	<b>22,210,464</b>	<b>100</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>				
<b>Current liabilities</b>				
Notes payable	\$ -	-	6,942	-
Accounts payable				
-Other customers	2,313,170	11	1,324,554	6
-Related parties	7,866,846	37	11,818,328	53
Accrued expenses	610,738	3	317,440	2
Other payables	30,843	-	158,890	1
Payables on forward exchange contract	-	-	3,244	-
Other current liabilities	447,566	2	240,278	1
	<u>11,269,163</u>	<u>53</u>	<u>13,869,676</u>	<u>63</u>
<b>Other liabilities</b>				
Estimated warranty reserve (Note 2))	1,553,961	7	1,089,229	5
Accrued pension liabilities (Notes 2) and 4)(f))	51,713	-	13,418	-
Deferred credits	78,028	-	90,105	-
Others	266,068	2	174,064	1
	<u>1,949,770</u>	<u>9</u>	<u>1,366,816</u>	<u>6</u>
<b>Total liabilities</b>	<b>13,218,933</b>	<b>62</b>	<b>15,236,492</b>	<b>69</b>
<b>Stockholders' equity</b>				
Capital stock, par value \$10 per share; authorized and issued 310,000,000 shares as of September 30, 2005 ; authorized and issued 280,000,000 shares as of September 30, 2004	3,100,000	15	2,800,000	13
Capital surplus				
Premium on stock issuance	2,104,500	10	2,104,500	9
Others	1,110	-	1,110	-
Retained earnings:				
Legal reserve (Note 2))	483,985	2	274,914	1
Undistributed earnings (Note 4)(i))	2,386,290	11	1,828,058	8
Cumulative translation adjustments	28,991	-	(34,610)	-
<b>Total stockholders' equity</b>	<b>8,104,876</b>	<b>38</b>	<b>6,973,972</b>	<b>31</b>
<b>Commitments and contingencies</b>				
<b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>	<b>\$ 21,323,809</b>	<b>100</b>	<b>22,210,464</b>	<b>100</b>

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

Reviewed only, not audited in accordance with generally accepted auditing standards

**INVENTEC APPLIANCES CORPORATION**

**Statements of Income**

Nine-month periods ended September 30, 2005 and 2004

(New Taiwan Dollars in Thousands, Except for Earnings Per Share )

	2005		2004	
	Amount	%	Amount	%
<b>Operating revenues:</b>				
Gross sales (Note (2))	\$ 72,448,050	100	42,285,356	100
Less: sales returns	(71,702)	-	(12,806)	-
Sales discounts and allowances	(121,087)	-	(20,064)	-
Net sales	<u>72,255,261</u>	<u>100</u>	<u>42,252,486</u>	<u>100</u>
<b>Operating cost:</b>				
Cost of sales	<u>(67,833,418)</u>	<u>(94)</u>	<u>(39,119,518)</u>	<u>(93)</u>
	4,421,843	6	3,132,968	7
Unrealized inter-company profits	(73,090)	-	(90,105)	-
Realized inter-company profits	158,132	-	120,103	-
<b>Gross profit</b>	<u>4,506,885</u>	<u>6</u>	<u>3,162,966</u>	<u>7</u>
<b>Operating expenses:</b>				
Selling	(1,765,029)	(3)	(1,378,995)	(3)
Administrative	(271,690)	-	(179,419)	-
Research and development	<u>(809,600)</u>	<u>(1)</u>	<u>(610,093)</u>	<u>(2)</u>
	(2,846,319)	(4)	(2,168,507)	(5)
<b>Operating income</b>	<u>1,660,566</u>	<u>2</u>	<u>994,459</u>	<u>2</u>
<b>Nonoperating income:</b>				
Interest income	17,080	-	17,699	-
Investment income under equity method	839,980	1	662,403	2
Gain on disposal of property, plant, and equipment	302	-	8,363	-
Gain on physical inventory	463	-	1,790	-
Foreign exchange gain	151,503	-	-	-
Others	<u>220,472</u>	<u>1</u>	<u>341,491</u>	<u>-</u>
	<u>1,229,800</u>	<u>2</u>	<u>1,031,746</u>	<u>2</u>
<b>Nonoperating expenses and loss:</b>				
Interest expense	(6,786)	-	(4,381)	-
Loss on disposal of property, plant, and equipment	(648)	-	(1,740)	-
Foreign exchange loss	-	-	(74,167)	-
Loss on obsolete and slow-moving inventories	(84,200)	-	(43,359)	-
Others	<u>(29,669)</u>	<u>-</u>	<u>(5,869)</u>	<u>-</u>
	<u>(121,303)</u>	<u>-</u>	<u>(129,516)</u>	<u>-</u>
<b>Income before income tax</b>	<u>2,769,063</u>	<u>4</u>	<u>1,896,689</u>	<u>4</u>
<b>Income tax expense (Notes (2) and (4)(g))</b>	<u>(482,050)</u>	<u>(1)</u>	<u>(322,435)</u>	<u>-</u>
<b>Net income</b>	<u>\$ 2,287,013</u>	<u>3</u>	<u>1,574,254</u>	<u>4</u>
	<b>Before</b>	<b>After</b>	<b>Before</b>	<b>After</b>
	<b>Tax</b>	<b>Tax</b>	<b>Tax</b>	<b>Tax</b>
<b>Primary earnings per share (Notes (2) and (4)(i))</b>	<u>\$ 8.93</u>	<u>7.38</u>	<u>7.10</u>	<u>5.90</u>
<b>Primary earnings per share after retroactive adjustments</b>	<u>-</u>	<u>-</u>	<u>6.40</u>	<u>5.31</u>

