

**INVENTEC APPLIANCES CORPORATION**  
**FINANCIAL STATEMENTS**  
**DECEMBER 31, 2005 AND 2004**  
**AND**  
**INDEPENDENT AUDITORS' REPORT**

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# Inventec Appliances Corporation

## Financial Statements

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## **Independent Auditors' Audit Report**

The Board of Directors  
Inventec Appliances Corporation,

We have audited the accompanying balance sheets of Inventec Appliances Corporation as of December 31, 2005 and 2004, and the related statements of income, statements of changes in stockholders' equity and cash flows for the years ended December 31, 2005 and 2004. These financial statements are the responsibility of the management of Inventec Appliances Corporation. Our responsibility is to express an opinion to these financial statements based on our audit.

We conducted our audits in accordance with "Rules Governing Certified Public Accountant's Examination and Certification of Financial Statements" and auditing standards generally accepted in the Republic of China. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the 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 the management, as well as evaluation 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 Inventec Appliances Corp. as of December 31, 2005 and 2004, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the Republic of China.

Inventec Appliances Corp. has prepared consolidated financial statements of the year ended December 31, 2005, on which we have expressed an unqualified opinion.

Taipei, Taiwan, R.O.C.  
February 23, 2006

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### **Note to Readers**

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

**INVENTEC APPLIANCES CORPORATION**  
**BALANCE SHEETS**  
**December 31, 2005 and 2004**  
**(New Taiwan Dollars in Thousands, Except for Share Data)**

	December 31, 2005		December 31, 2004	
	Amount	%	Amount	%
<b>ASSETS</b>				
<b>Current assets</b>				
Cash (Note 4.a)	\$ 2,999,079	9	3,393,183	13
Accounts receivable, net of allowance for doubtful accounts (Notes (2) and 4.b)				
-Related parties(Note5)	2,199,769	6	1,321,385	5
-Non-related parties	19,233,296	54	15,988,341	59
Other financial assets - current	545,468	2	66,764	-
Inventories, less allowance for inventory obsolescence (Notes 2 and 4.c)	3,090,925	9	1,678,312	6
Other current assets	287,364	1	134,859	-
	<u>28,355,901</u>	<u>81</u>	<u>22,582,844</u>	<u>83</u>
<b>Long-term equity investments (Notes 2 and 4. d)</b>				
Long-term equity investments accounted for under the equity method	5,283,277	15	3,038,835	12
Long-term equity investments accounted for under the cost method	60,200	-	91,850	-
	<u>5,343,477</u>	<u>15</u>	<u>3,130,685</u>	<u>12</u>
<b>Other financial assets - non-current</b>				
	<u>415,963</u>	<u>1</u>	<u>4,870</u>	<u>-</u>
<b>Property, plant, and equipment (Notes 2 and 4. e)</b>				
Land	279,855	1	279,855	1
Buildings	284,957	1	284,957	1
Machinery	616,544	2	548,524	2
Mold and tools	30,206	-	30,206	-
Furniture and office facilities	44,858	-	46,495	-
Other equipment	187,627	1	181,101	1
	<u>1,444,047</u>	<u>5</u>	<u>1,371,138</u>	<u>5</u>
Less: accumulated depreciation	(560,770)	(2)	(428,301)	(1)
Construction in progress				
Prepayment for equipment	15,929	-	999	-
	<u>899,206</u>	<u>3</u>	<u>943,836</u>	<u>4</u>
<b>Intangible assets</b>				
Deferred pension cost (Note 2)	62,390	-	61,052	-
<b>Other assets</b>				
Deferred income tax assets - non-current (Notes 2 and 4.g)	-	-	272,803	1
Others	52,313	-	58,250	-
	<u>52,313</u>	<u>-</u>	<u>331,053</u>	<u>1</u>
<b>TOTAL ASSETS</b>	<b>\$ 35,129,250</b>	<b>100</b>	<b>27,054,340</b>	<b>100</b>

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

**INVENTEC APPLIANCES CORPORATION**  
**BALANCE SHEETS (CONTINUED)**  
**December 31, 2005 and 2004**  
(New Taiwan Dollars in Thousands, Except for Share Data)

	December 31, 2005		December 31, 2004	
	Amount	%	Amount	%
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>				
<b>Current liabilities</b>				
Accounts payable				
-Related parties (Note 5)	\$ 19,732,240	56	15,568,225	58
-Non-related parties	1,015,183	3	1,378,999	5
Income Tax Payable(Notes 2 and 4.g)	-	-	108,366	-
Accrued expenses	803,819	2	480,621	2
Other payables	30,490	-	137,296	1
Other current liabilities	336,486	1	175,239	1
	21,918,218	62	17,848,746	67
<b>Other liabilities</b>				
Estimated warranty reserve (Note 2)	1,396,264	4	1,399,833	5
Accrued pension liabilities (Notes 2 and 4.f)	41,080	-	53,593	-
Others	534,754	2	364,760	1
	1,972,098	6	1,818,186	6
<b>Total liabilities</b>	23,890,316	68	19,666,932	73
<b>Stockholders' equity</b>				
Capital stock, par value \$10 per share; authorized 400,000,000 and issued 333,000,000 shares as of December 31, 2005 ; authorized and issued 280,000,000 shares as of December 31, 2004 (Note 4.h)	3,330,000	9	2,800,000	10
Capital surplus				
Additional paid-in capital	4,322,860	12	2,104,500	8
Others	1,110	-	1,110	-
Retained earnings				
Legal reserve (Note 2)	483,985	1	274,914	1
Undistributed earnings (Note 4.i)	3,089,442	10	2,344,512	9
Other adjustments to stockholders' equity				
Cumulative translation adjustments	20,752	-	(137,628)	(1)
Net loss not recognized as pension cost (Notes 2 and 4.f)	(9,215)	-	-	-
Total stockholders' equity	11,238,934	32	7,387,408	27
<b>Commitments and contingencies (Note 7)</b>				
<b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>	<b>\$ 35,129,250</b>	<b>100</b>	<b>27,054,340</b>	<b>100</b>

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

**INVENTEC APPLIANCES CORPORATION**  
**BALANCE SHEETS (CONTINUED)**  
**December 31, 2005 and 2004**  
(New Taiwan Dollars in Thousands, Except for Share Data)

