

INVENTEC CORPORATION
FINANCIAL STATEMENTS
SIX MONTHS ENDED JUNE 30, 2004 AND 2003
AND
INDEPENDENT AUDITORS' REPORT

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Inventec Corporation

Financial Statements

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Independent Auditors' Report

Inventec Corporation:

We have audited the accompanying balance sheets of Inventec Corporation as of June 30, 2004 and 2003, and the related statements of income, changes in stockholders' equity, and cash flows for the six months 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.

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

As described in Note 4.d, as of June 30, 2004 and 2003, long-term equity investments of Inventec Corporation were \$10,206,725 thousand and \$10,328,985 thousand, respectively. Equity earnings related thereto for the six months ended June 30, 2004 and 2003, were \$354,474 thousand and \$549,967 thousand, respectively, which were recognized based upon the financial statements prepared by the investee companies and not audited in compliance with the audit procedures mentioned in the preceding paragraph.

In our opinion, except for the effects of any adjustments that might have emerged had the financial statements of investee companies been audited by independent accountants, the financial statements referred to above present fairly, in all material respects, the financial position of Inventec Corporation as of June 30, 2004 and 2003, and the results of its operations and its cash flows for the six months then ended in conformity with the "Rules Governing Auditing and Certification of Financial Statements by Certified Public Accounts" and generally accepted accounting principles of the Republic of China.

Taipei, Taiwan, R.O.C.
August 6, 2004

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 audit such financial statements are those generally accepted and applied in the Republic of China.

INVENTEC CORPORATION
BALANCE SHEETS
JUNE 30, 2004 AND 2003
(New Taiwan Dollars in Thousands, Except for Share Data)

| | June 30, 2004 | | June 30, 2003 | |
|--|----------------------|------------|----------------------|------------|
| | Amount | % | Amount | % |
| ASSETS | | | | |
| Current Assets: | | | | |
| Cash and cash equivalents (Notes 2 and 4.a) | \$ 10,387,718 | 16 | 6,023,172 | 14 |
| Notes receivable (Note 2) | | | | |
| - Other customers | 18 | - | 1,190 | - |
| - Related parties | 8,747 | - | 984 | - |
| Accounts receivable - less allowance for doubtful accounts (Notes 2 and 4.b) | | | | |
| - Other customers | 13,779,188 | 22 | 6,843,568 | 16 |
| - Related parties | 5,925,841 | 9 | 5,741,192 | 14 |
| Other financial assets - current | 17,376,065 | 27 | 6,104,090 | 15 |
| Inventories, net of allowance for market value decline and obsolescence (Notes 2 and 4.c) | 1,839,596 | 3 | 1,885,282 | 5 |
| Prepayments and other current assets | 98,129 | - | 118,401 | - |
| Deferred tax assets - current (Notes 2 and 4.i) | 683,449 | 1 | 392,355 | 1 |
| | <u>50,098,751</u> | <u>78</u> | <u>27,110,234</u> | <u>65</u> |
| Long-term equity investments (Notes 2 and 4.d) | | | | |
| Accounted for under the equity method | 10,206,725 | 16 | 10,328,985 | 25 |
| Accounted for under the cost method | 1,865,114 | 3 | 1,574,802 | 4 |
| | <u>12,071,839</u> | <u>19</u> | <u>11,903,787</u> | <u>29</u> |
| Other financial assets - non-current (Notes 6) | | | | |
| | <u>56,752</u> | <u>-</u> | <u>60,498</u> | <u>-</u> |
| Property, Plant, and Equipment (Notes 2 and 4.e) | | | | |
| Land | 788,144 | 1 | 788,870 | 2 |
| Buildings | 427,252 | 1 | 427,252 | 1 |
| Machinery | 527,561 | 1 | 906,773 | 2 |
| Transportation equipment | 26,332 | - | 24,458 | - |
| Furniture and office facilities | 952,338 | 2 | 913,699 | 2 |
| Other equipment | 213,822 | - | 220,297 | 1 |
| Less: Accumulated depreciation | (1,376,396) | (2) | (1,601,474) | (4) |
| Construction in progress | - | - | 3,394 | - |
| Prepayment on equipment | 885 | - | 2,630 | - |
| | <u>1,559,938</u> | <u>3</u> | <u>1,685,899</u> | <u>4</u> |
| Intangible Assets(Notes 2 and 4.h) | | | | |
| Deferred Pension Cost | 117,546 | - | - | - |
| Other Assets: | | | | |
| Deferred debits - intercompany loss (Note 2) | 194,663 | - | 194,663 | - |
| Other assets (Notes 2 and 4.f) | 161,768 | - | 815,706 | 2 |
| | <u>356,431</u> | <u>-</u> | <u>1,010,369</u> | <u>2</u> |
| TOTAL ASSETS | \$ 64,261,257 | 100 | 41,770,787 | 100 |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | | | |
| Current Liabilities: | | | | |
| Shortterm-Debt (Note 4.g) | \$ 581,735 | 1 | - | - |
| Notes payable | | | | |
| - Other vendors | 449,801 | 1 | 725,110 | 2 |
| - Related parties | 125 | - | 4,746 | - |
| Accounts payable | | | | |
| - Other vendors | 14,279,235 | 22 | 7,044,381 | 17 |
| - Related parties | 16,293,928 | 25 | 4,732,839 | 11 |
| Income tax payable | 87,850 | - | 146,381 | - |
| Accrued expenses | 567,137 | 1 | 451,641 | 1 |
| Advance collection | 26,961 | - | 47,110 | - |
| Other current liabilities | 3,080,662 | 5 | 1,357,012 | 3 |
| Estimated warranty reserve (Note 2) | 990,994 | 1 | 746,146 | 2 |
| | <u>36,358,428</u> | <u>56</u> | <u>15,255,366</u> | <u>36</u> |
| Other Liabilities: | | | | |
| Accrued pension liabilities (Notes 2 and 4.h) | 346,956 | 1 | 183,964 | - |
| Deferred tax liabilities - non-current (Notes 2 and 4.i) | 384,341 | 1 | 283,799 | 1 |
| Deferred credits - intercompany profits (Note 2) | 121,452 | - | 255,180 | 1 |
| Other liabilities | 450 | - | 2,564 | - |
| | <u>853,199</u> | <u>2</u> | <u>725,507</u> | <u>2</u> |
| Total Liabilities | <u>37,211,627</u> | <u>58</u> | <u>15,980,873</u> | <u>38</u> |
| Stockholders' Equity | | | | |
| Capital Stock, par value \$10 per share; authorized 2,500,000,000 shares, 2,026,000,000 shares issued and outstanding as of June 30, 2004; authorized 2,000,000,000 shares, 1,835,000,000 shares issued and outstanding as of June 30, 2003. | 20,260,000 | 31 | 18,350,000 | 44 |
| Stock Dividend to be Distributed (Note 4.j) | 1,111,000 | 2 | 1,910,000 | 5.00 |
| Capital Surplus (Note 2) | | | | |
| Additional paid-in capital | 447,723 | 1 | 447,723 | 1 |
| Capital surplus of long-term investments | 121,064 | - | 121,064 | - |
| Other | 177 | - | 177 | - |
| Retained Earnings: | | | | |
| Legal reserve (Note 2) | 3,333,254 | 5 | 2,910,055 | 7 |
| Undistributed earnings (Notes 2 and 4.i) | 1,698,763 | 3 | 1,894,344 | 5 |
| Cumulative translation adjustments (Note 2) | 78,649 | - | 156,551 | - |
| Total Stockholders' Equity | <u>27,050,630</u> | <u>42</u> | <u>25,789,914</u> | <u>62</u> |
| Commitments and Contingencies (Note 2 and 7) | | | | |
| TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY | \$ 64,262,257 | 100 | 41,770,787 | 100 |