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

Reviewed only, not audited in accordance with generally accepted auditing standards

INVENTEC APPLIANCES CORPORATION

Statements of Cash Flows

Nine-month periods ended September 30, 2005 and 2004

(New Taiwan Dollars in Thousands)

	2005	2004
<b>Cash flows from operating activities:</b>		
Net income	\$ 2,287,013	1,574,254
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	106,156	97,750
Amortization	69,913	78,020
Gain on disposal of property, plant, and equipment	346	(6,555)
Gain on disposal of deferred assets	-	(637)
Write-off properties	3,275	-
Provision for inventory devaluation	84,200	43,359
Investment income recognized under the equity method	(839,980)	(662,403)
Estimated warranty reserve	154,128	512,865
Royalty reserve	64,720	62,381
Reversal of allowance for bad debts	(3,704)	-
Change in operating assets and liabilities:		
Notes and accounts receivable	6,596,494	(6,630,427)
Other financial assets - current	(259,704)	(93,848)
Inventories	(1,142,110)	(567,471)
Other current assets	(101,672)	9,326
Deferred income tax assets and liabilities, net	205,875	12,638
Notes and accounts payable	(6,771,836)	7,125,260
Income tax payable	(108,366)	(374,495)
Accrued expenses	130,117	(37,791)
Other payables	(78,023)	(16,946)
Forward exchange contract payable	-	3,244
Other current liabilities	276,955	33,814
Accrued pension liabilities	(1,880)	(14,321)
Deferred credits	(85,784)	(29,998)
<b>Net cash provided by operating activities</b>	586,133	1,118,019
<b>Cash flows from investing activities:</b>		
Increase in long-term equity investments	(180,069)	(1,180,673)
Purchase of property, plant, and equipment	(102,159)	(140,885)
Purchase of deferred assets	(13,350)	(25,642)
Proceeds from disposal of property, plant, and equipment	1,207	31,852
Proceeds from disposal of deferred assets	-	1,408
Other financial assets - non-current	(817)	(890)
Increase in other assets	(482,429)	-
Increase in other liabilities	400	-
<b>Net cash used in investing activities</b>	(777,217)	(1,314,830)
<b>Cash flows from financing activities:</b>		
Decrease in other liabilities	-	(4,628)
Issuance of common stock for cash	-	780,000
Remuneration to directors and supervisors	(56,449)	(51,916)
Employee bonuses	(111,715)	(101,138)
Cash dividends	(1,568,000)	(1,316,000)
<b>Net cash used in financing activities</b>	(1,736,164)	(693,682)
<b>Net decrease in cash</b>	(1,927,248)	(890,493)
<b>Cash at beginning of the period</b>	3,393,183	4,531,096
<b>Cash at end of the period</b>	\$ 1,465,935	3,640,603
<b>Supplemental disclosures of cash flow information:</b>		
Cash paid during the period for interest (excluding capitalized interest)	\$ 6,786	4,381
Cash paid during the period for income tax	384,541	684,292
<b>Purchase of property, plant, and equipment with cash and other payables:</b>		
Increase in property, plant, and equipment	\$ 73,729	152,598
Add: Other payables - beginning of the period	59,273	39,681
Less: Other payables - end of the period	(30,843)	(51,394)
Cash paid	\$ 102,159	140,885

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

**Reviewed only, not audited in accordance with generally accepted auditing standards**

**INVENTEC APPLIANCES CORPORATION**

**Notes to Financial Statements**

(Amounts expressed in thousand, except for per share information and unless otherwise noted)

**(1) Organization and Business**

Inventec Appliances Corporation (the "Company") was organized on April 25, 2000 and incorporated on May 12, 2000. On November 22, 2002, the Company was merged with Inventec Online Corp., with the Company as the surviving entity in which Inventec Corporation is the primary shareholder. The Company engages primarily in manufacture and sales of wire and wireless communication and digital accessory products.

As of September 30, 2005 and 2004, the Company had 1,845 and 1,309 employees, respectively.

**(2) Summary of Significant Accounting Policies**

The Company's financial statements were prepared in accordance with generally accepted accounting principles of the Republic of China. Summary of significant accounting policies and their measurement basis is as follows:

**(a) Foreign Currency Translation**

Foreign currency transactions are recorded at the exchange rates prevailing at the transaction dates. At the balance sheet date, monetary assets and liabilities denominated in foreign currencies are translated using the exchange rates prevailing on that date. The resulting exchange gains or losses from settlement or translations of monetary assets and liabilities are reflected in the accompanying statements of income.

**(b) Assets Impairment**

Effective January 1, 2005, the Company adopted Statement of Financial Accounting Standards No.35 (SFAS 35) "Accounting for Asset Impairment". According to SFAS 35, the Company assesses at each balance sheet date whether there is any indication that an asset (individual asset or cash-generating unit) other than goodwill may have been impaired. If any such indication exists, the Company estimates the recoverable amount of the asset. The Company recognizes impairment loss for an asset whose carrying value is higher than the recoverable amount.

The Company reserves an impairment loss recognized in prior periods for assets other than goodwill if there is indication that the impairment loss recognized no longer exists or has decreased. The carrying value after the reversal should not exceed the recoverable amount or the depreciated or amortized balance of the assets assuming no impairment loss was recognized in prior periods.

The Company assesses the cash-generating unit to which goodwill is allocated on an annual basis and recognizes an impairment loss on the excess of carrying value over the recoverable amount.