	<b>December 31, 2005</b>		<b>December 31, 2004</b>	
	<b>Amount</b>	<b>%</b>	<b>Amount</b>	<b>%</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>				
<b>Current liabilities</b>				
Accounts payable				
-Related parties (Note 5)	\$ 19,732,240	56	15,568,225	58
-Non-related parties	1,015,183	3	1,378,999	5
Income Tax Payable(Notes 2 and 4.g)	-	-	108,366	-
Accrued expenses	803,819	2	480,621	2
Other payables	30,490	-	137,296	1
Other current liabilities	336,486	1	175,239	1
	<u>21,918,218</u>	<u>62</u>	<u>17,848,746</u>	<u>67</u>
<b>Other liabilities</b>				
Estimated warranty reserve (Note 2)	1,396,264	4	1,399,833	5
Accrued pension liabilities (Notes 2 and 4.f)	41,080	-	53,593	-
Others	534,754	2	364,760	1
	<u>1,972,098</u>	<u>6</u>	<u>1,818,186</u>	<u>6</u>
<b>Total liabilities</b>	<u>23,890,316</u>	<u>68</u>	<u>19,666,932</u>	<u>73</u>
<b>Stockholders' equity</b>				
Capital stock, par value \$10 per share; authorized 400,000,000 and issued 333,000,000 shares as of December 31, 2005 ; authorized and issued 280,000,000 shares as of December 31, 2004 (Note 4.h)	3,330,000	9	2,800,000	10
Capital surplus				
Additional paid-in capital	4,322,860	12	2,104,500	8
Others	1,110	-	1,110	-
Retained earnings				
Legal reserve (Note 2)	483,985	1	274,914	1
Undistributed earnings (Note 4.i)	3,089,442	10	2,344,512	9
Other adjustments to stockholders' equity				
Cumulative translation adjustments	20,752	-	(137,628)	(1)
Net loss not recognized as pension cost (Notes 2 and 4.f)	(9,215)	-	-	-
Total stockholders' equity	<u>11,238,934</u>	<u>32</u>	<u>7,387,408</u>	<u>27</u>
<b>Commitments and contingencies (Note 7)</b>				
<b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>	<u><u>\$ 35,129,250</u></u>	<u><u>100</u></u>	<u><u>27,054,340</u></u>	<u><u>100</u></u>

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

**INVENTEC APPLIANCES CORPORATION**  
**STATEMENTS OF OPERATIONS**  
**FOR THE YEARS ENDED DECEMBER 31, 2005 and 2004**  
(New Taiwan Dollars in Thousands, Except for Earnings Per Share )

	<u>2005</u>		<u>2004</u>	
	<u>Amount</u>	<u>%</u>	<u>Amount</u>	<u>%</u>
<b>Operating revenues:</b>				
<b>Gross sales (Note 2)</b>	\$ 113,813,279	100	76,043,290	100
Less: sales returns	(229,574)	-	(14,562)	-
Sales discounts and allowances	(177,711)	-	(31,217)	-
<b>Net sales</b>	<u>113,405,994</u>	<u>100</u>	<u>75,997,511</u>	<u>100</u>
Cost of sales	<u>(107,640,684)</u>	<u>(95)</u>	<u>(71,189,111)</u>	<u>(94)</u>
Gross profit	5,765,310	5	4,808,400	6
Less: Unrealized inter-company profits	(111,582)	-	(158,132)	-
Add: Realized inter-company profits	<u>158,132</u>	<u>-</u>	<u>120,103</u>	<u>-</u>
	<u>5,811,860</u>	<u>5</u>	<u>4,770,371</u>	<u>6</u>
<b>Operating expenses:</b>				
Selling	(2,370,769)	(2)	(2,137,475)	(3)
Administrative	(607,146)	-	(324,086)	(1)
Research and development	<u>(1,208,595)</u>	<u>(1)</u>	<u>(906,168)</u>	<u>(1)</u>
	<u>(4,186,510)</u>	<u>(3)</u>	<u>(3,367,729)</u>	<u>(5)</u>
<b>Operating income</b>	<u>1,625,350</u>	<u>2</u>	<u>1,402,642</u>	<u>1</u>
<b>Non-operating income:</b>				
Interest income	30,055	-	24,777	-
Investment income accounted for under the equity method	1,500,496	1	696,386	1
Foreign exchange gain	95,900	-	-	-
Others	<u>534,860</u>	<u>-</u>	<u>417,101</u>	<u>1</u>
	<u>2,161,311</u>	<u>1</u>	<u>1,138,264</u>	<u>2</u>
<b>Non-operating expenses and loss:</b>				
Interest expense	(8,176)	-	(6,532)	-
Other investment loss	(44,850)	-	-	-
Foreign exchange loss	-	-	(32,647)	-
Losses on Inventory Obsolescence	(198,288)	-	(52,081)	-
Others	<u>(79,527)</u>	<u>-</u>	<u>(9,221)</u>	<u>-</u>
	<u>(330,841)</u>	<u>-</u>	<u>(100,481)</u>	<u>-</u>
<b>Income before income tax</b>	3,455,820	3	2,440,425	3
<b>Income tax expense (Notes 2 and 4.g)</b>	<u>(465,655)</u>	<u>-</u>	<u>(349,717)</u>	<u>-</u>
<b>Net income</b>	<u>\$ 2,990,165</u>	<u>3</u>	<u>2,090,708</u>	<u>3</u>
	<u>Before</u>	<u>After</u>	<u>Before</u>	<u>After</u>
	<u>Tax</u>	<u>Tax</u>	<u>Tax</u>	<u>Tax</u>
<b>Primary earnings per share (Notes 2 and 4.j)</b>	<u>\$ 11.01</u>	<u>9.53</u>	<u>9.03</u>	<u>7.74</u>
<b>Primary earnings per share after retroactive adjustments</b>			<u>8.16</u>	<u>6.99</u>

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

**INVENTEC APPLIANCES CORPORATION**  
**STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY**  
**FOR THE YEARS ENDED DECEMBER 31, 2005 and 2004**  
(New Taiwan Dollars in Thousands, Except for Share Data)