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

INVENTEC CORPORATION
STATEMENTS OF INCOME
SIX MONTHS ENDED JUNE 30, 2004 AND 2003
(New Taiwan Dollars in Thousands, Except for Share Data)

| | 2004 | | 2003 | |
|---|---------------------|------------------|-------------------|------------------|
| | Amount | % | Amount | % |
| Operating Revenue: | | | | |
| Net sales | \$ 58,616,071 | 100 | 38,327,931 | 100 |
| Technical service revenue | 1,757 | - | 4,413 | - |
| Net operating revenue | 58,617,828 | 100 | 38,332,344 | 100 |
| Operating Cost: | (55,461,109) | (95) | (35,487,821) | (92) |
| | 3,156,719 | 5 | 2,844,523 | 8 |
| Realized intercompany profits | (13,627) | - | (31,771) | - |
| Unrealized intercompany profits | 3,075 | - | 99,201 | - |
| Gross margin | 3,146,167 | 5 | 2,911,953 | 8 |
| Operating Expenses: | | | | |
| Selling expenses | (1,269,515) | (2) | (1,225,871) | (3) |
| Administrative expenses | (369,720) | (1) | (504,684) | (1) |
| Research and development expenses | (700,210) | (1) | (652,764) | (2) |
| | (2,339,445) | (4) | (2,383,319) | (6) |
| Income from Operations | 806,722 | 1 | 528,634 | 2 |
| Non-Operating Revenues: | | | | |
| Interest revenue | 60,862 | - | 52,397 | - |
| Investment income accounted for under the equity method(Note 4.d) | 354,474 | 1 | 549,967 | 1 |
| Dividend income(Note 4.d) | 480 | - | 600 | - |
| Gain on disposition of property | 18,097 | - | 14,348 | - |
| Foreign exchange gain | - | - | 14,030 | - |
| Other revenue | 355,273 | 1 | 229,819 | 1 |
| | 789,186 | 2 | 861,161 | 2 |
| Non-Operating Expenses: | | | | |
| Interest expense | (7,604) | - | (255) | - |
| Loss on disposal of properties | (25) | - | - | - |
| Foreign exchange loss | (319,990) | (1) | - | - |
| Losses on inventory devaluation and obsolescence | (15,935) | - | (1,073) | - |
| Other expenses | (7,269) | - | (20,568) | - |
| | (350,823) | (1) | (21,896) | - |
| Income before income tax | 1,245,085 | 2 | 1,367,899 | 4 |
| Income tax benefit(Note 4.h) | 14,668 | - | 86,771 | - |
| Net Income | \$ 1,259,753 | 2 | 1,454,670 | 4 |
| | Before Tax | After Tax | Before Tax | After Tax |
| Earnings per share (Notes 2 and 4.k) | | | | |
| Basic | \$ 0.61 | 0.62 | 0.75 | 0.79 |
| Earnings per share after retroactive adjustment | | | | |
| Basic | \$ - | - | 0.68 | 0.72 |

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

INVENTEC CORPORATION
STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
SIX MONTHS ENDED JUNE 30, 2004 AND 2003
(New Taiwan Dollars in Thousands)

| | Capital Stock | Stock Dividend to be Distribted | Capital Surplus | Retained Earnings | | Cumulative Translation Adjustment | Total |
|---|----------------------|---------------------------------------|--------------------|-------------------|---------------------------|---|-------------------|
| | | | | Legal Reserve | Undistributed Earnings | | |
| Beginning balance, January 1, 2003 | \$ 18,350,000 | - | 568,964 | 2,575,062 | 3,828,661 | 220,647 | 25,543,334 |
| 2002 earnings distribution and appropriation: | | | | | | | |
| Legal reserve | - | - | - | 334,993 | (334,993) | - | - |
| Compensation to directors and supervisors | - | - | - | - | (90,448) | - | (90,448) |
| Employee bonus | - | - | - | - | (136,046) | - | (136,046) |
| Employee bonus in stock dividends | - | 75,000 | - | - | (75,000) | - | - |
| Stock dividends | - | 1,835,000 | - | - | (1,835,000) | - | - |
| Cash dividends distributed | - | - | - | - | (917,500) | - | (917,500) |
| Net income for the six months ended June 30, 2003 | - | - | - | - | 1,454,670 | - | 1,454,670 |
| Translation adjustment to long-term investments (net of income tax of \$21,365) | - | - | - | - | - | (64,096) | (64,096) |
| Ending balance, June 30, 2003 | \$ 18,350,000 | 1,910,000 | 568,964 | 2,910,055 | 1,894,344 | 156,551 | 25,789,914 |
| Beginning balance, January 1, 2004 | \$ 20,260,000 | - | 568,964 | 2,910,055 | 4,685,416 | 85,901 | 28,510,336 |
| 2003 earnings distribution and appropriation: | | | | | | | |
| Legal reserve | - | - | - | 423,199 | (423,199) | - | - |
| Compensation to directors and supervisors | - | - | - | - | (114,264) | - | (114,264) |
| Employee bonus | - | - | - | - | (169,615) | - | (169,615) |
| Employee bonus in stock dividends | - | 97,000 | - | - | (97,000) | - | - |
| Stock dividends | - | 1,013,000 | - | - | (1,013,000) | - | - |
| Cash dividends distributed | - | - | - | - | (2,431,200) | - | (2,431,200) |
| Net income for the six months ended June 30, 2004 | - | - | - | - | 1,259,753 | - | 1,259,753 |
| Adjustment arising from change in ownership percentage in an investee | - | - | - | - | 1,872 | - | 1,872 |
| Translation adjustment to long-term investments (net of income tax of \$2,418) | - | - | - | - | - | (7,252) | (7,252) |
| Ending balance, June 30, 2004 | \$ 20,260,000 | 1,110,000 | 568,964 | 3,333,254 | 1,698,763 | 78,649 | 27,049,630 |

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

INVENTEC CORPORATION
STATEMENTS OF CASH FLOWS
SIX MONTHS ENDED JUNE 30, 2004 AND 2003
(New Taiwan Dollars in Thousands)

| | <u>2004</u> | <u>2003</u> |
|---|----------------------|--------------------|
| Cash flows from operating activities: | | |
| Net income | \$ 1,259,753 | 1,454,670 |
| Adjustment to reconcile net income to net cash provided by operating activities: | | |
| Depreciation | 119,259 | 145,505 |
| Amortization | 137,223 | 135,427 |
| Gain on disposal and scrapping of properties | (6,856) | (5,981) |
| Gain on disposal and scrapping of deferred assets | (1,442) | (1,585) |
| Provision for inventory market decline | 15,935 | 1,073 |
| Foreign currency exchange loss (gain), net | (25,242) | (12,497) |
| (Reversal) Provision for doubtful accounts | (5,215) | 47 |
| Gain on investments recognized under the equity method in excess of cash dividends received | 427,881 | 728 |
| Provision for warranty reserve | 237,812 | 240,592 |
| Change in assets and liabilities: | | |
| Notes and accounts receivable | (3,417,399) | 1,702,926 |
| Other financial assets - current | (6,895,669) | (3,303,806) |
| Inventories | (210,737) | 647,731 |
| Prepayments and other current assets | (23,758) | (37,496) |
| Deferred tax assets and liabilities, net | (98,166) | (205,668) |
| Notes and accounts payable | 10,334,318 | (2,094,039) |
| Income tax payable | 87,850 | 146,381 |
| Accrued expenses | (194,474) | (59,652) |
| Advance collection | (91,172) | 19,415 |
| Deferred credits - intercompany profits | 132 | 41,857 |
| Other current liabilities | 22,206 | (21,954) |
| Accrued pension liabilities | 21,903 | 24,229 |
| Net cash provided by (used in) operating activities | <u>1,694,142</u> | <u>(1,182,097)</u> |
| Cash flows used in investing activities: | | |
| Increase in long-term investments | (521,172) | (303,575) |
| Purchase of property and equipment | (244,992) | (87,534) |
| Purchase of deferred assets | (142,263) | (175,969) |
| Proceeds from disposal of property and equipment | 13,089 | 18,794 |
| Proceeds from disposal of deferred assets | 10,040 | 3,441 |
| Other financial assets - non-current | (150) | 9,881 |
| (Increase) Decrease in other assets | (21,151) | 255 |
| Net cash used in investing activities | <u>(906,599)</u> | <u>(534,707)</u> |
| Cash flows from financing activities: | | |
| Increase in short-term debt | 581,735 | - |
| (Decrease) increase in other liabilities | (234) | 1,561 |
| Net cash used in financing activities | <u>581,501</u> | <u>1,561</u> |
| Effect of changes in foreign exchange rate | <u>25,242</u> | <u>12,497</u> |
| Net increase (decrease) in cash and cash equivalents | <u>1,394,286</u> | <u>(1,702,746)</u> |
| Cash and cash equivalents, beginning of the period | <u>8,993,432</u> | <u>7,725,918</u> |
| Cash and cash equivalents, end of the period | <u>\$ 10,387,718</u> | <u>6,023,172</u> |
| Supplemental disclosures of cash flow information: | | |
| Cash paid during the period for interest | <u>\$ 7,472</u> | <u>257</u> |
| Cash paid during the period for income taxes | <u>\$ -</u> | <u>-</u> |
| Investing and financing activities with no effects on cash flows: | | |
| Undistributed employee bonuses and compensation to directors and supervisors | <u>\$ 283,879</u> | <u>226,494</u> |
| Undistributed cash dividends | <u>\$ 2,431,200</u> | <u>917,500</u> |
| Acquisition of properties with cash and other payables: | | |
| Increase in property and equipment | \$ 85,472 | 91,432 |
| Add: Other payables - beginning of the period | 168,072 | 5,044 |
| Less: Other payables - end of the period | (8,552) | (8,942) |
| Cash paid | <u>\$ 244,992</u> | <u>87,534</u> |

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

INVENTEC CORPORATION
NOTES TO FINANCIAL STATEMENTS
Six Months Ended June 30, 2004 and 2003
(New Taiwan Dollars in Thousands, Unless Otherwise Stated)

1 Overview

The Company engages primarily in developing, manufacturing, processing and trading of computers, word processors and related products. Significant historical events are the following:

1975- The Company was founded with a registered capital of \$1,000 to produce calculators and telephone sets.