**Reviewed only, not audited in accordance with generally accepted auditing standards**

**INVENTEC APPLIANCES CORPORATION**

**Notes to Financial Statements**

(Amounts expressed in thousand, except for per share information and unless otherwise noted)

**(c) Allowance for Doubtful Accounts**

Allowance for doubtful accounts is based on the results of the Company's evaluation of the collectibility of outstanding receivable balances.

**(d) Inventories and Allowance for Inventory Market Decline and Obsolescence**

Inventories are stated at the lower of cost or fair value on a perpetual inventory basis. Cost is determined using the weighted – average method. Fair value is determined by replacement cost or by net realizable value. A provision for inventory devaluation is recorded when the market values of inventories are less than their cost basis. Allowance for inventory obsolescence is provided for inventory items which remain unsold for over 6 months.

**(e) Long-Term Equity Investments**

Long-term equity investments in which the Company has equity ownership of less than 20% or has no significant influence are carried at cost. For listed investee companies, an allowance for market decline is provided for when market prices are lower than cost. For non-listed investee companies, loss on investment is immediately recognized if impairment in investment is deemed other than temporary.

Long-term equity investments in which the Company can exercise significant influence are accounted for under the equity method. Exchange differences from translation of foreign-denominated financial statements at year-end are reflected as translation adjustments under stockholders' equity.

Unrealized profits/losses on inter-company transactions are eliminated and deferred. Gains and losses which resulted from depreciable asset transactions are recognized ratably over the economic lives of these depreciable assets, while those from other assets are recognized immediately.

Long-term equity investments in which the Company has controlling interest are accounted for under the equity method and the Company is required to prepare consolidated financial statements for each of the periods ended December 31, and June 30, according to the rules set forth in the Statement of Financial Accounting Standards ("SFAS") and by the Securities and Futures Bureau ("SFB") under the Ministry of Finance ("MOF").

**(f) Property, Plant, Equipment and Depreciation**

Property, plant, and equipment are stated at cost. Major additions, improvements, and replacements are capitalized. Depreciation is calculated using the straight-line method over the economic useful lives less salvage value.



**Reviewed only, not audited in accordance with generally accepted auditing standards**

**INVENTEC APPLIANCES CORPORATION**

**Notes to Financial Statements**

(Amounts expressed in thousand, except for per share information and unless otherwise noted)

Economic lives of major property and equipment are as follows:

Building	32 to 45 years
Machinery	1 to 8 years
Transportation equipment	5 years
Furniture and office facilities	1 to 10 years
Mold and tools	1 year
Power equipment	1 to 15 years
Other equipment	1 to 10 years
Renovation	1 to 10 years
Leased assets	3 to 5 years

Gains and losses on disposal of properties are reflected under nonoperating income or expense.

**(g) Deferred Expenses**

Deferred expenses consist of telephone line charges, which are capitalized and amortized equally over 5 years. Molds and tools and software costs are amortized equally over 12 months.

**(h) Warranty Reserve**

A warranty reserve is provided for products sold with warranty based on estimated warranty cost and in consideration of past experience and is charged against current expense.

**(i) Royalty Reserve**

A royalty reserve is provided for royalty being paid on certain products with royalty based on historical royalty charge and according to its nature. This reserve is classified under non-current liabilities.

**(j) Pension Plan**

The Company has a pension plan covering all regular employees, under which pension payment is commensurate with years of service. The Company contributes annually to the pension fund and deposits in a government designated account. The pension fund is not reflected in the Company's financial statements. Effective July 1, 2005, the Company adopted the "Labor Pension Act" (the "Act") that prescribes a defined contribution pension scheme for those employees who were covered by the Labor Standards Law prior to the enforcement of this Act but chose to be subject to the pension mechanism under this Act or those employees who are employed after the enforcement of this Act. In accordance with this Act, the Company contributes monthly to the Labor Pension Fund for the employee individual pension fund accounts at the rate of 6% of the employee's monthly wages.

**Reviewed only, not audited in accordance with generally accepted auditing standards**

**INVENTEC APPLIANCES CORPORATION**

**Notes to Financial Statements**

(Amounts expressed in thousand, except for per share information and unless otherwise noted)

For defined benefit pension plan, the Company adopted SFAS No. 18 and secured an actuarial report on pension liabilities with December 31 as the measurement date. Provision for pension expense commenced on April 25, 2000, and unrecognized net transitional obligations are amortized equally over 15 years.

For defined contribution pension plan, the contributions are reflected as current pension expense.

**(k) Commitments and Contingencies**

If loss from a commitment or contingency is deemed highly likely and the amount can be reasonably estimated, then such loss is immediately recognized. Otherwise, only the nature of such loss is disclosed in notes to the financial statements.

**(l) Non-Trading Financial Derivatives**

According to the SFAS, foreign exchange forward contracts for hedging are recorded at spot rates on the contract date and adjusted at year-end based on year-end exchange rate, with exchange gains and losses included in current earnings. Premium or discount, which represents the difference between the contract and the spot rates, is recognized ratably over the term of forward contracts. The forward contract receivable is netted against related payables and the net amount is reflected either as an asset or a liability.

**(m) Revenue Recognition**

Revenue is recognized when title to the product and risk and benefits of ownership are transferred to the customer; otherwise recognition is deferred until conditions are met.

**(n) Classification of Capital and Operating Expenditures**

Expenditures that benefit the Company in future years are capitalized, while immaterial expenditures or those with no future benefits are treated as current expense or loss.