	<u>Retained Earnings</u>				<u>Stockholders' Equity Adjustment</u>		<u>Total</u>
	<u>Common Stock</u>	<u>Capital Surplus</u>	<u>Legal Reserve</u>	<u>Accumulated Profit</u>	<u>Cumulative Translation Adjustments</u>	<u>Net Loss Not Recognized as Pension Cost</u>	
<b>Balance as of January 1, 2004</b>	\$ 2,350,000	1,520,610	82,632	2,170,140	(28,827)	-	6,094,555
2004 earnings distribution:							
Legal reserve	-	-	192,282	(192,282)	-	-	-
Remuneration to directors and supervisors	-	-	-	(51,916)	-	-	(51,916)
Employee bonuses-cash	-	-	-	(101,138)	-	-	(101,138)
Employee bonuses-stock	20,000	-	-	(20,000)	-	-	-
Stock dividends	235,000	-	-	(235,000)	-	-	-
Cash dividends	-	-	-	(1,316,000)	-	-	(1,316,000)
Capital increase in cash	195,000	585,000	-	-	-	-	780,000
Net Income for the year ended December 31, 2004	-	-	-	2,090,708	-	-	2,090,708
Cumulative Translation Adjustments of Long-Term Investment	-	-	-	-	(108,801)	-	(108,801)
<b>Balance as of December 31, 2004</b>	<u>2,800,000</u>	<u>2,105,610</u>	<u>274,914</u>	<u>2,344,512</u>	<u>(137,628)</u>	<u>-</u>	<u>7,387,408</u>
2005 earnings distribution:							
Legal reserve	-	-	209,071	(209,071)	-	-	-
Remuneration to directors and supervisors	-	-	-	(56,449)	-	-	(56,449)
Employee bonuses-cash	-	-	-	(111,715)	-	-	(111,715)
Employee bonuses-stock	20,000	-	-	(20,000)	-	-	-
Stock dividends	280,000	-	-	(280,000)	-	-	-
Cash dividends	-	-	-	(1,568,000)	-	-	(1,568,000)
Capital increase in cash	230,000	2,218,360	-	-	-	-	2,448,360
Net Income for the year ended December 31, 2005	-	-	-	2,990,165	-	-	2,990,165
Net loss not recognized as pension cost	-	-	-	-	-	(9,215)	(9,215)
Cumulative Translation Adjustments	-	-	-	-	158,380	-	158,380
<b>Balance as of December 31, 2005</b>	<u><u>\$ 3,330,000</u></u>	<u><u>4,323,970</u></u>	<u><u>483,985</u></u>	<u><u>3,089,442</u></u>	<u><u>20,752</u></u>	<u><u>(9,215)</u></u>	<u><u>11,238,934</u></u>

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

**INVENTEC APPLIANCES CORPORATION**  
**STATEMENTS OF CASH FLOWS**  
**FOR THE YEARS ENDED DECEMBER 31, 2005 and 2004**  
(New Taiwan Dollars in Thousands)

	<b>2005</b>	<b>2004</b>
<b>Cash flows from operating activities:</b>		
Net income	\$ 2,990,165	2,090,708
Adjustments to reconcile net income to net cash provided by (used in) operating activities		
Depreciation	143,867	132,132
Amortization	91,625	111,324
Loss (Gain) on disposal of property, plant, and equipment	329	(6,555)
Gain on disposal of deferred assets	-	(637)
Provision for inventory market decline	198,288	52,081
Provision for doubtful accounts	235,807	48,571
Investment income recognized under the equity method	(1,500,496)	(696,386)
Provision/(reversal) for Estimated warranty reserve	(3,569)	823,469
Provision for royalty reserve	82,779	82,816
Loss on investment under the cost method	44,850	-
Change in operating assets and liabilities:		
Accounts receivable	(4,639,865)	(11,582,775)
Other financial assets - current	(229,109)	(44,188)
Inventories	(1,610,901)	(754,996)
Other current assets	18,148	20,763
Deferred income tax assets and liabilities, net	216,678	(82,283)
Accounts payable	3,800,199	10,922,660
Income tax payable	(108,366)	(266,129)
Accrued expenses	323,198	125,390
Other payables	(59,474)	(46,419)
Other current liabilities	158,703	(35,853)
Accrued pension liabilities	(23,066)	(19,929)
Deferred credits	(47,767)	43,709
<b>Net cash provided by operating activities</b>	<b>82,023</b>	<b>917,473</b>
<b>Cash flows from investing activities:</b>		
Increase in long-term investments	(552,773)	(1,177,673)
Purchase of property, plant, and equipment	(200,673)	(181,842)
Purchase of other assets	(31,870)	(45,637)
Proceeds from long-term investments returned	6,800	-
Proceeds from disposal of property, plant, and equipment	1,286	31,853
Proceeds from disposal of deferred assets	-	1,408
Other financial assets - non-current	(411,093)	(890)
Increase in other liabilities	-	6,449
<b>Net cash used in investing activities</b>	<b>(1,188,323)</b>	<b>(1,366,332)</b>
<b>Cash flows from financing activities:</b>		
Capital increase in cash	2,448,360	780,000
Remuneration to directors and supervisors	(56,449)	(51,916)
Employee bonuses	(111,715)	(101,138)
Cash dividends	(1,568,000)	(1,316,000)
<b>Net cash provided by (used) in financing activities</b>	<b>712,196</b>	<b>(689,054)</b>
<b>Net decrease in cash</b>	<b>(394,104)</b>	<b>(1,137,913)</b>
<b>Cash, the beginning of the year</b>	<b>3,393,183</b>	<b>4,531,096</b>
<b>Cash, the end of the year</b>	<b>\$ 2,999,079</b>	<b>3,393,183</b>
<b>Supplemental disclosures of cash flow information:</b>		
Cash paid during the period for interest	<b>\$ 8,176</b>	<b>6,532</b>
Cash paid during the period for income tax	<b>388,468</b>	<b>698,129</b>
Unpaid remuneration to directors and supervisors and employee bonuses		
<b>Purchase of property, plant, and equipment with cash and other payables:</b>		
Increase in property, plant, and equipment	\$ 154,670	201,434
Add: Other payables and rents payables - beginning of the period	59,273	39,681
Less: Other payables and rents payables - end of the period	(13,270)	(59,273)
Cash paid	<b>\$ 200,673</b>	<b>181,842</b>

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

**INVENTEC APPLIANCES CORPORATION**  
**Notes to Financial Statements**

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

**(1) Organization and Business**

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

As of December 31, 2005, the Company had 1,571 employees.

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

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

**(a) Foreign Currency Translation**

Non-forward foreign currencies denominated contracts are recorded at spot rates as transactions occur. Foreign exchange gains and losses on settlement of foreign currency denominated assets and liabilities and those year-end adjustments to foreign currency denominated assets and liabilities at spot rates on the balance sheet date are included in current earnings.

Under SFAS No. 14, the balance sheet accounts of any of the Company's offshore subsidiaries, which are denominated in currencies other than the New Taiwan dollar, are translated at exchange rates prevailing at the end of year. Stockholders' equity is translated at historical rates except for the beginning balance of retained earnings. Revenue and expense accounts are translated using the weighted-average exchange rates during the year. Gains and losses resulting from such translations are recorded as a cumulative translation adjustment, a separate component of stockholders' equity.

**(b) Allowance for Doubtful Accounts**

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

**(c) Inventories**

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

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

Long-term equity investments in which the Company has less than 20% equity ownership and has no significant influence over the investee companies are stated at cost, unless the investee companies' shares are traded in the OTC exchange or listed on a stock exchange, where the lower of cost or market method is adopted. For the equity investments in non-listed investee companies, if evidence suggests that investment value impairment may be other than temporary and that possibility of recovery is remote, loss is recognized immediately.