1989- The Company started to manufacture laptops and word processors.

The Company invested in Inventec Besta Co., Ltd.

The Company commenced to manufacture a series of electronic dictionaries as well as language CDs.

1990- The Company built overseas manufacturing plants to manufacture telephone and facsimile machines through investing in Inventec Electronics (M) SDN. BHD.

1991- The Company invested in Inventec Electronics (Shanghai) Co., Ltd. through its investment in Inventec Corporation (Hong Kong) Co., Ltd. to expand software business.

1993- Mass production of PDA's commenced.

1994- The Company invested in Inventec Electronics (Nanking) Co., Ltd., Inventec Electronics (Tianjin) Co., Ltd., Inventec Electronics (Beijing) Co., Ltd. and Inventec Electronics (Xi'an) Co., Ltd. to engage in software business.

1995- Mass production of multi-function, multimedia Pentium-computers commenced and a site at Wu-Ku Industrial Park for plant expansion was purchased.

1996- Operation of the factory in Wu-Ku commenced.

A site at Lin-Ko Industrial Park was acquired by the Company for factory expansion and construction was launched.

The Company's stock was listed in Taiwan Stock Exchange in November.

1997- Operation of the factories in Lin-Ko Industrial Zone commenced.

Subsidiaries of the Company in Scotland, Singapore and the United States were registered and engaged in assembling and after-sales services.

1998- The Company established Inventec Holding (North America) Co., Ltd. for after-sale services of its U.S. subsidiaries.

1998 The Company purchased Ta-Shi plant in Tao-Yuan. Production of servers and desktops commenced.

INVENTEC CORPORATION
NOTES TO FINANCIAL STATEMENTS (CONT'D)

- 1999- The Company sold its personal learning system department and related trademark, patents, and copyrights to the investee company Inventec Besta Co., Ltd.
- The Company sold its investment in Inventec Electronic (Xi'an) Co., Ltd. to its investee company Inventec Besta Co., Ltd.
 - The Company purchased a second factory at Wu-Ku Industrial Park for business in information appliance (IA).
 - The Company established Inventec Multimedia and Telecom Corp. for multimedia products and communication related businesses.
 - The Company established Inventec Micro-Electronics Corp. to manufacture telecommunication equipment.
 - The Company established Inventec Online Corp. for software development.
- 2000- The PDA division was transferred to Inventec Appliances Corp. and asset valuation was used as the basis of the Company's investment.
- The Company established Inventec Communication and Technology Co. for investing activities.
 - The Company sold its investment in Inventec Electronics (M) SDN. BHD. to the investee company Inventec Communication and Technology Co. to integrate operation and business.
 - Investee companies Inventec Multimedia and Telecom Corp. and Inventec Communication and Technology Co. merged to reinforce administrative efficiency, integrate resources, and reduce costs. Inventec Multimedia and Telecom Corp. is the continuing company after the merger.
 - The Company invested in Inventec Corporation (Cayman) Co., Ltd. for further investment in Inventec Corporation (Shanghai) Co., Ltd., of which parts assembling is the major line of its business.
- 2001- The Company invested in Inventec Tomorrow Studio Corporation for editorial tasks of book and electronic publication and sales.
- 2002- Inventec Online Corp. and Inventec Appliances Corp. merged to integrate resources. Inventec Appliances Corp. is the surviving company after the merger.
- 2003- The Company sold its investment in Inventec Appliance (Shanghai) Co., Ltd. to investee Appliances Corp.
- The Company invested in Inventec Corporation (Cayman) Co., Ltd. which invested in Inventec (Pudong) Corp. Inventec (Pudong) Corp. engages in parts assembling.
- 2004- The Company invested in Inventec Enterprise System Corp. was engaged in parts assembling .

INVENTEC CORPORATION
NOTES TO FINANCIAL STATEMENTS (CONT'D)

- The Company invested in Inventec (Czech) S.R.O. was engaged in parts assembling.
- The Company invested in Inventec Corporation (Cayman) Co., Ltd. which invested in Inventec (Pudong) Technology Corp. and Inventec (Shanghai Service) Co., Ltd. engages in parts assembling.
- The Company reduced shareholding in Inventec Tomorrow Studio Corp. and accounted for under the cost method.

As of June 30, 2004, the average number of employees was 2,014.

2 Summary of Significant Accounting Policies

The Company's financial statements were prepared in accordance with "Rules Governing Auditing and Certification of Financial Statement by Certified Public Accounts" and generally accepted accounting principles of the Republic of China. Summary of significant accounting policies and their measurement basis are as follows:

a Cash Equivalents

Cash equivalents are Treasury bills, commercial paper, or banker's acceptances with maturities within three months. Commercial paper and banker's acceptance are stated at cost and valued by the specific identification method. At year-end, interest receivables are accrued on unsold investments.

b Notes and Accounts Receivable and Allowance for Doubtful Accounts

Allowance for doubtful accounts is based on the age and results of the Company's evaluation of the collectibility of outstanding receivable balances. Allowance for receivables outstanding beyond 1 year and of customers with financial difficulties is fully provided, net of likely collectible amount.

c Inventories and Allowance for Inventory Market Decline and Obsolescence

Inventories are stated at cost on a perpetual inventory basis by the weighted-average method and valued at the lower of cost or market at year-end. Allowance for inventory market decline is provided for when the market value of inventories is lower than cost, and valuation is based on the total amount of inventories. Allowance for inventory obsolescence is provided for obsolete or slow-moving (over 6 months) items, net of estimated useful or salvage values.

d Long-Term Equity Investments

Long-term equity investments where the Company cannot exercise significant influence are stated at cost. If an investee company is a listed company, an allowance for market decline is provided when market price is lower than cost, with unrealized market decline charged to stockholders' equity. For non-listed companies, should evidence suggest investment value impairment may be other than temporary and the possibility of recovery remote, loss is recognized immediately, and the restated book value is the new cost.

INVENTEC CORPORATION
NOTES TO FINANCIAL STATEMENTS (CONT'D)

Long-term equity investments where the Company can exercise significant influence are accounted for under the equity method. Premium or discount on investments is amortized equally over 5 years. Exchange differences from translation of foreign- denominated financial statements at year-end are reflected as translation adjustments under stockholders' equity. If the fiscal year of the investee company is different from that of the Company, equity earnings of an investee company are recognized according to equivalent ownership at year-end closing. If the current audited financial statements are unavailable on a timely basis, gain or loss on investments are recognized in the following year based upon the current equivalent ownership of the investee company at year-end.

Unrealized intercompany transactions are eliminated and recorded as deferred debits. Regardless of downstream or upstream transactions, unrealized inter-company gains and losses are eliminated in proportion to shareholding ratio, except for in downstream transactions, where gain or loss must be fully eliminated when controlling interests exist. Unrealized gains and losses resulting from transactions between investee companies are eliminated in proportion to shareholding ratio if controlling interests exist. Otherwise the unrealized gains or losses are eliminated according to the product of shareholding ratio. Gains and losses resulted from transactions of depreciable assets are recognized ratably over their economic lives, while those from other assets are recognized immediately.

Cost and gains or losses on disposition of long-term equity investments are determined by the weighted-average method. Capital surplus from disposition of such investments is reduced by the percentage sold, with gains and losses included in current earnings.