**(o) Income Tax**

The Company adopted the SFAS No. 22, "Accounting for Income Taxes" to make inter- and intra-period income tax allocation. Tax effects of deductible temporary differences, unused investment tax credits, and operating loss carryforwards are treated as deferred tax assets, whereas those of taxable temporary differences are accounted for as deferred tax liabilities. A valuation allowance is provided for deferred tax assets by assessing whether it is more likely than not such assets will be realized. Adjustments to prior years' income taxes are reflected as current income taxes.

The 10% surtax on undistributed earnings is reported as current expense on the date when the stockholders resolved not to distribute the earnings during their annual meeting.

**(p) Earnings per Share (EPS)**

EPS is calculated using the weighted-average shares outstanding during the year. In the event of capital increase through capitalization of retained earnings or capital surplus, EPS is retroactively adjusted by the capitalization ratio, regardless of the period when the incremental shares are outstanding.

**Reviewed only, not audited in accordance with generally accepted auditing standards**

**INVENTEC APPLIANCES CORPORATION**

**Notes to Financial Statements**

(Amounts expressed in thousand, except for per share information and unless otherwise noted)

**(3) Reasons for and Effects of Accounting Changes:**

The Company adopted Statement of Financial Accounting Standards No.35 "Accounting for Asset Impairment" in 2005. However, no impairment loss was provided because no impairment was noted of the assets.

**(4) Summary of Major Accounts**

**(a) Cash**

	<u>September 30, 2005</u>	<u>September 30, 2004</u>
Cash on hand	\$ 544	470
Demand deposits	379,665	655,752
Time deposits	200,000	900,000
Negotiable certificate of deposits	-	1,000,000
Foreign currency deposits	885,726	1,084,381
Total	<u>\$ 1,465,935</u>	<u>3,640,603</u>

**(b) Accounts Receivable**

	<u>September 30, 2005</u>	<u>September 30, 2004</u>
Accounts receivable - other customers	\$ 9,144,629	10,510,575
Less: allowance for doubtful accounts	(44,867)	-
Net	9,099,762	10,510,575
Accounts receivable - related parties	1,617,705	1,893,176
Total	<u>\$ 10,717,467</u>	<u>12,403,751</u>

**(c) Inventories**

	<u>September 30, 2005</u>	<u>September 30, 2004</u>
Raw materials	\$ 2,245,967	820,624
Work in process	235,617	203,889
Finished goods	171,447	275,709
Inventories in transit	191,619	232,666
Subtotal	2,844,650	1,532,888
Less: provision for obsolescence	(108,428)	(33,379)
Net	<u>\$ 2,736,222</u>	<u>1,499,509</u>
Insurance coverage for inventories	<u>\$ 2,940,904</u>	<u>1,035,164</u>

**Reviewed only, not audited in accordance with generally accepted auditing standards**

**INVENTEC APPLIANCES CORPORATION**

**Notes to Financial Statements**

(Amounts expressed in thousand, except for per share information and unless otherwise noted)

**(d) Long-Term Equity Investments**

<u>Investee</u>	<u>September 30, 2005</u>			<u>September 30, 2004</u>		
	<u>Equity Holding</u>	<u>Book Value</u>	<u>Original Investment</u>	<u>Equity Holding</u>	<u>Book Value</u>	<u>Original Investment</u>
<b><u>Under equity method</u></b>						
Inventec Appliances (Cayman) Holding Corp.	100.00%	\$ 4,261,506	2,609,326	100.00%	3,137,176	2,506,188
Gainia Intellectual Asset Services, Inc.	48.30%	6,336	6,400	48.30%	5,033	6,400
Subtotal		<u>4,267,842</u>	<u>2,615,726</u>		<u>3,142,209</u>	<u>2,512,588</u>
<b><u>Under cost method</u></b>						
Darly 3 Venture Corporation	4.98%	10,200	10,200	4.98%	20,000	20,000
Telewise Communicatons, Inc.	6.98%	-	10,008	6.98%	-	10,008
Hi Top Communications Corp.	7.41%	30,000	30,000	7.41%	30,000	30,000
Advanced Image Technology Corp.	19.50%	44,850	44,850	-%	-	-
Tai Yi Precision Corporation	1.67%	12,000	12,000	-%	-	-
Subtotal		<u>97,050</u>	<u>107,058</u>		<u>50,000</u>	<u>60,008</u>
<b><u>Prepayment for Long-Term Investments</u></b>						
Advanced Image Technology Corp.		-	-		44,850	44,850
Akom Technology Corporation		8,000	8,000		-	-
Subtotal		<u>8,000</u>	<u>8,000</u>		<u>44,850</u>	<u>44,850</u>
Total		<u>\$ 4,372,892</u>	<u>2,730,784</u>		<u>3,237,059</u>	<u>2,617,446</u>

For the nine-month periods ended September 30, 2005 and 2004, income from investments in investee companies accounted for under the equity method were as follows:

<u>Investee</u>	<u>2005</u>	<u>2004</u>
Based on financial statements prepared by investee companies:		
Inventec Appliances (Cayman) Holding	\$ 839,116	662,362
Gainia Intellectual Asset Services, Inc.	864	41
Total	<u>\$ 839,980</u>	<u>662,403</u>

The Company invested in Inventec Appliances (Cayman) Holding Corp., a wholly-owned holding company, which engages in various investments.