Long-term equity investments in which the Company can exercise significant influence are accounted for under the equity method. Investee companies in which the Company has controlling interest are accounted for under the equity method and the Company is required to prepare consolidated financial statements for each of the periods ended December 31, and June 30.

## INVENTEC APPLIANCES CORPORATION

### Notes to Financial Statements (continued)

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

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

#### (e) Property, Plant, Equipment and Depreciation

Property, plant, and equipment are stated at cost. Major additions, improvements, and replacements are capitalized. Maintenance and repairs are recognized as current expenses; Gain and loss on disposal of properties, plant, and equipment is reflected under non-operating income or expense.

Depreciation is calculated using the straight-line method over the economic useful lives less salvage value.

Economic lives of major property and equipment are as follows:

Building	3 to 55	years
Machinery	3 to 8	years
Mold and tools	1	year
Furniture and office facilities	3 to 10	years
Other equipment	3 to 15	years

#### (f) Assets Impairment

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

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

#### (g) Deferred Expenses

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

#### (h) Warranty Reserve

A warranty reserve is provided for products sold with warranty based on estimated warranty cost and in consideration of past experience. It is recognized as current or non-current liabilities depending on its nature and charged against current expense.

#### (i) Royalty Reserve

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

## INVENTEC APPLIANCES CORPORATION

### Notes to Financial Statements (continued)

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

#### (j) Pension Plan

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

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

For defined contribution pension plan, the Company contributes to the Labor Pension Fund at the rate of 6% of the employee's monthly wages; contributions are reflected as current pension expense.

#### (k) Legal Reserve and Capital Surplus

A legal reserve is used exclusively to offset cumulative losses or to increase capital. Capitalization of the legal reserve is permitted only until it reaches 50% of the total paid-in capital, and only 50% thereof can be capitalized.

Under the ROC Company Law, capital surplus can only be used to offset cumulative losses and increase capital. Capitalization of capital surplus shall conform to the ratio set forth by the ROC SFB.

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

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

#### (m) Revenue Recognition

Revenue is recognized when title to the product and risk and reward of ownership are transferred to the customer. Otherwise recognition is deferred until criteria are met.

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

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

**INVENTEC APPLIANCES CORPORATION**

**Notes to Financial Statements (continued)**

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

**(o) Income Tax**

The Company adopts the SFAS No. 22, "Accounting for Income Taxes" to make inter- and intra-period income tax allocation. Tax effects of deductible temporary differences, loss carryforwards and unused investment tax credits are treated as deferred tax assets, whereas those of taxable temporary differences are accounted for as deferred tax liabilities. A valuation allowance is provided for deferred tax assets by assessing whether it is more likely than not such assets will be realized. Income tax expenses or benefit that resulting in the recognitions of unrealized profit and changes in capital surplus, which reflected on stockholders' equity instead of current profit and loss, are respectively disclosed in net. Adjustments to prior years' income taxes are reflected as current income taxes.

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

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

Basic EPS is computed based on the weighted-average number of common shares issued and outstanding. In the event of capitalization of retained earnings, capital surplus, or employee bonus, the number of share is retroactively adjusted for additional shares issued.

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

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

**(4) Summary of Major Accounts**

**(a) Cash**

	<u>December 31, 2005</u>	<u>December 31, 2004</u>
Cash on hand	\$ 696	496
Cash at bank		
Demand deposits	1,615,093	943,810
Checking accounts	-	988
Time deposits	300,000	1,000,000
Negotiable certificate of deposits	600,000	1,400,000
Foreign currency deposits	483,290	47,889
Total	<u>\$ 2,999,079</u>	<u>3,393,183</u>

**(b) Accounts Receivable**

	<u>December 31, 2005</u>	<u>December 31, 2004</u>
Accounts receivable - related parties	\$ 2,217,104	1,321,385
Less: allowance for doubtful accounts	(17,335)	-
Net	<u>2,199,769</u>	<u>1,321,385</u>
Accounts receivable - non-related parties	19,281,867	16,036,912
Less: allowance for doubtful accounts	(48,571)	(48,571)
Net	<u>19,233,296</u>	<u>15,988,341</u>
Total	<u>\$ 21,433,065</u>	<u>17,309,726</u>

**INVENTEC APPLIANCES CORPORATION**

**Notes to Financial Statements (continued)**

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

**(c) Inventories**

	<b>December 31, 2005</b>	<b>December 31, 2004</b>
Raw materials	\$ 1,535,549	832,048
Work in process	319,871	195,867
Finished goods	1,200,527	390,845
Inventories in transit	275,367	301,653
Subtotal	<u>3,331,314</u>	<u>1,720,413</u>
Less: Allowances for obsolescence	(240,389)	(42,101)
Net	<u><b>\$ 3,090,925</b></u>	<u><b>1,678,312</b></u>
Insurance coverage for inventories	<u><b>\$ 2,940,904</b></u>	<u><b>1,035,164</b></u>

**(d) Long-Term Investments**

<b>Investee</b>	<b>Cost of Investment</b>	<b>December 31, 2005</b>		<b>December 31, 2004</b>	
		<b>Shareholding Ratio</b>	<b>Book Value</b>	<b>Shareholding Ratio</b>	<b>Book Value</b>
<b>Carried under the equity method</b>					
Inventec Appliances (Cayman) Holding Corp.	2005-USD 89,694 2004-USD 73,400	100.00%	\$ 5,277,693	100.00%	3,033,363
Gainia Intellectual Asset Services, Inc.	6,400	48.30%	5,584	48.30%	5,472
Subtotal			<u>5,283,277</u>		<u>3,038,835</u>
<b>Carried under the cost method</b>					
Darly 3 Venture Corporation	2005-10,200 2004-17,000	4.98%	10,200	4.98%	17,000
Telewise Communications, Inc.	10,008	6.98%	-	6.98%	-
Hi Top Communications Corp.	30,000	7.41%	30,000	7.41%	30,000
Advanced Image Technology Corp.	44,850	19.50%	-	19.50%	44,850
Tai Yi Precision Corporation	12,000	1.67%	12,000	-	-
Akom Technology Corporation	8,000	16.67%	8,000		
Subtotal			<u>60,200</u>		<u>91,850</u>
Total			<u><b>\$ 5,343,477</b></u>		<u><b>3,130,685</b></u>

Gains on investment accounted for under the equity method based on the audited financial statements prepared by investee companies for the year ended December 31, 2005 and 2004 were as follows:

<b>Investee</b>	<b>Year Ended December 31,</b>	
	<b>2005</b>	<b>2004</b>
Inventec Appliances (Cayman) Holding Corp.	\$ 1,500,384	695,906
Gainia Intellectual Asset Services, Inc.	112	480
Total	<u><b>\$ 1,500,496</b></u>	<u><b>696,386</b></u>

The Company invested in Inventec Appliances (Cayman) Holding Corp., a wholly-owned holding company, which engages in various investments. In 2005 and 2004, the amount of investment in Inventec Appliances (Cayman) Holding Corp. increased by US\$16,294 and \$32,982, respectively.