Long-term equity investments where the Company has controlling interest are accounted for under the equity method and consolidated financial statements are required according to rules set forth in the Statement of Financial Accounting Standards ("SFAS") and by the Securities and Futures Commission ("SFC") under the Ministry of Finance ("MOF"). Consolidation is not required when preparing interim financial statements.

e Property, Plant, Equipment and Depreciation

Property, plant, and equipment are stated at cost. Major additions, improvements, and replacements are capitalized. Depreciation is applied by the straight-line method based on estimated economic lives. Assets still in use after full depreciation may continue to be depreciated by their estimated economic lives. Economic lives of major property and equipment are the following:

| | |
|---------------------------------------|----------------|
| Buildings | 10 to 50 years |
| Machinery | 2 to 11 years |
| Transportation equipment | 3 to 6 years |
| Furniture and office facilities | 2 to 18 years |
| Power equipment | 2 to 16 years |
| Renovation and leasehold improvements | 2 to 20 years |
| Miscellaneous equipment | 2 to 16 years |

Gain and loss on disposal of properties are included in current earnings. Non-operating properties are listed as other assets. Properties with no operating value are reclassified as other assets and carried at the lower of book or net realizable value, and their costs and accumulated

INVENTEC CORPORATION
NOTES TO FINANCIAL STATEMENTS (CONT'D)

depreciation shall offset each other, with difference reported as current loss.

f Deferred Expenses

Telephone line charges and cost of power distributors are amortized equally over 5 years. Molds and tools are amortized equally over 12 months. Software costs are amortized at the ratio of its current total production over total current and estimated future production. If production ceases for over six months, then the software will be fully reflected as other losses.

g Pension Plan

The Company has a pension plan covering all regular employees, and pension payment is commensurate with years of service. The Company contributes annually to the pension fund and deposits in a government designated account. The pension fund is not reflected in the Company's financial statements. Effective 1995, the Company adopted SFAS No.18 and secured actuarial report on pension liabilities with December 31 as the measurement date. Provisions for pension expense commenced on January 1, 1996, and unrecognized net transitional obligations are amortized equally over 15 years.

h Foreign Currency Translation

Assets and liabilities of overseas subsidiaries are translated at the spot rate of the balance sheets date; stockholders' equity is translated by historical rate except for the beginning balance of retained earnings, where the spot rate at the beginning of the year is used. Income statement accounts are translated at the weighted-average rate of the year, with difference reflected as translation adjustments to stockholders' equity.

Foreign-denominated non-forward transactions are recorded at rates as transactions occur. Foreign exchange gain and loss on settlement of foreign-denominated assets and liabilities and those of year-end adjustment to foreign-denominated assets and liabilities by the spot rates then are included in current earnings.

i Non-Trading Financial Derivatives

According to the rule set forth by SFAS, hedging foreign exchange forward contracts are recorded at spot rates of the contract date and adjusted by the exchange rate at period-end, with exchange gain and loss included in current earnings. Difference between the contract and the spot rates is recognized ratably over the term of forward contracts. Forward contract receivables netting related payables are reflected as an asset or a liability.

j Capital Surplus

According to the Company Law, capital surplus is used exclusively to offset cumulative losses and increase capital. If the Company revalues properties and uses capital surplus to offset cumulative losses, it must first be restored by future earnings before dividends or other distributions can be made.

INVENTEC CORPORATION
NOTES TO FINANCIAL STATEMENTS (CONT'D)

k Legal Reserve

Legal reserve is used exclusively to offset cumulative losses or to increase capital. Capitalization of legal reserve is permitted only when it reaches 50% of the paid-in capital, and only 50% of it can be capitalized. It may not be used for any other purpose.

l Earnings Distribution and Dividend Policy

The Company's Articles of Incorporation prescribe that after-tax earnings shall first offset cumulative losses, and 10% of the rest be set aside as legal reserve. Special reserve may be appropriated for operations or to meet regulations. 7% and 3% of the remainder will be distributed as employee bonuses and compensation for directors and supervisors, respectively. The remaining balance is distributed according to the proposal presented to the annual stockholders' meeting by the Board of Directors.

In consideration of the Company's future funding needs and long-term budget planning, and in order to meet shareholders' demand of cash flow, annual cash dividends paid cannot be fewer than 10% of total current dividends.

m Commitments and Contingencies

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

n Revenue Recognition

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

o Warranty Reserve

An allowance is provided for products with warranty based on estimated warranty service cost, and the related liability is classified as current or non-current, depending on its nature.

p 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.

q Income Tax

The Company adopted the SFAS No. 22, "Accounting for Income Taxes" to make inter- and intra-period income tax allocation. Tax effects of deductible temporary differences, unused investment tax credits, and operating loss carryforwards are treated as deferred tax assets, whereas those of taxable temporary differences are accounted for as deferred tax liabilities. A valuation allowance is provided for deferred tax assets by assessing whether it is more likely than not such assets will realize. Adjustments to prior years' earnings are reported under stockholders' equity rather than included in current earnings. Income tax expense or benefits resulting from unearned gain or loss or changes in capital surplus are reported under respective

INVENTEC CORPORATION
NOTES TO FINANCIAL STATEMENTS (CONT'D)

accounts 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 of the annual stockholder's meeting declaring distribution of earnings.

r Earnings per Share ("EPS")

EPS is based on the effect of all common shares issued and outstanding and is calculated by dividing net income by the weighted-average shares outstanding during the year. In the event of capital increase through capitalization of retained earnings or capital surplus, EPS is retroactively adjusted to reflect the capital increase for all years presented in the financial statements, regardless of the outstanding period in which the incremental shares are issued.

3 REASONS FOR AND EFFECTS OF ACCOUNTING CHANGES: None.

4 SUMMARY OF MAJOR ACCOUNTS

a Cash and Cash Equivalents

| | <u>June 30, 2004</u> | <u>June 30, 2003</u> |
|---|----------------------|----------------------|
| Cash on hand | \$ 496 | 432 |
| Checking accounts | 3,459 | 11,275 |
| Demand deposits | 14,147 | 8,510 |
| Time deposits | 1,719,960 | 451,100 |
| Foreign currency time deposits | 4,278,877 | 5,471,223 |
| Foreign currency deposits | 1,083,528 | 80,632 |
| Cash equivalents (short-term bills and bonds) | 3,287,251 | - |
| Total | <u>\$ 10,387,718</u> | <u>6,023,172</u> |

b Accounts Receivable

| | <u>June 30, 2004</u> | <u>June 30, 2003</u> |
|---------------------------------------|----------------------|----------------------|
| Accounts receivable - other customers | \$ 13,780,093 | 6,845,855 |
| Less: Allowance for doubtful accounts | (905) | (2,287) |
| Net | 13,779,188 | 6,843,568 |
| Accounts receivable - related parties | 5,925,841 | 5,741,192 |
| Total | <u>\$ 19,705,029</u> | <u>12,584,760</u> |

INVENTEC CORPORATION
NOTES TO FINANCIAL STATEMENTS (CONT'D)

c Inventories

| | June 30, 2004 | June 30, 2003 |
|---|----------------------|----------------------|
| Raw materials | \$ 1,428,844 | 1,046,895 |
| Work in process | 306,903 | 419,741 |
| Finished goods | 557,447 | 890,804 |
| Supplies-in-transit | - | 1,575 |
| | 2,293,194 | 2,359,015 |
| Less: Allowance for market decline and obsolescence | (453,598) | (473,733) |
| Net | \$ 1,839,596 | 1,885,282 |
| Insurance coverage | \$ 2,600,000 | 3,512,420 |