For the nine-month periods ended September 30, 2005 and 2004, the Company invested \$12,000, \$8,000 and \$44,850 in Tai Yi Precision Corporation, Akom Technology Corporation and Advanced Image Technology Corp., respectively. These investees are accounted for under the cost method.

**(e) Property, Plant, and Equipment**

As of September 30, 2005 and 2004, insurance coverage for the property, plant, and equipment amounted to \$1,177,325 and \$1,071,800, respectively.

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**INVENTEC APPLIANCES CORPORATION**

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(Amounts expressed in thousand, except for per share information and unless otherwise noted)

**(f) Pension Plan**

The Company's pension fund and accrued pension liability as of September 30, 2005 and 2004, and the related pension expense for the nine-month periods then ended, were as follows:

	<u>2005</u>	<u>2004</u>
Pension fund asset balance	\$ 304,589	242,727
Pension expense:		
For defined benefit scheme	39,049	24,668
For defined contribution scheme	10,818	-
Accrued pension liability	51,713	13,418

**(g) Income Tax**

**(i) Deferred income tax assets and liabilities:**

	<u>September 30, 2005</u>		<u>September 30, 2004</u>	
	<u>Amount</u>	<u>Income Tax Effects</u>	<u>Amount</u>	<u>Income Tax Effects</u>
a. Total deferred tax assets	\$ 513,825		414,453	
b. Total deferred tax liabilities	(402,844)		(171,319)	
c. Temporary differences:				
- Unrealized foreign exchange loss	\$ 39,597	9,899	181,664	45,416
- Allowance for inventory obsolescence	108,428	27,107	33,379	8,345
- Investment income	(1,549,794)	(387,449)	(677,134)	(169,283)
- Cumulative translation adjustment for long-term investments	(38,654)	(9,664)	46,146	11,536
- Reserve for employee retirement benefit	(22,925)	(5,731)	(8,143)	(2,036)
- Reserve for employee welfare	6,060	1,515	9,220	2,305
- Unrealized inter-company profits	78,028	19,507	90,104	22,526
- Unrealized warranty reserve	1,553,961	388,490	1,089,229	272,307
- Royalty reserve	259,219	64,805	174,064	43,516
- Compensation reserve	-	-	24,000	6,000
- Unrealized devaluation loss on long-term investments under the cost method	10,008	2,502	10,008	2,502

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	<u>September 30, 2005</u>	<u>September 30, 2004</u>
(ii) Deferred tax assets – current	\$ 57,264	77,437
Deferred tax liabilities – current	-	-
Net	<u>\$ 57,264</u>	<u>77,437</u>
(iii) Deferred tax assets – non-current	\$ 456,561	337,016
Deferred tax liabilities – non-current	(402,844)	(171,319)
Net	<u>\$ 53,717</u>	<u>165,697</u>

(iv) The income tax expense for the nine-month periods ended September 30, 2005 and 2004 was calculated as follows:

	<u>2005</u>	<u>2004</u>
Income tax calculated on accounting income at statutory tax rate	\$ 692,256	474,162
Permanent differences	(2,471)	(1,345)
Temporary differences	(205,874)	(12,638)
Tax-exempt income	(15,510)	(15,442)
Investment tax credits used	(211,258)	(177,982)
10% surtax on unappropriated earnings	24,903	52,428
Current income tax payable	282,046	319,183
Income tax separately levied	1,885	1,125
Prior years' income tax adjustments	(7,755)	(10,511)
Income tax effect of temporary differences:		
Provision for inventory obsolescence, net	(16,582)	(2,473)
Investment income/loss recognized under equity method	209,779	165,590
Unrealized foreign currency exchange loss (gain), net	37,147	(18,611)
Pension cost reserve	2,293	3,580
Reserve for employee welfare	503	863
Unrealized inter-company profit	21,446	7,500
Compensation reserve	6,000	-
Royalty reserve	(16,180)	(15,595)
Warranty reserve	(38,532)	(128,216)
Income tax expense	<u>\$ 482,050</u>	<u>322,435</u>

(v) The Company's tax returns through 2002 have been assessed by the Tax Authority.

(vi) The Company's wireless communication and digital accessory products conform to Article 2, Paragraph 1 of the regulations regarding awards for newly emerging and strategic industries under manufacturing and technical service industries and are eligible for 5-year tax exemption.

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(vii) Stockholders' Imputation Tax Credit Account and Tax Rate:

	<u>September 30, 2005</u>	<u>September 30, 2004</u>
Imputation credit account balance	<u>\$ 21,441</u>	<u>56,551</u>
	<u>2004</u>	<u>2003</u>
Creditable ratio for earnings distribution to resident stockholders	<u>20.79%</u>	<u>22.19%</u>

(viii) Unappropriated Retained Earnings:

	<u>2005</u>	<u>2004</u>
Earned prior to January 1, 1998	<u>\$ -</u>	<u>-</u>
Earned after January 1, 1998	<u>2,386,290</u>	<u>1,828,058</u>
Total	<u>\$ 2,386,290</u>	<u>1,828,058</u>

**(h) Capital Increase**

On May 10, 2005, pursuant to resolutions of the annual stockholders' meeting, the Company increased its capital by \$300,000 by capitalizing its earnings of \$280,000 and employee bonuses of \$20,000. Its outstanding capital following this capital increase amounted to \$3,100,000 with July 20, 2005 as the record date. The Company had completed relevant registration process for this capital increase.