As of December 31, 2005 and 2004, any unrealized inter-company profits were eliminated by the stockholding ratio.

For the year ended December 31, 2005, the Company invested \$12,000 and \$8,000 in Tai Yi Precision Corporation and Akom Technology Corporation, respectively. The shareholding ratios were 1.67% and 16.67%, respectively. These investees are accounted for under the cost method.

**INVENTEC APPLIANCES CORPORATION**

**Notes to Financial Statements (continued)**

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

Darly 3 Venture Corporation, one of the investees accounted for under the cost method, filed for fund reduction in 2005. The capital returned amounted to \$6,800 was reflected, as the result of the fund reduction, the Company's current stockholding ratio is 4.98%.

Advanced Image Technology Corp., one of the investees accounted for under the cost method, has continued losses on its operation and the evidence suggests that impairment in the value of investment may be other than temporary and the possibility of recovery is considered remote, \$44,850 of loss of investment was recognized immediately.

For investees that the Company's has controlling interests over their operation, in accordance with SFAS and ruling of Securities and Futures Bureau, will be included in the Company's current consolidated financial statements, which has been prepared by the Company.

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

As of December 31, 2005 and 2004, insurance coverage for the property, plant, and equipment amounted to \$1,177,325 and \$1,071,800, respectively.

**(f) Pension Plan**

Pursuant to the Labor Standards Law, the Company contributes to the pension fund and deposits with Central Trust of China. As of December 31, 2005 and 2004, the changes in the pension fund account were shown below:

	<b>Year Ended December 31,</b>	
	<b>2005</b>	<b>2004</b>
Beginning Balance	\$ 259,682	203,738
Add: Current Contributed	65,037	53,237
Current Interest earned	4,186	2,707
Less: Current pension expenses	(3,315)	-
Ending Balance	<b>\$ 325,590</b>	<b>259,682</b>

For the year ended December 31, 2005 and 2004, actuarial assumptions used in pension costs calculation were as follows:

	<b>Year Ended December 31,</b>	
	<b>2005</b>	<b>2004</b>
Discount rate	3.00%	2.50%
Rate if increase in future compensation levels	2.00%	1.50%
Expected long-term rate of return on plan assets	3.00%	2.50%

**INVENTEC APPLIANCES CORPORATION**

**Notes to Financial Statements (continued)**

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

As of December 31, 2005 and 2004, the funded status reconciled with accrued pension expense per book was as follows:

	<u><b>December 31, 2005</b></u>	<u><b>December 31, 2004</b></u>
Benefit obligation		
Vested benefit obligation	\$ (34,163)	(23,859)
Non-vested benefit obligation	<u>(332,507)</u>	<u>(289,415)</u>
Accumulated benefit obligation	(366,670)	(313,274)
Effect of future salary increase	<u>(89,896)</u>	<u>(82,629)</u>
Estimated benefit obligation	(456,566)	(395,903)
Fair value of pension plan assets	<u>325,590</u>	<u>259,682</u>
Funded status	(130,976)	(136,221)
Unrecognized net transition benefit obligation	62,390	68,629
Unredognized gain on pension fund assets	99,111	75,051
Retroactive recognition of accrued pension liabilities	<u>(71,605)</u>	<u>(61,052)</u>
Accrued pension expense	<u><b>\$ (41,080)</b></u>	<u><b>(53,593)</b></u>

As of December 31, 2005 and 2004, the vested benefit of the Company's pension plan were \$35,535 and \$24,628, respectively.

As of December 31, 2005 and 2004, the components of net pension costs were as follows:

	<u><b>Year Ended December 31,</b></u>	
	<u><b>2005</b></u>	<u><b>2004</b></u>
Service cost	\$ 27,810	25,212
Interest cost	12,876	6,951
Expected return on pension plan assets	(8,239)	(5,094)
Unrecognized net transition benefit obligation	6,239	6,239
Un-amortised gain/(loss) on pension fund assets	3,285	-
Net pension cost	<u><b>\$ 41,971</b></u>	<u><b>33,308</b></u>

The Company adopted defined contribution pension plan to account for pension cost. As of December 31, 2005, the current pension expense was \$21,472 which is deposited with the Bureau of Labor Insurance.

**INVENTEC APPLIANCES CORPORATION**

**Notes to Financial Statements (continued)**

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

**(g) Income Tax**

(i) Deferred income tax assets and liabilities:

	<b>December 31,2005</b>		<b>December 31,2004</b>	
	<b>Amount</b>	<b>Income Tax Effects</b>	<b>Amount</b>	<b>Income Tax Effects</b>
<b>Deferred tax assets arising from deductible temporary differences:</b>				
-Recognition of unrealized foreign exchange loss	231,861	57,965	188,184	47,046
-Recognition of allowance for inventory obsolescence	240,389	60,097	42,101	10,525
-Bad debt losses	57,075	14,269	-	-
-Recognition of income from long-term investment accounted for under the equity method	(2,211,062)	(552,766)	(710,678)	(177,670)
-Cumulative translation adjustment	(27,670)	(6,918)	183,504	45,876
-Investment tax credit	-	108,207	-	-
-Reserve for employee retirement benefit	(36,817)	(9,204)	(13,751)	(3,438)
-Reserve for employee welfare	5,144	1,286	8,070	2,018
-Unrealized inter-company profit	116,045	29,011	163,812	40,953
-Unrealized warranty reserve	1,396,264	349,066	1,399,833	349,958
-Royalty reserve	277,278	69,320	194,499	48,625
-Compensation reserve	-	-	24,000	6,000
-Unrealized devaluation loss on long-term investment under the cost method	54,858	13,715	10,008	2,502
		<b>\$ 134,048</b>		<b>372,395</b>

(ii)

	<b>December 31,2005</b>	<b>December 31,2004</b>
Deferred tax assets - current	\$ 270,245	99,592
Deferred tax liabilities - current	-	-
Net	<b>\$ 270,245</b>	<b>99,592</b>
Deferred tax assets - non-current	\$ 432,691	453,911
Deferred tax liabilities - non-current	(568,888)	(181,108)
Net	<b>\$ (136,197)</b>	<b>272,803</b>

(iii) The components of income tax expenses were summarized as follows:

