

OFFERING CIRCULAR



King Yuan Electronics Co., Ltd.

(Incorporated as a company limited by shares in Taiwan, Republic of China)

U.S.\$120,000,000 Zero Coupon Convertible Bonds due 2005

Issue Price: 100 per cent.

The U.S.\$120,000,000 Zero Coupon Convertible Bonds due 2005 (the “**Bonds**”) will be issued in registered form by King Yuan Electronics Co., Ltd. (the “**Company**”) in reliance on Regulation S under the Securities Act of 1933, as amended (the “**Securities Act**”). The Bonds will not bear interest except in the limited circumstances set forth herein. On the Maturity Date, the Company will redeem the Bonds for an amount equal to 110.87 per cent. of their original principal amount, unless the Bonds have been previously purchased and cancelled, converted or redeemed.

The Bonds will be direct, unconditional, unsecured and unsubordinated obligations of the Company and will rank at least *pari passu* in right of payment with all other unsecured and unsubordinated debt of the Company, except as otherwise provided herein. Holders of the Bonds may convert the Bonds into the common shares, par value NT\$10 per share, of the Company (the “**Shares**”) at any time (subject to certain restrictions) on or after 18th May, 2002 and prior to the close of business (at the place the Bond is deposited for conversion) on 18th March, 2005. The Conversion Price will initially be U.S.\$0.700 per Share subject to adjustment in the manner provided herein and with a fixed exchange rate applicable on conversion of the Bonds of NT\$34.979 = U.S.\$1.00. In addition, the Conversion Price will be adjusted from time to time in certain circumstances relating to the then prevailing closing price of the Shares relative to the Conversion Price. The Shares are listed on the Taiwan Stock Exchange (the “**TSE**”) and application will be made to list the Shares issued on conversion of the Bonds on the TSE. On 10th April, 2002, the closing price of the Shares on the TSE was NT\$30.2 per Share.

The Company will, at the option of the holder of any Bond (the “**Bondholder**”), redeem all or part of the Bondholder’s Bonds on 18th April, 2004 at 107.12 per cent. of the principal amount. The Company has the option, having given not less than 40 days or more than 60 days notice to the Bondholders, to redeem all, or part only, of the Bonds on or at any time after 18th April, 2003 at their principal amount in the event that the closing price of the Shares in the TSE in U.S. Dollars, calculated at the prevailing exchange rate, for each of the 30 consecutive Trading Days (as defined herein), the last of which occurs not more than 10 days prior to the date upon which notice of such redemption is published, is at least 150 per cent. of the Conversion Price in effect on each such Trading Day translated into U.S. Dollars at the fixed exchange rate of NT\$34.979 = U.S.\$1.00. The Bonds may be redeemed in whole at any time at the Company’s option at the principal amount in the event that (i) the Bonds outstanding are less than 10 per cent. of the issue amount; or (ii) certain changes relating to Republic of China (“**ROC**” or “**Taiwan**”) taxation which will result in additional costs to the Company.

For a discussion of certain factors that should be considered in connection with an investment in the Bonds, see “**Risk Factors**” on page 10 herein.

Application has been made to list the Bonds on the Société de la Bourse de Luxembourg S.A. (the “**Luxembourg Stock Exchange**”).

The Bonds and Shares to be issued upon conversion of the Bonds have not been and will not be registered under the Securities Act, and may not be offered or sold within the United States or to, or for the account on behalf of, U.S. persons. The Bonds are not being offered in the ROC or in the United States.

*Sole Bookrunner
Lead Manager*



NSC Securities (Asia) Limited

Managers

Grand Cathay Securities Corporation

MasterLink Securities Corporation

Bank SinoPac, Offshore Banking Branch

Local Advisor



National Securities Corporation

The date of this Offering Circular is 17th April, 2002.

King Yuan Electronics Co., Ltd. (the “**Company**”), having made all reasonable inquiries, confirms that this Offering Circular contains all information with respect to the Company, the Bonds and the Shares which is material in the context of the issue and offering of the Bonds (including all information required by applicable laws of the ROC), that the information contained herein (save as set out below) is true and accurate in all material respects and is not misleading, that the opinions and intentions expressed herein are honestly held and have been reached after considering all relevant circumstances and are based on reasonable assumptions, that there are no other facts, the omission of which would, in the context of the issue and offering of the Bonds, make this Offering Circular as a whole or any of such information or the expression of any such opinions or intentions misleading in any material respects, that all reasonable inquiries have been made by the Company to verify the accuracy of such information, and that this Offering Circular does not contain an untrue statement of a material fact or omit to state a material fact required to be stated herein or necessary in order to make the statements herein, in the light of the circumstances under which they are made, not misleading. The Company accepts responsibility accordingly. Information provided herein with respect to the ROC, its political status and economy, has been derived from government and other public sources, and the Company accepts responsibility only for accurately extracting information from such sources.

The distribution of this Offering Circular and the offering and sale of the Bonds in certain jurisdictions may be restricted by law. Persons into whose possession this Offering Circular comes are required by the Company and the Managers (as defined in “Subscription and Sale”) to inform themselves about and to observe any such restrictions. For a description of certain further restrictions on offers and sales of the Bonds and distribution of this Offering Circular, see “Subscription and Sale”. This Offering Circular does not constitute an offer of, or an invitation by or on behalf of the Company or the Managers to subscribe for or purchase, any of the Bonds in any jurisdiction in which such offer or invitation would be unlawful.

No person is authorized in connection with the issue, offering or sale of the Bonds to give any information or to make any representation not contained in this Offering Circular and any information or representation not contained herein must not be relied upon as having been authorized by the Company or the Managers. Neither the delivery of this Offering Circular nor any sale or allotment made in connection with the issue of the Bonds shall, under any circumstances, constitute a representation or create any implication that there has been no change in the affairs of the Company since the date hereof or that the information contained herein is correct as of any time subsequent to its date.

The Bonds will be represented by beneficial interests in a permanent global certificate (the “**Global Certificate**”) in registered form, which will be registered in the name of a nominee of, and shall be deposited on 18th April, 2002, as the Closing Date with a common depositary for, Euroclear Bank S.A./N.V. as operator of the Euroclear System (“**Euroclear**”) and Clearstream Banking, *société anonyme* (“**Clearstream, Luxembourg**”).

The Company has prepared the audited financial statements as at and for the years ended 31st December, 1999, 2000 and 2001, in accordance with accounting principles generally accepted in the ROC.

NOTICE TO INVESTORS

Each purchaser of Bonds will be deemed to have represented and agreed as follows (terms that are defined in Regulation S under the Securities Act and used in the following section have the meanings assigned in Regulation S):

- (1) it is purchasing the Bonds for its own account or for an account with respect to which it exercises sole investment discretion, and it and any such account is outside the United States and is not a U.S. person;
- (2) it acknowledges that neither the Bonds nor the Shares issued upon conversion of the Bonds have been or will be registered under the Securities Act or with any securities regulatory authority of any jurisdiction and may not be offered or sold within the United States except as set forth below;
- (3) it understands and agrees that if in the future it decides to resell, pledge or otherwise transfer any Bond or beneficial interest therein, or any Shares issued upon conversion of the Bonds, it may do so only (i) in an offshore transaction meeting the requirements of Rule 903 or Rule 904 of Regulation S, (ii) pursuant to an exemption from registration under the Securities Act, if available, or (iii) pursuant to an effective registration statement under the Securities Act, and in each of cases (ii) and (iii), in accordance with applicable securities laws of the states of the United States;
- (4) it agrees to, and each subsequent holder is required to, notify any purchaser from it of a Bond or beneficial interest therein of the resale restrictions referred to in section (3) above, if then applicable;
- (5) it understands that, except in the circumstances referred to under the heading “The Form of the Bonds”, the Bonds, and beneficial interests therein, will be represented by the Global Certificate;
- (6) it understands that the Global Certificate will bear a legend to the following effect (unless otherwise agreed by the Company):

“THIS SECURITY HAS NOT BEEN AND WILL NOT BE REGISTERED UNDER THE UNITED STATES SECURITIES ACT OF 1933 (THE “SECURITIES ACT”) OR WITH ANY SECURITIES REGULATORY AUTHORITY OF ANY JURISDICTION AND, ACCORDINGLY, MAY NOT BE RESOLD, PLEDGED OR OTHERWISE TRANSFERRED TO A U.S. PERSON OR WITHIN THE UNITED STATES EXCEPT PURSUANT TO AN EXEMPTION FROM REGISTRATION UNDER THE SECURITIES ACT OR PURSUANT TO AN EFFECTIVE REGISTRATION STATEMENT UNDER THE SECURITIES ACT.

THIS LEGEND MAY BE REMOVED AFTER THE EXPIRATION OF FORTY DAYS FROM THE ORIGINAL ISSUANCE OF THE ZERO COUPON CONVERTIBLE BONDS DUE 2005 OF KING YUAN ELECTRONICS CO., LTD.”; and

- (7) it acknowledges that the Company and the Managers and others will rely upon the truth and accuracy of the foregoing acknowledgements, representations and agreements; and if it is acquiring the Bonds as a fiduciary or agent for one or more accounts, it represents that it has sole investment discretion with respect to each such account and that it has full power to make the foregoing acknowledgements, representations and agreements on behalf of each such account.

For further information about the requirements under the Indenture to effect exchanges or transfers of interests in the Global Certificates and of Bonds in certificated form, see “The Form of the Bonds”.

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Offering Circular contains forward-looking statements that involve risks and uncertainties. Forward-looking terminology include “may,” “will,” “expect,” “anticipate,” “estimate,” “continue,” “believe,” “forecast,” “project” and other similar words. Statements that include such terminology are forward-looking statements. The Company’s actual results could differ materially from those anticipated in these forward-looking statements as a result of the risks and uncertainties faced by the Company described elsewhere in this Offering Circular. The Company undertakes no obligation after the date of this Offering Circular to update publicly any forward-looking statements for any reason, even if new information becomes available or other events occur in the future which may affect information contained herein.

ENFORCEABILITY OF FOREIGN JUDGMENT IN THE ROC

King Yuan is a company limited by shares incorporated under the ROC Company Law. All of the Company’s directors and executive officers, and its respective supervisors are residents of the ROC and a substantial portion of the assets of the Company and such persons are located in the ROC. As a result, it may not be possible for investors to effect service of process upon the Company or such persons outside the ROC, or to enforce against any of them judgments obtained in courts outside the ROC.

Any final judgment obtained against the Company or such persons in any court other than the courts of the ROC in respect of any legal suit or proceeding arising out of or relating to the Bonds will be enforced by the courts of the ROC without further review of the merits only if the court of the ROC in which enforcement is sought is satisfied that: (i) the court rendering the judgment has jurisdiction over the subject matter according to the laws of the ROC; (ii) the judgment is not contrary to the public order or good morals of the ROC; (iii) if the judgment was rendered by default by the court rendering the judgment, the Company or such persons were served within the jurisdiction of such court, or process was served on the Company or such persons with judicial assistance of the ROC; and (iv) judgments of the courts of the ROC are recognized and enforceable in the court rendering the judgment on a reciprocal basis. Remittance out of the ROC of any amount recovered from enforcing a foreign judgment in the ROC is also subject to the Foreign Exchange Control Statute and regulations as described in “Appendix B — Foreign Investment and Exchange Controls in the ROC” herein.

TABLE OF CONTENTS

	Page		Page
Summary	1	The Form of the Bonds	77
Risk Factors	10	Description of the Shares	80
Use of Proceeds	17	Taxation	85
Market Price Information	18	Subscription and Sale	87
Dividends and Dividend Policy	19	Legal Matters	89
Exchange Rate	20	Accountants	89
Capitalization	21	General Information	90
Business	22	Summary of Significant Differences	
Selected Financial Information	38	between ROC GAAP and U.S. GAAP ...	92
Management's Discussion and Analysis of		Index to Financial Statements	F-1
Financial Condition and Results of		Appendix A — Taiwan, The Republic	
Operation	40	of China	A-1
Management and Employees	52	Appendix B — Foreign Investment and	
Principal Shareholders	57	Exchange Controls in the ROC	B-1
Changes in Issued Share Capital	57	Appendix C — The Securities Market	
Terms and Conditions of the Bonds	58	of The ROC	C-1

CERTAIN DEFINED TERMS, CONVENTIONS AND CURRENCY OF PRESENTATION

Except where the context otherwise requires, all references herein to “**King Yuan**” and the “**Company**” are to King Yuan Electronics Co., Ltd. All references herein to “**Taiwan**” or the “**ROC**” are to the island of Taiwan and other areas under the effective control of the Republic of China. All references herein to the “**ROC Government**” or the “**ROC Company Law**” are references to the government of the Republic of China and the Company Law of the Republic of China, respectively. All references herein to “**ROC GAAP**” are to the “Rules Governing Preparation of the Financial Statements of Securities Issuers” and accounting principles generally accepted in the ROC and “**U.S. GAAP**” are to accounting principles generally accepted in the United States, respectively. All references herein to the “**TSE**” are references to the Taiwan Stock Exchange and all references herein to the “**ROSE**” are to the ROC Over-the-Counter Stock Exchange. All references herein to the “**PRC**” are to the People’s Republic of China.

Except as otherwise indicated, all financial information set forth herein with respect to various members of the Company has been presented in New Taiwan Dollars.

The Company publishes its financial statements in New Taiwan Dollars, the lawful currency of the ROC. All references herein to “**New Taiwan Dollars**”, “**NT Dollars**” and “**NT\$**” are to New Taiwan Dollars and references to “**United States Dollars**”, “**U.S. Dollars**” and “**U.S.\$**” are to United States Dollars. All translations from New Taiwan Dollars to United States Dollars were made on the basis of the average of buying and selling exchange rates in Taipei for cable transfers in NT Dollars per U.S. Dollar as certified by Bank of Taiwan of NT\$34.98 = U.S.\$1.00 as of 31st December, 2001. All amounts translated into United States Dollars as described above are provided solely for the convenience of the reader, and no representation is made that the NT Dollar or U.S. Dollar amounts referred to herein could have been or could be converted into U.S. Dollar or NT Dollar, as the case may be, at any particular rate, the above rates or at all. See “Exchange Rate”. The closing rate between the NT Dollar and the U.S. Dollar on 10th April, 2002 was NT\$34.979 = U.S.\$1.00.

SUMMARY

The following summary is qualified in its entirety by the more detailed information and financial statements contained elsewhere herein.

King Yuan Overview

The Company is one of the leading independent providers of semiconductor test and other backend semiconductor manufacturing services on a stand-alone or turnkey basis in Taiwan. The Company offers a full integrated suite of test services and other backend integrated circuit (“IC”) processing services, which constitute the final procedures necessary to prepare semiconductor devices for further use. The test services provided by the Company cover a full range of both standard and customized test solutions, including wafer probing (“C/P”) and final test (“F/T”) for logic, mixed-signal and memory devices and burn-in. The semiconductors tested by the Company are extensively used in personal computers, personal computer peripherals, consumer products and telecommunication products. The backend semiconductor manufacturing services provided by the Company consist of wafer grinding and dicing, chip on board packaging (“COB”), test, ICs tape and reel and drop shipment of finished semiconductor devices. Through its strategic alliance with Amkor Technology Inc. (“Amkor”), the Company is able to offer its customers contract packaging services. The Company is also able to provide its customers all backend semiconductor manufacturing services from testing to drop-shipment on a turnkey basis.

The Company’s corporate headquarters, test and processing facilities are located in the semiconductor manufacturing corridor of Taiwan. Taiwan is home to the world’s largest independent wafer foundries and also one of the world’s leading suppliers of outsourced semiconductor manufacturing services. The Company’s close proximity to and relationships with Taiwan’s leading wafer foundries allow it to capture IC test and backend manufacturing business arising from the trend towards outsourcing and the growth of the semiconductor industry. This enables the Company to provide its customers with seamless services in Taiwan for all of their IC test and backend manufacturing needs, thereby minimizing the time required to deliver finished semiconductor devices to the market.

The Company’s customers include major fabless IC design companies, integrated device manufacturers and semiconductor foundries. The Company provides services to customers in both logic and memory semiconductor markets. In 2001, the Company’s top five customers were Macronix International Corporation, MediaTek Incorporation, Silicon Storage Technology, Inc., United Microelectronics Corporation and Vanguard International Semiconductor Corporation. The Company has established technical and sales teams near major customer facilities, including the Hsin-Chu Science-Based Industrial Park in Taiwan (“**Hsin-Chu Science Park**”), which work with its customers on developing and implementing new test technologies as tolerances of integrated circuitry become smaller and ICs become more sophisticated.

Although the Company experienced operating and net losses in 2001, the net revenues of the Company grew at a compound annual growth rate of 65.2 per cent. from NT\$521.2 million in 1997 to NT\$3,877.3 million (U.S.\$110.8 million) in 2001. The Company’s net revenues in 2001 decreased by 7.3 per cent. from its net revenues of NT\$4,181.6 million in 2000. The Company’s earnings before interest, income tax, depreciation and amortization were NT\$2,266.4 million and NT\$1,612.1 million (U.S.\$46.1 million) in 2000 and 2001 respectively, compared to NT\$ 894.2 million in 1999.

The Company has made significant investments in purchasing technologically advanced test machinery and equipment; which enable the Company to test highly parallel, high speed, high pin-count and highly integrated devices, such as optical image-sensing ICs and system on chip (“SOC”). As at 31st December, 2001, approximately 20 per cent. of the Company’s total employees have engineering background; such skilled labor complements the Company’s initiatives on such technologically advanced test machinery and equipment.

The Company was incorporated on 28th May, 1987 and its Shares have been listed on the TSE since May 2001. The Company’s headquarters are located at No. 1, Lane 99, Pu-Ding Road, Hsin-Chu 300, Taiwan, ROC, and its telephone number is 886-3-5751888.

Competitive Strengths

The Company believes that the following strengths contribute to its competitive position in the relevant markets:

High barriers to entry

It is difficult for potential competitors to enter into the test and backend semiconductor manufacturing services industry for the following reasons:

- High capital cost of the machinery and equipment required for testing;
- Competition for experienced research, development and management personnel; and
- The investment required to build long-term cooperative relationships and trust by customers. The Company has established close cooperative relationships with fabless IC design companies, integrated device manufacturers and semiconductor foundries. The Company believes that it is well regarded and trusted by customers for the range and quality of its services as well as its delivery lead times.

Market demand for backend semiconductor manufacturing services continues to grow

According to a report by World Semiconductor Trade Statistics in 2001, the worldwide semiconductor device market revenue will grow from U.S.\$149 billion in 1999 to U.S.\$239 billion in 2003, at an annual compound growth rate of 12.5 per cent. It is expected that the IC test business will grow vigorously with the strong demand in the global semiconductor market. The Company believes that it is well positioned to benefit from such growth.

Trend to outsourcing and specialization in the semiconductor industry

As specialization in the semiconductor industry increases, integrated device manufacturers and fabless IC design companies have gradually raised the percentage of outsourced process, in consideration of returns on operating capital and financial risk. With the expansion of the international reach of domestic wafer foundries and the active entry by domestic DRAM manufacturers into strategic alliances with leading international manufacturers, the domestic IC industry has generated significant business opportunities for the IC test industry. The Company has a full line of state of the art test equipment including both imported equipment and equipment designed and developed in-house and can provide a full spectrum of test services such as logic IC, mixed-signal IC and memory IC test and IC burn-in. The Company also provides other backend semiconductor manufacturing services, including wafer grinding and dicing, COB, tape and reel and drop shipment. The Company has also entered into an alliance agreement with Amkor. Amkor is one of the world's largest independent providers of semiconductor packaging and test services, and is one of the leading developers of advanced semiconductor packaging and test technologies. Through flexible contracting and subcontracting arrangements, the Company provides its customers with packaging or assembly services through Amkor. The Company believes this provides a competitive advantage in attracting and keeping customers who demand for one-stop turnkey backend semiconductor manufacturing services.

Advantage of geographic location

The Company's headquarters are in Taiwan and are located close to the Hsin-Chu Science Park. The Company believes that its close proximity to and strong relationship with Taiwan's leading fabless IC design companies, integrated device manufacturers and semiconductor foundries enable the customers to easily integrate all of their outsourced manufacturing needs and efficiently manage their supply chains. The Company's customers can enjoy shorter transportation times from upstream manufacturers and product delivery lead times. The Company also capitalizes on its proximity to its customers by offering design and new product validation services, and by providing feedback on new product designs. By becoming involved at the design stage, the Company believes that it is able to increase penetration and customer loyalty. In addition, the Company learns valuable market information about IC design trends and demand for new products that help the Company maintain its leading position.

Strategy

Offer full spectrum of test and other backend semiconductor manufacturing services

Many of the Company's customers require a wide range of test technologies which covers logic, mixed-signal and memory devices. They also require other backend semiconductor manufacturing services on a turnkey or stand-alone basis, which include wafer grinding and dicing, COB, test, tape and reel and drop shipment of the semiconductor devices directly to their customers. The Company believes that as semiconductor suppliers face shorter time-to-market demands and shorter product cycles, turnkey services will become an increasingly important aspect of the customers' manufacturing and product distribution strategies. The Company is one of a small number of vendors capable of providing such services on a turnkey basis.

The Company has also made significant investments to construct, fit out and equip large-scale test facilities that deploy hundreds of sophisticated test units, to ensure that the Company has the capability to design and perform the most technologically demanding test functions. The Company employs the most technologically advanced imported test machinery and equipment, and also cost-efficient test units designed and developed in-house. This gives the Company the ability to test highly parallel, high speed, high pin-count and highly integrated devices, such as optical image-sensing ICs, as well as the ability to achieve cost-efficient high volume test of lower speed ICs.

Leverage relationships with foundries and IC design service companies to provide total solution to the customers

The Company conducts joint marketing with semiconductor foundries and IC design service companies to capture the test and other backend semiconductor manufacturing requirements of their customers. These customers comprise principally IC design companies, integrated device manufacturers and systems original equipment manufacturers. The Company believes that by leveraging the relationships with foundries and IC design service companies, it is able to attract new customers as well as maintain its existing customers.

Focus on customer service

The Company believes that its ability to anticipate and meet its customers' needs is critical to attracting and retaining leading semiconductor suppliers as customers. The Company strives to work closely with its customers on developing and fulfilling their current and future semiconductor test needs. The Company positions itself as a high-tech service business and has a well established customer-oriented culture, and continuously enhances the quality, cost effectiveness, cycle times, and flexibility of its services. To provide a dedicated customer support infrastructure to its customers, the Company has established technical and sales teams strategically located near major customers' facilities and technology development and manufacturing centers, including the Hsin-Chu Science Park.

Further improve IC test and backend manufacturing technology

The Company intends to continually expand its portfolio of test and other backend semiconductor manufacturing technologies through internal development and joint development with customers. The Company believes that leading technology is its most valuable asset, and that the ability to offer leading test technologies is critical to attracting and retaining customers and maintaining high margins. The Company is currently developing new test technologies which allow it to test newly developed sophisticated semiconductors such as chips with SOC technologies and advanced radio frequency ("RF") chips which are utilized in telecommunication devices.

Expand the customer base and operations

The Company intends to expand its customer base geographically by targeting customers located in the United States, Japan and Europe. The Company will expand its current sales and marketing team and the operations of its United States subsidiary, KYEC USA Corp. Currently, the Company schedules frequent visits by its sales team to Japan to visit existing customers and to source for new customers. The Company has identified Europe as a potential market and intends to enhance its marketing efforts to European customers by scheduling regular visits by its sales and marketing team.

The Company also intends to expand its operations in South East Asia and the PRC. This will allow the Company to tap the business opportunities arising from the growing trend among its customers to locate their operations in these areas. By locating its operations closer to its customers, the Company believes that it can compete more effectively with other providers of test and other backend semiconductor manufacturing services with respect to delivery time and the pricing of its services.

The Issue

Issuer	King Yuan Electronics Co., Ltd.
Bonds	U.S.\$120,000,000 Zero Coupon Convertible Bonds due 2005 convertible into fully-paid common shares with a par value of NT\$10 each of the Company (“Shares”).
Issue Price	100 per cent.
The Offering	The Bonds will not be offered or sold in the ROC or in the United States. The Bonds will be offered only in offshore transactions in reliance on Regulation S under the U.S. Securities Act of 1933.
Closing Date	<u>18th April</u> , 2002
Maturity Date	<u>18th April</u> , 2005
Status	The Bonds will be direct, unconditional, unsecured and unsubordinated obligations of the Company and will rank at least <i>pari passu</i> without any preference or priority among themselves and shall at all times rank at least equally with all other present and future direct, unsecured and unsubordinated obligations of the Company.
Interest	No interest will be payable on the Bonds prior to the Maturity Date, except in certain circumstances following an event of default. See Condition 10 in “Terms and Conditions of the Bonds”
Withholding Tax	Premium (if any) and interest (if any) payable on the Bonds to non-residents of the ROC is subject to a withholding tax in the ROC equal to 20 per cent. of the gross amount of such premium (if any) and interest (if any). The Company will gross up such amounts as will result in the receipt by the Bondholders of the net amounts after such withholding or deduction equal to the amounts which would otherwise have been receivable by them had no such withholding or deduction been required.
Tax Redemption	The Company may redeem all but not part of the Bonds at their principal amount in the event of changes in ROC taxation which will result in additional costs to the Company to gross up for payment of principal, or to gross up for payments of premium (if any) or interest (if any), at the rate exceeding 20 per cent. See Condition 8(D) in “Terms and Conditions of the Bonds”

Conversion	Subject to prior redemption and otherwise provided herein, the Bonds are convertible at any time on or after <u>18th May</u>, 2002 and prior to the close of business (at the place at which the Bond is deposited for conversion) on <u>18th March</u>, 2005, except during any Closed Period (defined below), into Shares at a conversion price per Share (subject to adjustment in certain circumstances) (the “Conversion Price”) of NT\$<u>24.50</u> per Share, which is equivalent to US\$<u>0.700</u> per Share, determined on the basis of a fixed exchange rate of NT\$<u>34.979</u> = U.S.\$1.00 (the “Fixed Exchange Rate”). The Conversion Price will be subject to adjustment for, among other things, subdivision or consolidation of Shares, bonus issues of Shares, rights issues, distribution of stock dividends and other dilution events. Fractional Shares will not be issued or paid in cash, or in any other means. See Condition 6 in “Terms and Conditions of the Bonds — Conversion”. <u>To the extent permitted under the laws of the ROC</u>, the converting Bondholders will be entitled to the annual dividend distributions or other benefits if the conversion of the Bonds takes place prior to three (3) Taiwan business days (defined below) before the Company’s notification to the TSE in respect of a record date (and the relevant closure of the shareholders’ register) for determining the identity of shareholders who are entitled to such distributions in each relevant year. The Company shall, within five (5) Trading Days after the Conversion Date, issue and deliver the Shares converted from the Bonds to the converting Bondholder or its designee, subject to the requirements relating to the conversion in the Indenture are satisfied.
Conversion Price Reset . .	The Conversion Price shall be adjusted on each Reset Date (defined below), in the event that the average closing price of the Share on the TSE translated into U.S. Dollars at the then Prevailing Rate (defined below) for 30 consecutive Trading Days immediately prior to a Reset Date is less than the Conversion Price then in effect on the relevant Reset Date converted into U.S. Dollars at the Fixed Exchange Rate of NT\$<u>34.979</u> = US\$1.00; provided that the Adjusted Conversion Price (on a cumulative basis, if applicable) shall not be less than 80 per cent. of the initial Conversion Price after anti-dilution adjustments, if any. See Condition 6(D) in “Terms and Conditions of the Bonds — Conversion”.
Alternative Conversion Price Reset	The Bondholders are entitled, within seven Trading Days after <u>18th March</u>, 2004 and <u>18th March</u>, 2005 (each an “Alternative Reset Date”), to convert the Bonds at an Alternative Conversion Price equal to <u>88.0</u> per cent. and <u>85.0</u> per cent., respectively, of the then market price which is the lowest among the average closing prices of the Shares of 10, 15 and 20 Trading Days immediately preceding the applicable Alternative Reset Date. See Condition 6(E) in “Terms and Conditions of the Bonds — Conversion”.
Final Redemption	Unless previously redeemed, converted or repurchased and cancelled in the circumstances referred to in Condition 8 in “Terms and Conditions of the Bonds”, the Bonds will be redeemed at <u>110.87</u> per cent. of their principal amount in U.S. Dollars on <u>18th April</u>, 2005. See “Withholding Tax” above and Condition 8(A) in “Terms and Conditions of the Bonds — Redemption, Purchase and Cancellation”.

Redemption at the option of
the Company

The Company may, having given not less than 40 nor more than 60 days' notice to the Bondholders, call all, or part only, of the Bonds on or at any time one year after the Closing Date at their principal amount in the event that the closing price of the Shares on the TSE in U.S. Dollars at the prevailing rate for each of the 30 consecutive Trading Days, the last of which occurs not more than 10 days prior to the date upon which notice of such redemption is published, is at least 150 per cent. of the Conversion Price in effect on each such Trading Day translated into U.S. Dollars at the fixed exchange rate of NT\$34.979 = U.S.\$1.00. The Company may, having given the same notice, redeem the outstanding Bonds in whole, but not in part, at their principal amount (i) in the event that 90 per cent. of the Bonds have been previously redeemed, repurchased or converted, or (ii) in the event of changes in ROC taxation laws or regulations which will result in additional costs to the Company to gross up for payment of principal, or to gross up for payments of premium, if any, or interest, if any, at the rate exceeding 20 per cent. See Conditions 8(B) and 8(D) in "Terms and Conditions of the Bonds — Redemption, Purchase and Cancellation".

Redemption at the option of
Bondholders

Until and unless previously redeemed, converted or purchased and cancelled, the Company will at the bondholder's option redeem all or part of the Bondholder's Bonds on 18th April, 2004 at 107.12 per cent. of the principal amount. See Condition 8(C) in "Terms and Conditions of the Bonds — Redemption, Purchase and Cancellation".

Form and Registration of
the Bonds

The Bonds will be issued in registered form in the denomination of U.S.\$10,000 each. The Bonds will be offered and sold in principal amounts of U.S.\$10,000 or an integral multiple thereof. The Bonds will initially be represented by a Global Certificate deposited with The Bank of New York, as common depositary for, and registered in the name of a nominee for, Euroclear and Clearstream, Luxembourg. Beneficial interests in the Global Certificate will be shown on, and transfers thereof will be effected only through, records maintained by Euroclear and Clearstream, Luxembourg and their participants. Except as described herein, certificates for Bonds will not be issued in exchange for beneficial interests in the Global Certificate.

Governing Law

The laws of the State of New York, USA.

Trustee

The Bank of New York.

Listing

Application has been made to list the Bonds on the Luxembourg Stock Exchange. The Shares are listed on the TSE and application will be made for the Shares issuable upon conversion of the Bonds to be listed on the TSE.

Use of Proceeds

The net proceeds from the offering of the Bonds, after deducting underwriting fees, including selling concessions, and other expenses, are estimated to be approximately U.S.\$119.15 million. The net proceeds will be used to repay the bank loans associated with procurement of machinery and equipment.

Summary Financial Data

The summary income statement data for the years ended 31st December, 1999, 2000 and 2001 and the summary balance sheet data as of 31st December, 1999, 2000 and 2001 set forth below are derived from the Company's audited financial statements included in this Offering Circular and are qualified in their entirety by reference to such financial statements, including the notes thereto, and should be read in conjunction with them and with "Management's Discussion and Analysis of Financial Condition and Results of Operations" included elsewhere herein. Financial information for such periods may not be comparable to financial information for subsequent periods. The financial statements of the Company have been prepared and presented in accordance with ROC GAAP and reporting practices in the ROC. For a discussion of certain differences between ROC GAAP and U.S. GAAP, see "Summary of Significant Differences Between ROC GAAP and U.S. GAAP".

	As of 31st December,					
	1997	1998	1999	2000	2001	2001
	NT\$	NT\$	NT\$	NT\$	NT\$	U.S.\$
	(in millions)					
Income Statement						
Operating revenue-net	521.2	760.6	1,745.0	4,181.6	3,877.3	110.8
Cost of revenues	383.2	518.0	1,114.8	2,705.3	4,129.7	118.0
Gross profit (loss)	138.0	242.6	630.2	1,476.3	(252.4)	(7.2)
Operating expenses	58.3	76.7	130.8	305.8	436.8	12.5
Operating income (loss)	79.7	165.9	499.4	1,170.5	(689.2)	(19.7)
Non-operating income	1.8	10.0	11.3	43.1	153.1	4.4
Non-operating expenses	12.1	47.7	56.6	210.5	555.0	15.9
Income before income tax and minority interest	69.4	128.2	454.1	1,003.1	(1,091.1)	(31.2)
Income tax benefit (expense)	(3.4)	11.5	34.6	175.3	299.5	8.6
Net income (loss)	66.0	139.7	488.7	1,178.4	(791.6)	(22.6)
EBITDA ⁽¹⁾	116.0	299.3	894.2	2,266.4	1,612.1	46.1

- (1) EBITDA refers to earnings before interest, income tax, depreciation and amortization. EBITDA should not be construed as an alternative to operating income or any other measure of performance or as an indicator of the Company's operating performance, liquidity or cash flows generated by operating, investing and financing activities. The items of net income excluded from EBITDA are significant components in understanding and assessing the Company's financial performance, and the Company's computation of EBITDA may not be comparable with other similarly titled measures of other companies. The Company has included the information concerning EBITDA because the Company believes it is a useful supplement to cash flow data as a measure of the Company's performance.

	As of 31st December,					
	1997	1998	1999	2000	2001	2001
	NT\$	NT\$	NT\$	NT\$	NT\$	U.S.\$ ⁽¹⁾
	(in millions)					
Balance Sheet						
Current assets	201.8	412.5	1,151.1	3,050.6	916.2	26.2
Long-term investments	—	—	—	4.9	5.1	0.1
Property, plant and equipment	384.2	1,101.2	4,349.6	12,869.2	15,052.3	430.3
Other assets	18.1	38.5	40.1	291.0	2,042.1	58.4
Total Assets	604.1	1,552.2	5,540.8	16,215.7	18,015.7	515.0
Current liabilities	312.4	376.6	1,062.5	3,601.0	4,675.1	133.6
Long-term liabilities	43.6	—	1,363.4	3,412.8	4,939.1	141.2
Other liabilities	4.1	4.7	6.5	19.2	20.5	0.6
Total liabilities	360.1	381.3	2,432.4	7,033.0	9,634.7	275.4
Total stockholders' equity	244.0	1,170.9	3,108.4	9,182.7	8,381.0	239.6
Total liabilities and stockholder' equity	604.1	1,552.2	5,540.8	16,215.7	18,015.7	515.0
Per Share Data						
Earnings per Share ⁽²⁾	6.32	2.58	5.00	5.08	(1.81)	(0.05)
Adjusted earnings per Share ⁽³⁾ (in dollars)	1.42	0.78	1.94	3.06	(1.81)	(0.05)

- (1) Translated into United States Dollars using the exchange rate published by the Bank of Taiwan at 31st December, 2001 of NT\$34.98 = U.S.\$1.00.
- (2) Earnings per Share are calculated by dividing net income by the weighted average number of shares outstanding during each year before adjusting retroactively for the effect of stock dividends and employees' bonuses. However, no adjustment has been made with respect to the stock dividends and capitalization of employees' bonuses approved by the shareholders on 12th March, 2001.
- (3) Adjusted earnings per Share are calculated by dividing net income by the weighted average number of shares outstanding during each year after adjusting retroactively for the effect of stock dividends, including the stock dividends and capitalization of employees bonus approved by the shareholders on 12th March, 2001.

RISK FACTORS

Any potential investor in, and purchaser of, the Bonds (including the Shares issued pursuant to conversion thereof) must pay particular attention to the fact that the Company is governed in the ROC by a legal and regulatory environment which, in certain material respects, may differ from that which prevails in other countries. Prior to making an investment decision, all such prospective investors and purchasers should carefully consider all of the information contained in this Offering Circular, including the information set out below. The occurrence of any of the following risks could have a material adverse effect on the Company's business, results of operation, financial condition and future prospects or cause the market price of the Shares and the Bonds to fall significantly.

Risks Relating to The Company And The Company's Business

The Company experienced recent operating and net losses

The Company experienced operating and net losses in 2001, primarily because of the general downturn in the semiconductor industry commencing in the second quarter of 2001. Both the volume and the average unit prices of sales for 2001 were affected. In addition, due to negative market conditions, the Company's customers increasingly requested concessions on pricing, which was the primary cause of a 113.2 per cent. increase in sales returns and allowances, from NT\$43.9 million in 2000 to NT\$93.6 million (U.S.\$2.7 million) in 2001. There is no assurance that the Company will regain the levels of profitability that it has achieved in the past or that losses will not occur in the current period or future periods. The revenues for the first two months of 2002 decreased by 36.9 per cent. compared to the corresponding period in 2001.

If the Company and the Chairman of the Company do not successfully defend the securities litigation, the Company's business and financial condition may be adversely affected

One corporate and two individual shareholders have brought suit against the Company and the Chairman of the Company alleging that the Company tried to attract investors to purchase its shares before its initial public offering, which was conducted in May 2001, by means of untrue statements made by the Company and its management. The Chairman is named as the legal representative of the Company and in his personal capacity. The plaintiffs' allegations relate to the Company's published projections and other statements made by the Company and its management.

In addition to the civil proceedings, a criminal complaint has been filed with the office of the Hsin-Chu district attorney, seeking prosecution of the Company and the Chairman for making fraudulent statements. The case is currently under investigation by the district attorney.

Although the Company is vigorously defending the civil suit, no assurance can be given as to the final disposition. Moreover, there can be no assurance that other plaintiffs similarly situated may not bring similar claims, or seek to certify a class of plaintiffs for a class action. A successful class action could have a material adverse effect on the Company's financial position.

If prosecution is commenced and a guilty verdict is brought, the Company could suffer reputational damage. In addition, the demands placed on the time and resources of senior management by the necessity to defend civil or criminal proceedings could have an adverse impact on the management and operations of the Company.

If the Company is unable to maintain high capacity utilization rates, its losses may increase

The IC test business requires large capital expenditures for testing machinery and equipment. During the years 1999, 2000 and 2001, the Company incurred NT\$3,260.9 million, NT\$9,521.6 million and NT\$5,283.7 million of capital expenditures. The Company's fixed costs are correspondingly high, reflecting the financing costs and depreciation charges associated with these fixed assets. Given the high fixed costs of the Company's business, a high capacity utilization rate allows the Company to maintain higher margins because it allows the Company to allocate fixed costs over a greater number of units the Company tests. Increases or decreases in capacity utilization rates can have a significant effect on the Company's business. Accordingly, the Company's ability to maintain or enhance its margins will continue to depend, in part, on its ability to maintain high capacity utilization rates.

In order to maintain high capacity utilization rates, the Company must:

- ensure that its test technology meets the customers' needs; and
- install advanced equipment in anticipation of new business and improved market conditions.

There is no guarantee that a high utilization rate is sustainable. Beginning in the second quarter of 2001, the Company's capacity utilization rates have been negatively affected by an unexpected downturn in the semiconductor industry. As a result, the Company has incurred substantial operating losses and net losses for the year ended 31st December, 2001, and forecasts that losses will continue for the first half of 2002. There is no assurance that future declines in the semiconductor industry or other factors will not seriously harm capacity utilization or cause the Company to incur further losses.

The Company's operating results are subject to significant fluctuations

The Company's historical revenues and net profit or loss have varied, at times significantly, from quarter to quarter. The Company's future revenues and net profit or loss may vary significantly due to a combination of factors. These factors include:

- the Company's ability to quickly adjust to unanticipated declines or shortfalls in demand and market prices for its test services, due to its high percentage of fixed costs;
- timing of capital expenditures in anticipation of future orders;
- changes in prices of its test services;
- volume of orders relative to its test capacity; and
- the Company's ability to obtain adequate test equipment on a timely basis.

Due to the factors listed above, it is possible that the Company's future operating results or growth rates may be below the expectations of research analysts and investors.

The cyclical nature of the semiconductor industry makes the Company particularly vulnerable to economic downturns and changes in the semiconductor industry

The semiconductor industry is highly cyclical and economic downturns in the past have caused reduced demand in the Company's services, rapid erosion of average selling prices, low capacity utilization and production overcapacity in this industry. Beginning in the second quarter of 2001, the Company experienced intense competition as a result of general economic downturn and oversupply of test capacity in the local market. This caused average prices of many of the semiconductor test services to decrease significantly. These decreases in average prices and volume led to decreases in the Company's gross margins which seriously affected the Company's operating results. The Company expects that average prices for many of the existing services may decline in future economic downturns. If declines in average prices are not offset by reductions in the cost of providing these services, gross margins will decline and the Company's operating results may be materially and adversely affected.

The Company's profitability depends on its ability to respond to rapid technological changes in the semiconductor industry

The semiconductor industry is characterized by rapid increases in the diversity and complexity of semiconductors. As a result, the Company expects that it will need to constantly offer more sophisticated test technologies and processes in order to respond to competitive industry conditions and customer requirements. If the Company fails to develop, or obtain access to, advances in test technologies or processes, it may become less competitive and less profitable.

The Company is highly dependent on the personal computer industry and a downturn in the personal computer industry would likely influence the operating results adversely

A significant percentage of the Company's net operating revenue is derived from customers who use the test services of the Company to make semiconductors for personal computers and personal computer peripherals. In 1999, 2000 and 2001, a substantial portion of the Company's net operating revenues were attributable to customers whose products are primarily used in personal computers or personal computer peripherals. Any significant decrease in the demand for personal computers may therefore decrease the demand for the Company's services and would likely influence its operating results adversely. In addition, the declining average selling price of personal computers places significant pressure on the Company's revenue and gross profit margins as well as the prices of the components that are used in these personal computers and personal computer peripherals.

The Company depends on a limited number of customers for a substantial portion of its revenues and a loss of any one of these customers would result in the loss of a significant portion of its revenues

The Company is dependent on a limited number of customers for a substantial portion of its business. In 1999, 2000 and 2001, 50.3 per cent., 44.3 per cent. and 49.2 per cent. of its net operating revenues, respectively, were derived from the services provided to its top five customers. The Company expects that it will continue to depend on a relatively limited number of customers for a significant portion of its net operating revenues because of the concentration of demand for its products and services. The ability to maintain close and satisfactory relationships with its customers is important to the future success of the Company's business. None of the Company's customers is presently obligated to purchase test services or to provide the Company with binding forecasts of purchases for any period. If any of its significant customers reduces, delays or cancels its orders, the Company's business would be seriously harmed because each one of these customers accounts for a significant part of the Company's net operating revenues.

If capital resources required for the future expansion plans are not available, the Company may be unable to successfully implement its business strategy

The Company's business growth strategy will require substantial capital expenditures to fund equipment and facilities expansion. The growing demand for SOC and RF semiconductor test has and will continue to require significant capital expenditures on substrate test technology and equipment. In making these planned capital expenditures, the Company may need to obtain additional capital. It cannot be assured that additional financing will be available when the Company requires additional financing or available on terms satisfactory to it. If the Company is unable to obtain the necessary capital resources or financing, it will not be able to implement its business strategy, which could adversely affect the Company's future growth and operating results.

The Company may face significant competition from a number of competitors and from its customers' in-house test capabilities

The independent semiconductor backend process service industry is very competitive. The Company faces substantial competition from established test companies, including ASE Test Limited, ChipMos Technologies Inc., United Test Center and Siliconware Precision Industrial Limited. The Company also competes with the internal test capabilities of its customers who have in-house test capability, including semiconductor foundries, integrated device manufacturers and fabless IC design companies. Some of the competitors have invested substantial resources in substrate technology and have been able to market substrate packaging products for some time. Some of the Company's competitors have greater financial and other resources than the Company has, including established relationships with many large semiconductor companies which are the Company's current or potential customers. These relationships and lengthy qualification periods required by most of the Company's potential customers may prevent it from securing new customers. See "Business — Sales and Marketing — Qualification and Correlation by Customers".

In addition, the Company expects that there will be a significant increase in worldwide test capacity over the next few years. If growth in demand for this capacity fails to match the growth in supply, the Company expects more intense competition and pressure on the pricing of its services. Any significant increase in competition may erode the Company's margins and reduce its earnings or increase its losses.

If the outsourcing trend for test and other backend semiconductor manufacturing services does not continue, the Company could lose a significant number of its current customers and the Company may be unable to implement its business strategy plan

The Company depends on outsourcing of test and other semiconductor backend semiconductor manufacturing services by semiconductor foundries, integrated device manufacturers and fabless IC design companies. In recent years, semiconductor companies have increasingly subcontracted parts of the semiconductor production process, including test, to independent companies to reduce costs and shorten production cycles. However, there can be no assurance that the outsourcing trend will continue. If manufacturers become dissatisfied with the services of independent semiconductor test companies, they may return to utilizing in-house backend process capabilities, including test. Moreover, if there is an economic downturn, these manufacturers may choose to use their in-house capacities before subcontracting out the Company's services. A reversal of, or slowdown in, the outsourcing trend would seriously harm the Company's business and make it difficult for the Company to implement its growth plan.