d Long-Term Equity Investments

| Name of Investee Company | June 30, 2004 | | | June 30, 2003 | | |
|--|-----------------------|----------------------|----------------------------|-----------------------|-------------------|----------------------------|
| | Equity Holding | Book Value | Original Investment | Equity Holding | Book Value | Original Investment |
| Carried under the equity method | | | | | | |
| Inventec Besta Co., Ltd. | 38.69% | \$ 1,167,940 | 765,058 | 38.69% | 1,178,616 | 765,058 |
| Inventec Corporation (Hong Kong) Co., Ltd. | 100.00% | 428,686 | 42,655 | 100.00% | 335,516 | 8,705 |
| Inventec Corporation (Scotland) Co., Ltd. | 100.00% | 360,566 | 39,518 | 100.00% | 271,545 | 39,518 |
| Inventec Corporation (Singapore) Co., Ltd. | 100.00% | 6,800 | 6,888 | 100.00% | 6,849 | 6,888 |
| Inventec Holding (North America) Co., Ltd. | 100.00% | 446,288 | 159,003 | 100.00% | 404,729 | 159,003 |
| Inventec Multimedia and Telecom Corp. | 59.60% | 1,350,062 | 967,400 | 59.71% | 1,277,552 | 967,400 |
| Inventec Micro-Electronics Corp. | 70.48% | 399,413 | 401,625 | 70.48% | 423,025 | 401,625 |
| Inventec Appliances Corp. | 50.13% | 2,719,824 | 2,489,325 | 95.03% | 4,695,031 | 3,544,475 |
| Inventec Corporation (Cayman) Co., Ltd. | 100.00% | 3,104,477 | 3,188,058 | 100.00% | 1,538,001 | 1,632,423 |
| Inventec Tomorrow Studio Corp. | - | - | - | 60.00% | 198,121 | 298,800 |
| Inventec Eriterprise System Corp. | 100.00% | 152,796 | 200,000 | - | - | - |
| Inventec (Czech) S.R.O. | 100.00% | 69,873 | 69,873 | - | - | - |
| Subtotal | | 10,206,725 | | | 10,328,985 | |
| Carried under the cost method | | | | | | |
| Common Stock | | | | | | |
| WK Technology Fund IV | 1.52% | 40,000 | | 1.52% | 40,000 | Fair Value |
| SINA.COM | - | - | | 0.78% | 13,802 | 22,507 |
| Eastern Broadband | 0.15% | 100,000 | | 0.15% | 100,000 | |
| Storage Bank Inc. | 10.09% | 26,400 | | 10.09% | 26,400 | |
| Inventec Tomorrow Studio Corp. | 8.57% | 39,284 | | - | - | |
| Global Strategic Investment Fund | 6.45% | 100,000 | | - | - | |
| Subtotal | | 305,684 | | | 180,202 | |
| Preferred Stock | | | | | | |
| E28 Limited | | 1,394,600 | | | 1,394,600 | |
| 3UP SYSTEM INC. | | 65,980 | | | - | |
| Universal Network Machines, Inc. | | 98,850 | | | - | |
| Subtotal | | 1,559,430 | | | 1,394,600 | |
| Total | | \$ 12,071,839 | | | 11,903,787 | |

INVENTEC CORPORATION
NOTES TO FINANCIAL STATEMENTS (CONT'D)

For the six months ended, 2004 and 2003, investment income (loss) where the Company has controlling interest or can exercise significant influence were the following:

| <u>Name of investee company</u> | <u>Six Months Ended June 30,</u> | |
|---|----------------------------------|----------------|
| | <u>2004</u> | <u>2003</u> |
| Based on unaudited financial statements prepared by investee companies: | | |
| Inventec Besta Co., Ltd. | \$ (7,241) | (1,874) |
| Inventec Corporation (Hong Kong) Co., Ltd. | 38,395 | (41,955) |
| Inventec Corporation (Scotland) Co., Ltd. | 34,047 | 40,092 |
| Inventec Corporation (Singapore) Co., Ltd. | - | (222) |
| Inventec Holding (North America) Co., Ltd. | 30,424 | 22,415 |
| Inventec Multimedia and Telecom Corp. | 105,048 | 16,438 |
| Inventec Micro-Electronics Corp. | 89 | 4,683 |
| Inventec Appliances Corp. | 425,286 | 468,821 |
| Inventec Corporation (Cayman) Co., Ltd. | (220,812) | 52,152 |
| Inventec Tomorrow Studio Corp. | (3,558) | (10,583) |
| Inventec Eriterprise System Corp. | (47,204) | - |
| Total | <u>\$ 354,474</u> | <u>549,967</u> |

Registered capital of the wholly-owned subsidiary Inventec Corporation (Hong Kong.) Co., Ltd. was HK\$2,500 (US\$322), representing 2,500,000 shares. On January 2, 2003, the Company sold all shares of Inventec Appliances (Shanghai) Co., Ltd. originally held by Inventec Corporation (Hong Kong) Co., Ltd. to Inventec Appliance (Cayman) Holding Corp., an investee company of Inventec Appliances Corp. for US\$31,918, resulting in loss of US\$1,518. Recognition of the loss is deferred until the shares of Inventec Appliances (Shanghai) Co., Ltd. are sold to a non-related party. As of June 30, 2004, the Company received returned capital of US\$24,865. For the six months ended June 30, 2004, the company increased its investment by US\$1,000.

Effective March 1, 2001, wholly-owned subsidiary Inventec Corporation (Singapore) Co., Ltd. temporarily ceased operations. Its registered capital was SG\$350 (US\$250), representing 350,000 shares with par value of SG\$1. The Company is entitled to 349,625 shares, and 375 shares are registered under individuals. Shareholding ratio was 100%.

The wholly-owned subsidiary Inventec Corporation (Cayman) Co., Ltd. was founded in November 2000 which was approved by Investment Commission's Letter Ruling No. (89)(2)89037593. As of June 30, 2004, the registered capital for investments in Mainland China was US\$93,500, totaling 93,500,000 shares at par value of US\$1.

On May 30, 2003, the Company's shareholders meeting resolved to sale 105,515,000 shares of Inventec Appliance Corp. in order to meet the ownership diversification requirement for Inventec Appliances Corp's application for listed stocks. Consequently, shareholding ratio declined to 50.13%.

INVENTEC CORPORATION
NOTES TO FINANCIAL STATEMENTS (CONT'D)

In September 2003, the Company established Inventec (Czent) S.R.O, with a registered capital of CZK56,000 (US\$2,000), totaling 56,000,000 shares at par value of CZK 1. Shareholding ratio was 100%. In 2003, the Company established Inventec Enterprise System Corporation, with a registered capital of \$200,000. Shareholding ratio was 100%.

As of December 31, 2003, the Company invested \$100,000 in Global Strategic Investment Fund for 6.45% ownership. The investee is accounted for under the cost method.

In April 2004, the Company purchased 2,667,000 shares and 626,000 shares of convertible preferred stock of 3 UP SYSTEM INC. and Universal Network Machines, Inc. for US\$2,000 and US\$3,000, respectively. The preferred shares pay a dividend of US\$0.06 and 8% per annum, respectively. The dividend is neither cumulative nor participating and nor cumulative, participating, respectively.

On April 2004, Inventec Tomorrow Studio Corp an investee company accounted for under the equity method proceeded the capital reduction. The Company received the investment return with an amount of \$144,906. Soon after, the investee issued more shares for cash, and since the Company had not subscribed the shares, its share holding ratio on the investee decreased from 60% to 8.57%. As the result of change in the percentage of ownership in the investment, the investment is accounted for under the cost method.

The fiscal year of Inventec Corporation (Singapore) Co., Ltd. ends on March 31 and those of Inventec Holding (North America) Co., Ltd. and Inventec Corporation (Scotland) Co., Ltd. end on September 30.

Cash dividends from investee companies were the following:

| <u>Name of investee company</u> | <u>Six Months Ended June 30,</u> | |
|--|----------------------------------|----------------|
| | <u>2004</u> | <u>2003</u> |
| Inventec Corporation (Hong Kong) Co., Ltd. | \$ - | 524,385 |
| Inventec Appliances Corp. | 659,690 | - |
| Inventec Besta Co., Ltd. | 8,180 | 12,270 |
| Inventec Micro-Electronics Corp. | - | 14,040 |
| Inventec Multimedia and Telecom Corp. | 114,485 | - |
| WK Technology Fund IV | 480 | 600 |
| Total | <u>\$ 782,835</u> | <u>551,295</u> |

e Property, Plant, and Equipment

As of June 30, 2004 and 2003, fire and auto accident insurance coverage of the property, plant, and equipment amounted to \$3,430,598 and \$4,452,073, respectively.

For the six months ended, 2004 and 2003, interest capitalized was \$0.

INVENTEC CORPORATION
NOTES TO FINANCIAL STATEMENTS (CONT'D)

f Other Assets

| | <u>June 30, 2004</u> | <u>June 30, 2003</u> |
|--|----------------------|----------------------|
| Deferred expenses | \$ 61,293 | 89,315 |
| Rental assets, net of accumulated depreciation | 3,379 | 3,457 |
| Idle assets, net of accumulated depreciation | 59,055 | 699,302 |
| Prepayment for molds and tools | 38,041 | 23,632 |
| Overdue accounts in collection | 25,066 | 24,828 |
| Less: Allowance for doubtful accounts | (25,066) | (24,828) |
| Total | <u>\$ 161,768</u> | <u>815,706</u> |

On May 18, 1998, the Company provided idle land located at Nanjing East Road and demolished construction built thereupon. The construction of the new building and renovations was completed in late September 2002. The building is reflected under idle assets since the building is unused.

In November 2002, due to a change in operation policy, operating activities at the plant and factories located in Lin-Kou Industrial Park were decreased. Related land and buildings were transferred from property, plant, and equipment to idle assets. As of June 30, 2004, land, buildings, and facilities related to the factory were sold to non-related parties.