On April 27, 2004, pursuant to resolutions of the annual stockholders' meeting, the Company increased its capital by \$255,000 by capitalizing its earnings of \$235,000, and employee bonuses of \$20,000. Also, the Company resolved to further increase its capital in cash by issuing additional 19,500,000 shares at \$40 per share. Its outstanding capital following these capital increases amounted to \$2,800,000 with July 9, 2004 as the record date. The Company had completed relevant registration process for these capital increases.

**(i) Earnings Appropriation**

	<u>2005</u>	<u>2004</u>
Balance at January 1	<u>\$ 2,344,512</u>	<u>2,170,140</u>
Appropriation of prior year's earnings:		
Legal reserve	<u>(209,071)</u>	<u>(192,282)</u>
Remuneration to directors and supervisors and employee bonuses	<u>(168,164)</u>	<u>(153,054)</u>
Cash dividends	<u>(1,568,000)</u>	<u>(1,316,000)</u>
Capitalization of retained earnings and employee bonus	<u>(300,000)</u>	<u>(255,000)</u>
Add: Net income, current period	<u>2,287,013</u>	<u>1,574,254</u>
Balance at September 30	<u>\$ 2,386,290</u>	<u>1,828,058</u>

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**INVENTEC APPLIANCES CORPORATION**

**Notes to Financial Statements**

(Amounts expressed in thousand, except for per share information and unless otherwise noted)

**(j) Earnings per Share (EPS)**

For the nine-month periods ended September 30, 2005 and 2004, the basic earning per share is computed as follows:

	2005		2004	
	Before Tax	After Tax	Before Tax	After Tax
Net income available to common shareholders	<u>\$2,769,063</u>	<u>2,287,013</u>	<u>1,896,689</u>	<u>1,574,254</u>
Weighted-average number of outstanding (in thousands)	<u>310,000</u>	<u>310,000</u>	<u>267,000</u>	<u>267,000</u>
Outstanding shares retroactively adjusted	<u>310,000</u>	<u>310,000</u>	<u>296,370</u>	<u>296,370</u>
Basic earnings per share	<u>8.93</u>	<u>7.38</u>	<u>7.10</u>	<u>5.90</u>
Retroactively adjusted basic earning per share	<u>8.93</u>	<u>7.38</u>	<u>6.40</u>	<u>5.31</u>

**(k) Financial Instruments**

**(i) Financial Derivatives:**

1. Contract amount and credit risk:

	September 30, 2005		September 30, 2004	
	Contract amount		Contract amount	
Foreign currency forward contracts				
-Non-trading	USD	-	USD	8,000

The amount of credit risk is the sum of contracts with positive fair market value at the balance sheet date after netting the settlement of all contracts, and represents the Company's possible loss in the event of default by counter-parties.

2. Market risk:

Financial derivatives held by the Company are subject to market risk resulting from exchange rate fluctuations, whereas possible decreases in price are offset by exchange gain and loss on hedged foreign-currency-denominated assets and liabilities.

3. Liquidity risk, cash flow risk, and future cash demand:

Financial derivatives held by the Company are settled with banks using the cash generated from its operations.



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**Notes to Financial Statements**

(Amounts expressed in thousand, except for per share information and unless otherwise noted)

**(ii) Fair Value of Financial Instruments**

	<b>September 30, 2005</b>	
<b>Financial Assets</b>	<b>Book Value</b>	<b>Fair Value</b>
Book value equal to fair value	\$ 12,515,026	12,515,026
Long-term equity investments	4,372,892	4,366,918
Total financial assets	<b>\$ 16,887,918</b>	<b>16,881,944</b>
<b>Financial Liabilities</b>		
Book value equal to fair value	<b>\$ 11,722,048</b>	<b>11,722,048</b>

  

	<b>September 30, 2004</b>	
<b>Financial Assets</b>	<b>Book Value</b>	<b>Fair Value</b>
Book value equal to fair value	\$ 16,167,846	16,167,846
Long-term equity investments	3,237,059	3,213,369
Total financial assets	<b>\$ 19,404,905</b>	<b>19,381,215</b>
<b>Financial Liabilities</b>		
Book value equal to fair value	<b>\$ 14,057,135</b>	<b>14,057,135</b>

Method and assumptions used by the Company to evaluate the fair value of financial instruments are the following:

1. The fair values of short-term financial instruments are determined by their face value on the balance sheet. Because these instruments have short-term maturities, their face value serves as a reasonable basis in establishing the fair value. This method is applicable to cash and cash equivalents, notes and accounts receivable, other current assets, notes and accounts payable, and other current liabilities.
2. The book values of long-term investments accounted for under the cost or the equity method are based on audited or self-prepared financial statements of investee companies. Because there are no market quotes or reference reports for non-listed companies, the fair value of these investments is determined by their net equity worth or cost.
3. With respect to financial instruments such as refundable deposits that are indispensable guarantee for the ongoing operations of the Company, it is impossible to estimate the time necessary to accomplish the exchange of assets. Consequently, the fair market values of such financial instruments cannot be established. Therefore, the book value is used as the fair market value.
4. Fair values of non-trading foreign-denominated financial derivatives are determined by the amount the Company will pay or receive, assuming the contract is terminated on the balance sheet date. These fair values, which generally include unrealized gains and losses on currently unsettled contracts, are based on the pricing reports issued by financial institutions for most of the non-trading financial derivatives held by the Company.