If demand for the services of Taiwan's wafer foundries decreases, a significant source of the Company's sales would decrease, which would seriously harm the Company's business

In recent years, a substantial portion of the Company's net operating revenues were derived from the test of semiconductor wafers manufactured at Taiwan's wafer foundries. If the demand for foundry services offered by Taiwan's wafer foundries decreases for any reason, an important source of the Company's sales would be lost and the Company's operating results would be affected.

If the Company is unable to obtain equipment from its suppliers in a timely manner and at a reasonable cost, the Company's business may be adversely affected

The semiconductor test business is capital intensive and requires significant investment in expensive equipment manufactured by a limited number of suppliers. The market for semiconductor test equipment is characterized, from time to time, by intense demand, limited supply and long delivery cycles. From time to time, increased demand for new equipment may cause lead times for delivery to the Company to increase. In the past, increased demand for equipment has caused some equipment vendors to delay shipment of some or all of the Company's equipment orders. If the Company is unable to obtain equipment in a timely manner, it may be unable to meet customer orders or implement expansion plans, which could negatively impact on prospects as well as financial condition and results of operations. See "Business — Raw Materials and Equipment".

The Company depends on key management and the loss of any key management personnel may disrupt its business

The Company's success depends upon the continued service of key senior management. A majority of the senior management has served the Company for over three years and made substantial contributions to the Company's growth. The Company does not have employment contracts with its senior executives and none of the senior management is bound by a non-competition agreement. If the Company loses the services of key senior management it could be difficult to locate and integrate replacement personnel, which would adversely affect the Company's business.

The Company depends on its technical personnel and an inability to attract and retain them would jeopardize its operations

The Company's business depends on technology and, accordingly, the success of the Company depends on its ability to attract, retain and motivate large numbers of highly skilled employees, particularly engineering and technical personnel. Without sufficient numbers of skilled employees, the Company's operations and its ability to work with clients to design test processes for next generation ICs would be impaired. Competition for qualified engineering and technical employees in Taiwan is intense and replacement of qualified employees is difficult. The Company will require increased numbers of skilled employees at its proposed expansion facilities. If the Company is unable to attract, retain and motivate its engineering and technical personnel, the operations and expansion plans would be jeopardized and the operating efficiency would deteriorate.

Disruptions in the international trading environment may seriously decrease the international sales of the Company

A substantial portion of the Company's net operating revenues are derived from the provision of services to customers located outside of Taiwan. In 1999, 2000 and 2001, the Company's overseas customers accounted for 8.3 per cent., 27.2 per cent. and 27.9 per cent., respectively, of its net operating revenues. The Company expects sales to customers outside of Taiwan to continue to represent a significant portion of its net operating revenues. Disruptions in the international trading environment, including adverse changes in foreign government regulations, political unrest and international economic downturns, could negatively affect the business of the Company's customers and the demand for semiconductors and ICs. This could in turn adversely affect the business of the Company.

Exchange Rate Fluctuations

A substantial portion of the Company's net sales are denominated in NT Dollars, while the Company purchases a substantial amount of machinery and equipment in Japanese Yen and U.S. Dollars. Accordingly, the Company is exposed to movements in the exchange rates between U.S. Dollars and Japanese Yen on the one hand, and NT Dollars on the other hand. The Company recorded net exchange losses of NT\$11.7 million and NT\$25.2 million in 1999 and 2000, respectively, and net exchange gains of NT\$105.3 million (U.S.\$3.0 million) in 2001. The effect of future changes in currency exchange rates on the Company's results of operations cannot be accurately predicted. The Company, however, does not enter into forward foreign currency contracts or other financial derivatives to hedge the related foreign currency positions related to these transactions.

Risks Relating to the Offering

The Bondholders' ability to exercise their conversion rights may be limited

The Bonds are convertible into Shares at the option of the converting Bondholders pursuant to the terms of the Bonds. Purchasers of the Bonds will not be able to exercise their conversion right during the Closed Periods, as defined in the terms and conditions of the Bonds. Under current ROC law, regulations and policy, PRC persons are not permitted to hold or convert the Bonds or to register as shareholders of the Company.

A liquid market for the Bonds and Shares may not develop

Application has been made to have the Bonds listed on the Luxembourg Stock Exchange. However, there can be no assurance that an active trading market or a trading market for the Bonds will develop. The trading market for the Shares is the TSE on which the Shares were listed in May 2001. The Shares will not be listed on the Luxembourg Stock Exchange.

Shares eligible for future sale by the current shareholders may adversely affect the market price of the Shares

While the Company is not aware of any plans by any major shareholders to dispose of a significant amount of Shares, it cannot assure that one or more of the shareholders will not dispose of the Shares in the future. The Company also cannot predict the effect, if any, that future sales of the Shares, or the availability of the Shares for future sale, will have on the market price of the Shares prevailing from time to time. Sales of substantial amounts of common shares in the public market, or the perception that such sales may occur, could adversely affect the prevailing market price of the Shares.

Risks Relating to the ROC

The value of the Bondholders' investment may be adversely affected by the volatility of the ROC securities market

The ROC securities markets are smaller and more volatile than the securities markets in the United States and in certain European and other countries. In 1961, the Securities and Futures Commission established the Taiwan Stock Exchange to provide a marketplace for securities trading. The TSE is a corporation owned by government-controlled and private banks and enterprises. The TSE is independent of

entities transacting business through it, each of which pays a user's fee. Generally, all transactions in listed securities by brokers, traders and integrated securities firms must be made through the TSE. The TSE commenced operations in 1962. Since the early 1980s, the Securities and Futures Commission has actively encouraged new listings on the TSE and the number of listed companies grew from 119 in 1983 to 595 by the end of March 2002. As of 31st March, 2002, the market capitalization of companies listed on the TSE was NT\$11,570 billion. Any impairment of the liquidity of TSE listed companies could adversely affect the market price of the Shares.

The political status and international relations of the ROC may affect the Company and the Bonds

The Company is incorporated in the ROC. Significant assets of the Company are located in, and substantial revenues are derived from, its operations in the ROC. The ROC has a unique international political status. Since 1949, Taiwan and the Chinese mainland have been separately governed. The ROC, which was founded in 1912, governs Taiwan while the PRC, which was founded in 1949, has governed the Chinese mainland for the past 50 years. The ROC asserts that the ROC and the PRC are equal political entities which should enter into "state to state" relations, while the PRC claims that it is the sole government in China and that Taiwan is part of China. Although significant economic and cultural relations have been established during recent years between the ROC and the PRC, the PRC has refused to renounce the possibility that it may at some point use force to gain control over the ROC. These developments have from time to time had an adverse effect on the value of the TSE Index, ROSE Index and the price of the Shares. Relations between the ROC and the PRC may also have an adverse effect on the ROC's economy, the Company's results of operations and the market price and liquidity of the Shares and the Bonds. There can be no assurance that the present tensions will not worsen, which could have a significant adverse impact on the ROC's economy, the value of the TSE Index, ROSE Index, the price of the Shares and the Company's results of operations and financial condition.

The ROC congressional election on 1st December, 2001 was believed to increase political tensions between the ROC and the PRC. The election ended the Nationalist Kuomintang Party's role as the controlling party in the Legislative Yuan of ROC and the Democratic Development Party became the controlling party of the Legislative Yuan, as well as the Executive Yuan. Because the Democratic Development Party is to a certain extent considered as a supporter of the independence of Taiwan, the ROC-PRC relationship may be further tensed. The possibility of instability and uncertainty during this transition and thereafter could have significant adverse impact on the ROC's economy and investors may adopt a more cautious approach towards the ROC's securities markets and/or making investments in the ROC generally, and such factors may affect the price of the Shares and the Bonds.

Adverse economic conditions in Taiwan and Asia could affect the Company

Many economies in Asia, including the ROC, have recently experienced significant downturns and related difficulties. As a result of the decline in the values of the region's currencies, many Asian governments and companies have had difficulties in servicing foreign currency-denominated debt and many corporate borrowers have defaulted on their payment obligations. The currency fluctuations, as well as higher interest rates and other factors, have materially and adversely affected the economies of many countries and regions, including the ROC. The NT Dollar significantly weakened against the U.S. Dollar in the second half of 2001 negatively impacting the results of operations of many companies, see "Exchange Rates". Economic developments in Asia could materially and adversely affect the Company's business, results of operations and financial condition.

Financial reporting and accounting standards in the ROC differ from other countries; bonus share issuance

The Company is subject to financial reporting requirements in the ROC that differ in significant respects from those applicable to companies in certain other countries, including the United States and the United Kingdom. In addition, the Company's financial statements are prepared in accordance with the ROC GAAP, which differ in certain material respects from U.S. GAAP. See "Summary of Certain Differences Between ROC GAAP and U.S. GAAP". Potential investors should consult their own professional advisers for an understanding of such differences and how they might affect the financial information contained herein.

In particular, the Company paid employee bonuses of 15.0 per cent. of the after-tax profits, less prior years' losses and legal reserves, in the form of Shares and expects that, subject to shareholder approval, it will pay all or some of employee bonuses for the future periods in the form of Shares or cash. The Company granted an aggregate of 6,662,946 Shares and 15,511,500 Shares in years 2000 and 2001 to its employees, respectively. In such case, the number of Shares distributed is obtained by dividing the total nominal NT Dollar amount of the bonus by the par value of the Shares rather than their market value, which has generally been higher than par value. Under ROC GAAP, the distribution of employee bonus shares is treated as an allocation from retained earnings when the distribution of employees bonuses is approved by the shareholders, and the Company is not required to, and does not, charge the value of the employee bonus shares to income. Under U.S. GAAP, however, the Company would be required to initially accrue the bonus as compensation costs when services are rendered. When bonuses are approved by shareholders in the subsequent year, an additional compensation cost is recorded for the difference between the par value and the fair market value of the shares granted to employees. Correspondingly, the Company's net income and income per share calculated in accordance with U.S. GAAP will be reduced. These differences would be material.

In addition, because the Shares issued under the employee share bonus scheme are issued at less than market value, such issuances also have a dilutive effect on existing shareholders. However, the Conversion Price of the Bonds is adjusted for such issuances.

The Company's operation may be adversely affected by natural disasters in Taiwan

The Company's headquarters and some of its service facilities are in Hsin-Chu, Taiwan, which is vulnerable to natural disasters. Disruption of operations at the Company's facilities for any reason, including work stoppages, power outages, fire, earthquakes or other natural disasters, would cause delays in performing its services, which could lead customers to obtain services from other sources. For example, the Company has in the past experienced major power outages on 29th July and 21st September, 1999, each of which resulted in a brief suspension of operations. In September 1999, a major earthquake occurred, with its epicenter in central Taiwan. The earthquake caused interruptions to power supplies and significant damage to buildings across Taiwan. As a result of the earthquake, the Company was obliged to suspend its manufacturing operation in Taiwan for two days. After the 1999 earthquake, there were a number of earthquakes in Taiwan in 2000 and the 2001. However, the latest major earthquake experienced by Taiwan on 31st March, 2002 did not cause any disruption to the Company's operations. Similar incidents may occur in the future, which could have a material adverse effect on the Company's operating results.

USE OF PROCEEDS

The net proceeds from the offering of the Bonds, after deducting underwriting fees, including selling concessions, and other expenses, are estimated to be approximately U.S.\$119.15 million. The net proceeds will be used to repay the bank loans associated with the procurement of machinery and equipment.

MARKET PRICE INFORMATION

The Shares have been quoted and traded on the TSE since 9th May, 2001. The table below sets forth, for the periods indicated, the high and low closing prices and the average daily volume of trading activity on the TSE for the Shares (adjusted for the effects of rights issues, employee bonus issues and stock dividends) and the high and low of the daily closing values of the TSE Index.

		<u>Closing price per Share</u>		<u>Average daily trading</u>	<u>TSE Index</u>	
		<u>High</u>	<u>Low</u>	<u>Volume</u>	<u>High</u>	<u>Low</u>
		NT\$		Thousands of Shares	points	
2001	May (listed)	61.00	28.20	3,783	5,405.54	4,958.61
	June	29.90	20.00	2,069	5,271.30	4,768.55
	July	20.80	13.60	1,772	4,886.86	4,040.77
	August	16.00	10.45	2,827	4,687.33	4,310.32
	September	11.50	8.60	1,735	4,493.53	3,493.78
	October	8.75	6.35	1,786	4,065.10	3,446.26
	November	10.20	6.60	4,401	4,608.32	3,929.69
	December	16.90	9.20	7,208	5,551.24	4,646.61
2002	January	28.0	13.80	19,149	6,007.33	5,488.33
	February	31.30	21.00	8,734	5,968.61	5,499.79
	March (through 31st March)	27.20	19.90	17,257	6,242.64	5,680.78

Source: Taiwan Economic Journal Data Book

On 12th April, 2002, the reported closing price of the Shares was NT\$31.50 per Share and the TSE Index closed at 6,182.59.

DIVIDENDS AND DIVIDEND POLICY

To date the Company has not paid any cash dividends on the Shares. The Company has paid annual stock dividends on the Shares since 1998.

The following table sets forth the aggregate number of outstanding Shares entitled to dividends, as well as the stock dividends paid during each of the years indicated. The stock dividends per Share represent dividends paid in the fiscal year for the Shares outstanding on the record date applicable to the payment of these dividends.

	<u>Stock dividends per Common Share⁽¹⁾</u>	<u>Total Common Shares issued as stock dividends to shareholders and to employees</u>	<u>Outstanding Common Shares on record date⁽²⁾</u>
	NT\$	Shares	Shares
1998	3.7	16,000,000	70,000,000
1999	2.5	19,375,000	124,375,000
2000	5.0	68,850,446	263,225,446
2001 ⁽³⁾	6.0	173,446,768	436,672,214

(1) Holders of Shares receive as a stock dividend the number of Shares equal to the NT Dollar value per Share of the dividend declared multiplied by the number of Shares owned and divided by the par value of NT\$10 per share. Fractional Shares are not issued but are paid in cash.

(2) Aggregate number of Shares outstanding on the record date applicable to the dividend payment, including Shares issued in the previous year under the Company's employee bonus plan.

(3) Through 14th March, 2002, the Company does not intend to declare or distribute any other dividends, either in cash or shares, in 2002.

The Company has historically paid stock dividends on the Shares with respect to the preceding year after approval by the shareholders at the annual general meeting of shareholders. The form, frequency and amount of future cash or stock dividends on the Shares will depend upon the Company's earnings, cash flow, financial condition and other factors.

Except in certain limited circumstances, the Company is not permitted to distribute dividends or make other distributions to shareholders for any year in which the Company has no earnings. The ROC Company Law also requires that ten per cent. of the Company's annual earnings, less prior years' losses, if any, and outstanding tax, be set aside as a legal reserve until the accumulated legal reserve equals the paid-in capital. The Company may set aside a special reserve in accordance with the applicable laws and regulations. In addition, the Articles of Incorporation of the Company provide that the remaining portion of the earnings will be distributed as dividends and bonuses, according to the board of directors' resolution as approved by the shareholders, of which (1) the employee bonuses shall be 15 per cent. of the residual earnings approved by the shareholders, and (2) the remuneration of all directors and supervisors shall be one per cent. of the residual earnings approved by the shareholders.

In addition, the Articles of Incorporation of the Company further provide that when distributing dividends in any year, the Company may distribute cash dividends in an amount not in excess of 20 per cent. of the distributable dividends in that year. See "Description of The Shares — Dividends and Distribution".

EXCHANGE RATE

Fluctuations in the exchange rate between NT Dollars and U.S. Dollars will affect the U.S. Dollar equivalent of the NT Dollar price of the Shares on the TSE and, as a result, may affect the market price of the Bonds.

Set forth below are the period-end average of buying and selling exchange rates in effect between the NT Dollar and the U.S. Dollar, expressed in NT Dollars per U.S. Dollar, for the period indicated.

Period-End	NT\$ per U.S.\$1.00
1996	27.49
1997	32.64
1998	
1st Quarter	32.81
2nd Quarter	34.49
3rd Quarter	34.46
4th Quarter	32.21
1999	
1st Quarter	33.16
2nd Quarter	32.28
3rd Quarter	31.80
4th Quarter	31.46
2000	
1st Quarter	30.46
2nd Quarter	30.82
3rd Quarter	31.33
4th Quarter	33.08
2001	
1st Quarter	32.84
2nd Quarter	34.44
3rd Quarter	34.55
4th Quarter	34.98
2002	
January	34.97
February	35.01
March	<u>35.00</u>

Source: Bank of Taiwan

CAPITALIZATION

The following table sets forth the short-term debt, and the capitalization of the Company as of 31st December, 2001 and as adjusted to reflect the issuance of the Bonds.

	As of 31st December, 2001			
	Actual		As adjusted	
	NT\$'000	U.S.\$'000	NT\$'000	U.S.\$'000
Short-term debt⁽¹⁾				
Short-term loans	1,502,572	42,955	1,502,572	42,955
Short-term notes	99,825	2,854	99,825	2,854
Current portion of long-term loans	1,060,258	30,311	1,060,258	30,311
Current portion of lease obligations	240,241	6,868	240,241	6,868
Total Short-term debt	2,902,896	82,988	2,902,896	82,988
Long-term debt⁽²⁾				
Long-term loans, less current portion	4,698,906	134,331	4,698,906	134,331
Lease obligations, less current portion	240,196	6,867	240,196	6,867
Total Long-term debt	4,939,102	141,198	4,939,102	141,198
The Bonds now being issued	—	—	4,197,600	120,000
Shareholders' Equity				
Common stock ⁽³⁾	4,366,722	124,835	4,366,722	124,835
Capital reserve	4,590,339	131,228	4,590,339	131,228
Legal reserve	187,831	5,370	187,831	5,370
Retained earnings	(764,467)	(21,855)	(764,467)	(21,855)
Cumulative translation adjustments	597	17	597	17
Total Shareholders' Equity	8,381,022	239,595	8,381,022	239,595
Total capitalization⁽⁴⁾	13,320,124	380,793	17,517,724	500,793

Note:

- (1) The Company's short-term debt is discussed in more detail in Notes 4 and 6 to the Financial Statements.
- (2) The Company's long-term debt is discussed in more detail in Notes 4 and 6 to the Financial Statements.
- (3) As of 31st December, 2001, the Company's authorized and issued common stock amounted to NT\$7,000,000,000 and NT\$4,366,722,140 divided into 700,000,000 shares and 436,672,214 shares, respectively, each at a par value of NT\$10.
- (4) Total capitalization is the summation of long-term debt, the Bonds and shareholders' equity.
- (5) The translation rate was NT\$34.98 = U.S.\$1.00.

There has been no material change to the capitalization of the Company since 31st December, 2001.

BUSINESS

This Offering Circular contains certain forward-looking statements. When used in this Offering Circular, the words “believes,” “intends,” “anticipates” and similar expressions are intended to identify forward-looking statements. Such statements are subject to certain risks and uncertainties that could cause actual results to differ materially from those projected. Such risks and uncertainties include the timing and acceptance of new product introductions, the actions of the Company’s competitors and business partners, and those discussed above under “Risk Factors,” and “Management’s Discussion and Analysis of Financial Condition and Results of Operation”.

Overview

The Company is one of the leading independent providers of semiconductor test and other backend semiconductor manufacturing services on a stand-alone or turnkey basis in Taiwan. The Company offers a full integrated suite of test services and other backend integrated circuit (“IC”) processing services, which constitute the final procedures necessary to prepare semiconductor devices for further use. The test services provided by the Company cover a full range of both standard and customized test solutions, including wafer probing (“C/P”) and final test (“F/T”) for logic, mixed-signal and memory devices and burn-in. The semiconductors tested by the Company are extensively used in personal computers, personal computer peripherals, consumer products and telecommunication products. The backend semiconductor manufacturing services provided by the Company consist of wafer grinding and dicing, chip on board packaging (“COB”), test, ICs tape and reel and drop shipment of finished semiconductor devices. Through its strategic alliance with Amkor Technology Inc. (“**Amkor**”), the Company is able to offer its customers contract packaging services. The Company is also able to provide its customers all backend semiconductor manufacturing services from testing to drop-shipment on a turnkey basis.

The Company’s corporate headquarters, test and processing facilities are located in the semiconductor manufacturing corridor of Taiwan. Taiwan is home to the world’s largest independent wafer foundries and also one of the world’s leading suppliers of outsourced semiconductor manufacturing services. The Company’s close proximity to and relationships with Taiwan’s leading wafer foundries allow it to capture IC test and backend manufacturing business arising from the trend towards outsourcing and the growth of the semiconductor industry. This enables the Company to provide its customers with seamless services in Taiwan for all of their IC test and backend manufacturing needs, thereby minimizing the time required to deliver finished semiconductor devices to the market.

The Company’s customers include major fabless IC design companies, integrated device manufacturers and semiconductor foundries. The Company provides services to customers in both logic and memory semiconductor markets. In 2001, the Company’s top five customers were Macronix International Corporation, MediaTek Incorporation, Silicon Storage Technology, Inc., United Microelectronics Corporation and Vanguard International Semiconductor Corporation. The Company has established technical and sales teams near major customer facilities, including the Hsin-Chu Science-Based Industrial Park in Taiwan (“**Hsin-Chu Science Park**”), which work with its customers on developing and implementing new test technologies as tolerances of integrated circuitry become smaller and ICs become more sophisticated.

Although the Company experienced operating and net losses in 2001, the net revenues of the Company grew at a compound annual growth rate of 65.2 per cent. from NT\$521.2 million in 1997 to NT\$3,877.3 million (U.S.\$110.8 million) in 2001. The Company’s net revenues in 2001 decreased by 7.3 per cent. from its net revenues of NT\$4,181.6 million in 2000. The Company’s earnings before interest, income tax, depreciation and amortization were NT\$2,266.4 million and NT\$1,612.1 million (U.S.\$46.1 million) in 2000 and 2001 respectively, compared to NT\$894.2 million in 1999.

The Company has made significant investments in purchasing technologically advanced test machinery and equipment; which enables the Company to test highly parallel, high speed, high pin-count and highly integrated devices, such as optical image-sensing ICs and system on chip (“SOC”). As at 31st December, 2001, approximately 20 per cent. of the Company’s total employees have engineering background; such skilled labor complements the Company’s initiatives on such technologically advanced test machinery and equipment.

Industry Background

Semiconductors are critical components used in an increasingly wide variety of applications, including computer systems, communications equipment and systems, automobiles, consumer products and industrial automation and control systems. As performance has increased and size and cost have decreased, the use of semiconductors in these applications has grown significantly. According to a report by World Semiconductor Trade Services in 2001, worldwide semiconductor device market revenue will grow from U.S.\$149 billion in 1999 to U.S.\$239 billion in 2003, a compound annual growth of 12.5 per cent., driven by increased sales of communication semiconductors used in applications including computer modems, networking equipment, cellular phones and Internet and electronic commerce hardware and appliances.

The semiconductor manufacturing process

In the manufacturing process, semiconductor designs are physically embedded into round silicon wafers. Each wafer is then sliced into a number of semiconductor dies, which in turn are individually packaged into completed semiconductor devices and tested. A semiconductor package is a plastic or ceramic container that protects and insulates the enclosed semiconductor so that it can be attached to a printed circuit board. Leads on a leadframe or substrate are then connected by extremely fine gold wires to the input/output terminals on the chips, through the use of automated machines known as wire bonders, and encapsulated in molding compound. Semiconductor packages are an integral part of the basic functionality of semiconductor devices and contribute to their overall performance. After a semiconductor has been packaged, the semiconductor device undergoes final test to ensure performance, functionality and reliability. Independent providers of semiconductor manufacturing services generally specialize in either wafer fabrication or packaging and test of individual devices.

Increasing demand for outsourced semiconductor manufacturing services

Facing increasing design complexity, shorter time-to-market requirements, and shorter product life cycles, semiconductor companies are increasingly focusing their resources on their core competencies of product design, marketing and sales. This has led to a growing demand for outsourced semiconductor manufacturing services. Today, most major semiconductor companies, including those with their own manufacturing facilities, use independent packaging and test service providers for at least a portion of their manufacturing needs. According to a Dataquest report in 2000, total test service revenues for the semiconductor industry in 1999 were approximately U.S.\$10.0 billion of which revenues from independent test companies were U.S.\$0.8 billion, or 8.0 per cent. of total test revenues. According to the same report, independent test revenues are expected to grow at a compound annual growth rate of 47.1 per cent. from U.S.\$0.8 billion in 1999 to U.S.\$5.0 billion in 2003. Principal factors contributing to this outsourcing trend are:

- *Significant capital expenditures are required for semiconductor test facilities:* Backend semiconductor manufacturing services have evolved into increasingly complex processes that require substantial investment in specialized equipment and facilities. As a result, equipment must be utilized at a high capacity level in order to be cost effective. However, it has become increasingly difficult for semiconductor companies to sustain high levels of capacity utilization due to ever-shorter product life cycles and the need to continuously update or replace test equipment to accommodate new products. Independent providers of test services, on the other hand, can use their existing equipment at high utilization levels over a longer period of time by providing a broad range of services for a variety of customers.

Moreover, according to a report by Industrial Technology Information Service in 2001, the cost of a state-of-the-art wafer fabrication facility will grow from approximately U.S.\$200.0 million in 1983 to U.S.\$4.0 billion in 2002. As the cost to build wafer fabrication facilities has dramatically increased, semiconductor companies with their own manufacturing facilities have been forced to concentrate their capital resources on core wafer manufacturing activities. As a result, semiconductor companies are increasingly using independent test providers who are able to invest capital to develop new test technologies and expand their capacity.

- *Time-to-market pressures are increasing for semiconductor companies:* Consumers of electronic products are increasingly demanding more sophisticated devices and rapid access to the latest technologies. As a result, product life cycles are shortening which means

manufacturers that are first to market can earn significant rewards. In response, semiconductor companies are increasingly seeking to shorten their time-to-market for new products. Having the right backend process technology and capacity in place is a critical factor in reducing time-to-market. Semiconductor companies frequently do not have the equipment or expertise to implement new backend process solutions or sufficient time to develop these capabilities before introducing a new product into the market. For this reason, semiconductor companies are increasingly utilizing the resources and capabilities of independent providers of test and other backend semiconductor manufacturing services in order to deliver their new products to market more quickly.

- *Sophisticated expertise and technological innovation are necessary:* Semiconductor companies are facing ever-increasing demands for miniaturization, higher lead counts for more connections and improved thermal and electrical performance from semiconductor device packaging. As a result, the backend semiconductor manufacturing processes increasingly require sophisticated expertise and technological innovation. Moreover, the numerous test options required to support the proliferation of new semiconductor technologies make it extremely difficult for semiconductor companies to invest their time and resources in research and development in backend semiconductor manufacturing technology and capacity. By specializing, independent providers of backend semiconductor manufacturing services have developed substantial expertise in backend semiconductor manufacturing technologies. Semiconductor suppliers, who find it difficult to keep pace using their internal resources, increasingly rely on independent service providers as a key source for new technology development and innovation in the backend semiconductor manufacturing process.

As a result of these factors, outsourcing of semiconductor manufacturing services continues to grow. Integrated device manufacturers with their own manufacturing capabilities continue to outsource an increasing amount of their manufacturing needs. Moreover, fabless IC design companies have proliferated in recent years due to the rapid growth of computing, communications and the Internet. Fabless IC design companies outsource every step of the manufacturing process, including all backend semiconductor manufacturing processes, so that they can focus on their core competence of designing and marketing advanced semiconductor products. According to a report by Industry Technology Information Service in 2001, revenues of fabless IC design companies in Taiwan grew from U.S.\$8.6 billion in 1992 to U.S.\$115.2 billion in 2000, a compound annual growth rate of 38.3 per cent.

Competitive Strengths

The Company believes that the following strengths contribute to its competitive position in the relevant markets:

High barriers to entry

It is difficult for potential competitors to enter into the test and backend semiconductor manufacturing services industry for the following reasons:

- High capital cost of the machinery and equipment required for testing;
- Competition for experienced research, development and management personnel; and
- The investment required to build long-term cooperative relationships and trust by customers. The Company has established close cooperative relationships with fabless IC design companies, integrated device manufacturers and semiconductor foundries. The Company believes that it is well regarded and trusted by customers for the range and quality of its services as well as its delivery lead times.

Market demand for backend semiconductor manufacturing services continues to grow

According to a report by World Semiconductor Trade Statistics, the scale of the global market for semiconductors will grow from U.S.\$149 billion in 1999 to U.S.\$239 billion in 2003, at an annual compound growth rate of 12.5 per cent. It is expected that the IC test business will grow vigorously with the strong demand in the global semiconductor market. The Company believes that it is well positioned to benefit from such growth.

Trend to outsourcing and specialization in the semiconductor industry

As specialization in the semiconductor industry increases, integrated device manufacturers and fabless IC design companies have gradually raised the percentage of outsourced process, in consideration of returns on operating capital and financial risk. With the expansion of the international reach of domestic wafer foundries and the active entry by domestic DRAM manufacturers into strategic alliances with leading international manufacturers, the domestic IC industry has generated significant business opportunities for the IC test industry. The Company has a full line of state of the art test equipment including both imported equipment and equipment designed and developed in-house and can provide a full spectrum of test services such as logic IC, mixed-signal IC and memory IC test and IC burn-in. The Company also provides other backend semiconductor manufacturing services, including wafer grinding and dicing, COB, tape and reel and drop shipment. The Company has also entered into an alliance agreement with Amkor. Amkor is one of the world's largest independent providers of semiconductor packaging and test services, and is one of the leading developers of advanced semiconductor packaging and test technologies. Through flexible contracting and subcontracting arrangements, the Company provides its customers with packaging or assembly services through Amkor. The Company believes this provides a competitive advantage in attracting and keeping customers who demand for one-stop turnkey backend semiconductor manufacturing services.

Advantage of geographic location

The Company's headquarters are in Taiwan and are located close to the Hsin-Chu Science Park. The Company believes that its close proximity to and strong relationship with Taiwan's leading fabless IC design companies, integrated device manufacturers and semiconductor foundries enables the customers to easily integrate all of their outsourced manufacturing needs and efficiently manage their supply chains. The Company's customers can enjoy shorter transportation times from upstream manufacturers and product delivery lead times. The Company also capitalizes on its proximity to its customers by offering design and new product validation services, and by providing feedback on new product designs. By becoming involved at the design stage, the Company believes that it is able to increase penetration and customer loyalty. In addition, the Company learns valuable market information about IC design trends and demand for new products that help the Company maintain its leading position.

Strategy***Offer full spectrum of test and other backend manufacturing services***

Many of the Company's customers require a wide range of test technologies which covers logic, mixed-signal and memory devices. They also require other backend semiconductor manufacturing services on a turnkey or stand-alone basis, which include wafer grinding and dicing, COB, test, tape and reel and drop shipment of the semiconductor devices directly to their customers. The Company believes that as semiconductor suppliers face shorter time-to-market demands and shorter product cycles, turnkey services will become an increasingly important aspect of the customers' manufacturing and product distribution strategies. The Company is one of a small number of vendors capable of providing such services on a turnkey basis.

The Company has also made significant investments to construct, fit out and equip large-scale test facilities that deploy hundreds of sophisticated test units, to ensure that the Company has the capability to design and perform the most technologically demanding test functions. The Company employs the most technologically advanced imported test machinery and equipment, and also cost-efficient test units designed and developed in-house. This gives the Company the ability to test highly parallel, high speed, high pin-count and highly integrated devices, such as optical image-sensing ICs, as well as the ability to achieve cost-efficient high volume test of lower speed ICs.

Leverage relationships with foundries and IC design service companies to provide total solution to the customers

The Company conducts joint marketing with semiconductor foundries and IC design service companies to capture the test and other backend semiconductor manufacturing requirements of their customers. These customers comprise principally IC design companies, integrated device manufacturers and systems original equipment manufacturers. The Company believes that by leveraging the relationships with foundries and IC design service companies, it is able to attract new customers as well as maintain its existing customers.

Focus on customer service

The Company believes that its ability to anticipate and meet its customers' needs is critical to attracting and retaining leading semiconductor suppliers as customers. The Company strives to work closely with its customers on developing and fulfilling their current and future semiconductor test needs. The Company positions itself as a high-tech service business and has a well established customer-oriented culture, and continuously enhances the quality, cost effectiveness, cycle times, and flexibility of its services. To provide a dedicated customer support infrastructure to its customers, the Company has established technical and sales teams strategically located near major customers' facilities and technology development and manufacturing centers, including the Hsin-Chu Science Park.

Further improve IC test and backend manufacturing technology

The Company intends to continually expand its portfolio of test and other backend semiconductor manufacturing technologies through internal development and joint development with customers. The Company believes that leading technology is its most valuable asset, and that the ability to offer leading test technologies is critical to attracting and retaining customers and maintaining high margins. The Company is currently developing new test technologies which allow it to test newly developed sophisticated semiconductors such as chips with SOC technologies and advanced radio frequency ("RF") chips which are utilized in telecommunication devices.

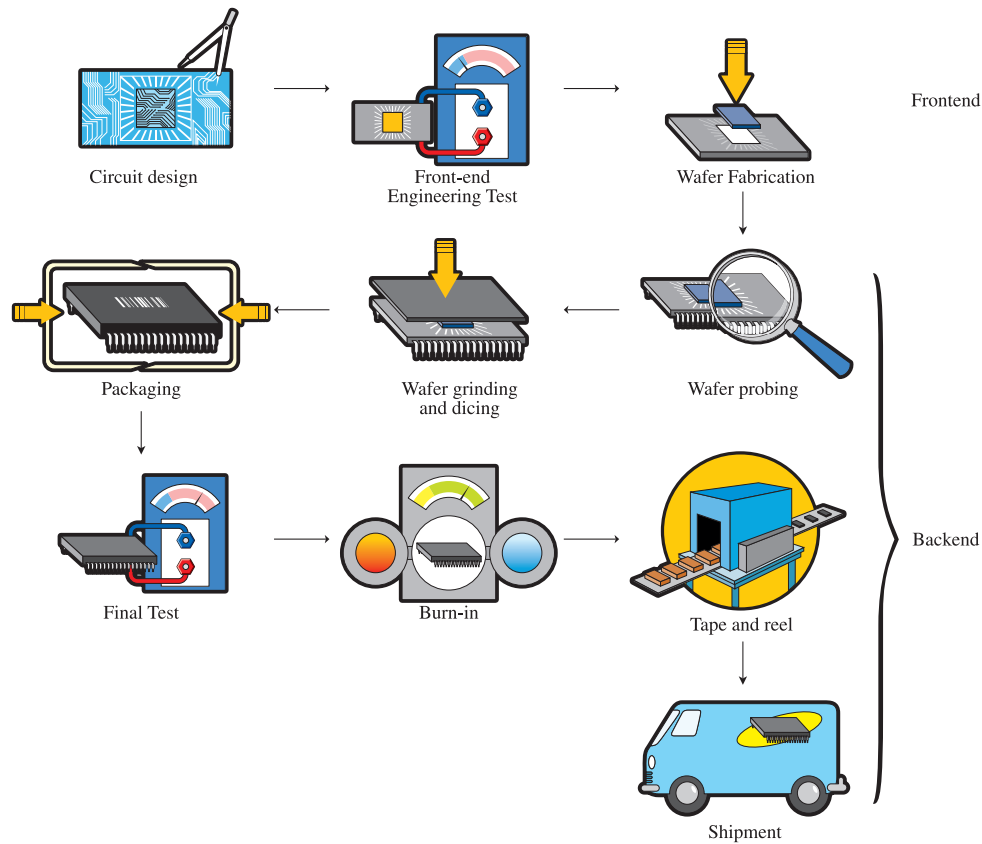
Expand the customer base and operations

The Company intends to expand its customer base geographically by targeting customers located in the United States, Japan and Europe. The Company will expand its current sales and marketing team and the operations of its United States subsidiary, KYEC USA Corp. Currently, the Company schedules frequent visits by its sales team to Japan to visit existing customers and to source for new customers. The Company has identified Europe as a potential market and intends to enhance its marketing efforts to European customers by scheduling regular visits by its sales and marketing team.

The Company also intends to expand its operations in South East Asia and the PRC. This will allow the Company to tap the business opportunities arising from the growing trend among its customers to locate their operations in these areas. By locating its operations closer to its customers, the Company believes that it can compete more effectively with other providers of test and other backend semiconductor manufacturing services with respect to delivery time and the pricing of its services.

Core Services

The manufacturing of semiconductors is a complex process that requires increasingly sophisticated engineering and manufacturing expertise. The manufacturing process may be divided into the following stages from circuit design to shipment:



Circuit Design	The design of a semiconductor is developed by laying out circuit components and interconnections. A complex circuit may be designed with as many as 20 layers of patterns or more.
Front-end engineering test	Throughout and following the design process, prototype semiconductors undergo front-end engineering test, which involves software development, electrical design validation, reliability and failure analysis.
Wafer fabrication	The process begins with the generation of a photomask through the definition of the circuit design pattern on a photographic negative, known as a mask, by an electron beam or laser beam writer. These circuit patterns are transferred to the wafers using various advanced processes.
Wafer probing*.	As part of the test process, each individual die is electrically tested, or probed, for defects. Dies that fail this test are marked to be discarded.
Wafer grinding and dicing*	Wafer grinding is a process that grinds the finished wafers to a designated thickness and dicing the wafers into dies, or chips.

Packaging	Packaging includes plastic packaging, also called assembly, and chip on board (“ COB ”). Plastic packaging is the processing of bare semiconductors into finished semiconductors, which serves to protect the die and facilitate electrical connections and heat dissipation. The patterned silicon wafer received from the customers are diced by means of diamond saws into separate dies, also called chips. Each die is attached to a leadframe or a laminate (plastic or tape) substrate by epoxy resin. Each chip is then encapsulated, generally in a plastic casing molded from a molding compound, with only the leads protruding from the finished casing, either from the edges of the package as in the case of the leadframe packages, or in the form of small bumps on a surface of the package as in the case of ball grid array or other laminate packages. At times, a chip is not encapsulated in a mold but is attached to a circuit board directly. This process is known as “chip on board”.
Final test*	Final test is conducted to ensure that the semiconductor device meets performance specifications. Final test involves using sophisticated test equipment and customized software programs to electrically test a number of attributes of packaged semiconductors, including functionality, speed, predicted endurance and power consumption. The final test of semiconductors is categorized by the functions of the semiconductors tested into logic/mixed-signal final test, and memory final test. Memory final test typically requires simpler test software but longer test time per device tested.
Burn-in*	Burn-in refers to the process of subjecting finished semiconductors to extreme hot and cold temperatures and high voltage over specified periods of time, depending on the circuitry and the intended use, to determine overall reliability under extreme conditions and to eliminate defective ICs.
Tape and reel*	Tape and reel is a process which involves the wrapping of finished semiconductors into continuous tape reels designed for use in customers’ automated surface mount technology lines.

* The Company is currently providing these services on a stand-alone or turnkey basis.

The Company is involved in providing backend semiconductor manufacturing services, including wafer probing, wafer grinding and dicing, COB, final test, burn-in, and tape and reel. Through Amkor, the Company also provides packaging services. See —“Sales and Marketing — Strategic Alliance” The table below sets out the Company’s total sales by the type of services for the periods indicated.

	Year ended 31st December,		
	1999	2000	2001
	NT\$’000	NT\$’000	NT\$’000
Test services			
Wafer probing	783,083	2,175,577	1,880,118
Final test	337,527	896,060	1,189,477
Burn-in	223,088	403,358	266,020
Other backend services			
Wafer grinding and dicing	154,214	345,070	336,194
Tape and reel	241,648	309,031	214,948
Others ⁽¹⁾	15,555	96,359	84,111
Total sales	1,755,115	4,225,455	3,970,868
Sales return and allowances	10,141	43,881	93,570
Net sales	1,744,974	4,181,574	3,877,298

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- (1) Include packaging and assembly for CMOS image sensor and sales of burn-in equipment.

Test services

Semiconductor test measures and ensures the performance, functionality and reliability of a semiconductor device. Testing a semiconductor device requires significant technical expertise and knowledge of the specific applications and functions of the semiconductors being tested. In addition to maintaining different types of advanced test equipment which enable the Company to test a variety of semiconductor functions, the Company works closely with the customers to design test and conversion programs to test particular semiconductor products on multiple equipment platforms effectively. The cost of any specific test is dependent on the time, usually measured in seconds, required to run a test which varies depending on the complexity of the semiconductor device and the customer's desired test program.

The Company conducts wafer probing and final test of logic ICs, including digital, analog and mixed-signal products, and memory ICs. Many of the Company's test customers also request drop shipment of the tested ICs directly to final destinations designated by the customers.

Wafer probing. After wafers are fabricated, each die on a wafer is electrically probed to ensure integrity and functionality of the IC. Dies that fail the test are marked to be discarded. Following wafer probing, the wafers are sent for wafer grinding and dicing.

For the years ended 31st December, 1999, 2000 and 2001, wafer probing services accounted for 44.6 per cent., 51.5 per cent. and 47.4 per cent. of the Company's total sales.

Final test. The Company conducts final test of a wide variety of logic and mixed-signal ICs, including complex, high-speed, as well as lower performance ICs. High-speed ICs include the chips used in personal computer components, such as audio chips; while most of the lower performance ICs include the chips used in switching equipment in telecommunication systems.

The Company provides final test services for a variety of memory products, such as state access memory circuits, diagram random access memory circuits and single-bit read only erasable programmable memory integrated circuits. The test of memory products requires different equipment than that used in logic and mixed-signal test. Memory test generally requires longer test time. The Company also provides final test services for highly parallel, high speed, high pin-count and highly integrated devices, such as optical image-sensing ICs and SOC.

For the years ended 31st December, 1999, 2000 and 2001, final test services accounted for 19.2 per cent., 21.2 per cent. and 30.0 per cent. of the Company's total sales.

Burn-in. In addition to wafer probing and final test services, the Company also provides burn-in services, in which a semiconductor is subjected to extreme hot and cold temperatures and high voltage over a period of time. Burn-in services are conducted to determine overall reliability under extreme conditions and to eliminate defective ICs.

For the years ended 31st December, 1999, 2000 and 2001, burn-in services accounted for 12.7 per cent., 9.5 per cent. and 6.7 per cent. of the Company's total sales.

Other backend semiconductor manufacturing services

Wafer Grinding and dicing. As part of its backend semiconductor manufacturing services, the Company grinds the wafers provided by the customers to designated thicknesses and dices the wafer into dies, or chips. The wafer grinding and dicing process requires high-precision technologies and equipment to achieve precise tolerances.

Packaging. Packaging includes plastic packaging and COB. Plastic packaging, or assembly, is the process of assembling bare semiconductors into finished semiconductors and serves to protect the die and facilitate electrical connections and heat dissipation. A COB refers to the process that a chip is not

encapsulated in a mold but is attached to a circuit board directly. As the Company's primary business consists of IC test services, it only conducts limited volume of CMOS image sensor simple packaging and COB to accommodate particular customer requirements.

In order to offer turnkey backend semiconductor manufacturing services, including packaging and assembly, the Company has recently entered into an alliance agreement with Amkor. Through flexible contracting and subcontracting arrangements, the Company provides its customers with packaging or assembly services through Amkor. Under the alliance agreement, the Company and Amkor may jointly market a package of turnkey backend semiconductor manufacturing services to customers. See "— Sales and Marketing — Strategic Alliance" for details.

Tape and reel. Tape and reel is a process which involves the wrapping of finished semiconductors into continuous tape reels designed for use in customers' automated surface mount technology lines.

For the years ended 31st December, 1999, 2000 and 2001, backend semiconductor manufacturing services excluding test services accounted for 22.6 per cent., 15.5 per cent. and 13.9 per cent. of the Company's total sales.

Drop shipment services

The Company offers drop shipment services for shipment of ICs directly to end users designated by the customers. Drop shipment services are provided mostly in conjunction with logic/mixed-signal test. The Company provides drop shipment services to a majority of its test customers. A substantial portion of the customers at each of the Company's facilities have qualified these facilities for drop shipment services. Since drop shipment eliminates the additional step of inspection by the customer before shipment to the end user, quality of service is a key consideration. The Company believes that the ability to successfully execute its full range of services, including drop shipment services, is an important factor in maintaining existing customers as well as attracting new customers.

Materials and Equipment

Materials

No materials are necessary for the Company's test operations. For other services, particularly tape and reel, the Company requires limited materials such as plastic tapes and wrapping materials. The Company purchases materials from major suppliers, including Advantek Taiwan Inc., Morrison & Co. Ltd, Sing Way Corporation, Teradyne Inc. and Kinsus Interconnect Technology Corp.