As of June 30, 2004 and 2003, insurance coverage of the above idle and rental assets both amounted to \$55,000.

g Short-term Debt

| <u>June 30, 2004</u> | <u>Period of Maturity</u> | <u>Range of Interest rates</u> | <u>Amount</u> | <u>Collateral</u> |
|----------------------|---------------------------------|------------------------------------|-------------------|-------------------|
| Credit Loan | June 25, 2004~ July 28, 2004 | 1.69%~1.78% | <u>\$ 581,735</u> | None |

h Pension Plan

The Company has a pension plan covering all employees, and payment is commensurate with years of service. 2 units are granted for each of the first 15 years of service, and 1 unit for each of the years thereafter, up to a maximum of 45 units. Any fraction of a year shorter than 6 months is counted as half a year and any fraction of a year longer than 6 months is counted as 1 year of service. Effective February 1987, the Company contributed to the pension fund deposited with Central Trust of China. As of June 30, 2004 and 2003, pension fund was \$408,091 and \$390,810, respectively.

INVENTEC CORPORATION
NOTES TO FINANCIAL STATEMENTS (CONT'D)

i Income Tax

(i) Deferred income tax assets and liabilities:

| | <u>June 30, 2004</u> | <u>June 30, 2003</u> |
|-------------------------------------|----------------------|----------------------|
| 1) Total deferred income tax assets | \$ 740,092 | 437,669 |
| 2) Total deferred income tax | (440,984) | (329,113) |

| | <u>June 30, 2004</u> | | <u>June 30, 2003</u> | |
|---|----------------------|---------------------------|----------------------|---------------------------|
| | <u>Amount</u> | <u>Income Tax Effects</u> | <u>Amount</u> | <u>Income Tax Effects</u> |
| 3) Temporary differences: | | | | |
| - Recognition of unrealized foreign exchange loss: deductible | \$ 72,361 | 18,090 | 75,186 | 18,796 |
| - Recognition of inventory obsolescence : deductible | 453,598 | 113,399 | 473,733 | 118,433 |
| - Recognition of warranty expenses: deductible | 990,994 | 247,749 | 746,146 | 186,537 |
| - Recognition of loss on overseas investments: taxable | (684,771) | (171,193) | (361,741) | (90,435) |
| - Recognition of gain on investments: taxable | (827,520) | (206,880) | (716,692) | (179,173) |
| - Recognition of unrealized intercompany profits: taxable | (146,780) | (36,695) | (29,284) | (7,321) |
| - Cumulative translation adjustment to long-term investments: taxable | (104,865) | (26,216) | (208,735) | (52,184) |
| - Recognition of pension expense: deductible | 226,571 | 56,643 | 181,255 | 45,314 |
| - Unused balance of investment tax credits | - | 304,211 | - | 68,589 |

| | <u>June 30, 2004</u> | <u>June 30, 2003</u> |
|---|----------------------|----------------------|
| (ii) Deferred income tax assets - current | \$ 683,449 | 392,355 |
| Deferred income tax liabilities - | - | - |
| Net | <u>\$ 683,449</u> | <u>392,355</u> |
| (iii) Deferred income tax assets - non- | \$ 56,643 | 45,314 |
| Deferred income liabilities - non- | (440,984) | (329,113) |
| Net | <u>\$ (384,341)</u> | <u>(283,799)</u> |

INVENTEC CORPORATION
NOTES TO FINANCIAL STATEMENTS (CONT'D)

(iv) Calculation of income tax expense:

| | Six Months Ended June 30, | |
|---|----------------------------------|-----------------|
| | 2004 | 2003 |
| Income tax calculated per statutory tax rate | \$ 311,261 | 341,965 |
| Permanent differences | (91,957) | (120,266) |
| Temporary differences | 86,004 | 137,079 |
| Tax-exempt income | (118,076) | (55,984) |
| Investment tax credits | (93,616) | (151,397) |
| Current income tax payable | 93,616 | 151,397 |
| Income tax separately levied | 811 | 923 |
| Prior years' income tax adjustments | (10,929) | (33,423) |
| Unused balance of investment tax credits | (12,162) | (68,589) |
| Income tax effect of temporary differences: | | |
| Provision and reversal of inventory obsolescence, net | (3,983) | (268) |
| Provision and reversal of loss on overseas investments, net | 22,847 | 49,977 |
| Provision and reversal of warranty reserve, net | (59,454) | (60,148) |
| Recognition of loss on investments | (29,487) | (112,976) |
| Recognition of unrealized intercompany gains, net | (2,729) | (11,609) |
| Recognition of unrealized foreign currency exchange loss (gain), net | (7,746) | 3,949 |
| Recognition of pension expense | (5,452) | (6,004) |
| Income tax benefit | <u>\$ (14,668)</u> | <u>(86,771)</u> |

(v) The Company's tax returns through 1998 have been assessed by the Tax Authority. Additional tax assessed for 1997 and 1998 was \$31,743 and \$51,737, respectively. The Company has petitioned for administrative relief.

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

| | June 30, 2004 | June 30, 2003 |
|---|----------------------|----------------------|
| Stockholder's imputation tax credit account | <u>\$ 407,728</u> | <u>\$ 376,894</u> |

2003 and 2002, after filing the corporate income tax returns, the actual imputation tax credit rate for earnings distributed to R.O.C. residents would approximately be 9.60% and 11.33%, respectively.

| Undistributed earnings: | June 30, 2004 | June 30, 2003 |
|--------------------------------------|----------------------|----------------------|
| Accumulated prior to 1997 and before | \$ 437,138 | \$ 477,632 |
| Accumulated after 1998 | 1,261,625 | 1,416,712 |
| Total | <u>\$ 1,698,763</u> | <u>\$ 1,894,344</u> |

INVENTEC CORPORATION
NOTES TO FINANCIAL STATEMENTS (CONT'D)

(vii) According to Article 6, Section 3 of the Statute of Upgrading Industries, unused investment tax credits which may be applied to offset income tax in the future are the following:

| Year of occurrence | Investment tax credits | Year of expiration |
|---------------------------|-------------------------------|---------------------------|
| 2003 | \$ 216,907 | 2007 |
| 2004 | 87,304 | 2008 |
| Total | \$ 304,211 | |

j Capital Increase

On May 27, 2004, pursuant to resolutions of the annual stockholders' meeting, the Company capitalized earnings of \$1,013,000, and employee bonuses of \$97,000, for a total of \$1,110,000. Total capital after the increase was \$21,370,000 with July 13, 2004 as the record date. The Company has not completed relevant registration change.

On May 30, 2003, pursuant to resolutions of the annual stockholders' meeting, the Company capitalized earnings of \$1,835,000 and employee bonuses of \$75,000, for a total of \$1,910,000. Total capital after the increase was \$20,260,000 with July 21, 2003 as the record date. The Company completed relevant registration change.

k Earnings Per Share

EPS is calculated by dividing net income by the weighted-average shares outstanding during the period. As of June 30, 2004 and 2003, weighted-average number of common shares outstanding were 2,026,000,000 and 1,835,000,000, respectively. As of June 30, 2003, the number of outstanding shares retroactively adjusted due to stock dividends was 2,026,000,000.

l Financial Instruments

- 1) Financial Derivatives: None.
- 2) Fair Value of Financial Instruments

| | June 30, 2004 | |
|--------------------------------|----------------------|-------------------|
| Financial Assets | Book Value | Fair Value |
| Book value equal to fair value | \$ 47,534,329 | 47,534,329 |
| Long-term investments | 12,071,839 | 12,263,539 |
| Total | \$ 59,606,168 | 59,797,868 |
| Financial Liabilities | | |
| Book value equal to fair value | \$ 35,687,429 | 35,687,429 |
| | \$ 35,687,429 | 35,687,429 |

INVENTEC CORPORATION
NOTES TO FINANCIAL STATEMENTS (CONT'D)

| June 30, 2003 | | |
|--------------------------------|----------------------|-------------------|
| Financial Assets | Book Value | Fair Value |
| Book value equal to fair value | \$ 24,774,694 | 24,774,694 |
| Long-term investments | 11,903,788 | 12,255,061 |
| Total | \$ 36,678,482 | 37,029,755 |
| Financial Liabilities | | |
| Book value equal to fair value | \$ 14,646,122 | 14,646,122 |

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

- a) The fair value of short-term financial instruments is determined by their face value on the balance sheet. Since such instruments will mature with short notice, the face value is a reasonable basis in establishing the fair value. The method is applicable to cash and cash equivalents, notes and accounts receivable, other current assets, short-term borrowings, notes and accounts payable, and other current liabilities.
- b) The book value of long-term investments is accounted for under the cost or the equity method based on self-prepared financial statements of investee companies. Since there are no market quotes or reference reports for non-listed companies, fair value of these investments are determined by their net equity worth or cost.
- c) With respect to financial instruments such as refundable deposits that are indispensable guarantee for the ongoing operations of the Company, it is impossible to estimate the time necessary to accomplish exchange of assets. Consequently, the fair market value of such financial instruments cannot be established. The book value is used as the fair market value.