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**Notes to Financial Statements**

(Amounts expressed in thousand, except for per share information and unless otherwise noted)

(iii) **Financial Instruments with Off-Balance-Sheet Credit Risk: None.**

(iv) **Information on Concentrations of Credit Risk:**

Concentrations of credit risk exist when changes in economic, industry or geographic factors similarly affect groups of counter-parties whose aggregate credit exposure is material in relation to the Company's total credit exposure. As of September 30, 2005 and 2004, the Company's contracts with credit risk concentration were the following:

<u>Accounts Receivable-By Region</u>	<u>September 30, 2005</u>	<u>September 30, 2004</u>
Domestic	\$ 409,611	585,433
Asia	809,872	1,943,126
Europe	4,333,676	1,709,451
Americas	4,349,305	7,228,915
Other	815,003	936,826
Total	<u>\$ 10,717,467</u>	<u>12,403,751</u>

**(5) Related Party Transactions**

**(a) Names of Related Parties and their Relationship with the Company**

<u>Name of Related Party</u>	<u>Relationship with the Company</u>
Inventec Corporation	Majority shareholder
Inventec Appliances (Cayman) Holding Corp.	A subsidiary
Inventec Appliances (BVI) Corp.	A third level subsidiary of the Company
Inventec Appliances (USA) Distribution Corp.	"
Inventec Appliances (Shanghai) Co., Ltd.	"
Inventec Appliances (Pudong) Co., Ltd.	"
Inventec Appliances (Nanjing) Co., Ltd.	"
Inventec Appliances (Jiangning) Co., Ltd.	"
Tapwave, Inc.	A company accounted for under the equity method by Inventec Appliances (Cayman) Holding Corp. (Note)
Inventec Micro-Electronics (BVI) Corporation	A subsidiary of Inventec Corporation
Inventec Besta Co., Ltd.	"

Note : In March 2004, Tapwave, Inc. (" Tapwave") increased its capital in cash; however, the Company did not subscribe to new shares resulting from this capital increase of Tapwave. Consequently, Tapwave was no longer a subsidiary of the Company since then because the Company lost its controlling interest as it decreased its equity holding in Tapwave to 16%. For this reason, only the sales transactions with Tapwave prior to March 2004 were disclosed.

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(Amounts expressed in thousand, except for per share information and unless otherwise noted)

**(b) Significant Transactions with Related Parties:**

**(i) Sales**

For the nine-month periods ended September 30, 2005 and 2004, sales to related parties were as follows:

	2005		2004	
	Amount	% of Net Sales	Amount	% of Net Sales
Inventec Appliances (BVI) Corp.	\$ 1,700,403	2%	2,587,870	6%
Inventec Appliances (USA) Distribution Corp.	5,025,858	7%	2,149,609	5%
Tapwave, Inc.	-	-%	6,681	-%
Others	78	-%	713	-%
Total	<u>\$ 6,726,339</u>	<u>9%</u>	<u>4,744,873</u>	<u>11%</u>

Prices of raw materials sold to Inventec Appliances (BVI) Corp. were negotiated. The collection term was three months.

Prices of graphic calculators and Personal Digital Assistant (PDA) sold to Inventec Appliances (USA) Distribution Corp. were negotiated. The collection term was approximately two to three months.

Prices of game consoles sold to Tapwave, Inc. were negotiated. The collection term was 45 days.

As of September 30, 2005 and 2004, unrealized gross margin of sales to related parties was \$73,090 and \$90,105, respectively.

**(ii) Purchases**

For the nine-month periods ended September 30, 2005 and 2004, purchases from related parties were as follows:

	2005		2004	
	Amount	% of Net Purchases	Amount	% of Net Purchases
Inventec Appliances (BVI) Corp.	\$ 61,924,197	90%	32,751,090	84%
Inventec Micro-Electronics (BVI) Corporation	-	-%	35,433	-%
Total	<u>\$ 61,924,197</u>	<u>90%</u>	<u>32,786,523</u>	<u>84%</u>

Prices of graphic calculators, PDAs, and MP3 players purchased from Inventec Appliances (BVI) Corp. were negotiated. The payment term was three months.

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Prices of raw materials of cell phone purchased from Inventec Micro-Electronics (BVI) Corporation were negotiated. The payment term was approximately two to three months.

**(iii) Others**

1. For the nine-month periods ended September 30, 2005 and 2004, business consulting fee and computer system expense paid to Inventec Corporation amounted to \$27,776 and \$24,699, respectively.
2. The Company sold properties and deferred assets to Inventec Appliances (BVI) Corp. at cost \$805 and \$48,482, respectively. Gain from the sale of properties and deferred assets for the nine-month periods ended September 30, 2005 and 2004 amounted to \$302 and \$7,993, respectively, and were recorded as unrealized gain on disposal of assets. As of September 30, 2005 and 2004, unrealized gain from sale of properties to affiliates was \$4,938 and \$0, respectively.
3. For the nine-month period ended September 30, 2004, processing charge and sundry expense paid to Inventec Besta Corp. amounted \$1,638.
4. For the nine-month period ended September 30, 2005, purchase of machinery from Inventec Corporation amounted to \$5,257.

**(iv) Financing to related parties (without interest accrued):**

The Company's financing to a related party for the nine-month period ended September 30, 2005 was as follows:

	September 30, 2005	
	Maximun Balance	Ending Balance
Inventec Appliances (BVI) Corp.	\$ 238,140	238,140

The Company reclassified the overdue trade receivables from Inventec Appliances (BVI) Corp. to the financing to related parties (reflected as other financial asset-current).