Equipment

The Company, like other companies in the same industry, makes large capital investments in test equipment. The Company purchases generally equipment with broad functionality and flexibility for use in multiple test application. The Company purchases test equipment from a variety of major international manufacturers, including Advantest Corporation, Agilent Technologies, Credence Systems Corporation, Schlumberger and Teradyne Inc. As of 31st December, 2001, the Company operated 233 logic and mixed-signal testers and 262 memory testers, of which 17 testers were consigned from customers. The Company generates test revenues from the consigned testers on a processing fee basis.

The Company will place orders for additional test equipment in future periods to the extent market conditions and demand for its services make it desirable to do so. Some of these equipment are only available from a limited number of vendors or are manufactured in relatively limited quantities and must be ordered in advance. See "Risk Factors — If the Company is unable to obtain equipment from its suppliers on a timely basis and at a reasonable cost, the Company's business may be adversely affected".

Research and Development

The current projects include developing software for parallel test of logic semiconductors, rapid automatic generation and cross-platform conversion of test programs to test logic/mixed-signal semiconductors, automatic code generation for converting and writing test programs, testing new products using existing machines and providing customers remote access to monitor test results. The

Company is also continuing the development of interface designs to provide for high-speed test by minimizing electrical noise. The research and development division and the sales personnel of the Company work closely with the customers in designing and modifying test software and with equipment vendors to increase the efficiency and reliability of test equipment.

The Company also focuses on improving the efficiency and technology of the test processes. The Company has successfully designed and manufactured burn-in ovens, including IC burn-in oven and LCD aging system both for the Company's own use and for outside sale. The research and development division is currently designing cost-efficient testers for low-speed semiconductors, where the Company seeks to increase market share.

For 1999, 2000 and 2001, the research and development expenditures of the Company totaled approximately NT\$27.0 million, NT\$50.7 million and NT\$58.2 million (U.S.\$1.7 million) respectively. These expenditures represented approximately 1.6 per cent., 1.2 per cent., and 1.5 per cent. of net revenues in 1999, 2000 and 2001 respectively. As of 31st December, 2001, the Company employed 59 employees in research and development departments.

Quality Control

The Company has instituted a comprehensive quality assurance program to ensure the implementation of its firmwide quality policy. The Company recognizes the need to maintain a strong reputation for quality as a means of retaining existing customers and securing additional orders from them as well as attracting new customers.

In order to implement the quality assurance program comprehensively, the Company has established a Quality System Division, which is responsible for:

- quality goal planning and follow-up;
- establishing and auditing the operation of the quality system;
- certification programs, including ISO_9001, QS_9000 and TL_9000;
- quality education and training;
- calibration control; and
- quality documentation control.

The Company conducts quality control by the following four steps:

- Discussing with the customers about the quality requirements for the services to be rendered;
- Trial testing of new products to verify the specified product requirements;
- Commercial production, during which the Company will conduct the following routine quality assurance programs:
 - Incoming Quality Control — inspecting the quality of materials and the ICs made available by the customers for the Company to test;
 - In-process Quality Control — monitoring the service process to ensure the least defect which is caused by the Company's service process;
 - Final Quality Control — inspecting the ICs before packaging them into the finished goods; and
 - Outgoing Quality Control — after packaging, the Company will further inspect the quality of the finished goods before shipping.

- The Company will request customers' feedback after the ICs have been delivered to the customers.

The Company has established quality control systems which are designed to ensure high quality service to customers, high quality product and test reliability and high production yields at the Company's facilities. In addition, the Company's test facilities have been qualified by all of its major customers after satisfying stringent quality standards prescribed by these customers.

The Company's test operations are undertaken in clean rooms where air purity, temperature and humidity are controlled. To ensure stability and integrity of its operations, the Company maintains clean rooms at its facilities that meet U.S. Federal 209E class 100, 1,000, and 10,000 standards. All of the Company's facilities have been certified as meeting the ISO 9001 quality standards by the International Standards Organization, Quality System 9000 or QS-9000 and the TL 9000 quality standard. The ISO 9001 certification is required by many countries in connection with sales of industrial products in these countries. The QS-9000 quality standard provides for continuous improvement with an emphasis on the prevention of defects and reduction of variation and waste in the supply chain. Like the ISO 9001 certification, the QS-9000 certification is required by some semiconductor manufacturers as a threshold indicating a company's quality control standards. The TL 9000 quality standard incorporates requirements from existing quality systems including ISO 9001 with additional telecommunication sector specific requirements covering hardware, software and services aspects. In addition, the Company has received various vendor awards from its customers for the quality of its services.

Facilities

The Company owns and operates two facilities in Taiwan. The Company's facilities are located in the semiconductor manufacturing corridor of Taiwan.

The following table sets out the location and primary use of the facilities of the Company as of 31st December, 2001:

<u>Facilities</u>	<u>Location</u>	<u>Commencement of Operation</u>	<u>Principal Usage</u>	<u>Floor Space</u>	<u>Number of Testers</u>
Headquarters	Hsin-Chu	July 2000	Administrative, logic circuit probing, tape and reel	16,407.6 m ²	138
Chung-Hwa Factory . .	Miao-Li	January 2000	Memory test, logic final test, packaging, burn-in services, wafer grinding and dicing	95,484.3 m ²	357
Chu-Nan Factory	Miao-Li	January 1998	The lease by the Company to Poppoly Optoelectronics Corp. has been terminated on February 2002. Currently idle	6,232.5 m ²	—

Headquarters

The Company's headquarters are located at No. 1, Lane 99, Pu-Ding Road, Hsin-Chu 300, Taiwan. The Company owns the land and the building where the headquarters are located. The Company engages in sales and marketing, research and development and logic circuit probing and provides administrative services at its headquarters.

Chung-Hwa Factory

The Company's Chung-Hwa Factory is located at 118, Chung-Hua Road, Chu-Nan, Miao-Li 350, Taiwan, which was bought by the Company in 1999 and commenced operations in March 2001. Chung-Hwa Factory is the Company's testing and operating center, including memory test, logic final test, COB, burn-in and wafer grinding and dicing. The total floor space for the Chung-Hwa Factory is 95,484.3 square meters.

Due to current zoning restrictions, the Company's Chairman, C. K. Lee, holds two lots of land adjacent to the Chung-Hwa Factory on trust for the Company, and is subject to an unconditional obligation to transfer the title of the land when the lots are rezoned.

In addition to the headquarters and Chung-Hwa Factory, the Company also owns a Chu-Nan site which is located in Miao-Li, Taiwan. The Company once leased the entire Chu-Nan site to Poppoly Optoelectronics Corp. for a monthly rental of NT\$1,960,000. The lease terminated in February 2002 and the Chu-Nan Factory is currently idle.

The total building area of the Company's facilities is 118,124.39 square meters. The Company believes that its existing production and office facilities are adequate to meet current requirements, and that suitable additional or substitute space will be available as needed to accommodate any further physical expansion of production, corporate operations and for any additional sales offices. The Company has not experienced any significant interruptions in production at any of its production facilities due to equipment failure or breakdown, raw material shortages, power interruptions, fire, labor disputes or other causes.

Competition

The Company operates in the highly competitive independent semiconductor test and backend services markets. The Company faces competition from a number of vendors, including other independent semiconductor test and backend service companies such as ASE Test Limited, ChipMos Technologies Inc., United Test Center and Siliconware Precision Industrial Limited. The Company also competes for the test business of foundries, integrated device manufacturers with in-house test capabilities and fabless IC design companies with their own in-house test capabilities. Some of these manufacturers have commenced, or may commence, in-house test operations in Taiwan and Asia. Furthermore, several independent packaging companies in Asia plan to enhance their current test capabilities.

Integrated device manufacturers that use the services provided by the Company continuously evaluate the Company's performance against their own in-house test capabilities. These integrated device manufacturers may have access to more advanced technologies, and greater financial and other resources than the Company does. The Company believes, however, that it can offer greater efficiency and lower costs while maintaining equivalent or higher quality for the following reasons:

- The Company tends to have lower unit costs because of higher utilization rate as compared to the in-house test operations of integrated device manufacturers since integrated device manufacturers are less able to utilize individual testers for long periods of time due to the constant evolution of test technology.
- The Company offers a wider range of services in terms of complexity and technology as compared to the in-house test operations of integrated device manufacturers.

Sales and Marketing

Sales and Marketing Division

The Company maintains sales and marketing offices in Taiwan and, through its subsidiary, KYEC USA Corp., in the United States. The principal sales and marketing team is located in the Hsin-Chu Headquarters. The Company's sales and marketing division currently employs approximately 53 employees, who are responsible for the marketing, sales and planning and customer service business. The Company's strategic partner, Amkor Technology Inc., has since January, 2002 seconded three sales personnel to the Company for joint promotion of the Company's and Amkor's business. The Amkor employees and the sales staff of the Company often call on prospective customers together. The Company conducts marketing research through its in-house customer service personnel and through its relationships with the customers and suppliers to keep abreast of market trends and developments.

Customers

The Company has over 100 customers, including the leading companies in semiconductor manufacturing business:

- Macronix International Corporation (“**Macronix**”)
- MediaTek Incorporation (“**MediaTek**”)
- Novatek Microelectronics Corporation Ltd. (“**Novatek**”)
- Silicon Storage Technology, Inc. (“**SST**”)
- Sunplus Technology Co., Ltd.
- Taiwan Semiconductors Manufacturing Corporation
- United Microelectronics Corporation (“**UMC**”)
- Vanguard International Semiconductor Corporation (“**Vanguard**”)
- Winbond Electronics Corporation (“**Winbond**”)

The Company’s five largest customers together accounted for approximately 50.3 per cent., 44.3 per cent. and 49.2 per cent. of the net sales in 1999, 2000 and 2001, respectively.

The following table sets forth the names, in alphabetical order, of the Company’s five largest customers for the periods indicated:

1999	2000	2001
MediaTek	MediaTek	Macronix
Novatek	Vanguard	MediaTek
UMC	SST	Vanguard
Vanguard	UMC	UMC
Winbond	Winbond	SST

The following table sets out a breakdown of the Company’s total sales by geographical region for the periods indicated:

Region	Year ended 31st December,					
	1999		2000		2001	
	(in millions, except percentages)					
	Amount	%	Amount	%	Amount	%
Taiwan	1,608.9	91.7	3,080.8	72.9	2,869.4	72.3
Asia	50.0	2.8	283.5	6.7	174.1	4.4
North America	96.2	5.5	861.2	20.4	923.0	23.2
Others	—	—	—	—	4.4	0.1
Total sales	1,755.1	<u>100.0</u>	4,225.5	<u>100.0</u>	3,970.9	<u>100.0</u>
Less: Sales returns and allowances	<u>10.1</u>		<u>43.9</u>		<u>93.6</u>	
Net Sales	<u>1,745.0</u>		<u>4,181.6</u>		<u>3,877.3</u>	

Qualification and Correlation by Customers

Customers generally require that the Company's facilities undergo a stringent "qualification" process during which the customer evaluates the operations, including engineering, delivery control and test capabilities. The qualification process typically takes up to two weeks, but can take longer depending on the requirements of the customer. In the case of the test operations, after the Company has been qualified by a customer and before the customer delivers semiconductors to the Company for testing in volume, a process known as "correlation" is undertaken. During the correlation process, the customer provides the Company with sample semiconductors to be tested and either provides the Company with the test program or requests that the Company develop a conversion program. In some cases, the customer also provides the Company with a data log of results of any test of the semiconductor which the customer may have conducted previously. The correlation process typically takes one to two days, but can take longer depending on the requirements of the customer.

Information Network System

The Company engages in backend semiconductor manufacturing services, which the customers will request for monitoring the process and obtaining manufacturing information from time to time. The solutions adopted by the Company to accommodate the customers' needs and to improve the quality internally include:

- provide manufacturing data to the customers through e-mail system;
- post manufacturing data in the FTP server for the customer to download the information, which will then be applied to the customers' own system for analysis; and
- utilize alliance management server and software to provide real-time manufacturing data for the customers' direct application.

The Company is one of the pioneers in the industry of providing e-business solutions. The Company evaluates the customers' IT system and installs necessary alliance manager hardware and software for the customers. Alliance manager (sourced in ExtricityTM) is the core software server that supports the design and execution of business processes, manages the integration of backend systems, and coordinates interactions with the Company and its customers. It provides a management environment for real-time visibility and control over the flow of information and the execution of business processes between the Company and its customers and their existing IT systems. The Company believes that, by utilizing the alliance manager system, it can efficiently control the manufacturing process and provide its customers with efficient services.

Pricing

Following the industry practice, the Company prices its test services primarily on the basis of the amount of time, measured in CPU seconds, taken by the automated test equipment to execute the test programs specific to the products being tested as well as the cost of the equipment.

The Company prices its other backend services primarily on the basis of cost and the Company's desired margins

Strategic Alliance

Amkor. On 14th September, 2001, the Company entered into an alliance agreement ("**Alliance Agreement**") with Amkor Technology, Inc. ("**Amkor**"), a U.S. company. Amkor is one of the world's leading providers of contract manufacturing services in the semiconductor industry and is considered to be one of the leading developers of advanced semiconductor packaging and test technology. Amkor's customers include, among others, Agere Systems, Inc., Altera Corporation, Infineon Technologies AG, Intel Corporation, LSI Logic Corporation, Motorola, Inc., Philips Electronics N.V., ST Microelectronics PTE, Texas Instruments, Inc. and Toshiba Corporation.

According to the Alliance Agreement, the Company and Amkor will collaborate to jointly provide turnkey packaging and test solutions and other related services to customers using assembly services provided by Amkor and the Company's test services. The term of the Alliance Agreement is one year subject to subsequent renewal.

Under the Alliance Agreement, the Company has a first right of refusal for undertaking the test services in a turnkey based backend semiconductor manufacturing project secured by Amkor, in consideration that it offers also a first right of refusal to Amkor for undertaking the assembly services in a turnkey based project secured by the Company. To this extent, Amkor may act as the Company's subcontractor for conducting packaging process; the Company's customers may choose to submit one order to the Company only, rather than to the Company and Amkor separately. The Company further covenanted that, during the term of the Alliance Agreement and six months thereafter, it will not engage in packaging or assembly operations of any kind (other than COB and the fulfilment of the existing commitments of the Company to its customers for CMOS image sensor simple packaging per mutual understanding).

Most of the customers which Amkor refers to the Company for the test services will be the foundries and IC design companies based in the United States and Japan, while most of the customers which the Company refers to Amkor for the packaging services will be the semiconductor manufacturers located in Taiwan and Japan. The Company believes that the joint promotional strategy will not only enlarge its customer base but also provide its existing customers more convenient one-shop services. The Company, by cooperating with Amkor, is capable to quote the customers for turnkey backend semiconductor manufacturing services, including semiconductor packaging and test.

Other alliances. The Company does not have other alliances as of the date of this Offering Circular. The Company is open, however, to any cooperative opportunities which will benefit its business through strategic alliances or otherwise.

Environmental Matters

Semiconductor test and tape and reel businesses involve no environmentally sensitive processes. The Company's facilities conducting such services are therefore free from environmental concerns and no anti-pollution devices are required to be installed in any of the Company's test and tape and reel facilities. The Company's wafer grinding and dicing process is, however, environmental sensitive. Liquid waste is produced at the stage where silicon wafers are diced into chips with the aid of diamond saws and cooled with running water. The Company has installed treatment equipment of liquid waste generated at all of the wafer grinding and dicing facilities. The Company believes that it has adopted adequate anti-pollution measures for the effective maintenance of environmental protection standards that are consistent with the semiconductor industry practice in Taiwan.

In addition, the Company believes that it is in substantial compliance with all material environmental regulations. The Company has not been subject to any material fines or legal action involving non-compliance with any relevant environmental regulations, nor is it aware of any threatened or pending action by any environmental regulatory authority in Taiwan.

Legal Proceedings

The Company is currently involved in two legal proceedings:

Contract Litigation

In April 2001, Watron Technology Corporation ("**Watron**"), an ROC incorporated company, instituted civil proceedings in the district court in Hsin-Chu against the Company, seeking payment of approximately NT\$16.4 million as damages for the Company's alleged breach of contract in providing die attachment and molding process on Watron's PI Tag chips. The Company counterclaimed that such breach was caused by Watron's failure to fulfill the conditions precedent of the contract and sought approximately NT\$14 million as damages. The district court ruled in favor of the Company and ordered Watron to pay the Company NT\$876,672 as damages. In March 2002, the Company appealed to the High Court of Taiwan against the amount of damages awarded. The Company does not believe that this litigation will have a significant effect on its financial condition or operating results.

Securities Litigation

In October 2001, Hwa Tsai Co., Ltd. (“**Hwa Tsai**”), an ROC incorporated company and a shareholder of the Company, along with two individual shareholders of the Company, brought civil proceedings in the district court in Hsin-Chu against the Company and the Chairman of the Company, seeking payment of approximately NT\$62.2 million in damages for losses suffered as a result of alleged misleading statements made by the Company and its management. The Chairman is named as a defendant in his capacity as legal representative of the Company and in his personal capacity. The plaintiffs, who purchased shares in the Company, allege that the published projections made, and subsequent revisions of the projections, under which the original profit projections were reduced by up to 97.0 per cent., caused the Company’s share price to fall, and themselves to suffer damages.

In addition, a criminal complaint relating to the same matters and alleging that the Company and the Chairman violated various provisions of the ROC Securities and Exchange Law and Criminal Law has been filed with the district attorney for Hsin-Chu.

The Company believes that the original projections and other statements, and the subsequent revisions of the projections, were based on assumptions that were reasonable at the times they were made. Moreover, the Company believes that the original projections and the related assumptions and statements, and the subsequent revisions, complied with applicable regulations for preparation of financial projections.

The Company believes that it will be able to demonstrate that the projections, in light of the circumstances prevailing at the time of the publication, were not materially misleading, and that the Company and the Chairman have not committed any of the violations alleged. See “Risk Factors — If the Company and the Chairman of the Company do not successfully defend the securities litigation, the Company’s business and financial condition may be adversely affected”.

Insurance

The Company maintains insurance policies with independent third parties in respect of buildings, goods in transits equipment and certain inventories covering loss due to fire, explosion, earthquake, typhoon, flood and certain other risks. While the Company believes its insurance policies to be adequate and in line with industry norms in Taiwan, significant damage to any of the Company’s facilities could have a material adverse effect on the Company. Insurance coverage on property, plant and equipment amounted to approximately NT\$14,562.1 million (U.S.\$416.3 million) as of 31st December, 2001. In addition, the Company carries insurance policies for directors’ liabilities. The Company also carries business interruption insurance.

SELECTED FINANCIAL INFORMATION

The selected income statement data for the years ended 31st December, 1999, 2000 and 2001 and the selected balance sheet data as of 31st December, 1999, 2000 and 2001 set forth below are derived from the Company's audited financial statements included in this Offering Circular and are qualified in their entirety by reference to such financial statements, including the notes thereto, and should be read in conjunction with them and with "Management's Discussion and Analysis of Financial Condition and Results of Operations" included elsewhere herein. Financial information for such periods may not be comparable to financial information for subsequent periods. The financial statements of the Company have been prepared and presented in accordance with ROC GAAP and reporting practices in the ROC. For a discussion of certain differences between ROC GAAP and U.S. GAAP, see "Summary of Significant Differences Between ROC GAAP and U.S. GAAP".

	As of 31st December,					
	1997	1998	1999	2000	2001	2001
	NT\$	NT\$	NT\$	NT\$	NT\$	U.S.\$
	(in millions)					
Income Statement						
Operating revenue-net	521.2	760.6	1,745.0	4,181.6	3,877.3	110.8
Cost of revenues	<u>383.2</u>	<u>518.0</u>	<u>1,114.8</u>	<u>2,705.3</u>	<u>4,129.7</u>	<u>118.0</u>
Gross profit (loss)	138.0	242.6	630.2	1,476.3	(252.4)	(7.2)
Operating expenses	<u>58.3</u>	<u>76.7</u>	<u>130.8</u>	<u>305.8</u>	<u>436.8</u>	<u>12.5</u>
Operating income (loss)	79.7	165.9	499.4	1,170.5	(689.2)	(19.7)
Non-operating income	1.8	10.0	11.3	43.1	153.1	4.4
Non-operating expenses	<u>12.1</u>	<u>47.7</u>	<u>56.6</u>	<u>210.5</u>	<u>555.0</u>	<u>15.9</u>
Income before income tax and minority interest	69.4	128.2	454.1	1,003.1	(1,091.1)	(31.2)
Income tax benefit (expense)	<u>(3.4)</u>	<u>11.5</u>	<u>34.6</u>	<u>175.3</u>	<u>299.5</u>	<u>8.6</u>
Net income (loss)	<u>66.0</u>	<u>139.7</u>	<u>488.7</u>	<u>1,178.4</u>	<u>(791.6)</u>	<u>(22.6)</u>
EBITDA ⁽¹⁾	<u>116.0</u>	<u>299.3</u>	<u>894.2</u>	<u>2,266.4</u>	<u>1,612.1</u>	<u>46.1</u>

- (1) EBITDA refers to earnings before interest, income tax, depreciation and amortization. EBITDA should not be construed as an alternative to operating income or any other measure of performance or as an indicator of the Company's operating performance, liquidity or cash flows generated by operating, investing and financing activities. The items of net income excluded from EBITDA are significant components in understanding and assessing the Company's financial performance, and the Company's computation of EBITDA may not be comparable with other similarly titled measures of other companies. The Company has included the information concerning EBITDA because the Company believes that it is a useful supplement to cash flow data as a measure of the Company's performance.

	As of 31st December,					
	1997	1998	1999	2000	2001	2001
	NT\$	NT\$	NT\$	NT\$	NT\$	U.S.\$
	(in millions)					
Balance Sheet						
Current assets	201.8	412.5	1,151.1	3,050.6	916.2	26.2
Long-term investments	—	—	—	4.9	5.1	0.1
Property, plant and equipment	384.2	1,101.2	4,349.6	12,869.2	15,052.3	430.3
Other assets	18.1	38.5	40.1	291.0	2,042.1	58.4
Total Assets	<u>604.1</u>	<u>1,552.2</u>	<u>5,540.8</u>	<u>16,215.7</u>	<u>18,015.7</u>	<u>515.0</u>
Current liabilities	312.4	376.6	1,062.5	3,601.0	4,675.1	133.6
Long-term liabilities	43.6	—	1,363.4	3,412.8	4,939.1	141.2
Other liabilities	4.1	4.7	6.5	19.2	20.5	0.6
Total liabilities	<u>360.1</u>	<u>381.3</u>	<u>2,432.4</u>	<u>7,033.0</u>	<u>9,634.7</u>	<u>275.4</u>
Total stockholders' equity	<u>244.0</u>	<u>1,170.9</u>	<u>3,108.4</u>	<u>9,182.7</u>	<u>8,381.0</u>	<u>239.6</u>
Total liabilities and stockholder' equity	<u>604.1</u>	<u>1,552.2</u>	<u>5,540.8</u>	<u>16,215.7</u>	<u>18,015.7</u>	<u>515.0</u>
Per Share Data						
Earnings per Share ⁽²⁾	6.32	2.58	5.00	5.08	(1.81)	(0.05)
Adjusted earnings per Share ⁽³⁾ (in dollars)	<u>1.42</u>	<u>0.78</u>	<u>1.94</u>	<u>3.06</u>	<u>(1.81)</u>	<u>(0.05)</u>

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- (1) Translated into United States Dollars using the exchange rate published by the Bank of Taiwan at 31st December, 2001 of NT\$34.98 = U.S.\$1.00.
- (2) Earnings per Common Share are calculated by dividing net income by the weighted average number of shares outstanding during each year before adjusting retroactively for the effect of stock dividends and employees' bonuses. However, no adjustment has been made with respect to the stock dividends and capitalization of employees' bonuses approved by the shareholders on 12th March, 2001.
- (3) Adjusted earnings per Share are calculated by dividing net income by the weighted average number of shares outstanding during each year after adjusting retroactively for the effect of stock dividends, including the stock dividends and capitalization of employees bonus approved by the shareholders on 12th March, 2001.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATION

This discussion and analysis should be read in conjunction with the Financial Statements of the Company included elsewhere in this Offering Circular. Those financial statements have been prepared in accordance with ROC GAAP, which differ in certain material respects from U.S. GAAP. See "Summary of Significant Differences between ROC GAAP and U.S. GAAP". The Company has not quantified the effect of the differences that would arise in the event its financial condition and results of operations were restated or reconciled to U.S. GAAP; however, some of these differences could be material. See "Risk Factors — Risks Relating to the ROC — Financial reporting and accounting standards in the ROC differ from other countries; bonus share issuance". This Offering Circular contains the financial statements of the Company ended 31st December, 1999, 2000 and 2001.

This discussion and analysis contains forward-looking statements. These statements are subject to certain risks and uncertainties, including those discussed below and in Risk Factors, that could cause actual results to differ materially from the expectations expressed in such forward-looking statements. Readers are cautioned not to place undue reliance on any forward-looking statements.

Overview

The Company is one of the leading independent providers of semiconductor test and other backend semiconductor manufacturing services on a stand-alone or turnkey basis in Taiwan. The Company offers a full range of test services including wafer probing and final test for logic, mixed-signal and memory devices and burn-in. The other backend semiconductor manufacturing services provided by the Company consist of wafer grinding and dicing, chip on board packaging, ICs tape and reel and drop shipment of finished semiconductor products. The Company also provides its customers a turnkey solutions for all the customers' backend semiconductor manufacturing needs, including test and packaging to drop shipment. The Company provides its customers packaging services as part of its turnkey solution through its strategic alliance partner, Amkor Technology Inc.

The Company's customers include major fabless IC design companies, integrated device manufactures and semiconductor foundries. In 2001, the Company's top five customers in alphabetical order were Macronix International Corporation, MediaTek Incorporation, Silicon Storage Technology, Inc., United Microelectronics Corporation and Vanguard International Semiconductor Corporation. According to Dataquest report in 2000, test services provided by independent test companies, including the Company, accounted for 8.0 per cent. of the total test services in terms of derived revenues in 2000. In addition, according to Dataquest, independent test revenues are expected to grow at a compound annual growth rate of 47.1 per cent. from 1999 to 2003. The Company has established technical and sales teams near major customer facilities, including the Hsin-Chu Science Park, which work with its customers on developing and implementing new test technologies as tolerances of integrated circuitry become smaller and ICs become more sophisticated. The Company's financial performance depends on the success of its customers, whose success in turn depends on the growth and viability of the personal computers and computer peripherals, consumer electronics and telecommunications industries, which have at all times been subject to pronounced cyclicity.

The majority of the Company's sales have derived from test services, which accounted for 76.6 per cent., 82.2 per cent. and 84.0 per cent. of the total sales for the years of 1999, 2000 and 2001, respectively. Sales for other backend semiconductor manufacturing services as a whole accounted for 22.6 per cent., 15.5 per cent., and 13.9 per cent. of the Company's total sales for years 1999, 2000 and 2001, respectively.

The percentage of net revenues derived from sales to related parties has declined from 24.1 per cent. in 1999 to 13.2 per cent. in 2001, as the Company has increased sales to unrelated customers and diversified its product lines to include a full range of IC test and other backend semiconductor manufacturing services.

The Company's major direct costs include materials for backend semiconductor manufacturing services, factory overheads, including depreciation and utilities, and direct labor costs. One of the main factors affecting the Company's unit manufacturing costs is the utilization rate of the testers and other equipment that the Company employs. This depends on variables such as the market conditions and

customer demands. Because most of the Company's manufacturing costs are fixed costs such as depreciation of the equipment, especially the testers, the higher the utilization rate, the lower the Company's unit costs.

The Company's operating expenses are selling and general administrative expense, and research and development expense. Manufacturing expenses consist of compensation expenses, depreciation and amortization of equipment, insurance, research and development fees, indirect materials, lease payments, and miscellaneous costs such as travel and shipping expenses, etc.

Selling and general administrative expenses consist of compensation expenses, service fees, depreciation and amortization of tangible and intangible assets, professional fees and expenses, selling commission, advertising and promotion expense, lease payments, local taxes, doubtful account and others.

Research and development expenses consist of indirect materials costs, depreciation of research and development equipment, amortization of software acquisition costs, compensation expenses, lease payments, and others.

Basis of Presentation

Financial Statements

This Offering Circular contains the financial statements of the Company as of and for the years ended 31st December, 1999, 2000 and 2001.

Under ROC GAAP, the Company is required to consolidate financial results of any subsidiary (any corporation or other business entity more than 50 per cent. of the outstanding voting stock of which is owned directly or indirectly by the Company) whose total assets or net sales exceed 10 per cent. of the Company's non-consolidated total assets or net sales, as the case may be. In addition, the ROC Securities and Futures Commission ("SFC") requires the Company to consolidate the financial statements of each subsidiary whose total assets or net sales exceeded three per cent. of the Company's non-consolidated total assets or net sales, if the total assets or net sales of all non-consolidated subsidiaries of the Company exceeds 30 per cent. of the Company's non-consolidated total assets or net sales, as the case may be. The Company has only one subsidiary, KYEC USA, Inc. Neither the total assets nor net sales of such subsidiary exceeds three per cent. of the Company's total assets or net sales, respectively, and therefore the operating results of KYEC USA, Inc. are incorporated in the Company's financial statements by equity method, rather than consolidation. The Company does not provide consolidated financial statements and all financial and operating results of the Company included in this Offering Circular are on a non-consolidated basis.

Employee bonus Shares

The Company has historically paid employee bonuses of not less than 15.0 per cent. of the after-tax profits, less prior losses and legal and special reserves, in the form of Shares. The Company expects that it will continue to pay such employee bonuses, subject to shareholder approval, in respect of years in which it reports net profits. The Company granted its employees bonuses in the aggregate of 6,662,946 Shares and 15,511,500 Shares in 2000 and 2001, with respect to its distributable profits in 1999 and 2000, respectively.

The number of Shares distributed is obtained by dividing the total nominal NT Dollar amount of the bonus by the par value of the Shares, or NT\$10 per Share, rather than their market value at the date of grant, which has generally been higher than par value. Under ROC GAAP, the distribution of employee bonus shares is treated as an allocation from retained earnings, and the Company is not required to, and does not, charge the value of the employee bonus shares to income. Under U.S. GAAP, however, employees bonus expense is initially accrued when services are rendered. When a distribution of bonus is approved by the shareholders in the subsequent year, an additional compensation expense is recorded for the difference between the amount initially recorded and the fair market value of shares granted to employees. The effect of these differences in the Company's earnings, if reported in U.S. GAAP, would be material, and in some cases could even change net earnings into net loss.

Revenues

The following table sets out the Company's net sales for the three years ended 31st December, 1999, 2000 and 2001 by product category:

	Year ended 31st December,		
	1999	2000	2001
	NT\$'000	NT\$'000	NT\$'000
Test services			
Wafer probing	783,083	2,175,577	1,880,118
Final test	337,527	896,060	1,189,477
Burn-in	223,088	403,358	266,020
Other backend services			
Wafer grinding and dicing	154,214	345,070	336,194
Tape and reel	241,648	309,031	214,948
Others ⁽¹⁾	15,555	96,359	84,111
Total sales	1,755,115	4,225,455	3,970,868
Sales return and allowances	10,141	43,881	93,570
Net sales	1,744,974	4,181,574	3,877,298

(1) Includes packaging and assembly for CMOS image sensor and sales of burn-in equipment.

The markets for the Company's services are subject to a certain degree of seasonality. These markets exhibit particular strength toward the end of each year in connection with holiday season sales. Accordingly, as illustrated by the following table, the Company's third- and fourth-quarter revenues are ordinarily higher, and its first- and second-quarter sales are ordinarily lower, than average.

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total
	NT\$'000				
1999	286,972	408,337	477,035	572,630	1,744,974
2000	624,368	868,612	1,222,857	1,465,737	4,181,574
2001	1,330,382	919,362	759,636	867,918	3,877,298

(1) The quarterly sales information is unaudited.

The seasonal sales pattern was superseded by a general downturn in the semiconductor industry commencing in the second quarter of 2001, and the effects of the terrorist attacks of 11th September, 2001. Both the volume and the unit price of the Company's sales for 2001 were affected.

Sales revenues are recorded when services are provided and the products are delivered to the customers.

Results of Operations

The following table summarizes certain items from the results of operations of the Company for the three years ended 31st December, 1999, 2000 and 2001 as a percentage of net operating revenues.

	Year ended 31st December,					
	1999		2000		2001	
	Amount	%	Amount	%	Amount	%
	(in NT\$ million)		(in NT\$ million)		(in NT\$ million)	
Net operating revenues	1,745.0	100.0	4,181.6	100.0	3,877.3	100.0
Cost of sales	1,114.8	63.9	2,705.3	64.7	4,129.7	106.5
Gross profit	630.2	36.1	1,476.3	35.3	(252.4)	(6.5)
Operating expenses	130.8	7.5	305.8	7.3	436.8	11.3
Operating income (loss)	499.4	28.6	1,170.5	28.0	(689.2)	(17.8)
Non-operating income	11.3	0.6	43.1	1.0	153.1	4.0
Non-operating expenses	56.6	3.2	210.5	5.0	555.0	14.3
Income before income taxes, minority interest	454.1	26.0	1,003.1	24.0	(1,091.1)	(28.1)
Income tax benefit (expense)	34.6	2.0	175.3	4.2	299.5	7.7
Net income (loss)	488.7	28.0	1,178.4	28.2	(791.6)	(20.4)

Net revenues for the first two months of 2002

The Company's unaudited net revenues for February 2002 were NT\$282.3 million, compared to net revenues of NT\$421.2 million for February 2001, representing a decrease of 33.0 per cent. The Company's total net revenues for the two months ended 28th February, 2002 were NT\$570.4 million, representing a decrease of 36.9 per cent. compared to the corresponding period of 2001. The Company expects that its results for at least the first quarter of 2002 will be affected.

2001 Compared to 2000

Operating Revenues. Total operating revenues declined from NT\$4,225.5 million in 2000 to NT\$3,970.9 million (U.S.\$113.5 million) in 2001, a decrease of 6.0 per cent., resulting from the general downturn in the semiconductor industry commencing in the second quarter of 2001. Both the volume and the average unit prices of sales for 2001 were affected. In addition, due to negative market conditions, the Company's customers increasingly requested concessions on pricing, which was the primary cause of a 113.2 per cent. increase in sales returns and allowances, from NT\$43.9 million in 2000 to NT\$93.6 million (U.S.\$2.7 million) in 2001.

In 2001, the operating revenues generated from test services accounted for 84.0 per cent. of total sales, and operating revenues generated from other backend semiconductor manufacturing services accounted for 13.9 per cent. of total sales.

As a result, the Company's revenues generated from test services decreased by 4.0 per cent. from NT\$3,475.0 million in 2000 to NT\$3,335.6 million (U.S.\$95.4 million) in 2001, principally resulting from the decrease in test revenues from wafer probing and burn-in, which outpaced an increase in final test revenues. In 2001, the Company increased its service capacity by installation of a number of new testers to perform final tests in accordance with its expectation of increased demand resulting in a 32.7 per cent. increase in final test revenues from NT\$896.0 million in 2000 to NT\$1,189.5 million (U.S.\$34.0 million) in 2001.

The Company's revenues derived from other semiconductor backend manufacturing services decreased by 15.7 per cent. from NT\$654.1 million in 2000 to NT\$551.1 million (U.S.\$15.8 million) in 2001. The decrease was attributable to the general decrease in demand for semiconductor backend

manufacturing services and resulting industry over-capacity. While the revenues derived from wafer grinding and dicing services remained relatively unchanged, the revenues derived from tape and reel services decreased by 30.4 per cent.

Cost of Sales. The Company's cost of sales includes primarily materials for backend semiconductor manufacturing services, factory overheads, including depreciation and utilities, and direct labor costs. In 2001, the Company's total cost of sales increased by 52.7 per cent. to NT\$4,129.7 million (U.S.\$118.1 million), driven principally by a significant increase in depreciation costs associated with the new testers purchased and installed by the Company and the completion of construction of the Company's new Chung-Hwa Factory building in 2001.

The Company started recording depreciation on the new testers when they were put on service in 2001. The Company's depreciation cost increased from NT\$1,049.2 million in 2000 to NT\$2,161.2 million (U.S.\$61.8 million) in 2001.

Gross margin decreased to (6.5) per cent. from 35.3 per cent. in 2000, primarily due to the decrease in sales accompanied by the significant increase in fixed costs, and in particular depreciation costs.

The Company outsourced packaging services to a number of packaging vendors when its customers require backend semiconductor manufacturing services on a turnkey basis. Packaging fees paid by the Company to the third-party packaging vendors are recorded as the Company's cost of sales. In 2001, the Company paid NT\$66 million (U.S.\$1.9 million) as packaging processing cost to the third-party packaging vendors.

Operating Expenses. Total operating expenses for 2001 were NT\$436.8 million (U.S.\$12.5 million), compared to NT\$305.8 million for 2000, an increase in 42.8 per cent.

➤ *Selling and general administrative expenses*

Selling and general administrative expenses increased by 48.4 per cent. in 2001 to NT\$378.6 million (U.S.\$10.8 million). The increase was attributable to:

- Increase in compensation expenses due to the expansion of the Company's sales team;
- Increases in maintenance charge, utilities charges, insurance expenses and depreciation and amortization mainly in connection with the completion of newly constructed Chung-Hwa Factory building;
- Doubtful accounts relating to a particular customer; and
- Commissions paid to KYEC USA for sales and marketing in North America.

➤ *Research and development expenses*

Research and development expenses increased by 14.8 per cent. in 2001 to NT\$58.2 million (U.S.\$1.7 million). The increase was attributable to:

- Increase in compensation expenses due to the expansion of the Company's research and development team; and
- Increases in maintenance charge, utilities charges, insurance expenses and depreciation and amortization as the portion of these expenses in connection with research and development activities increased due to the completion of newly constructed Chung-Hwa Factory building.

Operating losses. Operating loss in 2001 was NT\$689.2 million (U.S.\$19.7 million), compared to operating income of NT\$1,170.5 million in 2000.

Non-operating income. Non-operating income increased by 255.6 per cent. to NT\$153.1 million (U.S.\$4.4 million) in 2001, due to increases in:

- Net exchange gains of NT\$105.3 million (U.S.\$3.0 million) primarily from the depreciation of Japanese yen;
- Gain on disposal of property, plant and equipment which consist of the equipment related to a terminated sales contract; and
- Gain on disposal of short-term investments, consisting of shares in bond funds.

Non-operating expenses. Non-operating expenses increased by 163.7 per cent. to NT\$555.0 million (U.S.\$15.9 million) in 2001, principally due to increases in:

- Interest expense, due to an increase in the principal amount of outstanding working capital loans;
- Other losses of NT\$168.7 million (U.S.\$4.8 million) in 2001, compared to NT\$0.9 million in 2000. These losses relate to:
 - compensation of NT\$102.0 million (U.S.\$2.9 million) payable in connection with the return of machinery and equipment to the vendor;
 - depreciation expense of NT\$36.6 million (U.S.\$1.0 million) in relation to idled assets consisting of plant, machinery and equipment not employed in production for a significant period; and
 - depreciation expense of NT\$23.8 million (U.S.\$0.7 million) in relation to leased assets;
- loss on disposal of property, plant, and equipment.

Net income (loss). Pre-tax loss for 2001 was NT\$1,091.1 million (U.S.\$31.2 million), compared to pre-tax income of NT\$1,003.1 million for 2000. Income tax benefit for 2001 was NT\$299.5 million (U.S.\$8.6 million), compared to NT\$175.3 million for 2000. As a result, the net loss in 2001 was NT\$791.7 million (U.S.\$22.6 million), compared to net income of NT\$1,178.4 million for 2000.

See Note 4(10) to the Financial Statements for information regarding income taxes.

2000 Compared to 1999

Operating Revenues. Net operating revenues increased from NT\$1,745.0 million in 1999 to NT\$4,181.6 million in 2000, an increase in 139.6 per cent.

The Company's revenues generated from test services increased by 158.6 per cent. from NT\$1,343.7 million in 1999 to NT\$3,475.0 million in 2000, principally resulting from the increases in wafer probing and final test revenues. The significant increases in test revenues were attributable to an increase in demand, the Company's customer base and an increase in the Company's service capacity. Also, the Company's revenues derived from other semiconductor backend manufacturing services increased by 65.2 per cent. from NT\$395.9 million in 1999 to NT\$654.1 million in 2000.

Cost of Sales. Generally in line with the increase in the sales revenue, the Company's total cost of goods sold increased from NT\$1,114.8 million in 1999 to NT\$2,705.3 million in 2000, a 142.7 per cent. increase. Cost of sales increased mainly due to increases in depreciation and amortization, utilities charges, maintenance charges and insurance expenses resulting from the completion of construction and commencement in operation of the Company's corporate headquarters and purchases of new testers. Compensation expenses also increased due to a salary increase and in increase in head count. Gross margin remained fairly unchanged in 1999 and 2000 at 36.1 per cent. and 35.3 per cent., respectively.

Operating expenses. Total operating expenses increased by 133.8 per cent. from NT\$130.8 million in 1999 to NT\$305.8 million in 2000. As a result, operating profit margins for 2000 decreased to 28.0 per cent., compared to 28.6 per cent. in 1999.

➤ *Selling and general administrative expenses*

Selling and general administrative expenses increased by 145.6 per cent. in 2000 to NT\$255.1 million. The increase was attributable to:

- Increase in compensation expenses due to a salary increase and expansion of the Company's sales team;
- Increases in maintenance charge, utilities charges, insurance expenses and depreciation and amortization mainly in connection with the completion of the Company's new headquarters building; and
- Commissions paid to KYEC USA for sales and marketing in North America.

➤ *Research and development expenses*

Research and development expenses increased by 87.9 per cent. in 2000 to NT\$50.7 million. The increase was attributable to:

- Increase in compensation expenses due to the expansion of the Company's research and development team; and
- Increases in maintenance charge, utilities charges, insurance expenses and depreciation and amortization as the portion of these expenses in connection with research and development activities increased in connection with the completion of the Company's new headquarters building.

Non-operating income. Non-operating income increased by 279.6 per cent. to NT\$43.1 million in 2000, primarily due to increases in gains on interest income and partially offset by decreases in gains on disposal of short-term investment.

Non-operating expenses. Non-operating expenses increased by 271.5 per cent. to NT\$210.5 million in 2000, principally due to increases in:

- interest expenses, caused by a decrease in the principal amount of outstanding working capital loans;
- net exchange loss of NT\$25.2 million compared to net exchange loss of NT\$11.7 million in 1999; and
- NT\$6.9 million or 527.4 per cent. decrease in loss on disposal of property, plant, and equipment.

Net income (loss). Pre-tax income for 2000 was NT\$1,003.1 million, representing 24.0 per cent. of net revenues, compared to pre-tax income of NT\$454.1 million for 1999, representing 26.0 per cent. of net revenues. Income tax benefit for 2000 was NT\$175.3 million, compared to NT\$34.7 million in 1999. Net income for 2000 was NT\$1,178.4 million, compared to NT\$488.7 million for 1999, representing an increase in 141.1 per cent.

Inventories and Receivables

Receivables are the principal components of the Company's current assets and require a significant amount of working capital support, particularly as the Company's sales continue to increase. Accordingly, control of receivables is a key aspect of the Company's business operations. In addition, the Company's inventories also form part of its current assets.

The following tables summarize the Company's inventories and receivables positions for the periods indicated below:

	Year ended 31st December,			
	1999	2000	2001	2001
	(in NT\$'000)	(in NT\$'000)	(in NT\$'000)	(in U.S.\$'000)
Receivables, net				
Notes receivable-trade	70,300	100,580	46,041	1,316
Accounts receivable-trade	371,494	1,281,446	593,174	16,958
Accounts receivable-related parties	152,693	73,376	82,807	2,367
	594,487	1,455,402	722,022	20,641
Less: Allowance for doubtful accounts	(198)	(198)	(12,200)	(349)
Allowance for sales return	—	—	(13,000)	(372)
Receivables, net	594,289	1,455,204	696,822	19,921
Average receivables turnover (days)	88	89	102	—
Inventories				
Raw materials	15,332	55,151	44,064	1,260
Work in progress	13,847	22,160	8,383	240
Finished goods	—	—	9,254	264
Inventory in transit	—	—	—	—
Merchandise inventory	—	—	—	—
Subtotal	29,179	77,311	61,701	1,764
Less: Allowance for inventory obsolescence and decline in market value	(782)	(782)	(4,870)	(139)
Inventories, net	28,397	76,529	56,831	1,625
Average inventory turnover (days)	9	7	6	—

Liquidity and Capital Resources

During 2001, the Company financed its operations primarily through long-term syndicated loans, short-term working capital borrowings and also through cash flow from operations. In 2000, the Company financed its operations primarily through cash flow from operations and debt and equity financing. The Company issued 70,000,000 new Shares for an aggregate cash consideration of NT\$4,900.0 million.