	<b>December 31, 2005</b>	<b>December 31,2004</b>
Current income tax expense(includes 10% surtax on undistributed earnings)	\$ 287,857	442,511
Deferred income tax expense (benefit)	185,553	(82,283)
Under/(over) accrual of prior year's income tax	(7,755)	(10,511)
Income tax expense	<b>\$ 465,655</b>	<b>349,717</b>

**INVENTEC APPLIANCES CORPORATION**

**Notes to Financial Statements (continued)**

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

(iv) The income tax expenses for the year ended December 31, 2005 and 2004 were calculated as follows:

	<b>For the Year Ended December 31,</b>	
	<b>2005</b>	<b>2004</b>
Income tax calculated by statutory rate	\$ 863,945	610,096
Permanent differences	(2,720)	(1,978)
Income tax separately levied	2,141	1,889
Tax-exempt income	(20,505)	(17,487)
10% surtax on undistributed earnings	24,903	52,428
Investment tax credits used	(285,717)	(284,720)
Unused investment tax credit	(108,207)	-
Under/(over) accrual of prior year's deferred income tax assets	(430)	-
Under/(over) accrual of prior year's income tax	(7,755)	(10,511)
<b>Income tax expense</b>	<b>\$ 465,655</b>	<b>349,717</b>

(v) The Company's tax returns and stockholders' imputation tax credit account through the calendar year 2002 have been assessed by the Tax Authority.

(vi) The Company's wireless communication and digital accessory products conform to "the Regulations Regarding Awards for Newly Emerging and Strategic Industries Under Manufacturing and Technical Service Industries" and "the Statute for Upgrading Industries ". Approbated by the Tax Authority, the Company is eligible for five-year income tax exemption since year 2003.

(vii) The balance of unused investment tax credit which may be used to offset against future income tax liabilities were as follows:

<b>Incurring Year</b>	<b>Investment Tax Credit</b>	<b>Year of Expiration</b>
2005 (Not ratified)	<b>\$ 108,207</b>	2009

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

As of December 31, 2005 and 2004, the balance of stockholders' imputation tax credit account was \$307,170 and \$384,762, respectively.

After filing the corporate income tax returns, tax credit for earnings distributed to R.O.C residents in year 2005 and 2004 were as follows:

	<b>For The Year Ended December 31,</b>	
	<b>2005 (Estimated)</b>	<b>2004 (Actual)</b>
Rates of tax credit for first earnings distributed (cash dividend)	9.94%	20.79%
Rates of tax credit for second earnings distributed (stock dividend)	9.94%	20.89%

As of December 31, 2005, the balance of undistributed retained earnings amounted to \$3,089,442, of which the entire portion was accumulated after January 1, 1998.

**INVENTEC APPLIANCES CORPORATION**  
**Notes to Financial Statements (continued)**

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

**(h) Capital Increase**

On May 10, 2005, pursuant to resolutions of the annual stockholders' meeting, the Company increased its capital by capitalizing its earnings of \$280,000 and employee bonuses of \$20,000, for a total of \$300,000 and the record date was July 20, 2005. The Company also resolved to further increase its capital in cash by issuing additional 23,000,000 of shares at \$108 per share. Its outstanding capital following these capital increases amounted to \$3,330,000 with November 8, 2005 as the record date. The Company had completed relevant registration process for these capital increases.

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

**(i) Dividend Policy and Earnings Distributions**

(i) Dividend Policy:

In consideration of the Company's long-term financial planning, funding needs and the stockholders' satisfaction regarding to cash in-flow, when after-tax earning occurs, annual cash dividends shall be distributed and shall be greater than 10% of the current year's total cash and stock dividends.

(ii) Earnings Distributions

The Company's Articles of Incorporation requires that after-tax earnings shall first offset cumulative losses, and 10% of the remainder be set aside as legal reserve. The remaining balance is distributed according to any proposals presented at the annual stockholders' meeting by the Board of Directors, of which remuneration of directors and supervisor cannot exceed 3% and 2% to 7% for employee bonus.

Pursuant to resolutions of the annual stockholders' meetings held on May 10, 2005 and April 27, 2004, the Company resolved to distribute retained earnings of 2003 and 2004. the summarized distribution are shown below:

	<b>For The Year Ended December 31,</b>	
	<b>2005</b>	<b>2004</b>
Dividends (dollar) distributed per common share		
-Cash dividends	\$ 5.6	5.6
-Stock dividends (face value)	1.0	1.0
Total	<b>\$ 6.6</b>	<b>6.6</b>
Employee bonuses-stock (face value)	\$ 20,000	20,000
Employee bonuses-cash	111,715	101,138
Remuneration to directors and supervisors	56,449	51,916
Total	<b>\$ 188,164</b>	<b>173,054</b>

The distributions stated above fulfilled the resolution of the Board of Directors meetings. Earnings per share after tax of 2004 and 2003 will decrease from \$7.74 and \$8.18 to \$7.04 and \$7.45 if the dividends mentioned above were all distributed in cash and were recognized as current expense.

**INVENTEC APPLIANCES CORPORATION**

**Notes to Financial Statements (continued)**

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

The Board of Directors has yet to submit the proposal for the distribution of 2005 earnings to the stockholders' meeting for resolutions. The information on the distribution of 2005 earnings will be announced through Market Observation Post System on the internet after the stockholders' meeting.

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

For the year ended December 31, 2005 and 2004, the basic earning per share is computed as follows:

	<b>Year Ended December 31,</b>			
	<b>2005</b>		<b>2004</b>	
	<b>Before Tax</b>	<b>After Tax</b>	<b>Before Tax</b>	<b>After Tax</b>
Net income	<u>\$ 3,455,820</u>	<u>2,990,165</u>	<u>2,440,425</u>	<u>2,090,708</u>
Weighted-average shares outstanding (in thousands)	<u>313,833</u>	<u>313,833</u>	<u>270,250</u>	<u>270,250</u>
Retroactively adjusted weighted- average number of shares outstanding (in thousands)			<u>299,205</u>	<u>299,205</u>
Basic earnings per share	<u>\$ 11.01</u>	<u>9.53</u>	<u>9.03</u>	<u>7.74</u>
Basic earnings per share-retroactively adjusted			<u>\$ 8.16</u>	<u>6.99</u>

**(k) Financial Instruments**

- (i) Financial Derivatives: None.
- (ii) Fair Value of Financial Instrument

	<b>December 31, 2005</b>		<b>December 31, 2004</b>	
	<b>Book Value</b>	<b>Fair Value</b>	<b>Book Value</b>	<b>Fair Value</b>
<b>Financial Assets</b>				
Book value equal to fair value	\$ 25,393,575	25,393,575	20,774,543	20,774,543
Long-term equity investments	5,343,477	5,368,618	3,130,685	3,120,300
Total financial assets	<u>\$ 30,737,052</u>	<u>30,762,193</u>	<u>23,905,228</u>	<u>23,894,843</u>
<b>Financial Liabilities</b>				
Book value equal to fair value	<u>\$ 22,241,810</u>	<u>22,241,810</u>	<u>18,103,271</u>	<u>18,103,271</u>