3) Financial Instruments with Off-Balance-Sheet Credit Risk:

As of June 30, 2004 and 2003, guarantees provided by the Company to related parties for their bank loans, please refer to Note 5.(b).(viii).

As of June 30, 2004 and 2003, promissory notes issued for bank loans, please refer to Note 7.

4) Information on Concentration of Credit Risk:

Concentrations of credit risk exist when changes in economic, industry or geographic factors similarly affect groups of counter-parties whose aggregate credit exposure is material in relation to the Company's total credit exposure. As of June 30, 2004 and 2003, the Company's contracts with credit risk concentration were the following:

INVENTEC CORPORATION
NOTES TO FINANCIAL STATEMENTS (CONT'D)

| Accounts Receivable, net - By Customers | June 30, 2004 | June 30, 2003 |
|--|----------------------|----------------------|
| HP | \$ 7,421,939 | 4,606,895 |
| TOSHIBA | 5,019,464 | 1,206,751 |
| Related Parties | 5,925,841 | 5,741,192 |
| Other | 1,337,785 | 1,029,922 |
| Total | \$ 19,705,029 | 12,584,760 |

5 Related Party Transactions

(a) Name of Related Party and their Relationship with the Company:

| <u>Name of Related Party</u> | <u>Relationship with the Company</u> |
|--|--|
| Inventec Besta Co., Ltd. | An investee company accounted for under the equity method |
| Inventec Corporation (Scotland) Co., Ltd. | A subsidiary |
| Inventec Multimedia and Technology Corp. | " |
| Inventec Micro-Electronic Corp. | " |
| Inventec Appliances Corp. | " |
| Inventec Corporation (Hong Kong) Co., Ltd. | " |
| Inventec Holding (North America) Co., Ltd. | " |
| Inventec Corporation (Cayman) Co., Ltd. | " |
| Inventec Eriterprise System Corp. | " |
| Inventec Tomorrow Studio Corp. | " |
| | (Accounted for under the cost method since April, 2004) |
| Inventec Electronics (Beijing) Co., Ltd. | A subsidiary of Inventec Corporation (Hong Kong) Co., Ltd. |
| Inventec Electronics (Nanking) Co., Ltd. | " |
| Inventec Electronics (Tianjin) Co., Ltd. | " |
| Inventec Appliances (Shanghai) Co., Ltd. | A third-level subsidiary of Inventec Appliances Corp. |
| Inventec Corp. (Shanghai) Co., Ltd. | A subsidiary of Inventec Corporation (Cayman) Co., Ltd. |
| Inventec (Pudong) Corp. | " |
| Inventec Electronics (M) SDN. BHD. | A subsidiary of Inventec Multimedia and Telecom Corp. |

INVENTEC CORPORATION
NOTES TO FINANCIAL STATEMENTS (CONT'D)

(b) Significant Transactions with Related Parties:

(i) Sales

| <u>Name of Related Party</u> | <u>Six Months Ended June30,</u> | | | |
|--|---------------------------------|-----------------------|-------------------|-----------------------|
| | <u>2004</u> | | <u>2003</u> | |
| | <u>Amount</u> | <u>% of Net Sales</u> | <u>Amount</u> | <u>% of Net Sales</u> |
| Inventec Electronics (M) SDN. BHD. | \$ 15,980 | - | 237,068 | 1% |
| Inventec Corporation(Scotland) Co., Ltd | 7,592,432 | 13% | 6,429,349 | 17% |
| Invertec Holding (North America) Co., Ltd. | 7,544,907 | 13% | 5,619,461 | 14% |
| Inventec Corporation (Hong Kong) Co., Ltd. | 43 | - | 845,781 | 2% |
| Others | 3,760 | - | 492 | - |
| Total | \$ 15,157,122 | 26% | 13,132,151 | 34% |

Prices of sale of motherboards to Inventec Electronics (M) SDN. BHD. are based on cost with collection terms varying between one to three months.

The Company sold work-in-process to the assembling department of Inventec Corporation (Scotland) Co., Ltd. and upon completion of assembling, finished products were sold to non-related parties. Prices of work-in-process are negotiated. Since Inventec Corporation (Scotland) Co., Ltd. is an overseas after-sales service and assembling center, no basis of price reference exists. Collection period is within two months.

The Company sold work-in-process to Inventec Holding (North America) Co., Ltd. Prices of work-in-process are negotiated. Since Inventec Holding (North America) Co., Ltd. is an overseas after-sales service and assembling center, no basis of price reference exists. Collection period is within three months.

Prices of finished goods sold to Inventec Corporation (Hong Kong) Co., Ltd. are the same as those with other clients. Collection period is within two months.

As of June 30, 2004 and 2003, unrealized gross profit of sales to related parties was \$13,627 and \$31,771, respectively.

(ii) Warranty Services and Product Maintenance

For the six months ended, 2004 and 2003, payment to related parties for service and maintenance expenses, after netting product warranty reserve, was the following:

| <u>Name of Related Party</u> | <u>Six Months Ended June 30,</u> | |
|--|----------------------------------|----------------|
| | <u>2004</u> | <u>2003</u> |
| Inventec Holding (North America) Co., Ltd. | \$ 141,617 | 164,212 |
| Inventec Corporation (Scotland) Co., Ltd. | 103,719 | 77,687 |
| Total | \$ 245,336 | 241,899 |

INVENTEC CORPORATION
NOTES TO FINANCIAL STATEMENTS (CONT'D)

(iii) Purchases

For the six months ended, 2004 and 2003, purchases of materials and goods were the following:

| Name of Related Party | Six Months Ended June30, | | | |
|--|--------------------------|-------------------|-------------------|-------------------|
| | 2004 | | 2003 | |
| | Amount | % of Net Purchase | Amount | % of Net Purchase |
| Inventec Corporation (Hong Kong) Co., Ltd. | \$ 42,981,630 | 77% | 20,109,207 | 58% |
| Inventec Electronics (M) SDN. BHD. | 122,146 | - | 368,469 | 1% |
| Inventec Holding (North America) Co., Ltd. | 31,359 | - | 78,377 | - |
| Inventec Corporation (Scotland) Co., Ltd. | 201,675 | 1% | 163,053 | - |
| Others | - | - | 7,320 | - |
| Total | \$ 43,336,810 | 78% | 20,726,426 | 59% |

The Company purchased motherboards from Inventec Electronics (M) SDN. BHD. at an agreed-upon price. The payment term is approximately one to three months.

The Company purchased finished goods and work in process from Inventec Corporation (Hong Kong) Co., Ltd. at an agreed-upon price. The payment term is approximately two to three months.

The Company purchased supplies used for warranty service from Inventec Holding (North America) Co., Ltd. at an agreed-upon price. The payment term is within two months.

The Company purchased supplies used for warranty service from Inventec Corporation (Scotland) Co., Ltd. at an agreed-upon price. The payment term is within two months.

(iv) Technical Service

The Company entered into an agreement with Inventec Besta Co., Ltd., which would pay royalty to the Company for use of patents and copyrights in the manufacturing of information and electronic-related products. Royalty is determined by sales volume. For the six months ended, 2004 and 2003, royalty collected from Inventec Besta Co., Ltd. was \$1,287 and \$247, respectively.

The Company entered into an agreement with Inventec Tomorrow Studio Corp. in which the Company collects royalty through production, distribution, and sale of Dr Eye 2002. Royalty is based on sales volume. For the six months ended, 2004 and 2003, royalty collected from Inventec Tomorrow Studio Corp. for the right to sale computer software amounted to \$470 and \$490, respectively.

(v) Purchase of Software

For the six months ended, 2004 and 2003, purchase of software for product development from Inventec Corporation (Hong Kong) Co., Ltd., reflected as deferred expense, was \$67,484 and \$101,652, respectively. Prices were negotiated with payment terms of two to three months.