Due to the decrease in the Company's sales, and the increase in costs, expenses and capital expenditures, in 2001, the Company has encountered problems of limited liquidity during the fourth quarter of 2001 and the first quarter of 2002. The Company has taken several steps to deal with this situation, including:

- Obtaining agreement of its banks to extend maturities under its long-term loans to November 2002;
- returning certain machinery and equipment to the vendor and termination of related purchase orders;
- leasing out of the Chu-Nan Factory to a customer under operating leases, which has been terminated in February 2002; and
- factoring receivables to accelerate receipt of cash.

Unused amounts under existing working capital lines were NT\$1,534.6 million (U.S.\$43.9 million) at 31st December, 2001.

Based on current levels of cash flow from operations, the Company is able to make required payments of interest and meet its other costs and expenses as they fall due. Under its loan agreements, the Company will be required to make total principal payments in 2002 in the amount of NT\$1,060.2 million in respect of long-term debt, and NT\$1,605.6 million in respect of short-term debt. Approximately U.S.\$74.70 million and U.S.\$44.45 million of the net proceeds of the Bonds will be applied toward the repayment of long- and short-term debt, respectively. The Company believes that, after giving effect to the issue and sale of the Bonds, it will have sufficient liquidity to fund its operations through the end of 2002. The Company expects that it will be necessary in the future to raise funds through the issue of equity securities, debt securities and bank loans to finance its operations and capital expenditures. There is no assurance that the Company will be able to raise such funds on terms that are acceptable to the Company, or at all.

Current ratio

As a consequence of the factors described above, the Company's current ratio at 31st December, 2001 fell to 19.6 per cent. Under the terms of the Company's long-term loans, it is required to maintain certain financial ratios, including a current ratio of not less than 100 per cent., or be required to make compensation payments to the banks. See "— Liquidity and Capital Resources — Property, plant and equipment" below. Cash and cash equivalents at 31st December, 2001 stood at NT\$59.7 million (U.S.\$1.7 million), which is significantly lower than an optimal level for the operation of a business of the scale of the Company's business. Accounts receivable at 31st December, 2001 decreased by 55.7 per cent. to NT\$568.0 million (U.S.\$16.2 million) compared to NT\$1,281.2 million at 31st December, 2000. The accounts receivable balance was lower compared to the prior year-end mainly because of the decrease in sales from 2000 to 2001. Related party receivables increased by 12.9 per cent. to NT\$82.8 million (U.S.\$2.4 million) in 2001.

Inventories at 31st December, 2001 were NT\$56.8 million (U.S.\$1.6 million), compared to NT\$76.5 million at 31st December, 2000, a decrease of 25.7 per cent. The decrease in inventories relates principally to the reduction of the burn-in oven stocks.

Total current liabilities increased from NT\$3,601.0 million at 31st December, 2000 to NT\$4,675.1 million (U.S.\$133.7 million) at 31st December, 2001, an increase in 29.8 per cent. The increase is principally attributable to an increase in the current portion of long-term loans of NT\$837.9 million and payable to equipment suppliers of NT\$392.6 million. Interest rates on the long-term loans during 2001 ranged from 3.98 per cent. to 7.50 per cent.

Property, plant and equipment

Based on its estimation of expected demand, the Company invested cash of NT\$3,641.8 million, NT\$9,605.3 million and NT\$5,676.3 million (U.S.\$162.3 million) in the years 1999, 2000 and 2001, respectively, in the acquisition of property, plant and equipment. The following table shows the breakdown of the Company's capital expenditures for these years:

	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>Sub-total</u>
	(NT\$ million)			
Land, building and facilities	1,108.1	1,700.6	599.3	3,408.0
Machinery and equipment.	2,464.4	7,171.4	3,875.5	13,511.3
Others	69.3	733.3	1,201.4	2,004.1
Sub-total	3,641.8	9,605.3	5,676.3	18,923.4

These capital expenditures have been financed by proceeds of the issuance of shares for cash in the amount of NT\$6,350.0 million and long-term loans in the principal amount of NT\$5,759.2 million. As at 31st December, 2001, the Company has NT\$5,759.2 million (U.S.\$164.6 million) outstanding secured long-term loans from 20 financial institutions, of which NT\$1,060.3 million (U.S.\$30.3 million) will fall due in 2002. The following table shows the detail of the Company's long-term loans:

Lead Bank	Original	Outstanding	Final Maturity	Annual Principal Repayment Amount						
	Principal	Principal								
	Amount	Amount		2001	2002	2003	2004	2005	2006	2007
	(NT\$'000)	(NT\$'000)		(NT\$'000)						
Chiao-Tung Bank ⁽¹⁾	360,000	290,700	January 2006	69,300	68,400	68,400	68,400	68,400	17,100	—
Chiao-Tung Bank ⁽²⁾	400,000	400,000	October 2007	—	19,000	76,000	76,000	76,000	76,000	77,000
China Development Industrial Bank and other 4 banks ⁽³⁾	995,000	918,464	September 2004	76,536	382,680	306,144	229,640	—	—	—
China Development Industrial Bank and other 16 banks ⁽⁴⁾	4,000,000	4,000,000	November 2005	—	571,428	1,142,864	1,142,864	1,142,844	—	—
Hsin-Chu International Commercial Bank ⁽⁵⁾	150,000	150,000	June 2006	—	18,750	37,500	37,500	37,500	18,750	—
Total	5,905,000	5,759,164		145,836	1,060,258	1,630,908	1,554,404	1,324,744	111,850	77,000

- (1) Principal repayable in 20 quarterly installments, starting from 25th January, 2001. Except for the first installment that the Company needs to repay NT\$18 million, the Company is obligated to repay NT\$17 million in each quarter. Interests are payable monthly.
- (2) Principal repayable in 20 equal installments in each quarter, starting from 5th October, 2002. Interests are payable monthly.
- (3) Principal repayable on a quarterly basis. The principal repayment due from 20th December, 2001 to 20th September, 2002, totaled NT\$306,144,000 has been extended to 15th November, 2002, provided that the Company will repay the less of such total principal amount due upon completion of the Offering or such funding activities or the amount not less than 50 per cent. of the proceeds from the Bonds or from other fund raising activities in the capital market to the banks immediately within ten days after completion of such fund raising activities. Thereafter, the Company will pay NT\$76,536,000 in each installment for six quarters and NT\$76,568,000 in the last installment.
- (4) Principal repayable in seven equal installments on a semi-annual basis, starting from 20th November, 2002. Interests are payable monthly.
- (5) Principal repayable in 16 equal installments in each quarter, starting from 26th June, 2002. Interests are payable monthly.

The Company covenants with China Development Industrial Bank and other banks in the NT\$995.0 million syndicated loan due September 2004 and NT\$4,000.0 million syndicated loan due November 2005 that it will maintain current assets to current liability ratio at not less than 100 per cent. and debt to equity ratio at not less than 100 per cent. as well. The Company is subject to a quarterly compensatory charge of 0.1 per cent. per annum for non-compliance.

Net property, plant and equipment increased by 17.0 per cent. at 31st December, 2001 to NT\$15,052.3 million (U.S.\$430.3 million), compared to NT\$12,869.2 million at 31st December, 2000. A 71.4 per cent. increase in machinery and equipment and a 94.6 per cent. increase in building and facilities representing the Company's new Chung-Hwa Factory were substantially offset by the transfer of property, plant and equipment with a total net book value of NT\$1,169.4 million (U.S.\$33.4 million) to the following categories under "other assets":

- assets to be disposed of, consisting of IC testing machinery and equipment to be sold back to the manufacturer, upon termination of the purchase order of such equipment, net book value NT\$650.8 million (U.S.\$18.6 million);

- facilities leased to others pursuant to a lease that has been terminated in February 2002, consisting of Chu-Nan Factory, net book value NT\$273.3 million (U.S.\$7.8 million);
- idled assets, equipment, net book value NT\$245.3 million (U.S.\$7.0 million); and

Other assets increased to NT\$2,042.2 million (U.S.\$58.4 million), compared to NT\$291.0 million at 31st December, 2000. Depreciation of assets classified under “other assets” is recorded as a non-operating expense in “other losses”, rather than in operating costs as would be the case under U.S. GAAP. Accordingly, the Company’s operating loss for 2001 reported in accordance with U.S. GAAP would be corresponding larger; however, the amount of the net loss would not be affected.

Commitments and contingencies

At 31st December, 2001, the Company had entered into construction contracts for the expansion of factory facilities totaling NT\$882.4 million (U.S.\$25.2 million), of which amount a total of NT\$202.8 million (U.S.\$5.8 million) was un-accrued as of 31st December, 2001. Such NT\$202.8 million will be accrued upon the Company’s acceptance of the factory facilities.

Open letters of credit at 31st December, 2001 totaled NT\$28.5 million (U.S.\$0.8 million).

At 31st December, 2001, the Company was named as defendant in two civil actions. Hwa Tsai Co., Ltd. and two other investors brought civil proceedings against the Company and its chairman, seeking payments of approximately NT\$62.2 million (U.S.\$1.8 million) in damages for losses suffered as a result of alleged misleading statements made by the Company and its management. Watron Technology Corporation instituted civil proceedings against the Company, seeking payment of approximately NT\$16.4 million as damages for the Company’s alleged breach of contract. The Company counterclaimed and sought for NT\$14 million (U.S.\$0.4 million) as damages. The district court ruled in favor of the Company and ordered Watron to pay the Company NT\$876,672. The Company appealed to the High Court of Taiwan against the amount of damages awarded. In addition, a criminal complaint has been filed and is under investigation by the District Attorney for Hsin-Chu in relation to the same matters in the first civil action above and the alleged violations of the Securities and Exchange Law and Criminal Law. See “Business — Litigation”.

Quantitative and Qualitative Disclosures about Market Risk

The financial market risks to which the Company is exposed are principally risks relating to changes in exchange rates and interest rates.

Foreign Currency Risk

A substantial portion of the Company’s net sales are denominated in NT Dollars, while the Company purchases a substantial amount of machinery and equipment in Japanese Yen and U.S. Dollars. Accordingly, the Company is exposed to movements in the exchange rates between U.S. Dollars and Japanese Yen on the one hand, and NT Dollars on the other hand. The Company recorded net exchange losses of NT\$11.7 million and NT\$25.1 million in 1999 and 2000, respectively, and net exchange gains of NT\$105.3 million (U.S.\$3.0 million) in 2001.

The effect of future changes in currency exchange rates on the Company’s results of operations cannot be accurately predicted. The Company continuously reviews its positions in relation to the various relevant currencies, and may enter into foreign currency forward contracts where available when it considers it appropriate to do so in order to hedge exposure. The Company, however, does not have any hedging contracts of any nature currently in effect.

To the extent possible, the Company attempts to match the currencies of its costs and expenses to the currencies of its revenues.

Interest Rate Risk

The Company has not entered into interest swaps or other hedging arrangements.

The following table shows long- and short-term bank loans outstanding at 31st December, 1999, 2000 and 2001:

Short-term loans:

	<u>Principal amount</u> (NT\$ in millions)	<u>Interest Rate⁽¹⁾</u>
1999	220.2	0.9%–7.21%
2000	1,776.5	0.99%–8.0867%
2001	1,502.6	0.78%–7.60%

Long-term loans:

	<u>Principal amount</u> (NT\$ in millions)	<u>Interest Rate⁽²⁾</u>
1999	1,363.4	4.78%–7%
2000	3,330.0	6.655%–7.5%
2001	5,759.2	3.98%–6.9%

(1) Floating interest rate

(2) Floating interest rate except for the discount rate for long-term notes payable

Income Tax

The Company is subject to income taxes in the ROC. The statutory income tax rate applicable to the Company in the ROC is 25.0 per cent.

The Company benefits from tax incentives generally available to ROC companies, including tax credits currently at rates ranging between five per cent. and 20 per cent. of the amount spent on qualifying machinery and equipment, at a rate of 35 per cent. for qualifying research and development, costs and employee training expenses. An additional tax credit may also be available to the Company, equal to 50 per cent. of the amount for the qualifying research and development costs or employee training expenses in the previous two years. If the tax credit cannot be fully utilized in the current year, the balance may be carried forward for up to four years. The available tax credit in each year is limited to 50 per cent. of the corporate tax payable in that year, except for the last of the four years for which there is no limit. The Company's income tax saving from such programs were approximately NT\$55.0 million, NT\$133.0 million and NT\$0.0 million for 1999, 2000 and 2001, respectively. In addition, the Company recorded approximately NT\$(1,068.4) million (U.S.\$(30.5) million) as losses in 2001. The losses can be carried forward in a period of five years subsequent to the year the Company recorded as losses as tax benefits.

In order to increase ROC's competitive ability, an amendment to the ROC Income Tax Law (the "Amendment") was enacted on 1st January, 1998, to integrate the corporate income tax and the shareholder dividend tax with the aim of eliminating the double taxation effect for resident shareholders of ROC corporations. In accordance with the Amendment, a 10 per cent. retained earnings tax will be imposed on a company for its after-tax earnings generated after 1st January, 1998 which are not distributed in the following year. The retained earnings tax so paid will further reduce the retained earnings available for future distributions. When the company declares dividends out of those retained earnings, a maximum amount of up to 10 per cent. of the declared dividends will be credited against the 20 per cent. withholding tax imposed on the Non-ROC Holders.

In 2000 and 2001, the Company recorded no income tax liabilities in respect of such ten per cent. retained earnings tax. If the Company does not distribute all earnings within the specified period in the future, it will be subject to the ten per cent. retained earnings tax in respect of the undistributed amount, which could increase the Company's income tax liability.

MANAGEMENT AND EMPLOYEES

Directors

The Company's board of directors is elected by the shareholders in a general meeting at which a quorum, consisting of a majority of all issued and outstanding common shares, is present. The Chairman is elected by the board from among the directors. The Company's seven-member board of directors is responsible for the management of the Company's business.

The term of office for the Company's directors is three years from the date of election. Directors may serve any number of consecutive terms and may be removed from office at any time for a valid reason by a resolution adopted at a general meeting of shareholders.

The following table sets forth the name of each of the Company's current directors, his position in the Company, the percentage of Shares held, and other significant positions in the Company or in unrelated companies held by them. None of the Company's Directors holds significant positions in other entities or institutions.

<u>Name</u>	<u>Position</u>	<u>Percent of Shares held⁽¹⁾</u>
C. K. Lee	Director and Chairman	3.32%
D. F. Lin	Director and President	1.66%
Bright Shiao	Director and Executive Vice-President	2.76%
Ben Lu	Director	1.22%
H. T. Lin	Director and Assistant Vice President	1.48%
Pu Wen Xiong	Director	1.05%
Zheng Jiang Xi	Director	2.55%

(1) As of 8th March, 2002.

Supervisors

The Company currently has three supervisors, each serving a three-year term. Supervisors are typically elected at the time that directors are elected. The supervisors' duties and powers include investigation of the Company's business condition, inspection of the Company's corporate records, verification and review of financial statements presented by the Company's board of directors at shareholders' meetings, convening of shareholders' meetings when the board of directors does not or cannot convene a shareholders' meeting and/or such meeting as may be necessary for the benefit of the shareholders of the Company, representing the Company in negotiations with the Company's directors and notification, when appropriate, to the board of directors to cease acting in contravention of any applicable law or regulation or the Company's Articles of Incorporation or resolution adopted at the shareholders' meeting. Each supervisor is elected by the Company's shareholders and cannot concurrently serve as a director, management officer or other staff member. The ROC Company Law requires at least one supervisor to be in office at all times and that a supervisor's term of office be no more than three years.

The following table sets forth the name of each of the Company's current supervisors, his or her position in the Company, the percentage of Shares and other significant positions held by him or her.

<u>Name</u>	<u>Position</u>	<u>Percent of Shares held⁽¹⁾</u>	<u>Other significant positions held</u>
Ben Yang ⁽²⁾	Supervisor	0.44%	President of Pacific Venture Group Capital Co., Ltd
Cao Li Wen	Supervisor	0.13%	—
Xie Qi Jun	Supervisor	0.23%	—

(1) As of 8th March, 2002.

(2) Nominated by H-Com Venture Capital Co., Ltd.

In accordance with ROC law, a person may serve as the Company's director or supervisor in his personal capacity or as the representative of another legal entity. Of the current directors and supervisors, only one was nominated by H-Com Venture Capital Co., Ltd.; the remaining directors and supervisors serve in their personal capacity.

Executive Officers

The following table sets forth information relating to the Company's executive officers.

Name	Position	Years with the Company	Age
Bright Shiao	Executive Vice President	10	42
S. B. Chang	Director of Research and Development Division (I)	4	39
Raymond Yin	Assistant Vice President of Research and Development Division (II)	4	40
A. H. Liu	Vice President of Manufacturing Center	2	43
Gauss Chang	Assistant Vice President of Business Center	2	37
P. K. Hung	Chief Financial Officer	0.1	43

Biographies of Directors, Supervisors and Executive Officers

C. K. Lee, aged 46, joined the Company in 1991 and has served as a director and the Chairman of the Company since February 1998. Before joining the Company, Mr. Lee served as a Senior Manager in United Microelectronics Corporation. Mr. Lee holds a bachelors' degree in shipping and transportation management from National Taiwan Ocean University.

D. F. Lin, aged 44, has served as a director and President of the Company since February 1998. Before joining the Company, Mr. Lin served as the Vice President of Macronix International Corporation and has a total of 20 years of experience in semiconductor manufacturing and testing. He holds a bachelor's degree in electrical engineering from Chung Yuan Christian University in the ROC.

Bright Shiao, aged 42, has served as a director and Executive Vice President of the Company since November 1991. Before joining the Company, Mr. Shiao served as the President of Don-Sun Motor Co, Ltd and has a total of 21 years of experience in business management. He holds a college degree in electronics from Southern Taiwan University of Technology in the ROC.

Ben Lu, aged 45, has served as a director of the Company since November 1991. Before joining the Company, he served as the assistant manager of United Microelectronics Corporation and has about 20 years of experience in semiconductor manufacturing. He holds a bachelor's degree in physics from Tamkang University in the ROC.

H. T. Lin, aged 41, has served as Vice President of Logic & Mixed Signal C/P Test Division since August 1996. Before joining the Company, he was an assistant manager of United Microelectronics Corporation. He holds a bachelor's degree in electronic engineering from Oriental Institute of Technology in the ROC.

Pu Wen Xiong, aged 59, has served as a director of the Company since November 1991. Before joining the Company, Mr. Pu served as the Chairman of Xian Ji Realty Co., Ltd. He has 20 years of experience in business management.

Zheng Jiang Xi, aged 65, has served as a director of the Company since November 1991. Before joining the Company, Mr. Zheng served as the director of Universal Textile Co., Ltd. He has 20 years of experience in business management.

Ben Yang, aged 46, has served as a supervisor of the Company since January 2002. Before joining the Company, Mr. Yang served as a President of Pacific Venture Group Capital Co., Ltd. He holds a master's degree in mechanical engineering from University of California, Santa Barbara Branch.

Cao Li Wen, aged 47, has served as a supervisor of the Company since April 1999. Before joining the Company, Ms. Cao served as a lawyer of Lee Xiang United Law Offices. She holds a bachelor's degree in law from Soochow University.

Xie Qi Jun, aged 45, has served as a supervisor of the Company since April 1999. Before joining the Company, Mr. Xie served as a doctor of Xiang An Clinic. He holds a bachelor's degree in medicine from Taipei Medical University.

S. B. Chang, aged 39, joined the Company as Director of Research and Development Division (I) in February 1998. Before joining the Company, he was a project manager of Macronix International Corporation. He holds a master's degree in electrical engineering and computer science from National Central University in the ROC.

Raymond Yin, aged 40, joined the Company in February 1997 and became the Director of Research and Development Division (II) in April 2001. Before joining the Company, Mr. Yi served as a manager of Macronix International Corporation. He holds a bachelor's degree in electrical engineering from National Cheng Kung University in the ROC.

A. H. Liu, aged 43, joined the Company as the Vice President of Quality System Division in March 2000. Before joining the Company, he served as a manager of Ford Motors (Taiwan) Co., Ltd. He holds a doctorate degree in mechanical engineering from North Carolina State University in the United States of America.

Gauss Chang, aged 37, joined the Company as the Director of Sales and Marketing Division in 2000. Before joining the Company, he served as a manager of Winbond Electronics Corporation. He holds a master's degree in business management from Saginaw Valley State University in the United States of America.

P. K. Hung, aged 43, joined the Company as the chief financial officer in March 2002. Before joining the Company, he had been a chief financial officer of the Japanese branch of UMC for 18 years. He holds a bachelor's degree in public finance from National Cheng-chi University in ROC.

Compensation of Directors, Supervisor and Executive Officers

In 2001, the Company paid to its directors, supervisors, and the executive officers approximately NT\$10.3 million (U.S.\$0.3 million) in aggregate cash remuneration.

Interests of Management in Certain Transactions

None of the directors, supervisors or executive officers of the Company serves as directors, supervisors or executive officers of companies with which the Company does business.

Employees

Overview

The Company had the following number of employees as of the period indicated:

	As of 31st December,		
	1999	2000	2001
Administrative	66	132	115
Research and development	32	54	59
Engineering/technical operations	1,163	2,736	2,397
Sales & marketing	2	41	48
Total	<u>1,263</u>	<u>2,963</u>	<u>2,619</u>

As of 31st December, 2001, all of the Company's employees worked on a full-time basis, of which 2.3 per cent. were engaged in research and product development, 6.2 per cent. in sales, marketing, general and administration and 91.5 per cent. in engineering/technical operations. The average age of the employees is 28.3 years old. None of the Company's employees is represented by collective bargaining organization, such as a union, or subject to any bargaining agreements.

As of 31st December, 2001, approximately 67.8 per cent. of the Company's research and development personnel held a bachelor's degree or higher educational qualification and approximately 60.1 per cent. of the Company's senior to mid-ranking management and administration personnel held a bachelor's degree or higher educational qualification. The Company places considerable importance on the recruitment, training and retention of a team of qualified and experienced engineers to oversee and manage the Company's Taiwan manufacturing operations.

The Company's employees in the ROC are not unionized and the Company has not experienced any significant labor disputes in the past three years.

Employee remuneration

The salaries of the Company's employees in the ROC are adjusted based on industry standards, inflation and individual performance. The Company pays year-end bonus to the employees equivalent to an average of one months' salary. In addition, the Articles of Incorporation of the Company provide that the Company's employees are entitled to employee bonuses out of the earnings (subject to compliance with the requirements of the ROC Company Law) which may be paid in cash or stock. See "Description of The Shares". Stock bonuses of 15.5 million shares, were paid to employees in respect of the 2001 financial year. The number of the Shares issuable being calculated by reference to the par value of NT\$10 per Share, notwithstanding that the market value of the Shares as of the date of declaration and distribution of the stock bonuses were higher than NT\$10 per Share. In addition, ROC law requires that the Company's employees be given pre-emptive rights to subscribe for between 10 per cent. to 15 per cent. of any rights issues or share offerings of the Company, except issuances in connection with exercise of employee stock options, warrant exercises, conversion of bonds, mergers and spin-offs or by way of a private placement. Currently, the Company does not have any share option schemes.

Employee retirement plan

The Company has established an employee defined-benefit retirement plan ("Retirement Plan"). This Retirement Plan provides for lump-sum payments to retiring employees in Taiwan based on the length of service, age and certain other factors. Every month, the Company deposits at least two per cent. (but up to a maximum of 15 per cent.) of employees' total monthly salaries with the Central Trust of China in accordance with the Retirement Plan. Actual payment of retirement benefits was financed by the pension fund, and any insufficiency will be paid by the Company.

All TSE listed companies are required to calculate their pension obligations based on actuarial valuation. Pursuant to ROC Financial Accounting Standard Statement No. 18, the Company recognized net periodic pension cost which includes service cost, interest cost, expected return on plan assets, amortization of unrecognized transition obligation, pension gains/losses and prior service cost based on an actuarial valuation.

Employee Insurance

The Company carries on its own account group insurance for its employees. The third-party group insurance covers the employee's emergency medical needs and accidental insurance. Such insurance policy also provides additional coverage for the family members of the employees free of charge.

PRINCIPAL SHAREHOLDERS

As of 2nd June, 2001, no person held more than 10 per cent. of the Company's shares.

CHANGES IN ISSUED SHARE CAPITAL

The following table shows the increases in the issued share capital of the Company since incorporation:

<u>Date of Issue</u>	<u>Type of Issue</u>	<u>Number of Shares Issued</u>	<u>Number of Shares Outstanding after Issue</u>
May 1987.	Incorporation	7,000	7,000
February 1990.	Rights Issue	2,500	9,500 ⁽¹⁾
July 1994.	Rights Issue	1,100,000	2,050,000
October 1995	Rights Issue	950,000	3,000,000
September 1996	Rights Issue	2,000,000	5,000,000
May 1997.	Rights Issue	4,000,000	9,000,000
September 1997	Rights Issue	8,000,000	17,000,000
February 1998.	Rights Issue	18,000,000	35,000,000
August 1998.	Rights Issue and stock dividends	19,975,000	54,975,000
September 1998	Stock dividends	10,025,000	65,000,000
December 1998.	Rights Issue	5,000,000	70,000,000
July 1999.	Rights Issue and stock dividends	29,375,000	99,375,000
December 1999.	Rights Issue	25,000,000	124,375,000
July 2000.	Rights Issue and stock dividends	138,850,446	263,225,446
July 2001.	Rights Issue and stock dividends	173,446,768	436,672,214

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- (1) In July 1994, the Company carried out a subdivision of the existing 9,500 shares of nominal value of NT\$1,000 each into 950,000 shares of nominal value of NT\$10 each.

TERMS AND CONDITIONS OF THE BONDS

The following terms and conditions (subject to amendment and except for the sentences in italics) will be endorsed on the Certificates issued in respect of the Bond. The Global Certificate contains provisions which apply to the Bonds when they are in the form of interests that are represented by the Global Certificate, some of which modify the effect of the terms and conditions set out below. See "The Form of the Bonds".

The issue of U.S.\$120,000,000 Zero Coupon Convertible Bonds Due 2005 (the "**Bonds**") of King Yuan Electronics Co., Ltd. (the "**Company**") was authorized by resolutions of the Board of Directors of the Company adopted on 11th December, 2001 and 7th February, 2002. The Bonds are constituted by an indenture (the "**Indenture**") to be dated as of 18th April, 2002 and to be made between the Company and The Bank of New York (the "**Trustee**"), which term includes any successor trustee under the Indenture for the holders of the Bonds (the "**Bondholders**"). The Company has entered into a paying and conversion agency agreement (the "**Agency Agreement**") to be dated as of 18th April, 2002 with the Trustee, The Bank of New York as the registrar (the "**Registrar**") and the principal paying transfer and conversion agent, (the "**Principal Agent**") and The Bank of New York (Luxembourg) S.A., as paying, transfer and conversion agent, appointed thereunder (the "**Paying Agent**", the "**Conversion Agent**" and the "**Transfer Agent**" and such expression shall include the Principal Agent) in relation to the Bonds. The Registrar, the Principal Agent, the Paying Agent, the Conversion Agent and the Transfer Agent together referred to as the "**Agents**". The statements in these Terms and Conditions ("**Conditions**") include summaries of, and are subject to, the detailed provisions of the Indenture. Copies of the Indenture and the Agency Agreement are available for inspection by the Bondholders during normal business hours at the principal office of the Trustee, being at the date hereof at 101 Barclay Street, 21st Floor West, New York, N.Y. 10286 USA. and at the specified offices of each of the Agents. The Bondholders are entitled to the benefit of the Indenture and are bound by, and are deemed to have notice of, all the provisions of the Indenture and the Agency Agreement.

1. Status

The Bonds constitute direct, unconditional, unsubordinated and (subject to the provisions of Condition 3) unsecured obligations of the Company and rank at least pari passu among themselves and (subject as aforesaid and other than any obligations preferred by mandatory provisions of law) with all other present and future direct, unconditional, unsubordinated and unsecured obligations of the Company.

2. Form, Denomination and Title

(A) *Form and Denomination*

The Bonds will be issued in registered form, without coupons, in denominations of U.S.\$10,000 and integral multiples thereof. The Bonds will be offered and sold in principal amounts of US\$10,000 or an integral multiple thereof and will be transferable in principal amounts of US\$10,000 or an integral multiple thereof. The Bonds are not issuable in bearer form. The Bonds will initially be represented by a global certificate (the "**Global Certificate**") deposited with The Bank of New York, as common depositary for, and registered in the name of a nominee for, Euroclear Bank S.A./N.V., as operator of the Euroclear System ("**Euroclear**") and Clearstream Banking, *société anonyme* ("**Clearstream, Luxembourg**").

Owners of interests in the Bonds will not be entitled to receive definitive physical certificates (the "**Definitive Certificate**") in respect of their Bonds except in the limited circumstances described in the Global Certificate. In the event that certificates do become issuable, a bond certificate (each a "**Certificate**") will be issued to each Bondholder in respect of its registered holding of Bonds. Each Bond and each Certificate will be serially numbered with an identifying number which will be recorded on the relevant Certificate and in the register of Bondholders which the Company will procure to be kept by the Registrar.

(B) *Title*

Title to the Bonds will pass only by transfer and registration in the register of Bondholders. The registered holder of any Bond will (except as otherwise required by law) be treated as its absolute owner for all purposes (whether or not it is overdue and regardless of any notice of ownership, trust or any interest in it or any writing on, or the theft or loss of, the Certificate issued in respect of it) and no person will be liable for so treating the holder. In these Conditions, “**Bondholder**” and (in relation to a Bond) “**holder**” mean the person in whose name a Bond is registered.

3. **Negative Pledge**

So long as any of the Bonds remain outstanding (as defined in the Indenture), the Company shall not, and shall ensure that none of its Principal Subsidiaries (as defined below), if any, will, create or permit to be outstanding any mortgage, charge, pledge, lien or other form of encumbrance (each an “**Encumbrance**”) upon the whole or any part of its, or, as the case may be, any such Principal Subsidiary’s, if any, undertaking, property, assets or revenues, present or future, to secure for the benefit of the holders of any International Investment Securities (as defined below) (i) payment of any sum due in respect of any such International Investment Securities, (ii) any payment under any guarantee of any such International Investment Securities or (iii) any payment under any indemnity or other like obligation relating to any such International Investment Securities without in any such case at the same time according to the Bonds, either the same security as is granted to or is outstanding in respect of such International Investment Securities, guarantee, indemnity or other like obligation or such other security as shall be approved by an Extraordinary Resolution (as defined in the Indenture) of the Bondholders.

As used herein, the term “**International Investment Securities**” means bonds, debentures, notes or investment securities of the Company or any other person evidencing indebtedness with a maturity of not less than one year from the date thereof which (a) either (i) are by their terms payable, or confer a right to receive payment, in any currency other than New Taiwan Dollars or (ii) are denominated or payable in New Taiwan Dollars and more than 50 per cent. of the aggregate principal amount thereof is initially distributed outside Taiwan, the Republic of China (the “**ROC**”) by or with the authorization of the issuer thereof and (b) are for the time being, or are capable of being, quoted, listed, ordinarily dealt in or traded on any stock exchange, quotation system or over-the-counter or other similar securities market outside the ROC.

“**Principal Subsidiary**” means any subsidiary (i) whose total revenues, as shown by the latest audited accounts (consolidated in the case of a company which itself has subsidiaries) of such Subsidiary, are at least 10 per cent. of the total revenues of the Company and its consolidated Subsidiaries as shown by the latest audited consolidated accounts of the Company or (ii) whose gross assets, as shown by the latest audited accounts (consolidated in the case of a company which itself has subsidiaries) of such Subsidiary are at least 10 per cent. of the gross assets of the Company and its consolidated Subsidiaries as shown by the latest audited consolidated accounts of the Company, which may be acquired or formed by the Company from time to time during the terms of the Bonds.

4. **No Interest**

No interest will be payable on the Bonds, except as provided in Condition 10.

5. **Transfers of Bonds; Issue of Certificates**

(A) *Transfers*

Subject to Condition 5(D) below, a Bond may be transferred upon the surrender at the specified office of any Transfer Agent (including the Transfer Agent in Luxembourg) of the individual Definitive Certificate in respect of the Bond to be transferred, together with the form of transfer endorsed thereon (if such Definitive Certificate has been issued) or, in the case of a Bond represented by the Global Certificate, delivery at such office of a form of transfer obtainable from any of the Transfer Agents (the “**Form of Transfer**”), duly completed and executed and any other evidence that such Transfer Agent may reasonably require. In the case of a transfer of only part of a holding of Bonds in respect of which a Certificate is issued, a new Certificate shall be issued to the transferee in

respect of the part transferred and a further new Certificate in respect of the balance of the holding not transferred shall be issued to the transferor. The Form of Transfer is available at the specified office of the Transfer Agent (including the Transfer Agent in Luxembourg).

Transfers of interests in the Bonds evidenced by the Global Certificate will be effected in accordance with the rules of the relevant clearing systems.

(B) Delivery of New Certificates

Each new Certificate to be issued upon a transfer of Bonds shall be available for delivery upon receipt by the Transfer Agent (including the Transfer Agent in Luxembourg) at its specified office of the relevant Certificate and the Form of Transfer. Delivery of the new Certificates shall be made at the specified office of such Transfer Agent to whom the relevant Certificate and the Form of Transfer shall have been surrendered or delivered or, at the option of the holder making such delivery or surrender as aforesaid and as specified in the relevant Form of Transfer or otherwise in writing, be mailed by uninsured post at the risk of the holder entitled to the new Certificate to such address as may be so specified, unless such holder requests otherwise and pays in advance to the relevant Transfer Agent the costs of such other method of delivery and/or such insurance as it may specify.

Except in the limited circumstances described in the Global Certificate, owners of interests in the Bonds represented by the Global Certificate will not be entitled to receive Definitive Certificates (if issued) in respect of their individual holdings of the Bonds.

(C) Formalities Free of Charge

Transfers of the Bonds will be effected without charge by or on behalf of the Company or any Transfer Agent, but only upon payment (or the giving of such indemnity as such Transfer Agent may require in respect) of any tax or other governmental charges which may be imposed in relation thereto.

(D) Restricted Transfer Periods

No Bondholder may require the transfer of a Bond to be registered (i) during the period of 15 days ending on the due date for any payment of principal and premium (if any) on the Bond; (ii) after such Bond has been called for redemption pursuant to Condition 8(B) or 8(D); (iii) after the Conversion Notice (as defined in Condition 6(B)) and the individual Definitive Certificate in respect of such Bond (if issued) have been deposited for conversion pursuant to Condition 6; or (iv) following exercise of the Bondholder's put option pursuant to Condition 8(C).

(E) Regulations

All transfers of Bonds and entries on the register of Bondholders will be made subject to the detailed regulations concerning transfer of Bonds (the "**Regulations**") set forth in the Agency Agreement. The Regulations may be changed by the Company, with the prior written approval of the Trustee and the Registrar. A copy of the Regulations will be mailed (at the Company's expense) by the Registrar to any Bondholder who asks for one and will also be available at the office of the paying and conversion agent in Luxembourg and elsewhere.

6. Conversion

On exercise of the Conversion Right (as defined below), the converting Bondholders pursuant to the election made by such Bondholder may: (a) elect to receive Shares in Taiwan, or (b) in the event the Company establishes a depositary receipt facility following the closing and subject to compliance with the terms and conditions of the deposit agreement established with such depositary receipt facility, elect to receive depositary shares representing the interests in the Shares and the Bondholder may direct the Company to procure that Shares transferred and delivered upon conversion of the Bonds are deposited with the custodian for the DR depositary (as defined below) for the issuance and delivery of the DRs (as defined below) by the DR Depositary.

In the event that the Company establishes a depositary receipt facility, it will have to procure additional Shares for deposit with the custodian for the DR Depositary. Such Shares could be procured by open market purchases or by issuing new Shares, subject to compliance with applicable ROC law and the Company's articles of incorporation.

In the event the Company does establish a depositary receipt facility, the procedure for Bondholders to convert the Bonds into DRs will be substantially similar to the conversion procedure for Bondholders to convert the Bonds into Shares. In each case, the Bondholder will deposit the individual Definitive Certificate (if issued) in respect of a Bond and the Conversion Notice (as defined herein) with the Conversion Agent. However, in the case of conversion into DRs, the Bondholder will direct that all of the Shares issuable upon conversion be deposited with the relevant DR Depositary for issuance of DRs or Temporary DRs (as defined below).

The Company shall, within five Trading Days after the Conversion Date, issue and deliver the Shares converted from the Bonds to the converting Bondholder or its designee, subject to the requirements relating to the conversion in the Indenture being satisfied.

The Indenture provides, in summary, that the term "Shares" means, when used to refer to the class or classes of the Company's capital stock into which the Bonds are convertible and when used in certain other instances, only the Company's common shares, NT\$10 par value per share, but that when used elsewhere, including in Condition 6(C), such term also includes shares of any other class or classes of the share capital of the Company authorized after the date of the Indenture which have no preference in respect of dividends or of amounts payable in the event of any voluntary or involuntary liquidation or winding-up of the Company.

(A) Conversion Right

- (i) *Conversion Period:* Each Bondholder has the right during the Conversion Period (as defined below) to convert any Bond into Shares, credited as fully paid, and may, if a depositary receipt facility has been established and depositary receipts representing the Shares ("DRs") have been issued, and subject to compliance with the terms and conditions of the relevant deposit agreement, direct in the Conversion Notice that all or some only of the Shares issuable upon conversion be deposited with the relevant DR depository (the "DR Depositary") for issuance of DRs or Temporary DRs, on and subject to the terms set forth herein (the "**Conversion Right**"). Subject to and upon compliance with the provisions of this Condition, the Conversion Right attaching to any Bond may be exercised, at the option of the holder thereof and as and to the extent provided herein, at any time on or after 18th May, 2002 and prior to the close of business (at the place where the Conversion Notice (as defined in Condition 6(B)) and the individual Definitive Certificate (if issued) in respect of such Bond are deposited for conversion) on 18th March, 2005 (or if such date shall not be a business day, on the immediately preceding business day at such place) (but in no event thereafter), or, if such Bond shall have been called for redemption prior to that date, then up to the close of business (at the place aforesaid) on the date seven days prior to the date fixed for redemption thereof (or if such day shall not be a business day at such place on the immediately preceding business day at such place) (the "**Conversion Period**"); provided, however, that the Conversion Right during any Closed Period shall be suspended and the Conversion Period shall not include any such Closed Period. "**Closed Period**" shall mean any period during which under the laws of the ROC the Company shall close its shareholders register, which period includes 60 days prior to the date of the annual meeting of shareholders ("**AGM**"), 30 days prior to an extraordinary shareholders' meeting and the period from the date three (3) Taiwan business days prior to the Company's notification to the TSE in respect of a record date (and the relevant closure of the shareholders' register) for determining the identity of shareholders entitled to receive annual dividend distribution or other rights or benefits to such record date or such other periods determined by ROC law applicable from time to time. The Company shall procure that the Bondholders are given not less than 10 days' nor more than 60 days' prior notice of any Closed Period in accordance with the provisions of the Indenture.

A "**Taiwan business day**" means a day (other than a Saturday or Sunday) on which commercial banks in Taipei are open for business.

Under current ROC law, regulation and policy, PRC persons are not permitted to hold or convert the Bonds or to register as a shareholder of the Company. Under current ROC law, a PRC person means an individual holding a passport issued by the PRC, a resident of any area of China under the effective control or jurisdiction of the PRC (but not including a special administrative region of the PRC such as Hong Kong or Macau, if so excluded by applicable laws of the ROC), any agency or instrumentality of the PRC and any corporation, partnership and other entity organized under the laws of any such area or controlled or beneficially owned by any such person, resident, agency or instrumentality.

Under current ROC law, a non-ROC converting Bondholder when exercising his Conversion Right to convert the Bonds into Shares is required (unless the Bondholder has the option under these Conditions to elect, and elects to receive DRs with respect to the Bonds to be converted. In such case, the Shares will be delivered to and deposited with a custodian appointed by the relevant DR Depositary) to appoint a local agent in the ROC with such qualifications as are set by the ROC Securities and Futures Commission ("ROC SFC"), to open a securities trading account with a local brokerage firm and a New Taiwan Dollar bank account, pay ROC withholding taxes, remit funds, exercise shareholders' rights, handle conversion application and perform such other matters as may be designated by such converting Bondholder (or its designee), on behalf of and as agent for such converting Bondholder (or its designee). In addition, such non-ROC converting Bondholder must also appoint a custodian bank to hold the securities for safekeeping, make confirmation and settlement, and report all relevant information. Under existing ROC laws and regulations, without opening such accounts, an investor in the Bonds would not be able to receive, hold, sell or otherwise transfer the Shares into which the Bonds may have been converted on the TSE or otherwise. See "Foreign Investment and Exchange Controls in the ROC" and "Description of the Shares".

- (ii) *Number of Shares and/or DRs Issuable on Conversion:* The number of Shares to be issued upon conversion of any Bond will be determined by dividing the principal amount of the Bond (translated into NT Dollars at the fixed rate NT\$34.979 = U.S.\$1.00) by the Conversion Price (as defined below) in effect on the Conversion Date as defined in Condition 6(B)(ii). Fractional Shares will not be issued or paid in cash, or in any other means. The number of DRs to be issued upon conversion of any Bond (if applicable) will be determined by dividing the principal amount of the Bond by the Conversion Price (as defined below) in effect on the Conversion Date, and dividing such quotient by the number of Shares represented by each DR on the Conversion Date as defined in Condition 6(B)(ii).

If a Certificate or Certificates in respect of more than one Bond shall be deposited for conversion at any one time by the same Bondholder, the number of Shares (and/or DRs, if applicable) to be issued upon conversion thereof will be calculated on the basis of the aggregate principal amount of the Bonds in respect of which the Certificate(s) were so deposited. Fractions of Shares (and/or DRs, if applicable) will not be issued on conversion, and cash adjustments will not be made in respect thereof by the Company. Notwithstanding the foregoing, in the event of a consolidation or reclassification of Shares (and DRs, if applicable) by operation of law or otherwise occurring after 1st July, 2002, the Company will upon conversion of the Bonds pay in U.S. Dollars a sum equal to such portion of the principal amount of the Bond or Bonds converted as corresponds to any fraction of a Share (and/or DR, if applicable) not issued as aforesaid if such sum exceeds U.S.\$10. For the purpose of calculating the amount of such payment, the Company shall use the exchange rate referred to above in this Condition 6(A)(ii).

- (iii) *Initial Conversion Price:* The price at which Shares will be issued upon conversion (the "**Conversion Price**") will initially be NT\$24.50 per Share, which is equivalent to US\$0.700 per Share based on the fixed exchange rate of NT\$34.979 = US\$1.00 but will be subject to adjustment in the manner provided in Conditions 6(C) and 6(D). The price at which DRs will be issued upon conversion, in the event that the Company establishes a depositary receipt facility, will be determined by multiplying, or dividing, as the case may be, the Conversion Price by the number of Shares represented by each DR on the Conversion Date and will be subject to adjustment in the manner provided in Conditions 6(C) and 6(D).

- (iv) *Revival on Default:* Notwithstanding the provisions of Condition 6(A)(i), if there shall be default in making payment in full in respect of any Bond which shall have been called for redemption prior to 18th April, 2005 on the date fixed for redemption thereof, the Conversion Right attaching to such Bond will continue to be exercisable up to and including the close of business (at the place where the relevant individual definitive Certificate (if issued) in respect of such Bond and the Conversion Notice (as defined in Condition 6(B) are deposited for conversion) on the date upon which the full amount of the monies payable in respect of such Bond has been duly received by the Trustee or the Principal Agent and notice of such receipt has been duly given to the Bondholders.

(B) *Conversion Procedure*

- (i) *Exercise Procedure:* To exercise the Conversion Right attaching to any Bond, the holder thereof must complete, execute and deposit at its own expense between 9:00 a.m. and 3:00 p.m. (local time at the specified office referred to below) on any business day (as defined below) during the Conversion Period at the specified office of a Conversion Agent outside of the ROC, a notice of conversion (a “**Conversion Notice**”) in duplicate, duly completed and signed, in the then current form obtainable from the specified office of any Conversion Agent, together with the relevant individual Definitive Certificate (if issued) and any certificates and other documents as may be required under the law of the ROC or the jurisdiction in which such Conversion Agent is located.

Bondholders who deposit a Conversion Notice during a Closed Period will not be permitted to convert their Bonds until the Trading Day following the last day of the Closed Period which (if all other conditions to convert have been fulfilled) will be the Conversion Date for such Bonds. Such Bondholders or the relevant DR Depository, as applicable, will not be registered as holders of Shares until the Conversion Date.