Method and assumptions used to establish the fair values of financial instruments are as follows:

1. The fair value of short-term financial instruments is determined by their face values stated on the balance sheet. Because such instruments will mature on short notice, the face value serves as reasonable basis for establishing the fair value. The method is applied to cash, accounts receivable, other current assets, notes payable, accounts payable and other current liabilities.
2. Because there are no market quotes or reference reports for non-listed companies, the fair value of these investments is determined by their net equity worth or cost, and the book value of these investments accounted for under the cost or the equity method are based on audited or self-prepared financial statements of investee companies. For investee companies that are listed company, the fair value of these investments is determined by its market value.
3. With respect to financial instruments such as refundable deposits that are indispensable guarantee for the on-going operation of the Company, it is impossible to estimate the time necessary to accomplish the exchange of assets. Consequently, the fair market value of such financial instruments cannot be established. Therefore, the book value is used as the fair market value.

**INVENTEC APPLIANCES CORPORATION**

**Notes to Financial Statements (continued)**

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

(iii) Financial Instrument with Off-Balance-Sheet Credit Risk:

Guarantee and Endorsements provided by the Company for related parties' bank loans are stated in note 5.

(iv) Concentration of Credit Ricks:

Group concentrations of credit risk exist if the transacting party is an individual or a number of counter-parties which engage in similar activities or activities in the same region or share other similar economic characteristics that would cause their ability to meet contractual obligations with changes in economic or other conditions. Implicit credit risk of the Company arises from accounts receivable. As of December 31, 2005 and 2004, the amounts of due from company A were 83% and 85% of the balance of the Company's accounts receivable. To minimize credit risk, the Company periodically evaluates company A's financial positions and the possibility of collecting trade receivables due from it. The Company believes that the possibility of arising bad debt losses is remote, since the condition of collecting these outstanding receivables is satisfied.

As of December 31, 2005 and 2004, the Company's contracts with credit risk concentration were the following:

<u>Accounts Receivable-By Region</u>	<u>December 31, 2005</u>	<u>December 31, 2004</u>
Domestic	\$ 210,862	400,327
Asia	1,346,428	1,420,766
Europe	3,844,781	2,864,205
Americas	15,271,216	12,375,488
Other	825,684	297,511
Total	<u>\$ 21,498,971</u>	<u>17,358,297</u>

**(5) Related Party Transactions**

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

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

**INVENTEC APPLIANCES CORPORATION**

**Notes to Financial Statements (continued)**

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

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

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

(i) Sales

For the year ended December 31, 2005 and 2004, sales to related parties were as follows:

	<b>Year Ended December 31,</b>			
	<b>2005</b>		<b>2004</b>	
	<b>Amount</b>	<b>% of Net Sales</b>	<b>Amount</b>	<b>% of Net Sales</b>
Inventec Appliances (BVI) Corp.	\$ 1,378,126	1%	2,885,281	4%
Inventec Appliances (USA) Distribution Corp.	6,573,117	6%	3,226,424	4%
Tapwave, Inc.	-	-%	6,681	-%
Others	1,348	-%	713	-%

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

In 2005, the company sold materials and work in process for further processing to Inventec Appliances (Shanghai) Co., Ltd. and Inventec Appliances (Pudong) Co., Ltd. via Inventec Appliances (BVI) Corp. All of the finished goods are repurchased back by the Company. To prevent double recording of sales, the inventory items sold to Inventec Appliances (BVI) Corp. is disclosed in net, yet receivables and payables are disclosed in aggregate.

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

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

As of December 31, 2005 and 2004, unrealized gross margin of sales to related parties, which is recognized as other liabilities - Deferred credit, was \$111,582 and \$158,132, respectively.

(ii) Purchases

For the year ended December 31, 2005 and 2004, purchases from related parties were as follows:

	<b>Year Ended December 31,</b>			
	<b>2005</b>		<b>2004</b>	
	<b>Amount</b>	<b>% of Net Purchases</b>	<b>Amount</b>	<b>% of Net Purchases</b>
Inventec Appliances (BVI) Corp.	\$ 103,559,640	91%	63,266,127	88%
Inventec Micro-Electronics (BVI) Corporation	-	-%	43,385	-%

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

**INVENTEC APPLIANCES CORPORATION**

**Notes to Financial Statements (continued)**

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

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

(iii) Property Transaction

1. In 2005, the Company sold properties to Inventec Appliances (Pudong) Co., Ltd. and Inventec Appliances (Shanghai) Co., Ltd. at the price of \$1,186 and the cost of the properties was \$867, resulting in a gain on disposal of properties of \$318.
2. In 2004, the Company sold properties and deferred assets to Inventec Appliances (BVI) Corp. at cost \$49,736. Unrealized gain on disposal of properties and deferred assets amounted to \$8,630 and was recorded as other liabilities - Deferred Credit.
3. In 2005, the Company has purchased machinery, at cost of \$5,257, from Inventec Corporation.

(iv) Others

1. For the year ended December 31, 2005 and 2004, business consulting fee and computer system expense paid to Inventec Corporation amounted to \$36,563 and \$20,238, respectively.
2. For the year ended December 31, 2004, rental expense and processing fees paid to Inventec Besta Corp. amounted \$2,313.

(v) Financing to related parties

The Company's financing to a related party for the year ended December 31, 2005 was as follows:

	<b>December 31, 2005</b>			
	<b>Maximum Balance</b>	<b>Ending Balance</b>	<b>Interest Rate</b>	<b>Current Interest</b>
Inventec Appliances (BVI) Corp.	\$ 437,142	437,142	-	-
Inventec Appliances (Pudong) Co., Ltd.	536,851	536,851	5%	6,478
<b>Total</b>	<b>\$ 973,993</b>	<b>973,993</b>		

Part of accounts receivable from Inventec Appliances (BVI) Corp., which have been outstanding for a period longer than six months since the expiration of the normal credit term, are classified as other receivable (disclosed as financing to related-parties) and sufficient allowance for doubtful account is provided thereon.

On June 28, 2005, pursuant to resolutions of the Board of Directors meeting, the Company rented machineries to Inventec Appliances (Pudong) Co., Ltd. by capital leasing. The rental is reclassified in accordance to its nature to other receivable - current/non-current.