INVENTEC CORPORATION
NOTES TO FINANCIAL STATEMENTS (CONT'D)

(vi) Others

- 1) In 1999, the Company sold properties, deferred assets, assets stated under expense, and trademarks to Inventec Besta Co., Ltd., resulting in a gain on property disposition of \$51,712 and other revenue of \$40,453. As of June 30, 2004 and 2003, unrealized gain on sale of properties to Inventec Besta Co., Ltd. was \$17,438 and \$17,599, respectively, with unrealized other revenue of \$3,887 and \$4,652, respectively.
- 2) In 2000, the Company invested in Inventec Appliances Corp. with properties, deferred assets, and assets stated under expense resulting in a gain on asset disposition of \$103,713 and other revenue of \$31,693. The Company sold properties and deferred assets, resulting in a gain on property disposition of \$1,156 and other revenue of \$6,427. As of June 30, 2004 and 2003, unrealized gain on sale of properties was \$54,122 and \$64,017, respectively, and unrealized other revenue was \$12 and \$25, respectively.
- 3) In 2003, the Company sold properties, deferred assets, and assets stated under expense to Inventec Corporation (Hong Kong) Co., Ltd. resulting in a gain on property disposition of \$44,946 and other revenue of \$2,562. As of June 30, 2004 and 2003, unrealized gain on sale of properties \$30,872 and \$18,390, respectively, and unrealized other revenue was \$1,494 and \$2,007, respectively.
- 4) In 2004 and 2003, general and administrative expenses collected from Inventec Appliances Corp., Inventec Micro-Electronic Corp., Inventec Multimedia and Telecom Corp., Inventec Besta Corp., Ltd. and Inventec Tomorrow Studio Corp. were \$77,316 and \$20,136, respectively, reflected as other revenue.
- 5) Accounts Receivable (Payable)

| | June 30, 2004 | | June 30, 2003 | |
|--|----------------------|-------------|----------------------|------------|
| | Balance | % | Balance | % |
| Total notes receivable | \$ 8,747 | 100% | 984 | 45% |
| Accounts Receivable: | | | | |
| Inventec Holding (North America) Co., Ltd. | \$ 3,438,933 | 18% | 2,289,410 | 18% |
| Inventec Corporation (Scotland) Co., Ltd. | 2,423,185 | 12% | 2,741,586 | 22% |
| Inventec Electronics (M) SDN. BHD. | 26,149 | - | 100,828 | 1% |
| Inventec Corporation (Hong Kong) Co., Ltd. | 37,365 | - | 609,102 | 5% |
| Other | 209 | - | 266 | - |
| Total | \$ 5,925,841 | 30% | 5,741,192 | 46% |
| Total other receivables | \$ 11,801 | 47% | 38,256 | 26% |
| Other Current Assets: | | | | |
| Inventec Corporation (Hong Kong) Co., Ltd. | \$ 16,895,688 | 97% | 5,851,399 | 96% |
| Inventec (Czech) S.R.O. | 18,028 | - | - | - |
| Other | 3,334 | - | 2,399 | - |
| Total | \$ 16,917,050 | 97% | 5,853,798 | 96% |

INVENTEC CORPORATION
NOTES TO FINANCIAL STATEMENTS (CONT'D)

| | | | | | |
|---|-----------|-------------------|------------|------------------|------------|
| Total notes payable | <u>\$</u> | <u>125</u> | - | <u>4,746</u> | - |
| <u>Accounts Payable:</u> | | | | | |
| Inventec Corporation (Hong Kong) Co., Ltd. | \$ | 16,252,630 | 53% | 4,605,255 | 39% |
| Inventec Electronics (M) SDN. BHD. | | 8,775 | - | 124,974 | 1% |
| Inventec Holding (North American) Co., Ltd. | | 9,187 | - | - | - |
| Inventec Corporation (Scotland) Co., Ltd. | | 23,336 | - | - | - |
| Other | | - | - | 2,610 | - |
| Total | <u>\$</u> | <u>16,293,928</u> | <u>53%</u> | <u>4,732,839</u> | <u>40%</u> |
| <u>Other Current Liabilities:</u> | | | | | |
| Inventec Corporation (Hong Kong) Co., Ltd. | <u>\$</u> | <u>51,591</u> | <u>2%</u> | <u>102,358</u> | <u>23%</u> |

(vii) Guarantee and Endorsements

| <u>Name of Related Party Guaranteed</u> | <u>June 30, 2004</u> | | <u>June 30, 2003</u> | | <u>Name of Bank</u> |
|--|----------------------|----------------|----------------------|----------------|------------------------|
| Inventec Corporation (Hong Kong) Co., Ltd. | USD | 15,000 | USD | 15,000 | Citibank, N.A. |
| Inventec Corporation (Cayman) Co., Ltd. | | 30,000 | | 30,000 | " |
| Inventec Appliances (Shanghai) Co., Ltd. | | - | | 8,000 | Bank of America |
| Inventec Electronics (Nanking) Co., Ltd. | | 1,500 | | 1,500 | " |
| Inventec Electronics (Tianjin) Co., Ltd. | | 2,500 | | 2,500 | " |
| Inventec Electronics (Beijing) Co., Ltd. | | 1,000 | | 1,000 | " |
| Inventec Corp. (Shanghai) Co., Ltd. | | 5,000 | | 25,000 | " |
| Inventec Corporation (Scotland) Co., Ltd. | USD | 28,000 | USD | 23,000 | Citibank, N.A. |
| " | GBP | 500 | GBP | 500 | Government of Scotland |
| Inventec Holding (North America) Co., Ltd. | USD | 2,000 | USD | 2,000 | Bank of America |
| Inventec (Pudong) Corp. | USD | 25,000 | USD | 5,000 | |
| Total | <u>USD</u> | <u>110,000</u> | <u>USD</u> | <u>113,000</u> | |
| | <u>GBP</u> | <u>500</u> | <u>GBP</u> | <u>500</u> | |

6 Pledged Assets

| <u>Asset</u> | <u>June 30, 2004</u> | <u>June 30, 2003</u> | <u>Purpose of pledge</u> | |
|---------------------|----------------------|----------------------|--------------------------|--|
| Refundable deposits | <u>\$</u> | <u>56,752</u> | <u>60,498</u> | Customs duties, and property deposits. |

7 Significant Commitments And Contingencies (Excluding Related Party Transactions)

- (a) As of June 30, 2004 and 2003, unused standby letters of credit were US\$186 and US\$712, respectively.
- (b) As of June 30, 2004 and 2003, promissory notes issued for bank loans totaled \$6,058,292 and \$6,058,543, respectively.

8 Significant Catastrophic Losses: None.

INVENTEC CORPORATION
NOTES TO FINANCIAL STATEMENTS (CONT'D)

9 Significant Subsequent Events:

On June 29, 2004, the Board of Directors resolved to sell shares of Inventec Electronics (Nanking) Co., Ltd. held by Inventec Corporation (Hong Kong) Co., Ltd. to Inventec Appliances (Cayman) Holding Corp, an investee of Inventec Appliances Corp. The shares were transferred for a price of US\$8,981. It has not been approved by Investment commission.

10 Other

- (a) Personnel, depreciation, and amortization expense incurred categorized as operating cost or expense are as follows:

| Categorized as Nature | Six months ended June 30, 2004 | | | Six months ended June 30, 2003 | | |
|---------------------------------------|--------------------------------|----------------------|---------|--------------------------------|----------------------|---------|
| | Operating Cost | Operating expense | Total | Operating Cost | Operating expense | Total |
| Personnel expense | | | | | | |
| Salary expense | \$ 238,891 | 528,131 | 767,022 | 319,083 | 602,368 | 921,451 |
| Health and labor insurance expense | 17,284 | 29,469 | 46,753 | 21,656 | 29,656 | 51,312 |
| Pension expense | 11,814 | 26,743 | 38,557 | 10,923 | 28,838 | 39,761 |
| Other expense | 11,118 | 35,272 | 46,390 | 4,172 | 56,259 | 60,431 |
| Depreciation expense | 45,503 | 67,888 | 113,391 | 55,347 | 66,364 | 121,711 |
| Amortization expense | 135,459 | 1,601 | 137,060 | 96,569 | 37,048 | 133,617 |

- (b) In October 13, 2000, Samsung Electronics Co., Ltd. (“Samsung”) named the Company and 10 other parties as defendants for patents infringement in United States District Court for the District of Texas. The plaintiff claimed that the defendants violated six of its U.S. patents. Five of the six claims have been dropped by Samsung. Patent No. 5333273 is currently under trial. The Company has appointed a counsel for the litigation. In November 2002, the Magistrate Judge ruled that unless the Company and Samsung object within a stated period of time, the trial will be tried by a federal judge. After the judge’s decision, the trial proceedings will continue. Litigation procedures will commence within a year after trial proceedings are underway.