If a DR facility has been established and DRs have been issued, the Conversion Notice shall contain an option for the Bondholder to elect to receive Shares and/or DRs upon such conversion. The Conversion Notice shall contain, inter alia, an appointment of a local agent by such converting Bondholder and an irrevocable instruction to exchange for Shares issued pursuant to Condition 6(B)(iii), as soon as Shares are available. A Conversion Notice once deposited may not be withdrawn without the consent in writing of the Company and the Conversion Agents, Principal Agent and Trustee be immediately notified in writing by such written consent of the Company accompanied by the relevant Conversion Notice. The price at which such Bonds will be converted will be the Conversion Price in effect on the Conversion Date.

In this Condition, “**business day**” means a day on which commercial banks are open for business in London, United Kingdom, and in the place where the Conversion Agent with whom the individual Definitive Certificate (if issued) and the Conversion Notice are deposited is open for business.

- (ii) *Taxes and Expenses; Deposit Date and Conversion Date:* As conditions precedent to conversion, together with the Conversion Notice, the Bondholder must pay to the relevant Conversion Agent all stamp, issue, registration, excise and similar taxes or duties or transfer costs (if any) arising on conversion in the country in which the Bond is deposited for conversion, or payable in any jurisdiction consequent upon the issue or delivery of Shares (and/or DRs, if applicable) or any other property or cash upon conversion to or to the order of a person other than the converting Bondholder. Except as aforesaid, the Company will pay the expenses arising in the ROC on the issue of Shares (and/or DRs, if applicable) on conversion of Bonds and all charges of the Conversion Agents (and the relevant DR Depository, if applicable) in connection therewith as provided in the Indenture and Agency Agreement. The date on which any Certificate and the Conversion Notice (in duplicate) relating thereto, together with any certificates and other documents as may be required under applicable law or a relevant deposit agreement (if applicable), are deposited with a Conversion Agent and the payments, if any, required to be paid by the Bondholder are made is hereinafter referred to as the “**Deposit Date**”. The “**Conversion Date**” applicable to a Bond shall mean the next day following the Deposit Date, which day both is

a Trading Day as defined in Condition 8(B) and occurs during the Conversion Period. Bondholders who deposit a Conversion Notice during a Closed Period will not be permitted to convert their Bonds until the Trading Day following the last day of that Closed Period.

- (iii) *Holder of Record*: With effect from the opening of business in the ROC on the Conversion Date, the Company will deem the converting Bondholder (or its designee) as indicated in the Conversion Notice to have become the holder of record of the number of Shares to be issued upon such conversion to such holder (disregarding any retroactive adjustment of the Conversion Price referred to below prior to the time such retroactive adjustment shall have become effective) and at such time, subject to Condition 6(B)(v), the rights of such converting Bondholder as a Bondholder with respect to such Bonds converted shall cease (except rights arising under Condition 6(B)(iv), 6(B)(vi) and 6(G)(ii)).

In the event that a converting Bondholder has the option under these Conditions to elect, and elects, to receive DRs, with effect from the opening of business in the ROC on the Conversion Date, the Company will deem the relevant DR Depositary to have become the holder of record of the number of Shares represented by such DRs to be issued upon such conversion (disregarding any retroactive adjustment of the Conversion Price referred to below prior to the time such retroactive adjustment shall have become effective) and upon delivery by the relevant DR Depositary to the Bondholder of the number of DRs or Temporary DRs into which the Bonds are convertible, subject to Condition 6(B)(v), the rights of such converting Bondholder as a Bondholder with respect to such Bonds converted shall cease (except rights arising under Condition 6(B)(iv), 6(B)(vi) and 6(G)(ii)).

- (iv) *Availability of Shares*: The Company shall, for the benefit of Bondholders, ensure that sufficient Shares are available as soon as possible (but no later than five Trading Days after the Conversion Dates).
- (v) *Delivery of Shares and/or DRs*: On the Conversion Date, the Company will register the converting Bondholder (or its designee) or the relevant DR Depositary (or its designee), as applicable, in the Company's register of shareholders as the owner of the number of Shares to be issued pursuant to Condition 6(B)(iii) upon conversion of such Bonds and, subject to any applicable limitations then imposed by ROC laws and regulations, according to the request made in the relevant Conversion Notice, procure that, as soon as practicable, and in any event within five Trading Days after the Conversion Date, there be delivered to the local agent appointed by the converting Bondholder, and/or to the relevant custodian, as agent for the relevant DR Depositary (if the converting Bondholder has the option under these Conditions to elect, and elects, to receive DRs), a certificate or certificates for the relevant Shares, registered in the name specified for that purpose in the relevant Conversion Notice, together with any other property or cash (including, without limitation, cash payable pursuant to Condition 6(A)(ii)) required to be delivered upon conversion and such assignments and other documents (if any) as may be required by law to effect the delivery thereof.

In the event a converting Bondholder has the option under these Conditions to elect, and elects, to receive DRs on exercise of its Conversion Right, the Company agrees to deliver to and deposit with the relevant custodian, as agent for the relevant DR Depositary, a sufficient number of Shares to represent the DRs such Bondholder is entitled to receive upon conversion. Such Shares will be registered in the name of the relevant DR Depositary or its nominee and deposited in accordance with the terms of the relevant deposit agreement.

- (vi) *Retroactive Adjustment of Conversion Price*: If the Conversion Date in relation to any Bond shall be on or after a date with effect from which an adjustment to the Conversion Price takes retroactive effect pursuant to any of the provisions referred to in Condition 6(C) and the Indenture and the relevant Conversion Date falls on a date when the relevant adjustment has not been reflected in the Conversion Price, the Company will, within 20 days after the effective date of such adjustment of the Conversion Price, issue and deliver

(to the local agent appointed by the converting Bondholder and/or, if applicable, to the relevant custodian, as agent for the relevant DR Depositary) such number of Shares as is equal to the excess of the number of Shares that would have been required to be issued on conversion of such Bond if the relevant retroactive adjustment had been made as at the said Conversion Date over the number of Shares previously issued pursuant to such conversion, and in such event and in respect of such number of Shares, references in Condition 6(B)(v) to the Conversion Date shall be deemed to refer to the date upon which such retroactive adjustment becomes effective (disregarding the fact that it becomes effective retroactively). Fractions of Shares will not be issued and no cash adjustment will be made in respect thereof.

- (vii) *Dividends and Other entitlements:* To the extent permitted under the laws of the ROC, the converting Bondholders will be entitled to the annual dividend distributions or other benefits if the conversion of the Bonds takes place prior to 3 Taiwan business days before the Company's notification to the TSE in respect of a record date (and the relevant closure of the shareholders' register) for determining the identity of shareholders who are entitled to such distributions in each relevant year. In the event a converting Bondholder has the option under these Conditions to elect, and elects, to receive DRs on exercise of its Conversion Right, and the Shares to be delivered to and deposited with the relevant custodian as agent for the relevant DR Depositary do not, by reason of the date of issue or otherwise, rank *pari passu* in all respects with the other deposited Shares under the relevant deposit agreement, the Company will procure that the relevant DR Depositary will arrange for the issue of temporary DRs (such temporary DRs being referred to herein as "**Temporary DRs**") in respect of such Shares which will form a different class of DRs from the other DRs until such time as the Shares which they represent become fully fungible with the other deposited Shares under the relevant deposit agreement. At such time, the Company will procure that the relevant DR Depositary will, without further action by the holder of the Temporary DRs, make DRs available for exchange; provided, however, to obtain such DRs, the related Temporary DRs must be surrendered to the relevant DR Depositary.
- (viii) *Conversion Agents:* The Company reserves the right, subject to the provisions of the Agency Agreement, at any time to vary or terminate the appointment of any Conversion Agent and to appoint further or other Conversion Agents; provided that the Company will at all times maintain a Conversion Agent having specified offices in London, the United Kingdom and, so long as the Bonds are listed on the Luxembourg Stock Exchange and the rules of the Luxembourg Stock Exchange so require, in Luxembourg. Notice of any such termination or appointment and of any changes in the specified offices of the Conversion Agents will be given promptly by the Company to the Bondholders in accordance with Condition 15 and to the Luxembourg Stock Exchange.

(C) *Adjustments to Conversion Price*

The Conversion Price will be subject to adjustment in the manner set forth in the Indenture upon the occurrence of certain events set out in the Indenture, including:

- (i) the making of a free distribution or bonus issue of Shares;
- (ii) subdivisions, consolidations or reclassifications of Shares;
- (iii) the declaration of a dividend in Shares (under the terms of the Indenture, no account is to be taken of, or credit given for, the par value of Shares issued in any stock dividend in calculating an appropriate conversion price adjustment, so that the full dilutive effect of stock dividends is provided for);
- (iv) the grant, issue or offer to the holders of Shares of rights or warrants to subscribe for or purchase Shares at less than the then Current Market Price (as defined in the Indenture) or to subscribe for or purchase any securities convertible into or exchangeable for Shares at less than the then Current Market Price;

- (v) the distribution to the holders of Shares of evidences of indebtedness of the Company or of shares of capital stock of the Company (other than Shares) or of assets (other than regular periodic dividends in cash) or of rights or warrants to subscribe for or purchase shares or securities (other than those mentioned in (iv) above);
- (vi) the issue of securities (other than the Bonds and those mentioned in (iv) above) convertible into or exchangeable for Shares at less than the then Current Market Price or of rights or warrants (other than those mentioned in (iv) above) to subscribe for or purchase Shares at less than the then Current Market Price or to subscribe for or purchase securities convertible into or exchangeable for Shares at less than the then Current Market Price;
- (vii) the issue of Shares (other than (a) Shares issued on conversion of convertible bonds, including the Bonds, or (b) Shares to shareholders of any company which merges with the Company upon such merger and in proportion to their shareholdings in such company immediately prior to such merger, or (c) in any of the circumstances described above but including Shares issued under any employee bonus or profit-sharing arrangements) at less than the then Current Market Price; and
- (viii) any other event or circumstance which would have in the determination of the Company or the Trustee an analogous effect to any of the events in (i) to (vii) above including, but not limited to, issues of receipts or certificates entitling holders to receive securities,

in accordance with the formulas stipulated in the Indenture. No adjustment will be made where such adjustment would be less than one per cent. of the Conversion Price then in effect; provided, however, that any adjustment that otherwise would be required to be made will be carried forward and taken into account in determining any subsequent adjustment. Any adjustment will be notified promptly by the Company to the Bondholders in accordance with Condition 15.

The Indenture provides that the Conversion Price may be reduced, as a result of any adjustment required by this Condition 6(C), below the par value of the Shares for the time being to the extent permitted by ROC law, provided that any Shares issued on conversion of Bonds at such reduced Conversion Price would be legally issued and non-assessable Shares.

The Trustee will not be obliged to monitor whether any event has occurred which might fall within (i) to (viii) above and until it has actual knowledge by way of express notice in writing from the Company to the contrary, shall assume that none has.

(D) Conversion Price Reset

The Conversion Price shall be adjusted on 18th April, 2003 (the “**First Reset Date**”) and 18th April, 2004 (the “**Second Reset Date**”) (each a “**Reset Date**”), in the event that the average closing price of the Share on the TSE translated into U.S. Dollars at the then Prevailing Rate (defined below) for 30 consecutive Trading Days immediately prior to a Reset Date (the “**Average Closing Price**”) is less than the Conversion Prices then in effect on the relevant Reset Date, in accordance with the following formula:

$$\text{Adjusted Conversion Price} = \frac{\text{Fixed Exchange Rate}}{\text{Prevailing Rate}} \times \text{Average Closing Price}$$

Such Adjusted Conversion Price shall be rounded upwards, if necessary, to the nearest NT\$0.01, provided that:

- (i) any adjustment to the Conversion Price pursuant to this Condition 6(D) shall be limited so that the Conversion Price adjusted in accordance with this Condition 6(D) shall not be less than 80 per cent. of the initial Conversion Price prevailing on 10th April, 2002 (as adjusted to reflect any adjustments required under Condition 6(C) above, which may have occurred prior to the Reset Date);

- (ii) the provisions of Condition 6(C) shall apply *mutatis mutandis* to this Condition 6(D) to ensure that appropriate adjustments shall be made to any Closing Price to reflect any adjustments made to the Conversion Price in accordance with Condition 6(C) during the period of calculation of the Average Closing Price;
- (iii) the Conversion Price shall not be reduced below the par value of the Shares (currently NT\$10 per share) unless, under applicable law then in effect, the Bonds could be converted at such reduced Conversion Price into legally issued, fully-paid and non-assessable Shares; and
- (iv) for the avoidance of doubt (x) any adjustments to the Conversion Price made pursuant to this Condition 6(D) shall only be downward adjustments and (y) an adjustment may be made in respect of the Second Reset Date notwithstanding that an adjustment may have been made in respect of a preceding Reset Date.

The “**Prevailing Rate**” for the translation of the Closing Prices shall be the arithmetic average of the closing rate for the purchase of U.S. Dollars with NT Dollars quoted by Taipei Forex Inc. at the close of business on each day of the 30 consecutive Trading Days preceding the relevant Reset Date. For the purpose of the formula in this Condition, the Prevailing Rate shall be expressed as the number of NT Dollars per U.S.\$1.00.

Any such adjustment shall become effective as of the relevant Reset Date and the Bondholders shall be notified of any adjustment to the Conversion Price within five days of the relevant Reset Date in accordance with Condition 15.

(E) *Alternative Conversion Price Reset*

To stimulate Bondholder’s interest to exercise their conversion right, Condition 6(E) provides an alternative. This is set in accordance with the regulations for underwriters’ assistance for public companies in the issuance of securities, which was amended by the Chinese Securities Association and was then filed for recordation with the ROC SFC. The Alternative Reset Date, the Alternative Conversion Price and the period of exercise (i.e. seven Trading Days) are set based on that regulations.

The Bondholders are entitled, within seven Trading Days after 18th March, 2004 and 18th March, 2005 (each an “**Alternative Reset Date**”), to convert the Bond at an Alternative Conversion Price equal to 88.0 per cent. and 85.0 per cent., respectively of the then market price.

The “**market price**” refers to the lowest among the average closing prices of the Shares on the TSE translated into U.S. Dollars at the then prevailing exchange rate for 10, 15 and 20 Trading Days immediately preceding the applicable Alternative Reset Date.

(F) *Mergers; Disposals*

The Company will not merge, amalgamate or consolidate with or into any other corporation or entity where the Company is not being the continuing entity or sell or transfer all, or substantially all, of the assets of the Company, whether as a single transaction or a number of transactions, related or not, to any corporation, entity or person or to one or more members of any group under the common control of any corporation, entity or person unless the Company shall have notified the Bondholders of such event in accordance with Condition 15 and the Company and such corporation, entity or person shall have executed an indenture supplemental to the Indenture in form and substance satisfactory to the Trustee providing that such corporation, entity or person shall assume the obligations of the Company under the Bonds, the Indenture and the Agency Agreement and providing that each Bond then outstanding shall be convertible into the class and amount of shares and other securities, cash and other property receivable upon such consolidation, amalgamation, merger, sale or transfer by a holder of the number of Shares (and/or DRs, if applicable) into which such Bond would have been convertible immediately prior to such consolidation, amalgamation, merger, sale or transfer (assuming for such purpose that the Bonds were convertible at the time of such consolidation, amalgamation, merger, sale or transfer) at the Conversion Price as adjusted from time to time pursuant to the Indenture. Such supplemental indenture will provide for adjustments which will be as nearly

equivalent as may be practicable to the adjustments provided for in the foregoing provisions to this Condition. The above provisions of this Condition 6(E) will apply in the same way to any subsequent or further consolidations, amalgamations, mergers, sales or transfers.

(G) *Conversion Undertakings*

- (i) *Depository receipts*: Subject to the ROC SFC'S separate approval, if required, the Company may, at its option, but is not required to, make arrangements satisfactory to the Trustee for the Bonds to be converted into depository receipts or other scrip evidencing Shares. Any such arrangements shall be in addition to the provisions of these Conditions relating to conversion into Shares.

The Company has not at the date of this Offering Circular established or authorized the establishment of any depository receipt facility. Accordingly, conversion into DRs is not currently available. If in the future a depository receipt facility is established or authorized by the Company, the Company will, to the extent permitted by applicable laws and regulations, make arrangements satisfactory to the Trustee for Shares issued on conversion of Bonds to be accepted for deposit (at the option of the converting Bondholder) into such depository receipt facility, subject always to the terms of such depository facility, which terms may include certification or other requirements as conditions to the acceptance for deposit of Shares issued on conversion of Bonds. There can be no assurance that the Company will in future establish or authorize any depository facility or that any arrangements for the deposit of Shares into such depository facility would be available to all Bondholders.

The Company shall give notice to the Conversion Agents, the Principal Agent and the Bondholders in accordance with Condition 15 and to the Luxembourg Stock Exchange within 14 days of the establishment of the depository receipt facility.

- (ii) *Closed Periods*: The Company undertakes to ensure that any Closed Period is as short a period as is reasonably practicable having regard to applicable ROC laws and regulation and practices.

7. **Payments**

(A) *Principal, Premium (if any) and Interest (if any)*

Payment of principal, premium (if any) and interest (if any) will be made against surrender of the relevant certificate at the specified office of any Agent by transfer to the registered account of the Bondholder or by U.S. Dollar check drawn on a bank in The City of New York, USA, mailed (provided that the Principal Agent shall have received the relevant funds in full from the Company in accordance with the Agency Agreement) to the registered address of the Bondholder if it does not have a registered account. Payments of principal and premium (if any) will only be made after surrender of the relevant individual Definitive Certificate (if issued) at the specified office of any Agent.

(B) *Registered Accounts*

A Bondholder's registered account means the U.S. Dollar account maintained by or on behalf of it with a bank in The City of New York, USA, details of which appear on the register of Bondholders at the close of business on the second business day (as defined below) before the due date for payment and a Bondholder's registered address means its address appearing on the register of Bondholders at that time.

(C) *Fiscal Laws*

All payments are subject in all cases to any applicable fiscal or other laws and regulations in the place of payment, but without prejudice to the provisions of Condition 9. No commissions or expenses shall be charged to the Bondholders in respect of such payments.

(D) *Payment Initiation*

Where payment is to be made by transfer to a registered account, payment instructions (for value the due date or, if that date is not a business day, for value the next following business day) will be initiated and, where payment is to be made by check, the check will be mailed (provided that the Principal Agent shall have received the relevant funds in full from the Company in accordance with the Agency Agreement), on the later of the due date for payment and the business day on which the relevant Certificate is surrendered (if applicable) at the specified office of an Agent.

(E) *Payment Delay*

Bondholders will not be entitled to any interest or other payment for any delay after the due date in receiving the amount due if the due date is not a business day, if the Bondholder is late in surrendering its Certificate (if applicable) or if a check mailed in accordance with this Condition arrives after the due date for payment.

(F) *Business Days*

In this Condition, “**business day**” means a day on which commercial banks are open for business in The City of New York, USA. and London, United Kingdom and, in the case of the surrender of a Certificate, in London, United Kingdom, and in the place where the Certificate is surrendered.

(G) *Partial Payments*

If the amount of principal and premium which is due on the Bonds is not paid in full, the Registrar will annotate the register of Bondholders with a record of the amount of principal and/or premium, in fact paid.

Distribution of payments with respect to the Global Certificates held through Euroclear or Clearstream, Luxembourg will be made to the holders holding through participants of Euroclear or Clearstream, Luxembourg, as the case may be, to the account of The Bank of New York, as common depositary for Euroclear and Clearstream, Luxembourg and will be credited by Euroclear or Clearstream, Luxembourg, as the case may be, to the cash accounts of the participants of Euroclear or Clearstream, Luxembourg, in accordance with the relevant system’s rules and procedures, to the extent received by the common depositary.

8. Redemption, Purchase and Cancellation

(A) *Redemption at Maturity*

Unless previously redeemed, converted or purchased and cancelled as herein provided, the Company will redeem the Bonds at 110.87 per cent. of their principal amount in U.S. Dollars on 18th April, 2005. The Bonds may be redeemed in whole or in part prior to that date only as provided in paragraphs (B), (C) and (D) below (but without prejudice to Condition 10).

(B) *Redemption at the Option of the Company*

- (i) On or at any time after 18th April, 2003, the Company may, having given not less than 40 nor more than 60 days’ notice to the Bondholders in accordance with Conditions 8(H) and 15 (which notice will be irrevocable), redeem all or part of the Bonds at their principal amount if the Closing Price of the Shares translated into U.S. Dollars at the prevailing exchange rate for each of the 30 consecutive Trading Days, the last of which occurs not more than 10 days prior to the date upon which notice of such redemption is published, is at least 150 per cent. of the Conversion Price then in effect, translated into U.S. Dollars at the fixed exchange rate of NT\$34.979 = US\$1.00, on each such Trading Day. If there shall occur an event giving rise to a change in the Conversion Price during any such 30 Trading Day period, appropriate adjustments for the relevant days shall be made for the purpose of calculating the Closing Price for such days. If the Closing Price cannot be determined for

one or more consecutive Trading Days, such day or days will be disregarded in the relevant calculation and will be deemed not to have existed when ascertaining such 30 Trading Day period.

- (ii) On or at any time after 18th April, 2003, the Company may, having given not less than 40 nor more than 60 days' notice to the Bondholders in accordance with Conditions 8(H) and 15 (which notice will be irrevocable), redeem all but not some only of the Bonds at their principal amount if 90 per cent. of the Bonds have been previously redeemed, repurchased, or converted and cancelled.

Upon the expiry of any such notice, the Company will be bound to redeem the Bonds to which such notice relates at the price aforesaid applicable at the date fixed for redemption.

The term "**Trading Day**" means a day on which the TSE is open for business but does not include a day when (a) no such last transaction price or closing bid and offered prices are reported and (b) (if the Shares are not listed or admitted to trading on such exchange) no such closing bid and offered prices are furnished as aforesaid. The "**Closing Price**" of the Shares for each Trading Day shall be the last reported transaction price of the Shares on the TSE for such day or, if no transaction takes place on such day, the last available reported transaction price of the Shares on the TSE in effect on the Trading Day immediately preceding such day or, if the Shares are not listed or admitted to trading on such exchange, the average of the closing bid and offered prices of Shares for such day as furnished by a leading independent securities firm licensed to trade on the TSE selected by the Company for the purpose.

(C) Redemption at the Option of Bondholders

The Company will, at the option of the holder of any Bond, redeem the Bonds held by that Bondholder on 18th April, 2004 (the "**Put Date**") at 107.12 per cent. of their principal amount.

To exercise such option the holder must deposit the individual Definitive Certificate in respect of such Bond (if issued) with any Agent and a duly completed redemption notice in the form obtainable from any of the Agents, not more than 60 nor less than 30 days prior to the Put Date. No Bond so deposited may be withdrawn (except as provided in the Agency Agreement) without the prior written consent of the Company and such written consent must be notified by the Company to the Principal Agent no later than seven days prior to the Put Date. The Company shall give the Bondholders not less than 30 nor more than 45 days' notice of the commencement of the period for the deposit of individual definitive Certificates for redemption (if issued) and the redemption notice pursuant to this paragraph (C) shall be given to the Bondholders by the Company in accordance with Condition 15. The exercise of the Bondholders' option under this Condition 8(C) shall override any exercise of the Company's right under Condition 8(B).

(D) Redemption for Taxation Reasons

At any time, the Company may, having given not less than 40 nor more than 60 days' notice to the Bondholders in accordance with Conditions 8(H) and 15 (which notice shall be irrevocable) redeem all but not some only of the Bonds at their principal amount, if (i) the Company determines immediately prior to the giving of such notice that it has or will become obliged to pay additional amounts as provided or referred to in Condition 9 as a result of any change in, or amendment to, the laws or regulations of the ROC or any political subdivision or any authority thereof or therein having power to tax, or any change in the general application or official interpretation of such laws or regulations, which change or amendment becomes effective on or after 1st July, 2002 and (ii) such obligation cannot be avoided by the Company taking reasonable measures available to it, provided that no such notice of redemption shall be given earlier than 90 days prior to the earliest date on which the Company would be obliged to pay such additional amounts were a payment in respect of the Bonds then due. Prior to the giving of any notice of redemption pursuant to this paragraph, the Company shall deliver to the Trustee a certificate signed by two directors of the Company stating that the obligation referred to in (i) above cannot be avoided by the Company taking reasonable measures available to it and the Trustee shall be entitled to accept such certificate as sufficient evidence of the satisfaction of

the condition precedents set out in (ii) above, in which event it shall be conclusive and binding on the Bondholders. Bonds in respect of which a notice of redemption has been given under Condition 8(B) and Condition 8(C) shall not be affected by any notice given subsequently under this Condition 8(D).

(E) *Purchase*

The Company may at any time and from time to time purchase Bonds in the open market or otherwise. Bonds so purchased will be surrendered and deemed cancelled and may not be reissued or resold.

(F) *Selection of Bonds*

In the case of redemption of some only of the Bonds pursuant to Condition 8(B)(i), where individual Definitive Certificates have been issued, the Bonds to be redeemed will be selected individually by lot by the Principal Agent, in such place as the Trustee shall approve and in such manner as the Trustee shall deem to be appropriate and fair not more than 60 days and not less than 30 days prior to the date fixed for redemption.

(G) *Cancellation*

All Bonds which are redeemed or converted or purchased and surrendered to any Agent will forthwith be cancelled in accordance with the provisions of the Agency Agreement. Certificates in respect of all Bonds cancelled will be forwarded to or to the order of the Principal Agent and such Bonds may not be reissued or resold.

(H) *Redemption Notices*

All notices to Bondholders given by or on behalf of the Company pursuant to this Condition will specify the date fixed for redemption, the redemption price, the Conversion Price as at the date of the relevant notice, the Closing Price of the Shares and the aggregate principal amount of the Bonds outstanding as at the latest practicable date prior to the publication of the notice and, in the case of a partial redemption, a list of the Bonds called for redemption.

9. **Taxation**

- (A) All payments of principal, premium (if any) and interest (if any) by the Company will be made free and clear of and without any deduction or withholding for or on account of any present or future taxes, duties, assessments or governmental charges of whatever nature imposed, levied, collected, withheld or assessed by or on behalf of the government of the ROC or any authority thereof or therein having power to tax, unless deduction or withholding of such taxes, duties, assessments or governmental charges is compelled by law.
- (B) Where such withholding or deduction is in respect of ROC withholding tax on premium or interest payments at the rate of up to and including 20 per cent., the Company will increase the amount of premium (if any) or interest (if any) paid by it to the extent required so that the net amount of premium (if any) or interest (if any) received by Bondholders (without prejudice to Condition 7) would be equal to the amounts which would have been receivable in the absence of any such withholding or deduction.
- (C) In the event that any such withholding or deduction in respect of principal or any additional withholding or deduction in excess of 20 per cent. in respect of interest (if any) or premium (if any) is required, the Company will pay such additional amounts by way of principal, premium (if any) and interest (if any), as will result in the receipt by the Bondholders of the amounts which would have been receivable in the absence of any such withholding or deduction, except that no such additional amounts shall be payable in respect of any Bond:
 - (i) to, or on behalf of, a holder who is subject to such taxes, duties, assessments or governmental charges in respect of such Bond by reason of his being connected with the ROC otherwise than merely by holding such Bond or by the receipt of principal in respect of the Bond; or

- (ii) if the individual Definitive Certificate in respect of such Bond (if issued) is surrendered more than 30 days after the relevant date except to the extent that the holder would have been entitled to such additional amount on surrendering the relevant Certificate for payment on the last day of such 30 day period. For this purpose, the “**relevant date**” in relation to any Bond means (a) the due date for payment in respect thereof or (b) (if the full amount of the monies payable on such due date has not been received by the Trustee or the Principal Agent on or prior to such due date) the date on which notice is duly given to the Bondholders that such monies have been so received.
- (D) References in these Conditions to principal, premium or interest shall be deemed also to refer to any increased or additional amounts which may be payable in respect thereof under this Condition or any undertaking given in addition to or substitution for it under the Indenture.

10. Events of Default

The Trustee at its discretion may, and if so requested in writing by the holders of not less than 25 per cent. in principal amount of the Bonds then outstanding or if so directed by an Extraordinary Resolution shall (but subject to being indemnified or secured by the holders to its satisfaction), give notice in writing to the Company that the Bonds are immediately due and payable, if any of the following events (an “**Event of Default**”) shall have occurred and be continuing:

- (i) there is failure to pay the principal of or any premium (if any) on any of the Bonds within 15 business days after the same shall become due and payable in accordance with these Conditions; or
- (ii) the Company defaults in performance or observance of or compliance with any of its other obligations (other than the covenant to pay the principal, premium (if any) or interest (if any) in respect of the Bonds) set out in the Bonds or the Indenture which default is incapable of remedy or, if in the opinion of the Trustee such default is capable of remedy, such default is not in the opinion of the Trustee remedied within 30 days (or such longer time as the Trustee may consider appropriate in relation to the jurisdiction concerned) after written notice of such default shall have been given to the Company by the Trustee; or
- (iii) any other present or future indebtedness of the Company, or any of its Principal Subsidiaries, for or in respect of monies borrowed or raised becomes (or becomes capable of being declared) due and payable prior to its stated maturity by reason of an event of default (howsoever described), or any such indebtedness is not paid when due or, as the case may be, within any applicable grace period originally provided for, or the Company or any of its Principal Subsidiaries fails to pay when due any amount payable by it under any present or future guarantee or indemnity or arrangement or obligation having a like or similar effect (howsoever described) for any monies borrowed or raised by any person, provided that the aggregate amount of the relevant indebtedness and guarantees in respect of which one or more events mentioned above in this paragraph (iii) have occurred and is continuing equals or exceeds U.S.\$5,000,000 or its equivalent in any other currency (determined as provided below), and provided further that where two or more of the Company and/or its Principal Subsidiaries are liable for the payment of the same relevant indebtedness or guarantee (whether liable jointly and severally, by way of guarantee, surety or otherwise), any such amount shall be counted once only; or
- (iv) an execution by a court having jurisdiction is levied or enforced or sued out, or other legal enforcement process is levied or sued out upon, commenced or issued upon, against or in respect of the whole or any substantial part of the undertaking, property, assets or revenues of the Company or any of its Principal Subsidiaries and in any such case is not discharged or stayed within 60 days (or such longer period as the Trustee may consider appropriate in relation to the jurisdiction concerned) of having been so levied, sued out, commenced or issued, unless the Company or such Principal Subsidiary is contesting such proceedings in good faith by appropriate proceedings; or

- (v) any person entitled to the benefit thereof shall institute appropriate legal proceedings to enforce any Encumbrance upon the whole or any substantial part of the assets or revenues of the Company or any Principal Subsidiary and the same is not stayed, discharged, released or satisfied (as the case may be) within 60 days of such proceedings; or
- (vi) the Company or any of its Principal Subsidiaries becomes bankrupt or insolvent, or consents to or suffers the appointment of an administrator, liquidator (except for the purpose of and followed by a voluntary solvent reorganization, merger, consolidation, amalgamation or other similar arrangement the terms of which have previously been approved by the Trustee or an Extraordinary Resolution of the Bondholders) or receiver (or other similar official) in bankruptcy or insolvency of the Company or any of its Principal Subsidiaries or in respect of the whole or any substantial part of the undertakings, property, assets or revenues of the Company or any of its Principal Subsidiaries or the Company or any of its Principal Subsidiaries stops, suspends or threatens to stop or suspend payment of all or a material part of (or of a particular type of) its debts; or
- (vii) an order issued by a court with competent jurisdiction is made or an effective resolution passed by the Company or any of its Principal Subsidiaries for the winding-up or dissolution of the Company or any of its Principal Subsidiaries (except for the purpose of and followed by a solvent reconstruction, merger, consolidation, amalgamation or other similar arrangement the terms of which are approved by the Trustee or an Extraordinary Resolution of the Bondholders); or
- (viii) the Company shall merge, amalgamate or consolidate with any other corporation or entity (with the Company not being the continuing entity) or shall sell or dispose of substantially all its business or assets whether as a single transaction or a number of transactions, related or not, to any person, unless the Company shall have notified the Bondholders of such event in accordance with Condition 15 (with a copy of such notice sent to the Luxembourg Stock Exchange) and the Company and such corporation, entity or person shall have executed an indenture supplemental to the Indenture in form and substance satisfactory to the Trustee providing that such corporation, entity or person shall assume the obligations of the Company under the Bonds, the Indenture and the Agency Agreement and providing that each Bond then outstanding shall be convertible into the class and amount of Shares and other securities, cash and other property receivable upon such consolidation, amalgamation, merger, sale or transfer by a holder of the number of Shares into which such Bond would have been convertible immediately prior to such consolidation, amalgamation, merger, sale or transfer (assuming for such purpose that the Bonds were convertible at the time of such consolidation, amalgamation, merger, sale or transfer) at the Conversion Price as adjusted from time to time pursuant to the Indenture; provided that such agreement by such other person shall not be required if such assumption shall be effective by operation of law; or
- (ix) any governmental authority or agency condemns, seizes, compulsorily purchases or expropriates all or a substantial part of the assets or shares of the Company or any of its Principal Subsidiaries; or
- (x) proceedings shall have been initiated against the Company or any of its Principal Subsidiaries under any applicable bankruptcy, insolvency or reorganization law and such proceedings shall not have been discharged or stayed within a period of 60 days (or such longer period as the Trustee may consider appropriate in relation to the jurisdiction concerned); or
- (xi) any action, condition or thing (including the obtaining or effecting of any necessary consent, approval, authorization, exemption, filing, license, order, recording or registration) at any time required to be taken, fulfilled or done in order to (i) enable the Company lawfully to enter into, exercise its rights and perform and comply with its obligations under the Bonds and the Indenture, (ii) ensure that those obligations are legally binding and enforceable (subject to the qualifications set out in the legal opinion issued in connection therewith) and (iii) make the Bonds and the Indenture admissible in evidence in the courts of the ROC is not taken, fulfilled or done, and such case is incapable of remedy or, if in the opinion of the Trustee is capable of remedy, is not in the opinion of the Trustee remedied within such period (being not less than 30 days) as the Trustee may consider reasonable; or

- (xii) any event occurs which under the laws of the ROC has an analogous effect to any of the events referred to in the foregoing paragraphs.

For the purposes of Condition 10 (iii) above, any indebtedness which is in a currency other than U.S. Dollars shall be translated into NT Dollars at the spot rate for the sale of U.S. Dollars against the purchase of the relevant currency quoted by any leading bank in the relevant market selected by the Trustee on any day when the Trustee requests such a quotation for such purposes. If no direct spot rate is available, a rate shall be calculated by reference to the cross-rates through U.S. Dollars and relevant currencies.

Upon any such notice being given to the Company, the Bonds will immediately become due and payable at 100 per cent. of their principal amount, and overdue interest on the amounts due, from the date on which such amounts first become due, shall be payable, to the extent permitted by law, at the rate of six (6) per cent. per annum.

For the purpose of this Condition, “**Subsidiary**” means any corporation or other business entity more than 50 per cent. of the outstanding voting stock of which is for the time being owned directly or indirectly by the Company, and “**Principal Subsidiary**” means any subsidiary (i) whose total revenues, as shown by the latest audited accounts (consolidated in the case of a company which itself has subsidiaries) of such Subsidiary at the time that event of defaults occurs, are at least 10 per cent. of the total revenues of the Company and its consolidated Subsidiaries as shown by the latest audited consolidated accounts of the Company or (ii) whose gross assets, as shown by the latest audited accounts (consolidated in the case of a company which itself has subsidiaries) of such Subsidiary at the time that event of defaults occurs are at least 10 per cent. of the gross assets of the Company and its consolidated Subsidiaries as shown by the latest audited consolidated accounts of the Company.

The term “**business day**” for the purpose of this Condition 10 means a day (other than a Saturday or Sunday) on which commercial banks and foreign exchange markets are open for business in Taipei, Taiwan, ROC.

11. Prescription

Claims in respect of (a) principal and premium (if any) and (b) interest (if any) will become unenforceable after 10 years (in the case of (a)) and five (5) years (in the case of (b)), from the relevant date for payment in respect thereof.

12. Enforcement

At any time after the Bonds shall have become due and payable, the Trustee may, at its discretion and without further notice, take such proceedings against the Company as it may think fit to enforce payment of the Bonds together with premium (if any) with respect thereto and to enforce the provisions of the Indenture, but it will not be bound to take any such proceedings unless (a) it shall have been so requested in writing by the holders of at least 25 per cent. in principal amount of the Bonds then outstanding or so directed by an Extraordinary Resolution and (b) it shall have been indemnified and/or secured to its satisfaction. No Bondholder will be entitled to proceed directly against the Company, unless the Trustee, having become bound to do so, fails to do so and such failure shall have continued for a period of 60 days and no direction inconsistent with such written request or Extraordinary Resolution has been given to the Trustee during such 60-day period by the holders of a majority in principal amount of the outstanding Bonds.

13. Meetings of Bondholders, Modification and Waiver

(A) Meetings

The Indenture contains provisions for convening meetings of Bondholders to consider any matter affecting their interests, including the sanctioning by Extraordinary Resolution of a modification of the Bonds or the provisions of the Indenture. The quorum at any such meeting for passing an Extraordinary Resolution will be two or more persons holding or representing over 50 per cent. in principal amount of the Bonds for the time being outstanding or, at any such meeting which has been adjourned, two or more persons being or representing Bondholders whatever the principal amount of the Bonds so held or represented unless the business of such meeting includes consideration of

proposals, inter alia, (i) to modify the maturity date of the Bonds, (ii) to reduce or cancel the amount of principal, premium or interest (if any) payable in respect of the Bonds, (iii) to change the currency of payment of the Bonds, (iv) to modify or cancel the right to convert the Bonds into Shares (except in accordance with Condition 6(B) and 13(B)) or to modify the circumstances in which the Bonds may be redeemed or converted at the option of the Company or to shorten the Conversion Period, (vi) to modify the provisions relating to the resetting of the Conversion Price, (vii) to modify the provisions concerning the quorum required at any meeting of the Bondholders or the majority required to pass an Extraordinary Resolution or sign a resolution in writing, in which case the necessary quorum for passing an Extraordinary Resolution will be two or more persons holding or representing over two-thirds, or at any adjourned such meeting over one-third, in principal amount of the Bonds for the time being outstanding. An Extraordinary Resolution passed at any meeting of Bondholders will be binding on all Bondholders, whether or not they are present at the meeting, and will be conclusive and binding upon all future Bondholders.

The Indenture provides that a written resolution signed by or on behalf of the holders of not less than 90 per cent. of the aggregate principal amount of Bonds outstanding shall be as valid and effective as a duly passed Extraordinary Resolution.

The Company shall prepare a supplement to this Offering Circular and notify the Bondholders (and the Luxembourg Stock Exchange) in accordance with Condition 15 in respect of any proposed Extraordinary Resolution relating to items (i) to (vii) above in this Condition 13(A).

(B) Modification of Conversion Right

Notwithstanding Condition 13(A)(iv) above, the Trustee may agree, without the consent of the Bondholders, to any modification to or variation of the Conversion Rights (including modification of and additions to the declarations and statements to be made by Bondholders in a Conversion Notice) which is in its opinion necessary or desirable to effect or facilitate conversion as contemplated in these Conditions and which is not materially prejudicial to the interests of the Bondholders. The Trustee's agreement may be subject to any condition which the Trustee requires; including, but not limited to, obtaining, at the sole expense of the Company, an opinion of a merchant or investment bank or legal or other expert. Any such modification shall be binding on all the Bondholders. The Company shall prepare a supplement to this Offering Circular and notify the Bondholders of such modification in accordance with Condition 15 and to the Luxembourg Stock Exchange as soon as practicable.

(C) Other Modifications and Waivers

The Trustee may (but shall not be in any way be obligated to) agree, without the consent of the Bondholders, to (i) any modification (except as mentioned above) of, or the waiver or authorization of any breach or proposed breach of, the Bonds or the Indenture which is not, in the opinion of the Trustee, materially prejudicial to the interests of the Bondholders or (ii) any modification of the Bonds or the Indenture which, in the Trustee's opinion, is of a formal, minor or technical nature or to correct a manifest error or to comply with mandatory provisions of law. In connection with such modification, waiver or authorization, the Trustee may require (at the sole expense of the Company) a certificate from the Company certifying, and a legal opinion advising the Trustee, that the modification, waiver or authorization is of a formal, minor or technical nature or to correct a manifest error or to comply with mandatory provisions of law. Any such modification, waiver or authorization will be binding on the Bondholders and, unless the Trustee agrees otherwise, any such modification will be notified by the Company to the Bondholders in accordance with Condition 15 and to the Luxembourg Stock Exchange as soon as practicable thereafter.

(D) Exercise of Trustee's Functions

In connection with the exercise of its functions (including but not limited to those in relation to any proposed modification, authorization or waiver) the Trustee shall have regard to the interests of the Bondholders as a class and shall not have regard to the consequences of such exercise for individual Bondholders and the Trustee shall not be entitled to require, nor shall any Bondholder be entitled to claim, from the Company or the Trustee, any indemnification or payment in respect of any tax consequences of any such exercise upon individual Bondholders.

14. Replacement of Certificates

If any Certificate is mutilated, defaced, destroyed, stolen or lost, it may be replaced at the specified office of the Registrar upon payment by the claimant of such costs as may be incurred in connection therewith and on such terms as to evidence and indemnity as the Company may reasonably require (which terms will require, inter alia, that if such Certificate is subsequently deposited for conversion into Shares there shall be paid to the Company on demand NT\$34.979 for each U.S.\$1.00 of the principal amount of such Bond). Mutilated or defaced Certificates must be surrendered before replacements will be issued.

15. Notices

In addition to the provisions set forth in the Global Certificate, if applicable, all notices to Bondholders shall be validly given if in writing in English and mailed to them at their respective addresses in the register of Bondholders maintained by the Registrar, and, so long as the Bonds are listed on the Luxembourg Stock Exchange and the rules of that exchange so require, published in a leading newspaper having general circulation in Luxembourg (which is expected to be the *Luxemburger Wort*).

Any such notice shall be deemed to have been given on the later of the date of such publication and the seventh day after being so mailed.

16. Indemnification

The Indenture contains provisions for the indemnification of the Trustee and for its relief from responsibility, including provisions relieving it from taking proceedings to enforce payment unless indemnified to its satisfaction.

17. Agents

The names of the initial Agents and Registrar and their specified offices are set out at the end of this Offering Circular. The Company reserves the right, subject to the provisions of the Agency Agreement, at any time to vary or terminate the appointment further or other Agents, provided that the Company will at all times maintain Agents having specified offices in London and so long as the Bonds are listed on the Luxembourg Stock Exchange and the rules of the Luxembourg Stock Exchange so require, an agent in Luxembourg, a Registrar and a Principal Agent. Notice of any such termination or appointment, of any changes in the specified offices of the Agents or of any change in the identity or specified office of the Registrar or the Principal Agent will be given promptly in accordance with Condition 15 by the Company to the Bondholders, the Trustee and the Luxembourg Stock Exchange.

18. Governing Law and Jurisdiction

(A) *Governing Law*

The Indenture and the Bonds are governed by and shall be construed in accordance with the laws of the State of New York, USA.

(B) *Jurisdiction*

The courts of the State of New York sitting in the Borough of Manhattan, The City of New York, and the federal courts of the United States sitting in the Borough of Manhattan, The City of New York, have jurisdiction to settle any disputes which may arise out of or in connection with the Indenture or the Bonds and accordingly any legal action or proceedings arising out of or in connection with the Indenture or the Bonds (“**Proceedings**”) may be brought in such courts. The Company has in the Indenture irrevocably submitted to the jurisdiction of such courts.

(C) *Agent for Service of Process*

The Company has irrevocably appointed CT Corporation System of 111 Eighth Avenue, New York, NY10011, U.S.A. as its authorized agent for service of process in New York in any Proceedings.

THE FORM OF THE BONDS

The Bonds will be issued in registered form, without coupons, in denominations of U.S.\$10,000 and integral multiple thereof. The Bonds are not issuable in bearer form.

The Bonds will be represented by a global certificate (the “**Global Certificate**”) which will be deposited with the Trustee as common depositary for, and registered in the name of a nominee for, Euroclear and Clearstream, Luxembourg. Upon the issuance of the Global Certificate, Euroclear and Clearstream, Luxembourg will credit, on their internal systems, the respective principal amounts of the individual beneficial interests in the Bonds represented by the Global Certificate to the accounts of persons who have accounts with Euroclear and Clearstream, Luxembourg (“**participants**”). These accounts will initially be designated by or on behalf of the Managers. Ownership of beneficial interests in the Global Certificate will be limited to participants and persons who hold interests through participants. Beneficial interests in the Global Certificates will be shown on, and transfers thereof will be effective only through, records maintained by Euroclear and Clearstream, Luxembourg and their participants.

The Company expects that Euroclear and Clearstream, Luxembourg, or their nominee, upon receipt of any payment of principal, premium (if any) or interest (if any) in respect of the Bonds represented by the Global Certificate will credit the accounts of the participants with payments of principal, premium (if any) or interest (if any) on the date payable in amounts proportionate to their respective interests in such Bonds as shown on the records of Euroclear and Clearstream, Luxembourg or their nominees. The Company also expects that payments by such participants to owners of beneficial interests in the Bonds held through such participants will be governed by standing instructions and customary practices. Such payments will be the responsibility of the participants.