(vi) Accounts Receivable (Payable)

	<b>December 31, 2005</b>		<b>December 31, 2004</b>	
	<b>Balance</b>	<b>%</b>	<b>Balance</b>	<b>%</b>
<b>Accounts receivable:</b>				
Inventec Appliances (BVI) Corp.	\$ 825,684	4	297511	2
Inventec Appliances (USA) Distribution Corp.	1,391,394	6	1023798	6
Others	26	-	76	-
<b>Total</b>	<b>\$ 2,217,104</b>	<b>10</b>	<b>1,321,385</b>	<b>8</b>

**INVENTEC APPLIANCES CORPORATION**

**Notes to Financial Statements (continued)**

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

	<b>December 31, 2005</b>		<b>December 31, 2004</b>	
	<b>Balance</b>	<b>%</b>	<b>Balance</b>	<b>%</b>
<u>Accounts payable:</u>				
Inventec Appliances (BVI) Corp.	\$ 19,732,240	95	15,568,087	92
Other	-	-	138	-
<b>Total</b>	<b>\$ 19,732,240</b>	<b>95</b>	<b>15,568,225</b>	<b>92</b>
<u>Accrued expenses</u>				
Inventec Appliances (BVI) Corp.	\$ 32,256	4	10,167	2
Other	3,178	-	-	-
<b>Total</b>	<b>\$ 35,434</b>	<b>4</b>	<b>10,167</b>	<b>2</b>

(vii) Guarantee and Endorsements

As of December 31, 2005 and 2004, endorsements and guarantees provided by the Company for related parties' bank loans were as follows:

	<b>Amount of Guarantee</b>	
	<b>December 31, 2005</b>	<b>December 31, 2004</b>
Inventec Appliances (Cayman) Holding Corp.	US\$ 61,550	US\$ 46,550
Inventec Appliances (BVI) Corp.	6,500	6,500
Inventec Appliances (USA) Distribution Corp.	8,000	8,000
Inventec Appliances (Shanghai) Co., Ltd.	23,000	23,000
Inventec Appliances (Pudong) Co., Ltd.	55,000	40,000
Inventec Appliances (Jiangning) Co., Ltd.	44,000	19,000
Inventec Appliances (Nangjing) Co., Ltd.	1,500	1,500
Inventec Appliances (Shanghai) International Marketing Co., Ltd.	16,000	-
<b>Total</b>	<b>US\$ 215,550</b>	<b>US\$ 144,550</b>

**(6) Pledged Assets**

Assets pledged as collateral as of December 31, 2005 and 2004, were summarized as follows:

	<b>December 31, 2005</b>	<b>December 31, 2004</b>	<b>Purpose of pledge</b>
Refundable deposits	<b>\$ 5,692</b>	<b>4,870</b>	Deposits for buildings

**(7) Significant Commitments and Contingencies (Foreign Currency in thousands)**

- (a) As of December 31, 2005 and 2004, unused letters of credit were US\$439 and US\$73, JPY 7,160, respectively.
- (b) As of December 31, 2005 and 2004, the promissory notes issued for bank credit limits, Industrial Development Bureau (IDB) subsidies, and IDB Cooperation funds amounted to US\$ 25,500, EUR\$ 500, \$1,829,633 and US\$15,000, \$2,042,383, respectively.

**INVENTEC APPLIANCES CORPORATION**

**Notes to Financial Statements (continued)**

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

- (c) As of December 31, 2005 and 2004, promissory notes received for business demands and applications to the Ministry of Economic Affairs amounted to \$79,800 and \$150,248, respectively.
- (d) For year ended December 31, 2005 and 2004, the Company entered into a lease agreement to lease computers and software. Information regarding rental expense and future lease payments are as follows:

Year	Rent expense	Future rent due			
		2005	2006	2007	2008
2005	\$ 22,532	-	19,886	9,261	1,444
2004	\$ 14,529	17,392	11,891	2,677	-

- (e) In October 2001, FeiMa Communication (Qing Dao) Co., Ltd. filed a lawsuit against the Company. The local peoples' court in China ruled that the Company breached an agreement and is required to pay RMB5,000 and litigation expense of RMB33. In April 2003, the Company filed for an appeal. On May 20, 2005, the Company settled with FeiMa Communication (Qing Dao) Co., Ltd. out of court and paid RMB3,990.
- (f) On January 7, 2004, Mitake Information Corporation filed a lawsuit for patent infringement against the Company seeking for a compensation of \$1,000. The Company has provided the Intellectual Property Office with sufficient evidences, and the local district Court has ruled to dismiss this lawsuit.
- (g) Two international well-known technology companies alleged that the Company infringes certain patents by producing and selling mobile phone products. However, these two companies are not yet filing any law suit against the Company. The Company is aggressively preparing relevant data and intently negotiating with these two companies. As of December 31, 2005, the Company has exercised appropriate accounting procedures corresponding to such claim for infringement and believes the event mentioned above will not have material effect on the Company's operations.
- (h) Any Guarantee and Endorsement and Significant Commitments and Contingencies that the Company provides to related-parties are stated in note 5.
- (8) Significant Catastrophic Losses: None.**
- (9) Significant Subsequent Events: None.**

**INVENTEC APPLIANCES CORPORATION**

**Notes to Financial Statements (continued)**

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

**(10) Others**

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

Categorized as Nature	For the year ended December 31,					
	2005			2004		
	Operating Cost	Operating Expenses	Total	Operating Cost	Operating Expenses	Total
Personnel Cost						
Salary	504,811	943,743	1,448,554	522,273	666,156	1,188,429
Health and labor insurance	31,375	42,236	73,611	26,704	31,952	58,656
Pension	19,398	44,045	63,443	11,283	22,025	33,308
Other	35,524	32,556	68,080	27,419	26,404	53,823
Depreciation	63,801	80,066	143,867	63,374	68,758	132,132
Amortization	55,151	36,474	91,625	58,838	52,486	111,324

**(11) Business Segment Information**

**(a) Industry:**

The company does not engaged in business activities outside of the electronics industry.

**(b) Geographical region:**

The company conducts its businesses only domestically and has no overseas business units.

**(c) Exports:**

Region	For the Year Ended December 31,	
	2005	2004
America	\$ 67,127,039	\$ 46,431,143
Europe	31,750,701	13,393,725
Asia	9,709,826	8,455,869
Other	1,378,126	2,896,712
Total	<u>\$ 109,965,692</u>	<u>\$ 71,177,449</u>

**(d) Major Clients:**

In 2005 and 2004, clients with revenues over 10% of total revenues of the Company were the following:

2005			2004		
Name	Amount	%	Name	Amount	%
A	\$ 79,503,024	70%	A	53,397,828	70%
B	13,754,123	12%	B	1,762,053	2%