**(v) Accounts Receivable (Payable)**

	September 30, 2005		September 30, 2004	
	Balance	%	Balance	%
<u>Accounts receivable:</u>				
Inventec Appliances (BVI) Corp.	\$ 862,574	8%	944,060	8%
Inventec Appliances (USA) Distribution Corp.	726,738	7%	920,007	7%
Tapwave, Inc.	-	-%	28,975	-
Others	-	-%	134	-%
Total	<u>\$ 1,589,312</u>	<u>15%</u>	<u>1,893,176</u>	<u>15%</u>

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(Amounts expressed in thousand, except for per share information and unless otherwise noted)

	September 30, 2005		September 30, 2004	
	Balance	%	Balance	%
<u>Other receivables:</u>				
Inventec Appliances (BVI) Corp.	\$ 1,086	1%	7,708	10%
<u>Other financial assets-current</u>				
Inventec Appliances (BVI) Corp.	\$ 239,090	100%	-	-%
<u>Accounts payable:</u>				
Inventec Appliances (BVI) Corp.	\$ 7,866,846	77%	11,813,636	90%
Other	-	-%	4,692	-%
Total	\$ 7,866,846	77%	11,818,328	90%
<u>Accrued expenses</u>				
Inventec Appliances (BVI) Corp.	\$ -	-%	10,004	6%

**(v) Guarantee and Endorsements**

As of September 30, 2005 and 2004, endorsements and guarantees provided by the Company for related parties' bank loans were as follows:

	Amount of Guarantee		Name of Bank
	September 30, 2005	September 30, 2004	
Inventec Appliances (Cayman) Holding Corp.	US\$ 46,550	US\$ 38,000	Citibank, N.A.
	15,000	-	Bank of America
Inventec Appliances (BVI) Corp.	5,000	5,000	"
	1,500	1,500	Citibank, N.A.
Inventec Appliances (USA) Distribution Corp.	5,000	5,000	HSBC Bank
	3,000	10,000	Bank of America
Inventec Appliances (Shanghai) Co., Ltd.	15,000	15,000	HSBC Bank
	8,000	8,000	Bank of America
Inventec Appliances (Pudong) Co., Ltd.	-	15,000	"
	15,000	15,000	HSBC Bank
	10,000	-	SM Bank
	10,000	-	SC Bank
Inventec Appliances (Jiangning) Co., Ltd.	10,000	-	"
	34,000	9,000	HSBC Bank
Inventec Appliances (Nanjing) Co., Ltd.	1,500	-	Bank of America
Total	US\$ 179,550	US\$ 121,500	

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**(6) Pledged Assets**

Assets pledged as collateral as of September 30, 2005 and 2004, were summarized as follows:

	<u>September 30, 2005</u>	<u>September 30, 2004</u>	<u>Purpose of pledge</u>
Refundable deposits	<u>\$ 5,687</u>	<u>4,870</u>	Deposits for security box, building, counter, and mobile phone

**(7) Significant Commitments and Contingencies, Excluding Related Party Transactions (Foreign Currency in thousands)**

- (a) As of September 30, 2005 and 2004, unused letters of credit amounted to US\$1,449, JPY48,035, and EUR\$6, JPY30,260, respectively.
- (b) As of September 30, 2005 and 2004, the promissory notes issued for bank credit limits amounted to US\$25,000 and US\$15,000, respectively.
- (c) The Company entered into an agreement with Industrial Development Bureau (IDB) to obtain a grant from IDB for the research and development project. As of September 30, 2005 and 2004, the promissory notes issued for the grant from IDB, and IDB cooperation funds amounted to \$1,850,268 and \$2,242,083, respectively. At the same date, promissory notes received for aforementioned project from other cooperative partners and applications to the Ministry of Economic Affairs amounted to \$79,800 and \$135,448, respectively.
- (d) For the nine-month periods ended September 30, 2005 and 2004, the Company entered into a lease agreement to lease computers and software. Information regarding rental expense and future lease payments are as follows:

Year	Rent expense	Future rent due			
		2005	2006	2007	2008
2005	\$ 16,615	5,916	18,474	9,261	1,444
2004	\$ 10,716	19,669	9,172	703	-

- (e) In October 2001, FeiMa Communication (Qing Dao) Co.,Ltd. filed a lawsuit against the Company. The local peoples' court in China ruled that the Company breached an agreement and is required to pay RMB5,000 and litigation expense of RMB33. In April 2003, the Company filed for an appeal. On May 20, 2005, the Company settled with FeiMa Communication (Qing Dao) Co., Ltd. out of court, and paid RMB3,990.
- (f) On January 7, 2004, Mitake Information Corporation filed a lawsuit for patent infringement against the Company seeking for a compensation of \$1,000. The Company has provided the Intellectual Property Office with sufficient evidences, and the local district Court has ruled to dismiss this lawsuit.

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(Amounts expressed in thousand, except for per share information and unless otherwise noted)

(8) **Significant Catastrophic Losses: None.**

(9) **Significant Subsequent Events: None.**

(10) **Others**

Personnel cost, depreciation, and amortization incurred categorized as operating cost or expenses are as follows:

Categorized as Nature	For the nine months ended September 30,					
	2005			2004		
	Operating Cost	Operating Expenses	Total	Operating Cost	Operating Expenses	Total
Personnel Cost						
Salary	492,223	713,941	1,206,164	440,982	332,474	773,456
Health and labor insurance	23,184	30,260	53,444	20,550	16,754	37,304
Pension	15,243	34,624	49,867	16,074	8,594	24,668
Other	126,481	22,053	148,534	16,378	55,963	72,341
Depreciation	47,697	58,459	106,156	50,030	47,720	97,750
Amortization	43,400	26,513	69,913	37,473	40,547	78,020