Payments, transfers, exchanges and other matters relating to interests in the Bonds may be subject to various policies and procedures adopted by Euroclear and Clearstream, Luxembourg from time to time. Transfers between participants in Euroclear and Clearstream, Luxembourg, and conversions through participants in Euroclear and Clearstream, Luxembourg, will be effected in the ordinary way in accordance with the rules and operating procedures of Euroclear and Clearstream, Luxembourg. Neither the Company, the Trustee or any of their respective agents will have any responsibility or liability for the performance by Euroclear and Clearstream, Luxembourg or their participants of their respective obligations under the rules and procedures governing their operations, or for payments made on account of, or records relating to, interests in the Bonds held through Euroclear and Clearstream, Luxembourg and their participants.

Owners of interests in the Bonds will not be entitled to receive definitive physical certificates in respect of their interests in the Bonds except in the limited circumstances described below under “—Registration of Title”.

The holder of a registered Bond in definitive certificated form may transfer or exchange such Bond by surrendering it at the office or agency maintained by the Company for such purpose in London and, for so long as the Bonds are listed on the Luxembourg Stock Exchange and the rules of that exchange so require, in Luxembourg, which offices will initially be the corporate trust offices of the Trustee maintained in The City of New York or such other offices may be notified by the Trustee from time to time and, the offices of the Paying Agent in Luxembourg, respectively.

Any such Bond in physical certificated form issued prior to the 41st day following the original issuance of the Bonds shall bear the legend set out under “Notice to Investors”.

The Global Certificate

The Global Certificate contains provisions which apply to the Bonds that are represented by the Global Certificate, some of which modify the effect of the terms and conditions of the Bonds (the “**Conditions**”) set out in this Offering Circular. Terms defined in the Conditions have the same meaning in the paragraphs below. The following is a summary of those provisions:

Meetings

The registered holder (as defined in the Conditions) of the Global Certificate will be treated as being two persons for the purposes of any quorum requirements of a meeting of Bondholders and, at any such meeting, as having one vote in respect of each U.S.\$10,000 in principal amount of Bonds for which the Global Certificate is issued. The Trustee may allow a person with an interest in Bonds in respect of which the Global Certificate has been issued to attend and speak at a meeting of Bondholders on appropriate proof of his identity and interest.

Cancellation

Cancellation of any Bond following its redemption, conversion or purchase by the Company will be effected by a reduction in the principal amount of the Bonds in the register of Bondholders.

Trustee’s Powers

In considering the interests of Bondholders while the Global Certificate is registered in the name of a nominee for a clearing system, the Trustee may, without being obliged to do so, have regard to any information provided to it by such clearing system or its operator as to the identity (either individually or by category) of its accountholders with entitlements to Bonds and may consider such interests as if such accountholders were the holders of the Bonds.

Conversion

Subject to the requirements of Euroclear and Clearstream, Luxembourg, the Conversion Right attaching to a Bond in respect of which the Global Certificate is issued may be exercised by the presentation to or to the order of the Principal Agent of one or more Conversion Notices duly completed by or on behalf of a holder of a book-entry interest in the Bond. Deposit of the Global Certificate with the Principal Agent together with the relevant Conversion Notice shall not be required. The exercise of the Conversion Right shall be notified by the Principal Agent to the Registrar and the holder of the Global Certificate.

Payment

Payments of principal, premium (if any) and interest (if any) in respect of Bonds represented by the Global Certificate will be made without presentation or if no further payment is to be made in respect of the Bonds, against presentation and surrender of the Global Certificate to or to the order of the Principal Agent or such other Paying Agent as shall have been notified to the Bondholders for such purpose.

Notices

So long as the Bonds are represented by the Global Certificate and the Global Certificate is held on behalf of Euroclear and Clearstream, Luxembourg or the Alternative Clearing System (as defined below), notices to Bondholders may be given by delivery of the relevant notice to Euroclear and Clearstream, Luxembourg, for communication by it to entitled accountholders in substitution for notification as required by the Conditions except that so long as the Bonds are listed on the Luxembourg Stock Exchange and the rules of that exchange so require, notices shall also be published in a leading newspaper having general circulation in Luxembourg (which is expected to be the *Luxemburger Wort*).

Redemption at the Option of the Company

No drawing of Bonds will be required under Condition 8(F) in the event that the Company exercises its call option pursuant to Condition 8(B) in respect of less than the aggregate principal amount of Bonds in respect of which the Global Certificate is issued. Notices will be made by the Company in accordance with the previous paragraph and the Luxembourg Stock Exchange will be informed should the Company exercise the call option.

Redemption at the Option of Bondholders

The Bondholders' put option in Condition 8(C) may be exercised by the holders of the Global Certificate giving notice to the Principal Agent of the principal amount of Bonds in respect of which the option is exercised and presenting the Global Certificate for endorsement or exercise within the time limits specified in Condition 8(C).

Registration of Title

Certificates in definitive form for individual holdings of Bonds will not be issued in exchange for interests in Bonds in respect of which the Global Certificate is issued, except in case that (a) either Euroclear or Clearstream, Luxembourg (or any Alternative Clearing System on behalf of which the Bonds evidenced by the Global Certificate may be held) is closed for business for a continuous period of 14 days (other than by reason of holidays, statutory or otherwise) or announces an intention permanently to cease business or does in fact do so, or (b) the Bonds become immediately due and payable in accordance with the provisions of Condition 10 or if in connection with judicial proceedings brought by the Trustee, the Trustee has been advised that it is necessary or appropriate for definitive Certificates to be executed and delivered.

Transfers

Transfers of interests in the Bonds with respect to which the Global Certificate is issued shall be effected through the records of the relevant clearing system and its participants in accordance with the Conditions, the Agency Agreement and the rules and procedures of the relevant clearing system.

Enforcement

For the purposes of enforcement of the provisions of the Indenture against the Trustee, the persons named in a certificate of the holder of the Bonds in respect of which the Global Certificate is issued shall be recognized as the beneficiaries of the trusts set out in the Indenture, to the extent of the principal amount of their interest in the Bonds set out in the certificate of the holder, as if they were themselves the holders of Bonds in such principal amounts.

DESCRIPTION OF THE SHARES

The following is a summary of information relating to the share capital of the Company, including certain provisions of the Company's Articles of Incorporation (the "**Articles**"), the ROC Securities and Exchange Law (the "**Securities and Exchange Law**") and regulations promulgated thereunder and the ROC Company Law, all as currently in effect.

General

As of 31st March, 2002, the authorized share capital of the Company was NT\$7,000,000,000 divided into 700,000,000 common shares (the "**Shares**") with a par value of NT\$10 per Share, of which 140,000,000 Shares have been reserved for conversion of convertible bonds. As of 31st December, 2001, the paid-in capital was NT\$4,366,722,140, all of which are issued and outstanding and in registered form.

Under the ROC Company Law, any change in the Company's authorized share capital requires an amendment to the Articles, which in turn requires approval at the shareholders' meeting. Authorized but unissued Shares may be issued subject to ROC Company Law, upon terms that the Board of Directors may determine.

Other than the Bonds offered hereby, the Company has not issued any warrant, any convertible debt securities, exchangeable securities or debt securities with warrant attached.

The Articles of Incorporation

Article Two of the Company's articles of incorporation sets out the objects for which the Company was organized. These include:

- Design, manufacture, test, accessory, process, packaging and trade of integrated circuits;
- Manufacture, process and trade of burn-in oven and parts thereto;
- Export and import trade of the above products; and
- Quoting, bidding and selling of above products for foreign and domestic manufacturers.

Dividends and Distribution

Under the ROC Company Law, except under certain limited circumstances, an ROC company is not permitted to distribute dividends or make any other distributions to shareholders in any year in which the Company has no earnings.

The ROC Company Law also require that 10 per cent. of the Company's annual earnings, less prior years' losses, if any, and outstanding tax, be set aside as a legal reserve until the accumulated legal reserve equals the paid-in capital. The Company may set aside a special reserve in accordance with applicable laws and regulations. In addition, the Articles provide that, after the Company pay the income taxes, deduct losses incurred in prior years and deduct the legal reserve and any special reserve, the remaining portion of the earnings will be distributed as dividends and bonuses, according to the Board of Directors' resolution as approved by the shareholders, of which (1) the employee bonuses shall be 15 per cent. of the residual earnings approved by the shareholders, and (2) the remuneration of all directors and supervisors shall be one per cent. of the residual earnings approved by the shareholders.

At each annual ordinary shareholders' meeting, the Board of Directors of the Company submits to the shareholders for their approval any proposal for the distribution of a dividend or the making of any other distribution to shareholders from the Company's earnings (subject to compliance with the requirements mentioned above) for the preceding fiscal year. All common shares outstanding and fully paid as of the relevant record date are entitled to share equally in any dividend or other distribution so approved. Dividends may be distributed in cash, in the form of shares or a combination of the two, as determined by the shareholders at the meeting and provided that not more than 20 per cent. of the distributable dividends may be distributed in the form of cash. All or part of the dividends to shareholders may be reserved at the relevant annual shareholders' meeting as retained earnings for distribution in later years.

In addition, if the Company does not have losses, the Company is also permitted to make distributions to its shareholders of additional Shares by capitalizing reserves (including the legal reserve and capital surplus of premium from issuing stock and earnings from gifts received). However, amounts payable by capitalizing the legal reserve are limited to 50 per cent. of the total accumulated legal reserve and this capitalization can only be effected when the accumulated legal reserve exceeds 50 per cent. of the paid-in capital of the Company.

Preemptive Rights

Under the ROC Company Law, when the Company issues new shares for cash, existing shareholders who are listed on the shareholders' register as of the record date have preemptive rights to subscribe for the new issue in proportion to their existing shareholdings, while the Company's employees, whether or not they are existing shareholders, have a similar right to subscribe for 10 per cent. to 15 per cent. of the new issue. Any new shares that remain unsubscribed at the expiration of the subscription period may be offered to the public or specified persons at the discretion of the Board of Directors of the Company.

In addition, in accordance with the ROC Securities and Exchange Law, a public company listed on TSE or whose shares are traded on ROSE that intends to offer new shares for cash must conduct a public offering of at least 10 per cent. of the shares to be sold, except under certain circumstances or when exempted by the ROC SFC. This percentage can be increased by a resolution passed at shareholders' meeting, which would diminish the number of new shares subject to the preemptive rights of existing shareholders. According to the amended Securities and Exchange Law which became effective on 8th February, 2001, the preemptive right provisions will not apply to offerings of new shares through a private placement approved in a shareholders' meeting.

Meetings of Shareholders

The ordinary meeting of shareholders of the Company is usually held in Hsin-Chu City, Taiwan, as determined by the Board of Directors, within six months after the end of each calendar year. Extraordinary meetings of shareholders may be convened by resolution of the Board of Directors whenever they consider it necessary, and they must do so if requested in writing by shareholders holding not less than three per cent. of the paid-in capital who have held these shares for more than a year. Extraordinary meetings of shareholders may also be convened by a Supervisor of the Company under certain circumstances. Notice in writing of ordinary and extraordinary shareholders' meetings stating the place, time and purpose thereof must be dispatched to each shareholder of the Company at least 30 days and 15 days, respectively, prior to the date set for the meeting. Also, according to the regulations of the ROC SFC, the Company is required to publish notices of shareholders' meetings in a national daily newspaper.

Voting Rights

Under the ROC Company Law, a shareholder has one vote for each common share. As previously required by law, the Articles provide that the vote cast by a shareholder of more than three per cent. of the total issued and outstanding common shares will be discounted by one per cent. of that portion of the holding in excess of the three per cent. level. However, the ROC Company Law, amended on 25th October, 2001, eliminates this voting discount requirement. As the ROC Company Law will take precedence over any conflicts between the Articles and it, the voting discount requirement provisions of the Articles will no longer have effect.

Except as otherwise provided by law, a resolution can be adopted by the holders of at least a majority of the Shares represented at a shareholders' meeting at which the holders of a majority of all issued and outstanding Shares are present. The election of directors and supervisors at a shareholders' meeting is by means of cumulative voting unless the articles of incorporation of a company provide otherwise. Ballots for the election of directors are cast separately from those for the election of supervisors. Candidates for the offices of directors and supervisors may be nominated at the shareholders' meeting at which ballots for the election are cast. Under the ROC Company Law, the approval by at least a majority of the Shares represented at a shareholders' meeting in which a quorum of at least two-thirds of all issued and outstanding Shares are represented is required for major corporate actions, including:

- amendment to the Articles

- transfer of the whole or substantial part of the Company's business or assets
- execute, amend or terminate any contract that leases the Company's whole business, mandates the Company's operation to other persons, or operates frequently the business for the joint interest of the Company and other persons
- taking over of the whole of the business or assets of any other company which would have a significant impact on the Company's operations
- distribution of any stock dividend
- the dissolution or amalgamation of a company
- the merger or spin-off
- the removing of directors or supervisors.

Alternatively, the ROC Company Law provides that in the case of a public company, such as the Company, a resolution may be adopted by the holders of at least two-thirds of the Shares represented at a meeting of shareholders at which holders of at least a majority of issued and outstanding Shares are present. However, if a controlling company holds not less than 90 per cent. of its subordinate company's outstanding shares, the controlling company's merger with the subordinate company can be approved by board resolution adopted by majority consent at a meeting with two-thirds of directors present.

A shareholder may be represented at an ordinary or extraordinary meeting by proxy if a valid proxy form is delivered to the Company five days before the commencement of the ordinary or extraordinary shareholders' meeting. Except for trust enterprises or stock affair agents approved by the ROC SFC, where one person is appointed as proxy by two or more shareholders who together hold more than three per cent. of the total issued common shares, the votes of those shareholders in excess of three per cent. of the outstanding Shares shall not be counted.

Under the ROC Company Law, the Company may, by giving advance public notice, set a record date and close the register of shareholders for a specified period in order to determine the shareholders and pledgees that are entitled to rights pertaining to the Shares. The specified period required is as follows:

- ordinary shareholders' meeting — sixty days
- extraordinary shareholders' meeting — thirty days
- relevant record date for distribution of dividends, bonuses or other interests — five days

Other Rights of Shareholders

Under the ROC Company Law, dissenting shareholders of the Company are entitled to appraisal rights in the event of amalgamation, spin-off and various other major corporate actions within 20 days of the resolution approving the event. A dissenting shareholder may request that the Company redeem all of the shares owned by the shareholder at a fair price to be determined by mutual agreement. If an agreement cannot be reached, the valuation will be determined by a court order. For amalgamation or spin off, a dissenting shareholder may exercise its appraisal right by serving written notice on the Company before or during the related shareholders' meeting or by raising and registering its objection in the shareholders' meeting. For other major corporate actions, a dissenting shareholder may exercise its appraisal right by serving written notice on the Company before the related shareholders' meeting and by raising and registering its objection in the shareholders' meeting.

In addition to appraisal rights, within 30 days after the date of the shareholders' meeting, any shareholder has the right to annul any resolution adopted at a shareholders' meeting where the procedures were legally defective. However, if the court is of the opinion that such violation is not material and does not affect the result of the resolution, the court may reject or dismiss the shareholder's lawsuit. One or more shareholders who have held more than three per cent. of the issued and outstanding shares of the Company for over a year may require a supervisor to bring an action against a director for the director's liability to the

Company as a result of the director's unlawful actions or failure to act. In addition, one or more shareholders who have held more than three per cent. of the issued and outstanding shares of the Company for over a year may require the Board of Directors of the Company to convene an extraordinary shareholders' meeting by sending a written request to the Board of Directors.

Annual Financial Statements

Under the ROC Company Law, 10 days before the ordinary shareholders' meeting, the Company's annual audited financial statements must be available at the principal office of the Company in Hsin-Chu City, for inspection by the shareholders. According to the regulations of the ROC SFC, the Company is required to publish its annual, semi-annual and quarterly non-consolidated financial statements in a national daily newspaper, which are also available in the office of the paying and conversion agent in Luxembourg and elsewhere.

Transfers of Common Shares

Under the ROC Company Law, the transfer of Shares (in registered form) is effected by endorsement and delivery of share certificates. In order to assert shareholders' rights against the Company, the transferee must have his name and address registered on the Company's register of shareholders. Shareholders are required to register their respective specimen seal or chop with the Company. The settlement of trading of the common stock is normally carried out on the book-entry system maintained by Taiwan Securities Central Depository Co., Ltd.

Acquisition by the Company of its own Common Shares

Under the ROC Company Law, with minor exceptions, the Company cannot acquire its own Shares, and any Share acquired by the Company must be sold by the Company at the current market price within six months after its acquisition.

In addition, under the ROC Securities and Exchange Law, a company whose shares are listed on the TSE or traded on the ROSE may, pursuant to a board resolution adopted by a majority consent at a meeting attended by more than two-thirds of the directors and pursuant to the procedures prescribed by the ROC SFC, purchase its shares on the TSE or ROSE or by a tender offer for the following purposes:

- for transfer of shares to its employees;
- for conversion into shares from bonds with warrants, preferred shares with warrants, convertible bonds, convertible preferred shares or certificates of warrants issued by the company; and
- for maintaining its credit and its shareholders' equity; provided that the shares so purchased shall be cancelled thereafter.

The total Shares purchased by the Company shall not exceed 10 per cent. of its total issued and outstanding Shares. In addition, the total amount for purchase of the Shares shall not exceed the aggregate amount of the retained earnings, the premium from stock issues and the realized portion of the capital reserve.

The Shares purchased by the Company pursuant to the first two items above shall be transferred to the intended transferees within three years after the purchase, otherwise the Shares shall be cancelled. For the Shares to be cancelled pursuant to the third item above, the Company shall complete amendment registration for such cancellation within six months after the purchase.

The Shares purchased by the Company shall not be pledged or hypothecated. In addition, the Company may not exercise any shareholders' rights attaching to such Shares. The Company's affiliates (as defined in Article 369-1 of the ROC Company Law), directors, supervisors, managers and their respective spouses and minor children and/or nominees are prohibited from selling the Shares of the Company held by them during the period in which the Company purchases its own shares.

Liquidation Rights

In the event of the liquidation of the Company, the assets remaining after payment of all debts, liquidation expenses, taxes and distributions to holders of preferred shares, if any, will be distributed pro rata to the shareholders in accordance with the ROC Company Law.

Significant Shareholders and Transfer Restrictions

The ROC Securities and Exchange Law currently requires (1) each director, supervisor, manager or significant shareholder (i.e., a shareholder who, together with his or her spouse, minor children or nominees, holds more than 10 per cent. of the shares of a public company) to report any change in that person's shareholding to the issuer of the shares, and (2) each director, supervisor, manager or significant shareholder to report his or her intent to transfer any shares traded on the TSE or ROSE to the ROC SFC at least three days before the intended transfer, unless the number of shares to be transferred is less than 10,000. The ROC Securities and Exchange Law also limits the number of shares that can be sold or transferred on the TSE or ROSE by each director, supervisor, manager or significant shareholder per day.

Limitation on Shareholdings in the Company and Reporting Obligations

The ROC Securities and Exchange law requires each director, supervisor, manager or significant shareholder to report any change in that person's shareholding to the Company before each fifth day of each month and the Company shall report the same to the ROC SFC before the fifteenth day of each month. Such persons are also required to report to the Company immediately the pledge of their shares in the Company and the Company shall report the same to the ROC SFC within five days from the pledge date. A person or a person who along with other persons (as defined under the ROC SFC regulations) acquires more than 10 per cent. of the issued and outstanding Shares of the Company shall report to the ROC SFC, within ten days from the acquisition date, the acquisition purpose, funding sources and other information required by the ROC SFC.

TAXATION

The Bonds may be deemed by taxing authorities in various jurisdictions to be issued with original issue discount. Prospective investors should consult their own advisers concerning the tax consequences of an investment in Bonds or Shares.

ROC Taxation of Non-residents

The following is a summary under present law of the principal ROC tax consequences of the ownership and disposition of Bonds and Shares to a Non-Resident Individual or Non-Resident Entity that holds Bonds or Shares (each a “**Non-ROC Holder**”). As used in the preceding sentence, a “**Non-Resident Individual**” is a foreign national individual who owns Bonds or Shares and is not physically present in the ROC for 183 days or more during any calendar year and a “Non-Resident Entity” is a corporation or a non-corporate body that owns Bonds or Shares and is organized under the laws of a jurisdiction other than the ROC and has no fixed place of business or other permanent establishment in the ROC.

Dividends on the Shares

Dividends (whether in cash or Shares) declared by the Company out of retained earnings and paid out to holders of Shares are normally subject to ROC income tax collected by way of withholding at the time of distribution. The current rate of withholding for Non-ROC Holders adopted by the tax authorities is 20 per cent. of the amount of the distribution (in the case of cash dividends) or the par value of the Shares (in the case of stock dividends). Distributions of stock dividends declared by the Company out of capital reserves are currently not subject to ROC withholding tax. In accordance with the ROC Income Tax Law, a 10 per cent. retained earnings tax will be imposed on a company for its after-tax earnings generated after 1st January, 1998 which are not distributed in the following year. The retained earnings tax so paid will further reduce the retained earnings available for future distribution. When the company declares dividends out of those retained earnings, a maximum amount of up to 10 per cent. of the declared dividends will be credited against the 20 per cent. withholding tax imposed on the Non-ROC Holder.

Capital Gains

Under current ROC law, gain realized upon the sale or other disposition of securities is exempt from ROC income tax. This exemption will apply to a sale or other disposition of Bonds or Shares.

ROC law currently provides no specific provisions regarding the ROC income tax consequences of a conversion of Bonds into Shares. Without further clarification from the ROC tax authorities, it is impossible to conclude definitively that gain on the conversion of Bonds into Shares will not be deemed as taxable gain, additional interest income (subject to the 20 per cent. withholding tax) or otherwise subject to other ROC taxes. Transfers of Bonds by Non-ROC Holders are regarded as transactions outside the ROC and thus any gains derived therefrom are not subject to ROC income tax.

Securities Transaction Tax

The ROC Government imposes a securities transaction tax that will apply to sales of Bonds and Shares. The transaction tax, which is payable by the seller, is generally levied on sales of Shares at the rate of 0.3 per cent. of the transaction price. According to the amended Statute for Upgrading Industries, sales of the Bonds outside of the ROC are exempted from such securities transaction tax.

The securities transaction tax and/or gift tax may be imposed in relation to the converting Bondholder’s designation of other person to be the holder of Shares upon conversion of the Bonds.

There is no ROC stamp, issue or registration tax imposed on the issuance of Shares upon conversion of the Bonds.

Inheritance Tax and Gift Tax

ROC inheritance tax is payable on any property within the ROC of a deceased Non-Resident Individual, and ROC gift tax is payable on any property within the ROC donated by a Non-Resident Individual. Inheritance tax is currently imposed at rates ranging from two per cent. of the first NT\$600,000 to 50 per cent. of amounts in excess of NT\$100,000,000. Gift tax is imposed at rates ranging from four per

cent. of the first NT\$600,000 donated to 50 per cent. of amounts donated in excess of NT\$45,000,000. Under ROC inheritance and gift tax laws, the Bonds and Shares will be deemed to be located in the ROC without regard to the location of the owner.

Tax Treaty

At present, the ROC has income tax treaties with Indonesia, Singapore, New Zealand, Australia, South Africa, Gambia, Swaziland, Malaysia, Macedonia, Vietnam and The Netherlands. It is unclear whether a Non-ROC Holder will be considered to own Bonds or Shares for the purposes of such treaties. Accordingly, a holder of Bonds or Shares who is otherwise entitled to the benefit of a treaty should consult its own tax advisers concerning eligibility for benefit under the treaty with respect to Bonds or Shares.

Tax Reform

In order to increase Taiwan's competitiveness, an amendment to the ROC Income Tax Law ("**Amendment**") was enacted on 1st January, 1998, to integrate the corporate income tax and the shareholder dividend tax with the aim of eliminating the double taxation effect for resident shareholders of ROC companies. The Amendment will have the following effect upon Non-ROC Holders of the Shares.

A 10 per cent. retained earnings tax will be imposed on a company for its after-tax earnings generated after 1st January, 1998 which are not distributed in the following year. The retained earnings tax so paid will further reduce the retained earnings available for future distribution. When the Company declares dividends out of those retained earnings, a maximum amount of up to 10 per cent. of the declared dividends will be credited against the 20 per cent. withholding tax imposed on the Non-ROC Holders of its Shares.

Withholding Tax on Payments of Premium

Premium (if any) and interest (if any) payable on the Bonds to the Non-ROC Holders is currently subject to a withholding tax in the ROC equal to 20 per cent. of the gross amount of such premium (if any) and interest (if any) at the time of payment.

Subscription Rights

Distributions of subscription rights for the Shares in compliance with the ROC Company Law are not subject to ROC tax. Proceeds derived from sales of statutory subscription rights evidenced by securities are currently exempted from income tax but are subject to securities transaction tax, currently at the rate of 0.3 per cent. of the gross amount received. Proceeds derived from sales of statutory subscription rights that are not evidenced by securities are subject to capital gains tax at the rate of (i) 25 per cent. of the gains realized for Non-ROC Entity Holders, and (ii) 35 per cent. of the gains realized for Non-ROC Individual Holders. Subject to compliance with ROC law, the Company has the sole discretion to determine whether statutory subscription rights are evidenced by securities or not.

Proposed European Union ("EU") Withholding Tax Directive

In June 2000 the European Council agreed to amend a proposed EU Directive of June 1998 regarding the taxation of interest, discounts and premiums payable to individual residents of other EU Member States. Member States would be obliged either (a) to exchange information with other Member States regarding such savings income paid to individuals resident in another Member State or (b) withhold tax on such income at a rate to be agreed, provided that Member States that operate a withholding system must implement the exchange of information system as soon as conditions permit and in any case no later than seven years after implementation of the proposed Directive. Further to an agreement reached at the ECOFIN meeting in November 2000 the withholding tax and information reporting requirements would only apply to payments after 2002 with respect to debt issued on or after 1st March, 2001. It is impossible at this time to predict whether or in what form the proposed EU Directive, which requires the unanimous approval of all Member States, will eventually be adopted or what the effective dates of any withholding tax system that is adopted will be.

SUBSCRIPTION AND SALE

NSC Securities (Asia) Limited (the “**Lead Manager**”), Grand Cathay Securities Corporation, MasterLink Securities Corporation and Bank SinoPac, Offshore Banking Branch (together with the Lead Manager, the “**Managers**”) have, pursuant to a Subscription Agreement to be dated on 18th April, 2002 (the “**Subscription Agreement**”), severally and not jointly agreed with the Company to subscribe and purchase the Bonds at the issue price of 100 per cent. of their principal amount less the combined management and underwriting commission and selling fee of two per cent. on the aggregate principal amount of the Bonds. Pursuant to the Subscription Agreement, the Managers have agreed to reimburse certain of the Company’s expenses in connection with the issue of the Bonds.

The Company has agreed in the Subscription Agreement to indemnify the Managers with certain liabilities, including the liabilities under the Securities Act, in connection with the offering of the Bonds.

The Company has agreed in the Subscription Agreement that, for a period of 180 days from the date of the Subscription Agreement, neither it nor any person acting on its behalf will, without the prior written consent of the Lead Manager, issue, offer or sell any equity securities, or any securities convertible or exchangeable for equity securities, or any rights, warrants or options to subscribe for equity securities of the Company, or announce plans or otherwise make public an intention to do any of the foregoing, in each case outside of Taiwan or denominated in a currency other than NT Dollars, other than those pursuant to employee benefits plans or employee stock option plans or distributions of dividends or employee bonuses in the form of Shares and conversion of the Bonds.

The Bondholders who purchase the Bonds from the Managers may be required to pay stamp taxes and other charges in accordance with the laws and practice of the country of purchase in addition to the issue price of the Bonds.

Selling Restrictions

No action has been or will be taken in any jurisdiction that would permit a public offering of the Bonds or the Shares issuable upon conversion of the Bonds, or the possession, circulation or distribution of this Offering Circular or any other material relating to the Company, the Bonds or the Shares issuable upon conversion of the Bonds, in any jurisdiction where action for the purpose is required. Accordingly, neither the Bonds nor any Shares issuable upon conversion of the Bonds may be offered or sold, directly or indirectly, and neither this Offering Circular nor any other offering material or advertisements in connection with the Bonds or the Shares issuable upon conversion of the Bonds may be distributed or published, in or from any country or jurisdiction, except in compliance with any applicable rules and regulations of any such country or jurisdiction.

United States

Each Manager has acknowledged and agreed that the Bonds and the Shares to be issued upon conversion of the Bonds have not been and will not be registered under the Securities Act, and may not (i) as part of their distribution at any time or (ii) prior to the 40th day after the closing of the offering of the Bonds be offered or sold within the United States or to, or for the account or benefit of, U.S. persons. The Bonds are being offered and sold outside the United States to non-U.S. persons in reliance on Regulation S.

In addition, until 40 days after the closing of the offering of the Bonds, an offer or sale of the Bonds or the Shares to be issued upon conversion of the Bonds within the United States by any dealer (whether or not participating in the offering) may violate the registration requirements of the Securities Act.

United Kingdom

Each Manager has represented and agreed that:

- (1) it has not offered or sold and prior to the date six months after the issue of the Bonds will not offer or sell any Bonds to persons in the United Kingdom except to persons whose ordinary activities involve them in acquiring, holding, managing or disposing of investments (as principal

or agent) for the purposes of their businesses or otherwise in circumstances which have not resulted and will not result in an offer to the public in the United Kingdom within the meaning of the Public Offer of Securities Regulations 1995;

- (2) it has complied and will comply with all applicable provisions of the Act with respect to anything done by it in relation to the Bonds in, from or otherwise involving the United Kingdom; and
- (3) it has only issued or passed onto any person in the United Kingdom any document received by it in connection with the issue of the Bonds, if that person is of a kind described in Article 11(3) of the Financial Services Act 1986 (Investment Advertisements) (Exemptions) Order 1996 or is a person to whom such document may otherwise lawfully be issued or passed on.

The ROC

Each Manager has acknowledged and agreed that the Bonds may not be offered, sold or delivered, directly or indirectly, in the ROC, as part of the distribution of the Bonds.

Hong Kong

Each Manager has acknowledged and agreed that (1) it has not offered or sold and will not offer or sell in Hong Kong, by means of any document, any Bonds other than to persons whose ordinary business it is to buy or sell shares or debentures, whether as principal or agent, or in circumstances which do not constitute an offer to the public within the meaning of the Companies Ordinance (Cap. 32) of Hong Kong; and (2) it has not issued and will not issue any invitation or advertisement relating to the Bonds in Hong Kong (except if permitted to do so under the securities laws of Hong Kong) other than with respect to Bonds which are intended to be disposed of to persons outside Hong Kong or only to persons whose business involves the acquisition, disposal or holding, of securities, whether as principal or agent.

Japan

The Bonds and Shares have not been and will not be registered under the Securities and Exchange Law of Japan. Accordingly, each Manager has represented and agreed that it has not, directly or indirectly, offered or sold and will not, directly or indirectly, offer or sell any Bonds or Shares in Japan or to, or for the benefit of, any resident of Japan, except that the Managers may offer and sell such Bonds or Shares pursuant to an exemption from the registration requirements of, and otherwise in compliance with the Securities and Exchange Law of Japan and other applicable laws and regulations of Japan. As used in this paragraph, “**resident of Japan**” means any person resides in Japan, including any corporation or other entity organized under the laws of Japan.

Singapore

Each Manager has acknowledged and agreed that this Offering Circular has not been and will not be registered as a prospectus with the Registrar of Companies in Singapore. Accordingly, each Manager has represented and agreed that it has not offered or sold and will not offer or sell any Bonds nor has it circulated or distributed nor will it circulate or distribute this Offering Circular or any other offering document or material relating to the Bonds, directly or indirectly, (i) to persons in Singapore other than under circumstances in which such offer or sale does not constitute an offer or sale of the Bonds to the public in Singapore or (ii) to the public or any member of the public in Singapore other than pursuant to, and in accordance with the conditions of, an exemption invoked under Division 5A of Part IV of the Companies Act, Chapter 50 of Singapore and to persons to whom the Bonds may be offered or sold under such exemption.

LEGAL MATTERS

Certain legal matters with respect to the Bonds will be passed upon for the Company by Lee and Li, Attorneys at Law, and for the Managers by Baker & McKenzie, Hong Kong. Baker & McKenzie, Hong Kong will rely upon Lee and Li, Attorneys at Law, with respect to certain matters of ROC law. Lee and Li, Attorneys at Law will rely upon Baker & McKenzie, Hong Kong with respect to certain matters of United States federal and New York laws.

ACCOUNTANTS

The financial statements of King Yuan Electronics Co., Ltd. at 31st December, 1999, 2000 and 2001 and for the years then ended, appearing in this Offering Circular have been audited by Diwan, Ernst & Young, independent auditors, as set forth in their report thereon appearing elsewhere herein, and are included in reliance upon such report given upon the authority of such firm as experts in accounting and auditing.

GENERAL INFORMATION

The Company is registered with the Ministry of Economic Affairs of the ROC under a uniform registration number of 22507241. The Company's registered office is located at No. 1, Lane 99, Pu-Ding Road, Hsin-Chu 300, Taiwan, Republic of China, and the Company's telephone number is 886-3-5751888.

The Company, having made all reasonable inquiries, confirms that this Offering Circular contains all information with respect to the Company, the Bonds, and the Shares which is material in the context of the issue and offering of the Bonds (including all information required by applicable laws of the ROC), that the information contained herein (save as set out below) is true and accurate in all material respects and is not misleading, that the opinions and intentions expressed herein are honestly held and have been reached after considering all relevant circumstances and are based on reasonable assumptions, that there are no other facts, the omission of which would, in the context of the issue and offering of the Bonds, make this Offering Circular as a whole or any of such information or the expression of any such opinions or intentions misleading in any material respects, that all reasonable inquiries have been made by the Company to verify the accuracy of such information, and that this Offering Circular does not contain an untrue statement of a material fact or omit to state a material fact required to be stated herein or necessary in order to make the statements herein, in the light of the circumstances under which they are made, not misleading. The Company accepts responsibility accordingly. Information provided herein with respect to the ROC, its political status and economy, has been derived from government and other public sources, and the Company accepts responsibility only for accurately extracting information from such sources.

The Offering of the Bonds was authorized and approved by the Board of Directors of the Company on 11th December, 2001 and 7th February, 2002 and by the ROC Securities and Futures Commission ("ROC SFC") on 21st March, 2002 and 9th April, 2002.

The depositary and paying agent of the Company's Shares is Capital Securities Corporation, addressed at 14/F, No. 87 Chung-Shiao East Road, Section 4, Taipei, Taiwan, ROC.

Application has been made to list the Bonds on the Luxembourg Stock Exchange. The legal notice relating to the issue of the Bonds, and the Articles of Incorporation of the Company will be registered prior to the listing with the Chief Registrar of the District Court in Luxembourg (*Greffier en Chef du Tribunal d'Arrondissement de et à Luxembourg*), where such documents will be available for inspection and where copies thereof can be obtained upon request. According to Chapter VI, Article 3, point A/II/2 of the Rules and Regulations of the Luxembourg Stock Exchange the Bonds shall be freely tradable and therefore no transaction made on the Luxembourg Stock Exchange shall be cancelled.

Copies (and certified English translations where the documents are not in English) of the following documents may be inspected and freely obtainable at the specified office of the Paying and Conversion Agent in Luxembourg for as long as the Bonds are listed on the Luxembourg Stock Exchange:

- Articles of Incorporation of the Company;
- a copy of the reports of the independent accountants, the audited financial statements of the Company as at and for the years ended 31st December, 1999, 2000 and 2001;
- the Subscription Agreement relating to the Bonds;
- the Indenture constituting the Bonds (which includes the form of the Global Certificate); and
- the Paying and Conversion Agency Agreement.

In addition, copies of this Offering Circular and the most recent annual financial statements of the Company and semi-annual financial statements of the Company (in each case in English), will be available at the specified office of the Paying and Conversion Agent in Luxembourg free of charge for as long as the Bonds are listed on the Luxembourg Stock Exchange. All notices, including all financial notices concerning the Company and notices of the Company's general meetings, to holders of the Bonds will be published in a daily newspaper of general circulation (which is expected to be the *Luxemburger Wort*).

Except as disclosed herein, there has been no adverse material change in the financial position of the Company since 31st December, 2001, the date of the latest financial statements contained herein. The Company's financial statements are prepared on an unconsolidated basis. In accordance with ROC GAAP and ROC SFC rules, the Company does not prepare consolidated financial statements because none of its subsidiaries have total assets and operating revenues equal to or exceeding 10 per cent. of those of the Company and the combined assets and operating revenues of all subsidiaries do not exceed 30 per cent. of the Company's assets and operating revenues.

The Subscription Agreement, the Paying and Conversion Agency Agreement and the Indenture in connection with the Offering are governed by the laws of the State of New York.

Trading of the Bonds on the Luxembourg Stock Exchange has been accepted for clearance by Euroclear and Clearstream, Luxembourg. Relevant trading information for the Bonds is set forth below:

Common Code 014533117
ISIN XS0145331178

The Company has not at the date of this Offering Circular established or authorized the establishment of any depositary receipt facility. Accordingly, conversion into DRs is not currently available. If in the future a depositary receipt facility is established or authorized by the Company, the Company will, to the extent permitted by applicable laws and regulations, make arrangements satisfactory to the Trustee for Shares issued on conversion of Bonds to be accepted for deposit (at the option of the converting Bondholder) into such depositary receipt facility, subject always to the terms of such depositary facility, which terms may include certification or other requirements as conditions to the acceptance for deposit of Shares issued on conversion of Bonds. the Company will provide a supplement to this Offering Circular including the term, conversion rate and other information of such DRs if the DRs have been issued.

SUMMARY OF SIGNIFICANT DIFFERENCES BETWEEN ROC GAAP AND U.S. GAAP

Financial statements prepared in accordance with “Rules Governing Preparation of Financial Statements of securities Issuers” and generally accepted accounting principles in the Republic of China (collectively referred herein as “ROC GAAP”) differ in certain respects from U.S. GAAP. The following is a summary of the significant differences between ROC GAAP, as applicable to the Company, and U.S. GAAP. The summary below should not be considered to be exhaustive. Additionally, it may exclude certain differences that may affect the disclosure, presentation or classification of transactions or events in the Company’s financial statements. Further, this summary does not take into account numerous projects currently being undertaken by standard setting bodies in the United States and ROC, which could have an impact on the comparison between ROC GAAP and U.S. GAAP, which are applicable to the Company. Finally, no attempt has been made to identify all future differences between ROC GAAP and U.S. GAAP that may affect the financial statements as a result of transactions or events that may occur in the future.

ROC GAAP	U.S. GAAP
Marketable Securities	
(a) Under ROC GAAP, short-term marketable equity securities are carried at the lower of aggregate cost or market value. The unrealized losses of short-term marketable equity securities are recorded as investment loss in the incomes statement, while unrealized gains of short-term marketable equity securities are not recognized. Long-term marketable equity securities are carried at cost, or lower of aggregate cost or market value if the market price is available. The unrealized losses of long-term marketable equity securities are reported as a deduction of shareholders’ equity, while the unrealized gains are not recognized. (b) Under ROC GAAP, if an investor company invests in equity securities that are traded in an open market and uses the cost method for valuation purposes, then an investor company shall recognize losses if evidence suggests that the value of an investment has been impaired and it is unlikely that the stock price will recover. The new cost of the long-term investment is the book value after recognizing the losses.	(a) Under U.S. GAAP Statement of Financial Accounting Standards, (“SFAS”) 115, “Accounting for Certain Investments in Debt and Equity Securities”, debt and equity securities that have readily determinable fair values are to be classified as either trading, available-for-sale or held-to-maturity securities. Debt securities that the Company has the positive intent and ability to hold to maturity are classified as held-to-maturity securities and reported at amortized cost. Debt and equity securities that are bought and traded for short-term profit are classified as trading securities and reported at fair value, with unrealized gains and losses included in earnings. Debt and equity securities not classified as either held-to-maturity or trading securities are classified as available-for-sale securities and reported at fair value, with unrealized gains and losses excluded from earnings and reported in a separate component of stockholders’ equity. (b) Under U.S. GAAP, for individual securities classified as either available-for-sale or held-to maturity, an enterprise shall determine whether a decline in fair value below the amortized cost basis is other than temporary. If the decline in fair value is judged to be other than temporary, the cost basis of the individual security shall be written down to fair value as a new cost basis and the amount of the written-down shall be included in earnings. The new cost basis shall not be changed for subsequent recoveries in fair value. Subsequent increases in the fair value of available-for-sale securities shall be included in the other comprehensive income.

ROC GAAP**U.S. GAAP****Gains on Disposal of Property, Plant & Equipment**

Gains on the disposal of property, plant and equipment will first be credited to non-operating income and then transferred, after deducting the applicable income tax, to additional paid-in capital in the applicable fiscal year. The reclassification is no longer required for disposals made on and after 27th December, 2001, as a result of amendments to Regulation on Business Entity Accounting Handling in 2001.

Under U.S. GAAP, the transfer of such gain from retained earnings is not permitted.

Impairment of Long-Lived Assets and Long-lived Assets to be disposed of

ROC GAAP has no specific standards, which address impairment of long-lived assets and certain identifiable intangibles; normally such assets would be carried at cost less accumulated depreciation or amortization.

U.S. GAAP SFAS 121 requires entities to perform separate calculations for assets to be held and used to determine whether recognition of an impairment loss is required, and if so, to measure the impairment. If the sum of expected future cash flows, undiscounted and without interest charges, is less than an asset's carrying value, an impairment loss is recognized; if the sum of the expected future cash flows is greater than an asset's carrying value, an impairment loss cannot be recognized. Measurement of an impairment loss is based on the fair value of the asset. U.S. GAAP SFAS 121 also generally requires long-lived assets and certain identifiable intangible assets to be disposed of be recorded at the lower of the carrying value or fair value less cost to sell.

Stock Dividends

Under ROC GAAP, stock dividends are recorded at par with a charge to retained earnings.

Under U.S. GAAP, if the ratio of distribution is less than 25 per cent. of the same class of shares outstanding, the fair value of the shares issued should be charged to retained earnings.

Employee Bonuses

Under ROC GAAP, the employee bonuses and the remuneration to directors and supervisors, paid in accordance with the provisions of the Company's articles of incorporation applicable to the distribution of earnings, are recorded as an appropriation from retained earnings in the period shareholders' approval is obtained for the distribution of the Company's earnings. If the employee bonuses are settled through the issuance of common shares of the Company, the amount transferred from retained earnings is based on the par value of the common shares issued. The remuneration to directors and supervisors may not be settled through the issuance of common shares.

Under U.S. GAAP, remuneration to directors and supervisors should be recorded as compensation expense in the period when services are rendered. Also, employee bonus expense is initially accrued when services are rendered. When a distribution of bonus is approved by the shareholders in the subsequent year, an additional compensation expense is recorded for the difference between the amount initially recorded and the fair market value of shares granted to employees.

ROC GAAP**U.S. GAAP****Convertible Bonds — Convertible Feature**

When convertible securities are issued, ROC GAAP does not recognize or account for any beneficial conversion feature embedded in the securities.

Under U.S. GAAP, as prescribed in the Emerging Issues Task Force (“EITF”) Topic D-60, as amended by EITF 98-5, Accounting for the Issuance of Convertible Preferred Stock and Debt Securities with a Non-detachable Conversion Feature, such beneficial conversion features should be recognized and measured by allocating a portion of the proceeds equal to the intrinsic value of that feature to capital reserve. That amount should be calculated at the issuance date as the difference between the conversion price and the fair value of the common stock, multiplied by the number of shares into which the security is convertible (intrinsic value). As a result, a bond discount is recognized by allocating a portion of the proceeds equal to the intrinsic value of that feature to capital reserve.

Earnings Per Share

(a) Under ROC GAAP simple earnings per share is calculated by dividing net income by the weighted average number of shares outstanding during the year. Primary earnings per share are computed by taking simple earnings per share into consideration plus additional common share equivalents. Fully diluted earnings per share is calculated by taking primary earnings per share into consideration plus additional common shares that would have been outstanding if the dilutive share equivalents had been issued. The net income would also be adjusted for the interest derived from any underlying dilutive share equivalents. The weighted-average outstanding shares are restated for stock dividends issued and issuances of shares for employee bonuses.

(b) *Rights Issues*

There are no requirements under ROC GAAP to adjust earnings per share arising from the bonus element of a rights issue.

(a) Under U.S. GAAP, basic earnings per share are calculated by dividing net income by the weighted average number of shares outstanding during the year. Diluted earnings per share are calculated by taking into consideration additional common shares that would have been outstanding if the dilutive share equivalents had been issued. The net income would also be adjusted for the interest derived from any underlying dilutive share equivalents.

(b) *Rights issues*

Under U.S. GAAP, a rights issue with exercise price less than the fair value of the stock contains a bonus element that is similar to a stock dividend and is accounted for as such accordingly. As a result, the basic and diluted earnings per share shall be adjusted retroactively for the bonus element for all periods presented.

ROC GAAP**U.S. GAAP****Accounting for Pensions**

ROC Statement of Financial Accounting Standards (SFAS) No. 18, "Accounting for Pensions", is similar to U.S. SFAS No. 87 and provides accounting regulation regarding an employer's accounting for employee retirement plans, including pensions of companies covered by the Labors Standards Law which require contribution of a percentage of wages and salaries costs to an independent fund.

ROC SFSA No. 18 is effective for financial statements beginning in the year ended 31st December, 1995. However, net periodic pension cost is not calculated pursuant to an actuarial valuation until the year ending 31st December, 1996. Prior to 1996, pension expense under ROC GAAP was generally calculated as a fixed percentage of total annual salaries and wages.

Subsidiaries of listed companies (whether consolidated or not) must adopt this standard in the same period as the listed parent. No schedule has yet been set for implementation by other (i.e. unlisted) companies.

Under U.S. GAAP, companies have been required to recognize net periodic pension costs and related liabilities and assets based on actuarial valuations.

Principle of Consolidation

The consolidated financial statements include the accounts of the parent company and certain majority owned (50 per cent. or more) subsidiaries in accordance with the requirements of ROC Financial Accounting Standard ("FAS No. 7") and the regulations of the Taiwan Securities and Futures Commission ("SFC"). All inter-company accounts and transactions have been eliminated in the consolidated financial statements.

Pursuant to FAS No. 7 and the regulations of the SFC, if the total assets and operating revenues of a subsidiary are less than 10 per cent. of the total non-consolidated assets and operating revenue of the parent company, respectively, the subsidiary's financial statements may, at the option of the company, not be consolidated. Irrespective of the above test, when the total combined assets or operating revenue of all such non-consolidated subsidiaries constitute more than 30 per cent. of the parent company's total assets or operating revenue, then each individual subsidiary with total assets or operating revenue greater than 3 per cent. of the parent company's non-consolidated assets or operating revenue has to be included in the consolidation.

Under U.S. GAAP, there is no exclusion rule for consolidating majority owned (50 per cent. or more) subsidiaries.

ROC GAAP

U.S. GAAP

Reclassification of Certificates of Deposit

Under ROC GAAP, cash and cash equivalents include certificates of deposit.

Under U.S. GAAP, cash equivalents are short-term, highly liquid investments that are readily convertible to cash with original maturities of three months or less. Thus, certificates of deposit with original maturities of greater than three months are classified as cash equivalents under ROC GAAP but should be included in short-term investments for trading purpose under U.S. GAAP.

Gross Profit and Operating Income

Inventory loss provision and depreciation expenses from both idle assets and assets to be disposed are presented below the operating income subtotal in the statement of operations as permitted under ROC GAAP.

Under U.S. GAAP, the inventory provision and the depreciation expenses from both idle assets and assets to be disposed are included beyond the operating income subtotal in the statement of operations.

Income tax

Undistributed earnings generated after 1997 are subject to a 10 per cent. tax in compliance with the Income Tax Law of the ROC. Under ROC GAAP the 10 per cent. tax on undistributed earnings is recorded as an expense at the time shareholders resolve that its earnings shall be retained.

Under U.S. GAAP, the Company would measure its income tax expense in the period the earnings incurred, including the tax effects of temporary differences, using the tax rate that includes the tax on undistributed earnings.

INDEX TO FINANCIAL STATEMENTS

	<u>Page</u>
Report of Independent Auditors	F-3
Balance Sheets as of 31st December, 1999, 2000 and 2001	F-4
Statements of Income for the years ended 31st December, 1999, 2000 and 2001	F-6
Statements of Changes in Shareholders' Equity for the years ended 31st December, 1999, 2000 and 2001	F-7
Statements of Cash Flows for the years ended 31st December, 1999, 2000 and 2001	F-8
Notes to financial statements	F-10

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REPORT OF INDEPENDENT AUDITORS

The Board of Directors and Shareholders
Of King Yuan Electronics Co., Ltd.

We have audited the accompanying balance sheets of King Yuan Electronics Co., Ltd. as of 31st December, 1999, 2000 and 2001, and the related statements of income, changes in shareholders' equity, and cash flows for the years then ended. 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 generally accepted auditing standards 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 above present fairly, in all material respects, the financial position of King Yuan Electronics Co., Ltd. as of 31st December, 1999, 2000 and 2001, and the results of its operations and its cash flows for the years then ended, in conformity with generally accepted accounting principles in the Republic of China.

DIWAN, ERNST & YOUNG
CERTIFIED PUBLIC ACCOUNTANTS

Taipei, Taiwan
Republic of China
7th February, 2002

KING YUAN ELECTRONICS CO., LTD.**BALANCE SHEETS**
(Expressed in thousands)

		As of 31st December,			
	Notes	1999	2000	2001	
		NT\$	NT\$	NT\$	U.S.\$
Current assets					
Cash and cash equivalents	2, 4(1)	343,907	1,122,041	59,668	1,706
Restricted deposits-current	6	59,190	—	4,903	140
Short-term investments.	2	—	8,541	3,350	96
Notes receivable (Net)	2, 4(2)	70,300	100,580	46,041	1,316
Accounts receivable (Net)	2, 4(2), 6	371,296	1,281,248	567,974	16,237
Receivable from related parties	4(2), 5	152,693	73,376	82,807	2,367
Inventories (Net)	2, 4(3)	28,397	76,529	56,831	1,625
Deferred income tax (Net)	2, 4(20)	104,890	241,806	14,678	420
Other current assets		20,396	146,442	79,933	2,285
Total current assets		1,151,069	3,050,563	916,185	26,192
Long-term equity investments.					
	2, 4(4)	—	4,930	5,073	145
Property, plant and equipment					
	2, 4(5), 6				
Land		918,910	924,066	869,222	24,849
Buildings and facility.		257,261	1,637,419	3,185,688	91,072
Machinery and equipment.		3,265,919	7,388,822	12,667,241	362,128
Transportation equipment		11,223	15,314	15,687	449
Leased assets	2, 4(13)	—	494,736	737,954	21,096
Miscellaneous fixtures		22,887	74,415	80,174	2,292
Leasehold improvements		49,734	58,863	431	12
Office furniture.		18,621	119,107	232,172	6,637
Total Cost		4,544,555	10,712,742	17,788,569	508,535
Less: Accumulated depreciation		(593,539)	(1,631,353)	(3,694,634)	(105,621)
Plus: Prepayments on equipment		164,416	3,087,189	573,012	16,381
Construction in progress.		234,207	700,606	385,343	11,016
Net property, plant and equipment.		4,349,639	12,869,184	15,052,290	430,311
Other assets					
Leased assets to others.	4(6)	—	—	273,305	7,813
Idle assets	4(7)	—	—	245,347	7,014
Assets to be disposed of.	4(8)	—	—	650,826	18,606
Deposits out		5,946	10,459	4,605	132
Deferred assets	2	13,457	75,781	136,423	3,900
Deferred income tax (Net)	2, 4(20)	19,857	191,476	718,709	20,546
Restricted deposits-noncurrent.	6	887	1,387	1,000	29
Other.	4(9)	—	11,935	11,935	341
Total other assets		40,147	291,038	2,042,150	58,381
Total Assets.					
		5,540,855	16,215,715	18,015,698	515,029

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

KING YUAN ELECTRONICS CO., LTD.**BALANCE SHEETS (Continued)**
(Expressed in thousands)

	<i>Notes</i>	As of 31st December,			
		1999	2000	2001	
		NT\$	NT\$	NT\$	U.S.\$
Current liabilities					
Short-term loans	4(10)	220,199	1,776,464	1,502,572	42,955
Short-term notes	4(11)	—	—	99,825	2,854
Current portion of long-term loans	4(12)	—	222,372	1,060,258	30,311
Current portion of lease obligations	4(13)	—	156,313	240,241	6,868
Notes payable		89,769	341,621	315,218	9,011
Accounts payable		33,143	95,310	21,704	620
Payable from related parties	5	—	2,161	51,078	1,460
Payable to equipment suppliers		508,342	591,999	984,577	28,147
Income taxes payable	2, 4(20)	54,062	128,901	—	—
Accrued expenses and other current liabilities		<u>157,010</u>	<u>285,856</u>	<u>399,625</u>	<u>11,425</u>
Total current liabilities		<u>1,062,525</u>	<u>3,600,997</u>	<u>4,675,098</u>	<u>133,651</u>
Long-term Liabilities					
Long-term loans, less current portion	4(12)	1,363,370	3,107,628	4,698,906	134,331
Lease obligations, less current portion	2, 4(13)	<u>—</u>	<u>305,137</u>	<u>240,196</u>	<u>6,867</u>
Total long-term liabilities		<u>1,363,370</u>	<u>3,412,765</u>	<u>4,939,102</u>	<u>141,198</u>
Other Liabilities					
Accrued pension liabilities	2, 4(14)	<u>6,536</u>	<u>19,228</u>	<u>20,476</u>	<u>585</u>
Total other liabilities		<u>6,536</u>	<u>19,228</u>	<u>20,476</u>	<u>585</u>
Total Liabilities		<u>2,432,431</u>	<u>7,032,990</u>	<u>9,634,676</u>	<u>275,434</u>
Shareholders' Equity					
Common stock	4(15)	1,243,750	2,632,254	4,366,722	124,835
Capital reserve	4(16)	1,349,750	5,301,048	4,590,339	131,227
Legal reserve	4(17)	21,120	69,992	187,831	5,370
Retained earnings	4(18)	493,804	1,179,123	(764,467)	(21,854)
Cumulative translation adjustments	2	<u>—</u>	<u>308</u>	<u>597</u>	<u>17</u>
Total Shareholders' Equity		<u>3,108,424</u>	<u>9,182,725</u>	<u>8,381,022</u>	<u>239,595</u>
Total Liabilities and Shareholders' Equity		<u><u>5,540,855</u></u>	<u><u>16,215,715</u></u>	<u><u>18,015,698</u></u>	<u><u>515,029</u></u>

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

KING YUAN ELECTRONICS CO., LTD.**STATEMENTS OF INCOME**
(Expressed in thousands, except per share data)

	<i>Notes</i>	Year ended 31st December,			
		1999	2000	2001	
		NT\$	NT\$	NT\$	U.S.\$
Operating Revenues	2				
Sales revenue		1,755,115	4,225,455	3,970,868	113,518
Less: Sales allowances		<u>(10,141)</u>	<u>(43,881)</u>	<u>(93,570)</u>	<u>(2,675)</u>
Net operating revenues	2	1,744,974	4,181,574	3,877,298	110,843
Cost of goods sold		<u>(1,114,752)</u>	<u>(2,705,271)</u>	<u>(4,129,702)</u>	<u>(118,059)</u>
Gross Profit (Loss)		<u>630,222</u>	<u>1,476,303</u>	<u>(252,404)</u>	<u>(7,216)</u>
Operating Expenses	2				
Selling and administrative expenses		(103,864)	(255,083)	(378,584)	(10,823)
Research and development expenses		<u>(26,974)</u>	<u>(50,685)</u>	<u>(58,204)</u>	<u>(1,664)</u>
Total operating expenses		<u>(130,838)</u>	<u>(305,768)</u>	<u>(436,788)</u>	<u>(12,487)</u>
Operating Income (Loss)		<u>499,384</u>	<u>1,170,535</u>	<u>(689,192)</u>	<u>(19,703)</u>
Non-operating Income					
Interest income		6,320	39,793	8,472	242
Physical inventory gain		—	17	86	2
Foreign exchange gain		—	—	105,274	3,010
Gain on disposal of short-term investments		175	—	—	—
Gain on disposal of property, plant, and equipment		—	64	533	15
Reversals of market value decline of short-term investments		—	—	6,110	175
Other income		<u>4,845</u>	<u>3,177</u>	<u>32,634</u>	<u>933</u>
Total non-operating income		<u>11,340</u>	<u>43,051</u>	<u>153,109</u>	<u>4,377</u>
Non-operating Expenses					
Interest expense		(43,715)	(169,871)	(354,336)	(10,130)
Loss on decline in market value of short-term investments		—	(7,281)	—	—
Net loss from equity investment	4(4)	—	(351)	(146)	(4)
Foreign exchange loss		(11,692)	(25,171)	—	—
Loss on disposal of short-term investments		—	—	(4,214)	(120)
Loss on disposal of property, plant, and equipment		(1,099)	(6,895)	(23,553)	(673)
Inventory loss provision		—	—	(4,088)	(117)
Other losses		<u>(147)</u>	<u>(898)</u>	<u>(168,686)</u>	<u>(4,822)</u>
Total non-operating expenses		<u>(56,653)</u>	<u>(210,467)</u>	<u>(555,023)</u>	<u>(15,866)</u>
Income (Loss) Before Income Taxes		454,071	1,003,119	(1,091,106)	(31,192)
Income Tax Benefit	2, 4(20)	<u>34,651</u>	<u>175,316</u>	<u>299,455</u>	<u>8,561</u>
Net Income (Loss)		<u><u>488,722</u></u>	<u><u>1,178,435</u></u>	<u><u>(791,651)</u></u>	<u><u>(22,631)</u></u>
Earnings Per Share					
Net Income (in New Taiwan dollars)	2, 4(19)	<u>1.94</u>	<u>3.06</u>	<u>(1.81)</u>	<u>(0.05)</u>

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

KING YUAN ELECTRONICS CO., LTD.**STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY**
(Expressed in thousands)

	Common Stock	Capital Reserve	Legal Reserve	Retained Earnings	Cumulative Translation Adjustment	Total
	NT\$	NT\$	NT\$	NT\$	NT\$	NT\$
Balance as of 1st January, 1999	700,000	319,750	7,152	144,050	—	1,170,952
Appropriation and distribution of 1998 earnings:						
Appropriation for legal reserve	—	—	13,968	(13,968)	—	—
Stock dividends	105,000	—	—	(105,000)	—	—
Bonus to employee transferred to capital stock	18,750	—	—	(18,750)	—	—
Directors' and supervisors' remuneration	—	—	—	(1,250)	—	(1,250)
Capital reserve transferred to common stock	70,000	(70,000)	—	—	—	—
Stock issuance for cash	350,000	1,100,000	—	—	—	1,450,000
Net income for 1999	—	—	—	488,722	—	488,722
Balance as of 31st December, 1999	<u>1,243,750</u>	<u>1,349,750</u>	<u>21,120</u>	<u>493,804</u>	<u>—</u>	<u>3,108,424</u>
Appropriation and distribution of 1999 earnings:						
Appropriation for legal reserve	—	—	48,872	(48,872)	—	—
Stock dividends	373,125	—	—	(373,125)	—	—
Bonus to employee transferred to capital stock	66,629	—	—	(66,629)	—	—
Directors' and supervisors' remuneration	—	—	—	(4,442)	—	(4,442)
Capital reserve transferred to common stock	248,750	(248,750)	—	—	—	—
Stock issuance for cash	700,000	4,200,000	—	—	—	4,900,000
Transfer of gain from disposal of property, plant and equipment to capital reserve	—	48	—	(48)	—	—
Cumulative translation adjustment	—	—	—	—	308	308
Net income for 2000	—	—	—	1,178,435	—	1,178,435
Balance as of 31st December, 2000	<u>2,632,254</u>	<u>5,301,048</u>	<u>69,992</u>	<u>1,179,123</u>	<u>308</u>	<u>9,182,725</u>
Appropriation and distribution of 2000 earnings:						
Appropriation for legal reserve	—	—	117,839	(117,839)	—	—
Stock dividends	868,644	—	—	(868,644)	—	—
Bonus to employee transferred to capital stock	155,115	—	—	(155,115)	—	—
Directors' and supervisors' remuneration	—	—	—	(10,341)	—	(10,341)
Capital reserve transferred to common stock	710,709	(710,709)	—	—	—	—
Cumulative translation adjustment	—	—	—	—	289	289
Net loss for 2001	—	—	—	(791,651)	—	(791,651)
Balance as of 31st December, 2001 (in NT\$)	<u>4,366,722</u>	<u>4,590,339</u>	<u>187,831</u>	<u>(764,467)</u>	<u>597</u>	<u>8,381,022</u>
Balance as of 1st January, 2001 (in U.S.\$)	<u>124,835</u>	<u>131,227</u>	<u>5,370</u>	<u>(21,854)</u>	<u>17</u>	<u>239,595</u>

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

KING YUAN ELECTRONICS CO., LTD.**STATEMENTS OF CASH FLOWS**
(Expressed in thousands)

	Year ended 31st December,			
	1999	2000	2001	
	NT\$	NT\$	NT\$	U.S.\$
Cash flows from operating activities:				
Net income (loss)	488,722	1,178,435	(791,651)	(22,631)
Adjustments to reconcile net income to net cash provided by operating activities:				
Depreciation	390,191	1,073,145	2,283,237	65,273
Amortization	6,251	20,236	65,621	1,876
Bad debt expense	—	—	12,002	343
Deferred income taxes	(87,414)	(308,535)	(300,105)	(8,579)
Net loss from equity investment	—	351	146	4
Physical inventory gain	—	(17)	(86)	(2)
Inventory loss provision	—	—	4,088	117
Net loss on disposal of property, plant, and equipment	1,099	6,831	23,020	658
Loss on (Reversals of) decline in market value of short-term investments	—	7,281	(6,110)	(175)
Loss on disposal of short-term investments	—	—	4,214	120
(Increase) decrease in notes receivable	(35,355)	(30,280)	54,539	1,559
(Increase) decrease in accounts receivable	(198,821)	(909,952)	701,272	20,048
(Increase) decrease in receivables from related parties	(113,983)	79,317	(9,431)	(270)
(Increase) decrease in inventories	(2,241)	(48,115)	15,696	449
(Increase) decrease in other current assets	(17,112)	(126,046)	66,509	1,901
Increase (decrease) in notes payable	30,740	251,852	(26,403)	(755)
Increase (decrease) in accounts payable	(2,469)	62,167	(73,606)	(2,104)
Increase (decrease) in income taxes payable	34,712	74,839	(128,901)	(3,685)
Increase in accrued expenses and other current liabilities	85,000	131,007	152,345	4,355
Increase in accrued pension liability	2,732	12,692	1,248	36
Net cash provided by operating activities	<u>582,052</u>	<u>1,475,208</u>	<u>2,047,644</u>	<u>58,538</u>
Cash flows from investing activities:				
(Increase) decrease in restricted deposits	(17,077)	58,690	(4,516)	(129)
(Increase) decrease in short-term investments	—	(15,822)	7,087	203
Acquisition of property, plant and equipment	(3,260,910)	(9,521,640)	(5,283,694)	(151,049)
Increase in deferred assets	(7,222)	(82,560)	(126,263)	(3,610)
Cash received from disposal of property, plant and equipment	2,108	5,777	17,431	498
(Increase) decrease in deposits out	(3,576)	(4,513)	5,854	167
Acquisition of long-term investments	—	(4,973)	—	—
Acquisition of other assets	—	(11,935)	—	—
Net cash used in investing activities	<u>(3,286,677)</u>	<u>(9,576,976)</u>	<u>(5,384,101)</u>	<u>(153,920)</u>

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

KING YUAN ELECTRONICS CO., LTD.**STATEMENTS OF CASH FLOWS (Continued)**
(Expressed in thousands)

	Year ended 31st December,			
	1999	2000	2001	
	NT\$	NT\$	NT\$	U.S.\$
Cash flows from financing activities:				
Increase (decrease) in short-term loans	157,057	1,556,264	(273,892)	(7,830)
Increase in short-term notes	—	—	99,825	2,854
Increase in long-term loans	1,363,370	1,966,630	2,429,164	69,444
Increase in lease obligations	—	461,450	18,987	543
Cash received from issuance of stock	1,450,000	4,900,000	—	—
Directors' and supervisors' remuneration paid	(1,250)	(4,442)	—	—
Net cash provided by financing activities	<u>2,969,177</u>	<u>8,879,902</u>	<u>2,274,084</u>	<u>65,011</u>
Net increase in cash and cash equivalents	264,552	778,134	(1,062,373)	(30,371)
Cash and cash equivalents at the beginning of year	<u>79,355</u>	<u>343,907</u>	<u>1,122,041</u>	<u>32,077</u>
Cash and cash equivalents at the end of year	<u>343,907</u>	<u>1,122,041</u>	<u>59,668</u>	<u>1,706</u>
Supplemental disclosures of cash flows information:				
Interest paid during the year (excluding capitalized interest)	<u>41,413</u>	<u>155,047</u>	<u>362,606</u>	<u>10,366</u>
Income tax paid during the year	<u>17,822</u>	<u>58,421</u>	<u>130,723</u>	<u>3,737</u>
Investing activities partially paid by cash				
Acquisition of property, plant and equipment	3,641,831	9,605,297	5,676,272	162,272
Increase in payables to equipment supplier	(380,921)	(83,657)	(392,578)	(11,223)
Cash received from disposal of property, plant and equipment	<u>3,260,910</u>	<u>9,521,640</u>	<u>5,283,694</u>	<u>151,049</u>
Financing activities not affecting cash flows				
Retained earnings transferred to stock dividends, bonus to employee and capital reserve to transferred common stock	<u>193,750</u>	<u>688,504</u>	<u>1,734,468</u>	<u>49,585</u>
Directors' and supervisors' remuneration payable	<u>—</u>	<u>—</u>	<u>10,341</u>	<u>295</u>
Cumulative translation adjustment	<u>—</u>	<u>308</u>	<u>289</u>	<u>8</u>
Current portion of long- term loans and lease obligations	<u>—</u>	<u>378,685</u>	<u>1,300,499</u>	<u>37,179</u>

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

KING YUAN ELECTRONICS CO., LTD.**NOTES TO FINANCIAL STATEMENTS****1. HISTORY**

KING YUAN ELECTRONICS CO., LTD. (the “**Company**”) was incorporated under the Company Law of the Republic of China in July 1987. The Company major business activity is to engage in the business of testing and assembly service, and manufacture and selling IC Monitoring Burn-In machinery.

2. SUMMARY OF ACCOUNTING POLICIES**Cash and Cash Equivalents**

Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash, and so near their maturity that they present insignificant risk of changes in interest rates. Commercial papers, negotiable certificates of deposit, and bank acceptances with original maturities of three months or less at the investment date are considered to be cash equivalents.

Translation of Foreign Currency Transactions

The Company maintains its accounting records in New Taiwan dollars (“**NT Dollars**” or “**NT\$**”), Transactions denominated in foreign currencies are recorded in New Taiwan dollars using the exchange rates in effect at the dates of transactions. Assets and liabilities denominated in foreign currencies are translated into NT Dollars using the exchange rates in effect at the balance sheet date. Foreign exchange gains or losses are included in other incomes or losses. Exchange gains or losses on inter-company foreign currency transactions of a capital or long-term nature are included in cumulative translation adjustments, a separate component of shareholders’ equity.

Convenience Translation into U.S. Dollars

The Company prepares its financial statements in New Taiwan (“**NT**”) dollars, its reporting currency. The United States (“**U.S.**”) dollar amounts disclosed in the financial statements as of and for the year ended 31st December, 2001, are presented solely for the convenience of the reader and were translated at the average of buying and selling rates of NT\$34.98 to U.S.\$1.00 in effect on 31st December, 2001. Such translation amounts are unaudited and it should not be construed that the NT dollar amounts represent, or have been, or could be, converted into U.S. dollars at that or any other rate.

Short-term Investments

Short-term Investments are recorded at cost when acquired and are stated at the lower of aggregate cost or market value at the balance sheet date. The market value of listed equity securities or closed-end funds is determined by the average closing price during the last month of the fiscal year. The market value for open-ended funds is determined by their equity value is reported as a loss in the current year. In subsequent periods, recoveries of 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 collectibility and aging analysis of notes and accounts receivable and other receivables.

Inventories

Inventories are recorded at cost when acquired and stated at the lower of aggregate cost, based on weighted average method, or market value at the balance sheet date. The market values of raw materials and supplies are determined on the basis of replacement cost while finished goods on net realizable value. The allowance for loss on decline in market value and obsolescence is provided, when necessary.

Long-term Equity Investments

- (1) Investment income or loss from investments in both listed and unlisted companies is accounted for under the equity method provided that the Company owns over 20 per cent. of the voting outstanding shares of the investee company and has significant influence on operational decisions of the investee company.
- (2) Consolidated financial statements are prepared if the Company owns more than 50 per cent. of the invested company's shares. However, the financial statements of any subsidiary in which the total assets and total revenue for the current year are less than 10 per cent. of the Company's total assets and operating revenues are not included in the consolidated financial statements.

Property, Plant and Equipment

- (1) Property, plant and equipment are accounted at cost. Depreciation is provided on the straight-line basis over the following useful lives:

Buildings and facility	3 to 30 years
Machinery and equipment	3 to 10 years
Transportation equipment	5 years
Leased assets	4 to 5 years
Miscellaneous fixtures	3 to 10 years
Leasehold improvements	2 to 3 years
Office furniture	3 to 10 years

- (2) Improvements and replacements are capitalized and depreciated over their estimated useful lives while ordinary repairs and maintenance are expensed as incurred. When property, plant and equipment are disposed of, their original cost and accumulated depreciation are written off and related gain, net of income tax, is transferred to capital reserve in the current year. While, gain from disposal of property, plant and equipment shall not be transferred to capital reserve starting 2001 in accordance with an amendment to Taiwan's Company Law.

Lease agreement

Provided a lease agreement meets the capitalization criteria, the present value of the minimum lease payments net of executory costs is capitalized as an asset along with a corresponding liability. Leased equipments are depreciated on the straight-line basis over their estimated useful lives. The lease obligation is amortized over lease term using effective interest method. A lease that does not qualify as a capital lease is classified as an operating lease and the lease payment is recorded as rental expense.

Deferred Assets

Deferred assets are originally recorded at cost and amortized over their estimated useful lives, usually 1 to 3 years, using the straight-line method.

Revenue Recognition

Revenue is recognized when it is realized or realizable and when it is earned. Revenue from the sale of product is recognized when ownership is transferred to the customer, which normally occurs when shipment is made.

Capital Expenditures vs. Revenue Expenses

If expenditures increase the future service potential of plant assets, the expenditures are capitalized, while the others are expensed as incurred.

Income Tax

Provision for income tax includes deferred tax resulting from temporary differences and investment tax credits. Deferred tax assets and liabilities are recognized for the expected tax consequences of temporary differences between the tax bases of assets and liabilities and their reported amounts in the financial statements using enacted tax rates and laws that will be in effect when the difference is expected to reverse. Valuation allowance on deferred tax assets is provided to the extent that it is more likely than not that the tax benefits will not be realized. Over or under provision of prior years' income tax liabilities are included in the current year's income tax expense.

Undistributed earnings generated after 1998 would be subject to a 10 per cent. tax in compliance with ROC income tax law. The 10 per cent. tax on undistributed earnings is recorded as an expense at the time shareholders resolve that its earnings shall be retained.

Pension Plan

The Company has a funded defined benefit pension plan covering all regular employees. The net pension cost is computed based on an actuarial valuation in accordance with the provision of ROC FAS No. 18, which requires consideration of pension cost components such as service cost, interest cost, expected return on plan assets and amortization of net obligation at transition. The unrecognized net asset or obligation at transition is amortized on the straight-line basis over the employees average remaining service period (15 years). The prior service cost and gain or losses from the plan asset are amortized on the straight-line basis over the employees average remaining service period (11 years). The pension fund managed by an independently administered pension fund association.

Simple Earnings Per Share

Simple earnings per share are calculated by dividing net income by weighted average number of shares outstanding during the year. The weighted-average outstanding shares are restated for stock dividends issued.

3. REASONS AND EFFECT OF CHANGE IN ACCOUNTING PRINCIPLES

A transfer of gain on disposal of property, plant and equipment from earnings to additional paid-in-capital is required under ROC Company Law prior to 1st January, 2001. Pursuant to an amendment to the Company Law, a company shall not make such transfer for the gain on disposal of property, plant and equipment generated in 2001. There is no significant effect on the Company's financial statements as of 31st December, 2001 due to such change in accounting principle.

4. CONTENTS OF SIGNIFICANT ACCOUNTS

(1) Cash and Cash Equivalents

	As of 31st December,			
	1999	2000	2001	
	NT\$'000	NT\$'000	NT\$'000	U.S.\$'000
Cash on hand	3,100	366	366	10
Checking and saving accounts	340,807	990,675	59,302	1,696
Time Deposit	—	131,000	—	—
Total	<u>343,907</u>	<u>1,122,041</u>	<u>59,668</u>	<u>1,706</u>

(2) Notes Receivable and Accounts Receivable

	As of 31st December,			
	1999	2000	2001	
	NT\$'000	NT\$'000	NT\$'000	U.S.\$'000
Notes receivable	70,300	100,580	46,041	1,316
Allowance for doubtful accounts	—	—	—	—
Net	<u>70,300</u>	<u>100,580</u>	<u>46,041</u>	<u>1,316</u>
	As of 31st December,			
	1999	2000	2001	
	NT\$'000	NT\$'000	NT\$'000	U.S.\$'000
Accounts receivable	371,494	1,281,446	585,463	16,737
Secured accounts receivable	—	—	38,511	1,101
Loan on security	—	—	(30,800)	(880)
Total	371,494	1,281,446	593,174	16,958
Allowance for doubtful accounts	(198)	(198)	(12,200)	(349)
Allowance for sales discounts	—	—	(13,000)	(372)
Net	<u>371,296</u>	<u>1,281,248</u>	<u>567,974</u>	<u>16,237</u>

Please refer to Note 6 for accounts receivable pledged as collateral.

Receivable from Related Parties

	As of 31st December,			
	1999	2000	2001	
	NT\$'000	NT\$'000	NT\$'000	U.S.\$'000
Notes Receivable	82,583	3,918	1,253	36
Accounts receivable	<u>70,110</u>	<u>69,458</u>	<u>81,554</u>	<u>2,331</u>
Total	152,693	73,376	82,807	2,367
Allowance for doubtful as accounts	—	—	—	—
Net	<u>152,693</u>	<u>73,376</u>	<u>82,807</u>	<u>2,367</u>

(3) Inventories

	As of 31st December,			
	1999	2000	2001	
	NT\$'000	NT\$'000	NT\$'000	U.S.\$'000
Raw materials and Supplies	15,332	55,151	44,064	1,260
Work in process	13,847	22,160	8,383	240
Finished goods	—	—	9,254	264
Total	29,179	77,311	61,701	1,764
Allowance for loss on decline in market value and obsolescence.	(782)	(782)	(4,870)	(139)
Net	28,397	76,529	56,831	1,625

The insurance coverage over inventories amounted to approximately NT\$100,000,000, approximately NT\$300,000,000 and approximately NT\$300,000,000 as of 31st December, 1999, 2000 and 2001, respectively.

Inventories were not pledged.

(4) Long-term Equity Investments

Investee Company	Ownership %	As of 31st December,			
		1999	2000	2001	
		NT\$'000	NT\$'000	NT\$'000	U.S.\$'000
Investments accounted for under equity method:					
KYEC USA CORP.	100	—	4,930	5,073	145

Investment loss recorded under equity method totaled approximately NT\$351,000 and approximately NT\$146,000 for the year ended 31st December, 2000 and 2001, respectively.

Long-term investments were not pledged as of 31st December, 2000 and 2001.

The Company did not prepare the consolidated financial statements as of and for the two years ended 31st December, 2000 and 2001 and any period thereof according to ROC's consolidation rule.

(5) Property, Plant and Equipment

Total interest amounted (including capitalized interest) to approximately NT\$49,238,000, approximately NT\$169,871,000 and approximately NT\$421,676,000 for the years ended 31st December, 1999, 2000 and 2001, respectively. Total capitalized interest and the interest rates used were as follows:

	For the year ended 31st December,			
	1999	2000	2001	
	NT\$'000	NT\$'000	NT\$'000	U.S.\$'000
Capitalized interest	5,523	—	67,340	1,925
Interest rate used.	6.00%	—	6.48%	6.48%

The insurance coverage over property, plant and equipment amounted to approximately NT\$2,606,652,000, approximately NT\$9,675,259,000 and approximately NT\$14,562,064,000 as of 31st December, 1999, 2000 and 2001, respectively.

Please refer to Note 6 for property, plant and equipment pledged as collateral.

(6) Leased Assets To Others

	As of 31st December,			
	1999	2000	2001	
	NT\$'000	NT\$'000	NT\$'000	U.S.\$'000
Land	—	—	54,844	1,568
Buildings and facility.	—	—	141,519	4,046
Machinery and equipment.	—	—	148,233	4,238
Leasehold improvements	—	—	76	2
Miscellaneous fixtures	—	—	18	—
Total	—	—	344,690	9,854
Accumulated depreciation.	—	—	(71,385)	(2,041)
Net	—	—	273,305	7,813

The depreciation of leased assets, recorded in non-operating expenses, amounted to approximately NT\$23,835,000 for the year ended 31st December, 2001.

(7) Idle Assets

	As of 31st December,			
	1999	2000	2001	
	NT\$'000	NT\$'000	NT\$'000	U.S.\$'000
Cost:				
Buildings and facility.	—	—	164,055	4,690
Machinery and equipment.	—	—	152,799	4,368
Total	—	—	316,854	9,058
Accumulated depreciation:				
Buildings and facility.	—	—	(4,925)	(141)
Machinery and equipment.	—	—	(66,582)	(1,903)
Total	—	—	(71,507)	(2,044)
Net	—	—	245,347	7,014

The depreciation of idle assets, included in non-operating expenses, amounted to approximately NT\$36,597,000 for the year ended 31st December, 2001.

(8) Assets To Be Disposed

The Company has entered into an agreement to sell back certain machinery to the supplier, Advantest Taiwan, Inc, in November 2001. The machinery was recorded in “assets to be disposed” as of 31st December, 2001 because the title of underlying machinery has not been passed to Advantest yet. According to the sale-back agreement, the Company has to compensate the supplier by approximately NT\$102,092,000. The loss has been recognized in non-operating loss.

	As of 31st December,			
	1999	2000	2001	
	NT\$'000	NT\$'000	NT\$'000	U.S.\$'000
Machinery and equipment.	—	—	298,219	8,525
Prepayments on equipment	—	—	367,777	10,514
 Total	—	—	665,996	19,039
 Less: Accumulated depreciation.	—	—	(12,472)	(356)
 Book value.	—	—	653,524	18,683
Less: Allowance for loss of machinery and equipment on decline in market value . .	—	—	(2,698)	(77)
	—	—	650,826	18,606

(9) Other Assets — Land

The Company purchased several pieces of agricultural land, mainly located in Miao Li County, in 2000. However, due to limitation in trading, the Company can't own the title of the agricultural land. Instead, the title has been temporarily registered under the name of C.K. Lee, the chairman of the Company. The underlying land was accounted for under other assets, and security has been set forth to protect the Company's right to the land. Carrying value of the land amounted to approximately NT\$11,935,000 as of 31st December, 2001.

(10) Short-term Loans

	As of 31st December,			
	1999	2000	2001	
	NT\$'000	NT\$'000	NT\$'000	U.S.\$'000
Letter of credit	170,055	1,776,464	173,598	4,963
Working capital loans	50,144	—	1,328,974	37,992
 Total	220,199	1,776,464	1,502,572	42,955
 Interest rates.	0.9%–7.21%	0.99%–8.0867%	0.78%–7.60%	0.78%–7.60%

The Company's unused short-term lines of credits amounted to approximately NT\$452,301,000, approximately NT\$1,143,596,000 and approximately NT\$1,534,628,000 as of 31st December, 1999, 2000 and 2001, respectively.

Please refer to Note 6 for assets pledged for short-term loans.

(11) Short-term Notes

	As of 31st December,			
	1999	2000	2001	
	NT\$'000	NT\$'000	NT\$'000	U.S.\$'000
Secured short-term notes	—	—	100,000	2,859
Less: discount.	—	—	(175)	(5)
Net	—	—	99,825	2,854
Interest rates.	—	—	4.48%	4.48%

Please refer to Note 5(5) for assets pledged for long-term notes.

(12) Long-term Loans

Secured	Interest rates			Balance			
	As of 31st December,						
	1999	2000	2001	1999	2000	2001	
	%	%	%	NT\$'000	NT\$'000	NT\$'000	U.S.\$'000
Medium-term loan from Chiao Tung Bank	6.760	6.755	6.475	360,000	360,000	290,700	8,311
Repayable in 20 quarterly installments from January 2001 to January 2006 with interest due monthly							
Medium-term loan from Chiao Tung Bank	—	6.755	6.475	—	255,000	400,000	11,435
Repayable in 20 quarterly installments from October 2002 to October 2007 with interest due monthly							
Medium-term loans from 5 banks	6.650	6.655	4.305	655,000	995,000	918,464	26,257
Repayable in 13 quarterly installments from September 2001 to September 2004 (Remark 1 and 2) with interest due monthly							
Medium-term loans from 17 banks	—	7.200	3.980	—	1,620,000	4,000,000	114,351
Repayable in 7 semi-annual installments from November 2002 to November 2005 with interest due monthly (Remark 3)							
Medium-term loan from Hsinchu International Bank.	—	—	6.900	—	—	150,000	4,288
Repayable in 16 quarterly installments from June 2002 to June 2006 with interest due monthly							
Medium-term loan from Industrial Bank of Taiwan	4.780–7.00	7.500	—	348,370	100,000	—	—
Repayable in full at maturity with interest due monthly.							
Total long-term loans.	—	—	—	1,363,370	3,330,000	5,759,164	164,642
Less: Current portion.	—	—	—	—	(222,372)	(1,060,258)	(30,311)
Net	—	—	—	1,363,370	3,107,628	4,698,906	134,331

Remark 1: Repayable of 4 quarterly installments totaling approximately NT\$306,144,000 due within the period from 20th December, 2001 to 20th September, 2002 has been contractually extended and will be repaid in full on 15th November, 2002 with the condition that the Company shall repay no less than 50 per cent. of any funds raised from capital market at any time during the period from 20th December, 2001 to 15th November, 2002. Repayment shall be made to the banks within ten business days from completion of raising funds.

Remark 2: In terms of the loan agreement entered into between and by the Company and 5 banks, including China Development Industrial Bank, the Company's certain financial positions as of each year-end in the period from 2001 through 2004 shall be maintained as follows. Otherwise, the Company shall raise funds, by September of the following year of incompliance, by offering rights for cash or other financing instruments to the extent the terms can be complied.

(a) Ratio of current assets to current liabilities at no less than 100 per cent.;

(b) Ratio of debt to equity at no more than 100 per cent.;

Failing to comply with the above conditions, the Company will be subject to additional quarterly compensatory payments in the annual rate of 0.1 per cent.

Remark 3: In terms of the loan agreement entered into between and by the Company and 17 banks, including China Development Industrial Bank, the Company's certain financial positions as of each year-end over the duration of loan shall be maintained as follows. Otherwise, the Company shall raise funds, by September of the following year of incompliance, by offering rights for cash or other financing instruments to the extent the terms can be complied.

(a) Ratio of current assets to current liabilities at no less than 100 per cent.;

(b) Ratio of debt to equity at no more than 100 per cent.;

(c) Net worth of tangible assets at no less than NT\$7 billion; and

(d) Times of earnings before interest charges and income tax over interest charges at

(i) No less than 2 at all times from the date of this agreement through 31st December, 2002; and

(ii) No less than 3 for years since 2003.

Failing to comply with the above conditions, the Company will be subject to additional quarterly compensatory payments of the annual rate of 0.1 per cent.

The additional compensatory payment incurred due to the incompliance with debt covenants totaled to approximately NT\$3,992,000 for the year ended 31st December, 2001. Also, please refer to Note 6 for assets pledged for long-term loans.

(13) Lease Obligations

The Company entered into a lease agreement for equipment with certain suppliers. The lease term is from 1st May, 2000 to 15th May, 2004. The agreement states that the Company shall not remodel the equipment without permission from the lessor or lease the equipment to third parties. The leases provide for a bargain purchase option equal to \$1 at the end of the lease term. Cost of the leased equipment amounted to approximately NT\$494,736,000 and approximately NT\$737,954,000 as of 31st December, 2000 and 2001 respectively.

	As of 31st December,			
	1999	2000	2001	
	NT\$'000	NT\$'000	NT\$'000	U.S.\$'000
Lease obligations	—	521,176	524,350	14,990
Less: Discount	—	(59,726)	(43,913)	(1,255)
Net	—	461,450	480,437	13,735
Less: Current portion	—	(156,313)	(240,241)	(6,868)
Long-term portion	—	305,137	240,196	6,867

Lease obligations are repayable in 36 monthly installments starting the beginning of lease.

(14) Pension Fund

The components of net periodic pension cost were as follows:

	For the year ended 31st December,			
	1999	2000	2001	
	NT\$'000	NT\$'000	NT\$'000	U.S.\$'000
Service cost	6,850	27,699	22,079	631
Interest cost	1,236	1,813	4,189	120
Expected return on plan assets	(209)	(564)	(1,341)	(38)
Amortization	758	758	1,482	42
Net periodic pension cost	<u>8,635</u>	<u>29,706</u>	<u>26,409</u>	<u>755</u>

The funding status of pension plan is listed as follows:

	As of 31st December,			
	1999	2000	2001	
	NT\$'000	NT\$'000	NT\$'000	U.S.\$'000
Vested benefit obligation	52	—	—	—
Non-vested benefit obligation	<u>11,275</u>	<u>24,466</u>	<u>40,454</u>	<u>1,156</u>
Accumulated benefit obligation	11,327	24,466	40,454	1,156
Effect on projected salary increase	<u>16,561</u>	<u>45,349</u>	<u>37,027</u>	<u>1,059</u>
Projected benefit obligation	27,888	69,815	77,481	2,215
Market-related value of plan assets	<u>(8,675)</u>	<u>(22,343)</u>	<u>(49,211)</u>	<u>(1,407)</u>
Funded status	19,213	47,472	28,270	808
Unrecognized transition obligation	(9,854)	(9,096)	(8,338)	(238)
Unrecognized gain or loss	<u>(1,965)</u>	<u>(14,945)</u>	<u>3,215</u>	<u>92</u>
Accrued pension cost per actuarial report	7,394	23,431	23,147	662
Account Payable	(669)	(2,242)	(3,264)	(94)
Deposit in transit	—	(2,195)	—	—
Over (less) accrued	<u>(189)</u>	<u>234</u>	<u>593</u>	<u>17</u>
Accrued pension liability	<u>6,536</u>	<u>19,228</u>	<u>20,476</u>	<u>585</u>

The actuarial assumptions were as follows:

	For the year ended 31st December,		
	1999	2000	2001
Discount rate	6.50%	6.00%	4.50%
Rate of increase in future compensation levels	4.50%	5.00%	3.00%
Expected long-term rate on plan assets	6.50%	6.00%	4.50%

(15) Common Stock

On 20th April, 1999, the Company's shareholders resolved in the annual general meeting to issue 1,875,000 common shares in settlement of 1998 employee bonus. In addition, the shareholders also resolved to declare a 15 per cent. stock dividend, which resulted in the issuance of 10,500,000 shares, and to transfer NT\$70,000,000 from capital reserve to capital stock, which resulted in an issuance of 7,000,000 shares.

Following the resolution of the shareholders' meeting on 20th April, 1999, the Board of Directors effected a rights offering for an issuance of 10,000,000 common shares at NT\$30 per share. As a result of this rights offering, the Company issued 10,000,000 shares for a total consideration of NT\$300,000,000 in 6th July, 1999.

On 6th October, 1999, the Board of Directors also effected a rights offering for an issuance of 25,000,000 common shares at NT\$46 per share. As a result of this rights offering, the Company issued 25,000,000 shares for a total consideration of NT\$1,150,000,000 in 11th November, 1999.

Following the resolution of Shareholders' Meeting on 10th April, 2000, the Company increased its authorized capital to NT\$5,600,000,000, divided into 560,000,000 shares, each share at par of NT\$10. The shareholders further resolved in the meeting to issue 6,662,946 shares in settlement of 1999 employee bonus and to declare a 30 per cent. stock dividend, which resulted in an issuance of 37,312,500 shares. The Shareholders' Meeting also resolved to transfer approximately NT\$248,750,000 from capital reserve to capital stock, which resulted in an issuance of 24,875,000 shares.

Following the resolution of the shareholders' meeting on 10th April, 2000, the Board of Directors effected a rights offering for an issuance of 70,000,000 common shares at NT\$70 per share. As a result of this rights offering, the Company issued 70,000,000 shares for a total consideration of NT\$4,900,000,000 in 12th June, 2000.

Following the resolution of Shareholders' Meeting on 12th March, 2001, the Company increased its authorized capital to NT\$7,000,000,000. The shareholders further resolved in the meeting to issue 15,511,500 shares in settlement of 2000 employee bonus and to declare a 33 per cent. stock dividend, which resulted in an issuance of 86,864,398 shares. The Shareholders' Meeting also resolved to transfer approximately NT\$710,709,000 from capital reserve to capital stock, which resulted in an issuance of 71,070,870 shares.

As of 31st December, 2001, the Company's authorized and issued common stock amounted to NT\$7,000,000,000 and approximately NT\$4,366,722,000 divided into 700,000,000 shares and 436,672,214 shares, respectively, each at par of NT\$10.

(16) Capital Reserve

	As of 31st December,			
	1999	2000	2001	
	NT\$'000	NT\$'000	NT\$'000	U.S.\$'000
Additional paid-in capital	1,349,750	5,301,000	4,590,291	131,226
Gain on disposal of property, plant, and equipment	—	48	48	1
Total	<u>1,349,750</u>	<u>5,301,048</u>	<u>4,590,339</u>	<u>131,227</u>

According to the ROC Company Law, capital reserve shall be exclusively used to cover accumulated deficits when the legal reserve is insufficient to cover the deficits or distribution of stock dividends.

(17) Legal Reserve

According to the ROC Company Law, 10 per cent. of the Company's net income, after deducting previous years' losses, if any, is appropriated as legal reserve prior to any distribution until such reserve is equal to the Company's paid-in capital. When the legal reserve is equal to 50 per cent. of the paid-in stock, 50 per cent. of such reserve may be distributed to the Company's shareholders through the issuance of additional common share.

(18) Income Distributions

The Company's articles of incorporation provide that the net income, after deducting the previous years' losses and the appropriation to the legal and special reserves ("Distributable Earnings"), may be appropriated or distributed proportionally as follows:

- (1) Dividend to shareholders at 84 per cent. of the Company's Distributable Earnings;
- (2) Employee bonuses at 15 per cent. of the Company's Distributable Earnings; and
- (3) Remuneration for directors and supervisors' services at 1 per cent.

(19) Earnings Per Share (in shares)

	For the year ended 31st December,		
	1999	2000	2001
Common shares outstanding, beginning	70,000,000	124,375,000	263,225,446
Stock issuance for cash on 6th July, 1999.	4,904,110	—	—
Stock dividend declared, employee bonus shares and capital reserve transferred to common shares in 1999 (totally 27.68%)	19,375,000	—	—
Stock issuance for cash on 11th November, 1999	3,493,151	—	—
Stock dividend declared, employee bonus shares and capital reserve transferred to common shares in 2000 (totally 55.36%)	54,126,723	68,850,446	—
Stock issuance for cash on 12th June, 2000	—	38,825,137	—
Stock dividend declared, employee bonus shares and capital reserve transferred to common shares in 2001 (totally 65.89%)	<u>100,090,581</u>	<u>152,904,759</u>	<u>173,446,768</u>
Weighted average numbers of shares	<u>251,989,565</u>	<u>384,955,342</u>	<u>436,672,214</u>
Net Income (Loss) (in NT\$'000)	<u>488,722</u>	<u>1,178,435</u>	<u>(791,651)</u>
Earnings per share			
Net Income (Loss) (in NT\$)	<u>1.94</u>	<u>3.06</u>	<u>(1.81)</u>

(20) Income taxes

As of 31st December, 2001, unused tax credits available to reduce future tax payable were as follows:

Expiration Years	Unused Balances	
	NT\$'000	U.S.\$'000
2002	58,888	1,684
2003	66,893	1,912
2004	704,968	20,153
2005	<u>115,866</u>	<u>3,313</u>
Total	<u>946,615</u>	<u>27,062</u>

As of 31st December, 2001, net operating losses that can be carried forward for a period of five years were as follows:

Year incurred	Unused Balances	Unused Balances
	NT\$'000	U.S.\$'000
2001	<u>1,068,420</u>	<u>30,544</u>

The Company's income tax returns prior to 2000 have been finalized by tax authority.

At 31st December, 2001 the information related to imputation of shareholders' income tax is as follows:

	NT\$'000
Available shareholders' tax credit	<u><u>3,077</u></u>
Undistributed retained earnings for 2001	<u><u>(764,467)</u></u>
Expected rate of shareholders' tax credit	<u><u>—</u></u>

The components of deferred income tax assets and liabilities and income tax expense (benefit) are as follows:

(1)	As of 31st December,							
	1999		2000		2001			
	NT\$'000		NT\$'000		NT\$'000		U.S.\$'000	
Total deferred tax liabilities	2,030		—		18,255		522	
Total deferred tax assets.	126,777		433,282		1,251,642		35,782	
Valuation allowance for deferred tax assets.	—		—		500,000		14,294	
Temporary differences that generated deferred tax assets or liabilities:	Amount	Tax Effect	Amount	Tax Effect	Amount	Tax Effect	Amount	Tax Effect
Deductible temporary difference								
Recognition of employee welfare expense	6,275	1,569	10,200	2,550	7,120	1,780	204	51
Taxable temporary difference								
Recognition of unrealized foreign exchange gains.	8,120	2,030	—	—	73,018	18,255	2,087	522
Deductible temporary difference								
Recognition of unrealized loss of short-term investments on decline in market value	—	—	7,281	1,820	1,171	293	33	8
Deductible temporary difference								
Recognition of unrealized pension expense	—	—	14,507	3,627	15,756	3,939	450	113
Deductible temporary difference								
Recognition of unrealized foreign exchange loss	8,885	2,221	36,082	9,020	—	—	—	—
Deductible temporary difference								
Recognition of unrealized sales discounts	—	—	—	—	13,000	3,250	372	93
Deductible temporary difference								
Recognition of unrealized inventory provision	782	196	782	196	4,870	1,218	139	35
Deductible temporary difference								
Recognition of unrealized bad debt expense.	—	—	—	—	4,980	1,245	142	35
Deductible temporary difference								
Recognition of unrealized loss of machinery and equipment on decline in market value	—	—	—	—	2,698	674	77	19
Deductible temporary difference								
Recognition of unrealized loss on compensation of machinery and equipment	—	—	—	—	102,092	25,523	2,919	730
Deductible temporary difference								
Loss carry forward	—	—	—	—	1,068,420	267,105	30,544	7,636
Income tax credits.	122,791		416,069		946,615		27,062	

		As of 31st December,			
		1999	2000	2001	
		NT\$'000	NT\$'000	NT\$'000	U.S.\$'000
(2)	Deferred tax assets — current	106,920	241,806	91,821	2,625
	Valuation allowance for deferred tax assets — current	—	—	(58,888)	(1,683)
	Net deferred tax assets — current	106,920	241,806	32,933	942
	Net deferred tax liabilities — current . . .	(2,030)	—	(18,255)	(522)
	Net deferred tax assets and liabilities — current	104,890	241,806	14,678	420
(3)	Deferred tax assets — noncurrent	19,857	191,476	1,159,821	33,157
	Valuation allowance for deferred tax assets — noncurrent	—	—	(441,112)	(12,611)
	Net deferred tax assets — noncurrent . . .	19,857	191,476	718,709	20,546
	Net deferred tax liabilities — noncurrent . . .	—	—	—	—
	Net deferred tax assets and liabilities — Noncurrent	19,857	191,476	718,709	20,546
(4)	Income tax — current	54,062	132,638	—	—
	Net effect of deferred tax assets:				
	Income tax credit	(58,519)	(293,278)	(530,546)	(15,167)
	Loss carry forward	—	—	(267,105)	(7,636)
	Allowance for deferred tax assets . . .	(32,136)	—	500,000	14,294
	Other	3,241	(15,257)	(2,453)	(70)
	Other	(1,299)	581	649	18
	Income tax benefits	(34,651)	(175,316)	(299,455)	(8,561)

5. RELATED PARTY TRANSACTION

(1) Name and Relationship of Related Parties

Name of related parties	Relationship with the Company
C. K. Lee	The chairmen of the Company
D. F. Lin	President of the Company
Bright Shiao	Vice president of the Company
KYEC USA Corp. (KYEC USA)	Investee company
Mediatek Incorporation (Mediatek)	The two companies' chairmen of board of directors are close relatives.
Novatek Microelectronics Corp. (Novatek) (Remark 1)	The two companies' chairmen of board of directors are close relatives.
Amic Technology Incorporation (Amic) (Remark 1)	The two companies' chairmen of board of directors are close relatives.
Faraday Technology Corporation (Faraday)	The two companies' chairmen of board of directors are close relatives.
PixArt Imaging Inc. (PixArt)	The two companies' chairmen of board of directors are close relatives.
Yeong Chang Construction Corporation (Yeong Chang) (Remark 2)	The supervisor of the Company is the Chairman of Yeong Chang Construction Corporation

Remarks:

1. Since 30th June, 2000, Novatek and Amic were not the related parties.
2. Since 13th November, 2000, Yeong Chang was not a related party.

(2) Significant Related Party Transactions

a. Sales

Name of related parties	For the year ended 31st December,							
	1999		2000		2001			
	NT\$'000	Percentage	NT\$'000	Percentage	NT\$'000	Percentage	U.S.\$'000	Percentage
Mediatek	233,877	13.40%	415,963	9.94%	446,864	11.53%	12,774	11.53%
Novatek								
<i>(Remark)</i> . .	149,280	8.55%	59,378	1.42%	—	—	—	—
Faraday	32,231	1.85%	68,896	1.65%	46,703	1.20%	1,335	1.20%
Amic <i>(Remark)</i>	5,765	0.33%	24,162	0.58%	—	—	—	—
PixArt	—	—	17,812	0.43%	17,594	0.45%	503	0.45%
Total	<u>421,153</u>	<u>24.13%</u>	<u>586,211</u>	<u>14.02%</u>	<u>511,161</u>	<u>13.18%</u>	<u>14,612</u>	<u>13.18%</u>

Price and payment terms for the above sales were similar to those of regular customers.

Remarks: Novatek and Amic no longer qualified as related parties since 30th June, 2000. The corresponding amounts disclosed above exclude the results for the third and fourth quarter of 2000 and 2001, respectively.

b. Commissions paid to related party were as follows:

Name of related parties	For the year ended 31st December,			
	1999	2000	2001	
	NT\$'000	NT\$'000	NT\$'000	U.S.\$'000
KYEC USA	<u>—</u>	<u>2,161</u>	<u>5,583</u>	<u>160</u>

c. The Yeong Chang Construction Corporation provided its facility to the company with rental expense approximately NT\$4,987,000 and approximately NT\$7,400,000 for the years ended 31st December, 1999 and 2000, respectively.

d. The Company paid NT\$4,579,000 and NT\$6,541,000 to Yeong Chang for the years ended 31st December, 1999 and 2000, respectively, for repairing its facility.

(3) Receivables and payables resulting from the above transactions were as following:

a. Receivable from related parties:

Name of related parties	As of 31st December,			
	1999	2000	2001	
	NT\$'000	NT\$'000	NT\$'000	U.S.\$'000
Mediatek	101,733	48,135	61,309	1,752
Novatek	36,232	—	—	—
Faraday	10,197	9,613	18,739	536
Amic	4,531	—	—	—
PixArt	<u>—</u>	<u>15,628</u>	<u>2,759</u>	<u>79</u>
Total	<u>152,693</u>	<u>73,376</u>	<u>82,807</u>	<u>2,367</u>

b. Payable from related parties — operating:

Name of related parties	As of 31st December,			
	1999	2000	2001	
	NT\$'000	NT\$'000	NT\$'000	U.S.\$'000
KYEC USA	—	2,161	1,078	31

(4) Payable from related parties-financing

Name of related parties	For the year ended 31st December, 2001			
	Higher Balance	Ending Balance	Interest expense	Interest Rate
	NT\$'000	NT\$'000	NT\$'000	
C. K. Lee	33,000	33,000	—	—
Bright Shiao	17,000	17,000	—	—
Total	50,000	50,000	—	

- (5) Most of the Company's bank loans were severally and jointly secured by the Chairman and/or the President of the Company. The chairman of the Company also provided his investments in commercial paper in amount of approximately NT\$100,410,000 as a collateral for the Company to issue short-term notes.

6. ASSETS PLEDGED AS COLLATERAL

Account	As of 31st December,				Subject of collateral
	1999	2000	2001		
	NT\$'000	NT\$'000	NT\$'000	U.S.\$'000	
Land	918,910	924,066	869,222	24,849	Short-term and long-term loans
Leased Assets — Land.	—	—	54,844	1,568	Short-term and long-term loans
Buildings and facility.	50,145	440,565	868,225	24,821	Short-term and long-term loans
Leased Assets — Buildings and facility	—	—	46,771	1,337	Short-term and long-term loans
Idle Assets — Buildings and facility.	—	—	159,130	4,549	Long-term loans
Machinery and Equipment	963,838	2,493,644	6,340,763	181,268	Short-term and long-term loans
Leased assets	—	475,004	589,857	16,863	Financing lease
Restricted deposits.	60,077	1,387	5,903	169	Short-term loans and as guarantee security for foreign labor and as compensated deposit
Accounts receivable.	—	—	38,511	1,101	Short-term loans
Total	1,992,970	4,334,666	8,973,226	256,525	

7. COMMITMENTS AND CONTINGENT LIABILITIES

- (1) The Company's unused letters of credit amounted to approximately NT\$28,517,000 as of 31st December, 2001.
- (2) The Company has signed several construction contracts for the expansion of its factory space. As of 31st December, 2001, these construction contracts amounted to approximately NT\$882,445,000 with the un-accrued portion of the contracts in approximately NT\$202,809,000.
- (3) The promissory notes issued for bank loans as disclosed amounted to approximately NT\$11,067,887,000.
- (4) As of 31st December, 2001, the Company's Ratio of current assets to current liabilities was not in compliance with some limitations set forth in certain long-term debt covenants and, accordingly, the Company's Board of Directors has resolved to issue U.S.\$120,000,000 of Convertible Bonds on 7th February, 2002.
- (5) Watron Technology Corporation has taken a legal action against the Company, claiming a damage reimbursement of approximately NT\$16,440,000 plus interest for inventory damage during processing. The Company, on the other hand, files a claim on processing charges and interest, totaled approximately NT\$14,045,000, against Watron Technology Corporation. Both cases are currently under investigation at HsinChu District Court. The outcome is yet to be determined.
- (6) Hwa Tsai Co., Ltd. and several other investors allege the Company and its Chairman for violation of the Securities Exchange Law and seek for damage reimbursement of approximately NT\$62,213,000. The case is currently under jurisdiction of HsinChu District Court and the outcome is yet unforeseeable.

8. SIGNIFICANT DISASTER LOSS

None

9. SIGNIFICANT SUBSEQUENT EVENT

None

10. OTHER DISCLOSURES

The Company did not enter into any derivative financial instrument. Fair values of the non-derivative financial instruments are as following:

Non-derivative Instruments	As of 31st December,							
	1999		2000		2001			
	Book Value	Fair Value	Book Value	Fair Value	Book Value	Fair Value	Book Value	Fair Value
	NT\$'000		NT\$'000		NT\$'000		U.S.\$'000	
Assets								
Cash and cash equivalents	343,907	343,907	1,122,041	1,122,041	59,668	59,668	1,706	1,706
Restricted deposits . . .	60,077	60,077	1,387	1,387	5,903	5,903	169	169
Net short-term								
Investment	—	—	8,541	8,541	3,350	3,350	96	96
Notes and accounts receivable	594,289	594,289	1,455,204	1,455,204	696,822	696,822	19,920	19,920
Long-term investments.	—	—	4,930	—	5,073	—	145	—
Liabilities								
Short-term loans	220,199	220,199	1,776,464	1,776,464	1,502,572	1,502,572	42,955	42,955
Short-term notes	—	—	—	—	99,825	99,825	2,854	2,854
Payables.	631,254	631,254	1,028,930	1,028,930	388,000	388,000	11,091	11,091
Long-term loans (Including current portion)	1,363,370	1,363,370	3,330,000	3,330,000	5,759,164	5,759,164	164,642	164,642
Lease obligation (Including current portion)	—	—	461,450	470,504	480,437	488,183	13,735	13,956

Methods and assumptions used to measure fair values of financial instruments are as follow:

- (1) The fair values of the Company's short-term financial instruments are based on the book value of those instruments at reporting date due to the short maturity of those instruments. The method applied to cash and cash equivalents, restricted deposits, receivable, payable short-term loans and short-term notes.
- (2) The fair values of the Company's short-term investment and long-term investment are based on market prices at reporting date if market prices are available. The fair values of the Company's long-term investment are based on financial or any other information if market prices are not available.
- (3) The book value of long-term loans is used as fair value as the loans bear floating rates.
- (4) The fair value of lease obligation is estimated using discounted cash flow analysis based on the company's borrowing rates for similar types of borrowings.

11. SEGMENT INFORMATION

a. Operations in different industries

The Company operates predominantly in one industry segment, that being the testing of integrated circuits.

b. Operations in different geographic areas

The Company has no overseas segment.

c. Export sales

The export sales were approximately NT\$144,666,000, approximately NT\$1,138,893,000 and approximately NT\$1,081,872,000 for the years ended 31st December, 1999, 2000 and 2001, respectively, represent 8.29 per cent., 27.24 per cent. and 27.90 per cent. of total sales for the underlying periods.

d. Major customers

Revenues from customers representing over 10 per cent. of total net sales were as follows:

Customers	For the year ended 31st December,							
	1999		2000		2001			
	NT\$'000		NT\$'000		NT\$'000		U.S.\$'000	
	Amount	%	Amount	%	Amount	%	Amount	%
A	20,982	1.20	515,078	12.19	720,289	18.14	20,591	18.14
B	234,004	13.33	416,792	9.86	447,271	11.26	12,786	11.26
C	185,249	10.55	301,613	7.14	234,573	5.91	6,706	5.91
D	180,406	10.28	278,924	6.60	212,745	5.36	6,082	5.36
Total	<u>620,641</u>	<u>35.36</u>	<u>1,512,407</u>	<u>35.79</u>	<u>1,614,878</u>	<u>40.67</u>	<u>46,165</u>	<u>40.67</u>

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APPENDIX A — TAIWAN, THE REPUBLIC OF CHINA

The information set forth in this section has been extracted from various government and other publicly available publications, which have not been prepared or independently verified by the Company, the Managers or the Trustee or any of their respective affiliates or advisors in connection with the offering.

General

Taiwan is an island of 36,000 square kilometers located across the Taiwan Strait from the PRC. About one quarter of the island is arable and the remainder is mainly mountainous. Taiwan has a population of approximately 23 million and is one of the most densely populated areas of the world.

Political Status and International Relations

The ROC has a unique international political status. Although the Chinese nation has existed for several thousand years, since 1949, Taiwan and the Chinese mainland have been separately governed. The ROC, which was founded in 1912, governs Taiwan while the Peoples' Republic of China (the "PRC"), which was founded in 1949, has governed the Chinese mainland for the past 51 years. The ROC asserted that the ROC and the PRC are equal political entities which should enter into "state to state" relations while the PRC claims that it is the sole government in China and that Taiwan is part of China. Although relations between the ROC and the PRC have improved in a number of significant respects, the PRC has consistently refused to renounce the possibility that it may at some time use force to gain control over Taiwan.

Although the ROC is no longer a member of the United Nations, it maintains active trade and financial relations with most major economic powers and maintains trade missions in locations around the world. On 1st January, 2002, the ROC became the 14th member of the World Trade Organization and the ROC Government is currently seeking re-admission to the United Nations.

The ROC Government is organized into five branches or "Yuans", namely: the Executive Yuan, the Legislative Yuan, the Judicial Yuan, the Examination Yuan and the Control Yuan. The Executive Yuan formulates and implements national economic policy.

The ROC Government is headed by the President, who also serves as the commander-in-chief of the armed forces and is partially entrusted with the exercise of emergency powers. In the past, the National Assembly has elected the President and Vice President to six-year terms. However, beginning in 1996 the President and Vice President have been directly elected by the people for four-year terms. The President appoints the Premier and the Deputy Premier and Cabinet ministers on the recommendation of the Premier. The Premier heads the Executive Yuan (the Cabinet). The Legislative Yuan is the ROC's sitting legislative body, and is responsible for the enactment of all national laws. The Judicial Yuan administers the judicial system and vests judicial review powers in the Council of Grand Justices. The Control Yuan audits government accounts and has the power to investigate and impeach government officials. The Examination Yuan is empowered to examine and select government officials and establish pay scales and other terms of employment for the civil service.

Since 1986, the ROC Government has been implementing political liberalization. The ROC Government has made progress in democratizing the political process, resulting in the development of opposition political parties, the beginning of open elections, and tolerance for open public debates. As a result of these changes, one of the opposition parties, Democratic Progressive Party ("DPP"), has obtained a greater representation in the government. On 18th March, 2000, Mr. Chen Shui-bien, the DPP candidate, was elected President of the ROC.

Economy

The table below sets forth selected economic data relating to the ROC for the periods indicated.

	Year Ended December 31, (except where indicated)						
	1994	1995	1996	1997	1998	1999	2000
	(billions of U.S. Dollars, except where indicated)						
Real gross national product (percentage change)	6.1%	5.9%	5.4%	6.4%	4.3%	5.4%	6.0%
Consumer price index (age change)	4.1%	3.7%	3.1%	0.9%	1.7%	0.2%	1.3%
Industrial production index ⁽¹⁾	126.4	122.9	132.1	144.4	116.8	129.6	126.9
Exports	93.0	111.7	116.0	122.1	110.6	121.6	148.4
Imports	85.3	103.6	101.3	114.4	106.7	110.7	140.0
Trade balance	7.7	8.1	14.7	7.7	5.9	10.9	8.4
Current balance	6.5	5.5	10.9	7.1	3.4	8.4	8.9
Foreign exchange reserves	92.5	90.3	88.0	83.5	90.3	106.2	106.7
Government surplus (deficit) (NT\$ billions)	(237.5)	(313.4)	(395.0)	(319.8)	(302.5)	(557.9)	(434.9)

Note:

- (1) Industrial production index represents an index of the total annual value of ROC industrial production based on a scale with the year 1991 equaling 100.

Sources: Taiwan Statistical Data Book, Council for Economic Planning and Development, ROC; Quarterly National Economic Trends, Taiwan Area, Directorate General of Budget, Accounting and Statistics, Executive Yuan, ROC; Financial Statistics Monthly, Taiwan District, ROC; Economic Research Department, the Central Bank of China; and Monthly Statistics of the Republic of China, Directorate-General of Budget, Accounting and Statistics, Executive Yuan, ROC.

From 1981 to 1987, Taiwan's economy built up a significant current account surplus, peaking at U.S.\$18 billion in 1987. With exchange controls in place, the capital account stayed roughly in balance over the period, allowing Taiwan to accumulate official foreign exchange reserves in excess of U.S.\$76 billion by the end of that period. During the 1990's, the foreign exchange reserve increased to approximately U.S.\$90.5 billion by the end of 1998, making it one of the largest in the world. The increase in capital was one reason for the rapid share price inflation in the 1980's and early 1990's. The Central Bank of China acted to reduce the inflationary impact of this rapid acceleration in monetary growth through two measures. First, beginning in 1987, the Central Bank of China liberated outflow and restricted inflow of foreign currency and the NT Dollar was allowed to appreciate 50 per cent. against the U.S. Dollar by the end of 1989. Second, the Central Bank of China has since gradually relaxed monetary control as the demand for funds has risen due to increasing overseas investment, strong government spending on infrastructure and other capital projects and the revival of domestic private investment. However, since the Asian crisis in the fall of 1997, the NT Dollar has depreciated against the U.S. Dollar. In addition, inflation since the Asian crisis has been mild and was slightly negative in 2001.

APPENDIX B — FOREIGN INVESTMENT AND EXCHANGE CONTROLS IN THE ROC

The information presented in this appendix has been extracted from publicly available documents which have not been prepared or independently verified by the Company, the Managers, the Trustee or any of their respective affiliates or advisors in connection with the offering.

Foreign Investment

Historically, foreign investment in the ROC securities market has been restricted. From 1983 onwards, however, the ROC Government has from time to time enacted legislation and adopted regulations to permit foreign investment in the ROC securities market.

Overseas Corporate Bonds

Since 1989, the ROC SFC has approved a series of overseas corporate bond issues (“OCBs”) by ROC companies listed on the TSE in offerings directed outside the ROC. Since December 1994, the ROC SFC has also permitted ROC companies whose shares are traded on the ROSE to issue and offer OCBs.

Under the current ROC laws and policies, OCBs can be converted by bondholders (other than PRC persons) into shares of the relevant ROC companies or (subject to the ROC SFC approval) may be converted into depositary receipts issued under the sponsorship of the same ROC company or the shares of other companies, in case of exchangeable bonds. Public issuing companies may issue corporate debt in offerings outside the ROC. Proceeds from sales of the shares converted from OCBs may be used for re-investment in securities listed on the TSE or traded on the ROSE. These reinvestments will need to comply with the limitations and restrictions which apply to qualified foreign institutional investors or general foreign investors discussed below.

Under current ROC law, a converting bondholder when exercising the conversion right to convert the bonds into shares of an ROC company is required to appoint a local agent (with such qualifications as are set by the ROC SFC) to open a securities trading account with a local brokerage firm, remit funds, exercise shareholders’ rights and perform such other actions as may be designated by such converting bondholder, on behalf of and as agent for such converting bondholder. In addition, the converting bondholder is required to appoint a custodian bank to hold the securities and cash proceeds in safekeeping, make confirmations and settle trades and report all relevant information and such converting bondholder is also required to appoint a tax guarantor for filing tax returns and making tax payments.

Unless otherwise limited by the Central Bank of China, an ROC Company may, without obtaining further approvals from the Central Bank of China or any other government authority of the ROC, convert NT Dollars to other currencies, including U.S. Dollars, in respect of the proceeds of the redemption of the Bonds or payment of interest on, or the repayment of principal upon maturity of, the Bonds.

In addition, a non-ROC converting bondholder may, through its local agent and without obtaining prior approval from the Central Bank of China, convert NT Dollars into foreign currencies of net proceeds realized from the sale of the converted shares or any stock dividends relating to such shares, or any cash dividend or other cash distribution in respect of such shares, as well as for inward remittances of subscription payments in connection with a rights offering and tax payment.

Depository Receipts

In April 1992, the ROC SFC promulgated regulations permitting ROC companies with securities listed on the TSE, with the prior approval of the ROC SFC, to sponsor the issuance and sale to foreign investors of depositary receipts. Depositary receipts evidence depositary shares representing deposited shares of ROC companies. In December 1994, a series of new regulations (the “**Regulations**”) was promulgated by the ROC Ministry of Finance allowing companies whose shares are traded on the ROSE or listed on the TSE to sponsor, upon approval by the ROC SFC, the issuance and sale of depositary receipts. Any such approval will be granted (1) if the underlying shares are newly issued shares, for a fixed number of depositary receipts or (2) if the underlying shares are not newly issued shares, for a maximum number of depositary receipts and, with limited exceptions (as described below), may not be increased without additional approvals by the ROC SFC.

The Regulations, as amended, provide that any depositary receipt holder may, from three months after the issue date of the depositary receipts (in the case that the deposited shares are new shares) or immediately (in the case that the deposited shares are existing shares), request the depositary bank either to cause the underlying shares to be sold in the ROC and distribute the proceeds of such sale to the depositary receipt holder or to withdraw the underlying shares from the depositary receipt facility and deliver such shares to such holder. A citizen of the PRC is not permitted to withdraw and hold the Shares.

Under existing ROC laws and regulations, a depositary may, without obtaining further approvals from the Central Bank of China or any other government authority or agency of the ROC, convert NT Dollars into other currencies, including U.S. Dollars, in respect of the proceeds of the sale of shares represented by depositary receipts or received as stock dividends in respect of such shares and deposited into the depositary receipt facility and any cash dividends or distributions received in respect of such shares. In addition, a depositary may convert inward remittances of payments into NT Dollars for purchases of underlying shares for deposit in the depositary receipt facility against the creation of additional depositary receipts. A depositary must obtain foreign exchange approval from the Central Bank of China on a payment-by-payment basis for conversion from NT Dollars into foreign currencies in respect of the proceeds from the sale of subscription rights for new shares or the depositary's conversion from foreign currencies into NT Dollars for subscription payments in respect of rights offerings. It is expected that the Central Bank of China will grant such foreign exchange approval as a routine matter.

In addition, any such cash received by the depositary receipt holder (qualified as a QFII (as hereinafter defined) or a non-ROC resident foreign investor (“**General Foreign Investor**”)) may be used for further investment in ROC securities, subject to the requirements and restrictions generally applicable to QFIIs and General Foreign Investors (as applicable).

Direct Share Offerings

The ROC Government has permitted ROC companies listed on the TSE or the ROSE to issue shares directly (not through depositary receipt facilities) overseas.

Qualified Foreign Institutional Investors

The Executive Yuan has approved guidelines for direct investment in ROC securities listed on the TSE or ROSE or other ROC securities approved by the ROC SFC by certain qualified foreign institutional investors (each a “**QFII**”) that applied for and received, ROC SFC and, if applicable, Central Bank of China approval, including:

- (i) banks which hold securities assets of at least U.S.\$200 million and have experience in safekeeping or management of securities of assets and in international financial, securities or trust business;
- (ii) insurance companies which hold securities assets of at least U.S.\$200 million;
- (iii) fund management institutions which manage assets of at least U.S.\$200 million;
- (iv) general securities firms which have a net worth of at least U.S.\$100 million and experience in international securities investments;
- (v) offshore fund management companies which are more than 50 per cent. owned by a ROC securities investment trust enterprise provided that the funds to be invested do not come from sources in the ROC or PRC and are not owned by such offshore fund management companies;
- (vi) offshore securities firms which are more than 50 per cent. owned by a ROC securities firm, or other offshore securities firms which are wholly-owned by such offshore securities firms;
- (vii) offshore securities firms which are wholly-owned by a ROC securities firms, or other offshore securities firms which are more than 51 per cent. owned by such offshore securities firms;
- (viii) foreign government-owned investment institutions provided that all the funds to be invested shall be owned by the foreign government;

- (ix) pension funds;
- (x) mutual funds, unit trusts or investment trusts which have assets of at least U.S.\$200 million;
- (xi) trust companies which hold securities assets in trust of at least U.S.\$200 million and have experience in safekeeping or management of securities or assets and in international financial or trust businesses; and
- (xii) any other professional institutional investors which hold securities or assets of at least U.S.\$200 million.

Each QFII who wishes to invest directly in the ROC securities market is required to apply for an investment permit from the ROC SFC, provided that any application for investment exceeding U.S.\$50 million will require approvals from both the Central Bank of China and the ROC SFC. QFIIs who receive the permit(s) may currently invest up to U.S.\$3 billion, with certain limited exceptions. Except some restrictions imposed by specific law and regulation, from 1st January, 2001, the individual and aggregate foreign ownership of the issued share capital in a TSE listed company or a ROSE quoted company is not restricted. ROC custodians for QFIIs are required to submit to the Central Bank of China and the ROC SFC a report of trading activities and status of assets under custody and other matters every month. Capital remitted to the ROC under these guidelines may be remitted out of the ROC at any time after the date such capital is remitted to the ROC. Capital remitted out of the ROC may be returned to the ROC within the approved years of the outward remittance without ROC SFC approval so long as its aggregate inward remittance after netting off its aggregate outward remittance does not exceed the investment amount approved by the ROC SFC and the Central Bank of China (if applicable). Capital gains and income on investments may be remitted out of the ROC at any time.

General Foreign Investors

Except for QFIIs, General Foreign Investors (“**GFI**s”) may currently invest in ROC securities up to U.S.\$5 million (in the case of individual investors) and U.S.\$50 million (in the case of institutional investors) after obtaining approval issued by the TSE.

Foreign Investment Approval

With the exception of QFIIs, GFIs and investors in OCBs and depositary receipts, under existing ROC laws and regulations relating to foreign investment, investors (both institutional and individual) who are not ROC persons and wish to make direct investment in the shares of ROC companies are required to submit a Foreign Investment Approval (“**FIA**”) application to the Investment Commission of the MOEA or other government authority. The Investment Commission or such other government authority reviews each FIA application and approves or disapproves each application after consultation with other government agencies (such as the Central Bank of China and the ROC SFC). Under current law, any non-ROC person possessing an FIA may remit capital for the approved investment and is entitled to repatriate annual net profits, interest and cash dividends attributable to such investment. Stock dividends, investment, capital and capital gains attributable to such investment may be repatriated after approvals of the Investment Commission or other government authorities have been obtained.

Prohibited and Restricted Industries

In addition to the general restriction against direct investment by non-ROC persons in shares of ROC companies, non-ROC persons are currently prohibited from investing in certain industries in the ROC pursuant to the Negative List as amended by the Executive Yuan from time to time. The prohibition on foreign investment in the prohibited industries specified in the Negative List is absolute and provides no specific exemption from its application. Pursuant to the Negative List, certain other industries are restricted so that non-ROC persons may invest in such industries only up to a specified level and with the specific approval of the relevant competent authority which is responsible for enforcing the relevant legislation which the Negative List is intended to implement. The businesses the Company being engaged are not a prohibited or restricted industry under the Negative List.

Exchange Controls

The ROC's Foreign Exchange Control Statute and regulations thereunder provide that all foreign exchange transactions must be executed by banks designated to handle such business by the ROC Ministry of Finance and by the Central Bank of China. Current regulations favor trade-related foreign exchange transactions.

Consequently, foreign currency earned from exports of merchandise and services may now be retained and used freely by exporters, and all foreign currency needed for the import of merchandise and services may be purchased freely from the designated banks for conducting foreign exchange.

ROC companies and resident individuals may also, without foreign exchange approval, remit into and out of the ROC foreign currencies of up to U.S.\$50 million (or its equivalent) and U.S.\$5 million (or its equivalent), respectively, in each calendar year. The above limits apply to remittances involving a conversion between NT Dollars and U.S. Dollars or other foreign currencies. Furthermore, any remittance of foreign currency into the ROC by an ROC company or resident individual in a year will be offset by the amount remitted out of the ROC by the company or individual (as applicable) within its annual quota and will not use up its annual inward remittance quota to the extent of such offset. The above limits apply to remittance involving a conversion between NT Dollars and U.S. Dollars or other foreign currencies. A requirement is also imposed on all enterprises to register medium-and-long-term foreign debt with the Central Bank of China.

In addition, foreign persons may, subject to certain required documents, but without foreign exchange approval of the Central Bank of China, remit outside and into the ROC foreign currencies of up to U.S.\$100,000 (or its equivalent) for each remittance. The above limit applies only to remittances involving a conversion between NT Dollars and U.S. Dollars or other foreign currencies.

APPENDIX C — THE SECURITIES MARKET OF THE ROC

The information presented in this appendix has been extracted from publicly available documents which have not been prepared or independently verified by the Company, the Managers, the Trustee or any of their respective affiliates or advisors in connection with the offering.

In 1960, the ROC Government established the Securities and Exchange Commission to supervise and control all aspects of the securities market. The Securities and Exchange Commission of the ROC was restructured in early 1997 and renamed as the Securities and Futures Commission (“SFC”). In the 1970’s and the early 1980’s, the ROC Government implemented a number of steps designed to upgrade the quality and importance of the ROC securities market, such as encouraging listing on the TSE and establishing an over-the-counter market. In the mid-1980’s, the ROC Government began to revise its laws and regulations in a manner designed to facilitate the gradual internationalization of the ROC securities market.

The Taiwan Stock Exchange

In 1961, the ROC SFC established the Taiwan Stock Exchange (“TSE”) to provide a marketplace for securities trading. The TSE is a corporation owned by government-controlled and private banks and enterprises. The TSE is independent of entities transacting business through it, each of which pays a user’s fee. Generally, all transactions in listed securities by brokers, traders and integrated securities firms must be made through the TSE.

The TSE commenced operations in 1962. During the early 1980s, the ROC SFC actively encouraged new listings on the TSE and the number of listed companies grew from 119 in 1983 to 591 by the end of February 2002. As of the end of February 2002, the market capitalization of companies listed on the TSE was NT\$10,579 billion.

Historically, Taiwan companies have listed only shares and bonds on the TSE. However, the ROC SFC has encouraged companies to list other types of securities. In 1988, the ROC SFC permitted the issuance of the Taiwan’s first convertible bonds. Since 1989, there have been offerings of domestic convertible bonds and convertible preferred shares. In addition, beneficiary units evidencing beneficiary interests in closed-end investment funds and Dragon Bonds issued by Asian Development Bank are also listed on the TSE or traded on the ROSE. The ROSE also has regulations which permit foreign issuers to list their equity securities directly on the TSE or through the use of depositary receipts. To date, two foreign issuers have listed their equity securities on the TSE through the use of depositary receipts in accordance with these regulations.

The TSE requirements for listing are based on the following company attributes:

- the number and distribution of stockholders;
- length of time in business;
- amount of capital; and
- profitability.

However, special listing criteria apply to technology companies and key business engaging in national economic development.

The Over-the-Counter Market and the ROC Over-the-Counter Securities Exchange

To complement the TSE, the ROSE was established in September 1982 on the initiative of the ROC SFC to encourage the trading of securities of companies who do not qualify for listing on the TSE. As of 25th March, 2002, 372 companies have listed equity securities on the ROSE and the total market capitalization of those companies was NT\$695 billion.

In addition, the Emerging Market on the OTC was established on 2nd January, 2002 on the initiative of the ROC SFC to encourage trading of securities of companies that the public companies but do not qualify for listing on the TSE or the ROSE. The price of shares is decided by negotiation between securities firms and investors. As of 31st January, 2002, 78 companies have registered equity securities on the Emerging Market on the OTC.

The following table sets forth, for the periods indicated, certain information relating to the ROSE Index:

<u>Period Ended</u>	<u>Number of Listed Companies at Period End</u>	<u>Trading Value</u>	<u>Index High</u>	<u>Index Low</u>	<u>Index at Period End</u>
1995	41	2,796	101.96	94.02	101.96
1996	79	453,509	234.83	99.92	233.09
1997	114	2,310,659	343.99	210.22	245.05
1998	176	1,198,158	281.41	163.89	165.80
1999	264	1,994,031	207.18	138.99	207.18
2000	300	4,479,660	329.47	99.86	104.93
2001	333	14,121,96	136.23	106.74	136.23
2002 (through <u>31st March</u>) . . .	<u>378</u>	<u>22,077</u>	<u>156.96</u>	<u>135.26</u>	<u>155.06</u>

Sources: OTC Monthly Review; OTC Data Base; Taiwan Economic Journal.

Taiwan Stock Exchange Index

The TSE Index is calculated on the basis of a wide selection of listed shares weighted according to the number of shares outstanding. This weighted average method is also used for the Standard and Poor's Index in the United States and the Nikkei Stock Average in Japan. The TSE Index is compiled by dividing the market value by the base day's total market value for the index shares. The TSE Index is the oldest and most widely quoted market index in Taiwan.

The weighting of stocks in the index is fixed as long as the number of shares outstanding remains constant. When the total number of shares outstanding changes, the weight of each stock is adjusted. Stock splits and stock dividends are adjusted automatically. Cash dividends are not included in the calculation.

The following table shows for the periods indicated information relating to the TSE Index.

<u>Period Ended</u>	<u>Number of Listed Companies at the Period End</u>	<u>Index High</u>	<u>Index Low</u>	<u>Index at Period End</u>
1990	199	12,495.34	2,560.47	4,530.16
1991	221	6,305.22	3,316.26	3,377.06
1992	256	5,391.63	3,327.67	4,600.67
1993	285	6,070.56	3,135.56	6,070.56
1994	313	7,183.75	5,194.63	7,124.66
1995	347	7,051.49	4,503.37	5,173.73
1996	375	6,982.81	4,690.22	6,933.94
1997	404	10,116.84	6,820.35	8,187.27
1998	437	9,277.09	6,251.38	6,418.43
1999	462	8,608.91	5,475.00	8,448.84
2000	474	10,202.20	8,349.91	8,842.63
2001	584	6,104.24	3,446.26	5,551.24
2002 (through <u>31st March</u>) . . .	<u>595</u>	<u>6,242.64</u>	<u>5,488.33</u>	<u>6,182.59</u>

Source: Status of Securities Listed on Taiwan Stock Exchange.

As indicated above, the performance of the Taiwan Stock Exchange has in recent years been characterized by extreme price volatility.

Price Limits, Commissions, Transaction Tax and Other Matters

The TSE has placed limits on block trading and on the range of daily price movements. Transactions that involve 500 trading lots or more must be registered and executed pursuant to certain TSE guidelines. Fluctuations in the price of stock traded on the TSE are currently subject to a restriction of 7 per cent. above and below the previous day's closing price (or reference price set by the TSE if the previous day's closing price is not available because of lack of trading activity) in the case of equity securities, and 5 per cent. in the case of debt securities. Brokerage commissions are proposed by the TSE and approved by the ROC SFC. The current approved maximum brokerage commission is 0.1425 per cent. of the transaction price for equity securities; however, a lower rate may be charged to clients by securities firms at their sole discretion, provided that they must report such rate to the TSE. A securities transaction tax, currently levied at the rate of 0.3 per cent. of the transaction price, is payable by the seller of equity securities and a tax at the rate of 0.1 per cent. of the transaction price is payable by the seller of debt securities other than government bonds. Such securities transaction taxes are withheld at the time of the transaction giving rise to such taxes. According to the amended Statute for Upgrading Industries effective as of 1st February, 2002, no securities transaction tax will be imposed on the sale of the Bonds from 1st February, 2002 to 31st December, 2009. Sales of shares of companies listed on the TSE are currently sold in lots of 1,000 shares. Odd lot trading, or the purchase or sale of less than 1,000 shares, can be conducted in after-hours trading. Investors who desire to sell odd lots of shares of a listed company occasionally experience delays in effecting such sales.

Regulation and Supervision

The ROC SFC has been under the jurisdiction of the Ministry of Finance since 1981. The ROC SFC has extensive regulatory authority over companies listed on the TSE, companies whose shares are traded on the ROSE and unlisted publicly issuing companies whose capital exceeds the currently specified minimum amount of NT\$500 million. Such companies are generally required to obtain approval from, or registration with, the ROC SFC for all securities offerings. The ROC SFC has promulgated regulations requiring, unless otherwise exempted, periodic reporting of financial and operating information by all public companies. In addition, the ROC SFC is responsible for the establishment of standards for financial reporting and carries out licensing and supervision with respect to the other participants in the ROC securities markets. The ROC SFC has responsibility for implementation of the ROC Securities and Exchange Law and for overall administration of governmental policies in the ROC securities markets. It has extensive regulatory authority over the offering, issuing and trading of securities. In addition, the ROC Securities and Exchange Law specifically empowers the ROC SFC to promulgate rules under certain circumstances.

The ROC Securities and Exchange Law prohibits market manipulation. It permits a company to recover certain short-term trading profits made through purchases and sales within six months by directors, managerial personnel, supervisors and shareholders, together with their spouses, minor children and nominees, holding 10 per cent. or more of the shares of the company. The ROC Securities and Exchange Law prohibits trading by "insiders" based on non-public information that materially affects share price movement. Pursuant to the ROC Securities and Exchange Law, the term "**insiders**" includes directors, supervisors, managers and shareholders having more than 10 per cent. or more shareholding, together with their spouses, minor children and nominees, or any person who has learned such information due to an occupational or controlling relationship with the issuing company and any person who has learned such information from any of the foregoing. Sanctions can include prison terms. In addition, damages may be awarded to persons injured by the transaction.

The ROC Securities and Exchange Law also imposes criminal liability on certified public accountants and lawyers who make false certifications in their examination and audit of a company's contracts, reports and other evidentiary documents that are related to securities transactions. ROC SFC regulations require that financial reports of listed companies be audited by accounting firms consisting of at least three certified public accountants and be signed by at least two certified public accountants.

The ROC Securities and Exchange Law also provide for, among other things, regulations relating to public offerings of securities; measures to strengthen the capital structure of issuers; civil liability for material misstatements or omissions made by issuers; more stringent regulation of the securities activities of

officers, supervisors, directors and major shareholders of issuers; regulations regarding tender offers; and a significant expansion of the prohibitions against insider trading, including the imposition of treble civil damages and criminal sanctions.

The ROC SFC does not have criminal or civil enforcement powers under the ROC Securities and Exchange Law. Criminal actions may be pursued only by prosecutors. Under ROC law, civil actions may only be brought by plaintiffs who assert that they have suffered damages. The ROC SFC is directly empowered to curb abuses and violations of applicable laws and regulations only through administrative measures.

In addition to providing a market for securities trading, the TSE has primary responsibility for reviewing applications by issuers to list securities on the TSE and the ROSE has primary responsibility for reviewing applications by issuers to list securities on the ROSE. The ROC SFC reviews all securities offerings by listed companies. If issuers of listed securities violate relevant laws and regulations or encounter significant difficulties, the TSE and the ROSE may, with the approval of the ROC SFC, delist securities of such issuers.

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