

HOLTEK SEMICONDUCTOR INC. AND SUBSIDIARIES
Consolidated Financial Statements
December 31, 2001 and 2000
(With Independent Auditors' Report Thereon)

Independent Auditors' Report

The Board of Directors
Holtek Semiconductor Inc.

We have audited the consolidated balance sheets of Holtek Semiconductor Inc. and subsidiaries as of December 31, 2001 and 2000, and the related consolidated statements of income, changes in stockholders' equity, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with 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 disclosure in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Holtek Semiconductor Inc. and subsidiaries as of December 31, 2001 and 2000, and the results of their operations and their cash flows for the years then ended, in conformity with accounting principles generally accepted in the Republic of China.

Hsinchu, Taiwan (the Republic of China)
January 10, 2002

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

HOLTEK SEMICONDUCTOR INC. AND SUBSIDIARIES

Consolidated Balance Sheets

December 31, 2001 and 2000
(In thousands of New Taiwan dollars)

	<u>2001</u>	<u>2000</u>			
Assets			Liabilities and Stockholders' Equity		
Current assets:			Current liabilities:		
Cash and cash equivalents (note 3)	\$ 215,491	795,029	Accounts payable	\$ 438,206	628,678
Short-term investments (note 4)	841,113	853,999	Payables to related parties (note 14)	122,978	315,944
Accounts receivable, net of allowance for doubtful accounts of \$13,000 and \$28,000 as of December 31, 2001 and 2000, respectively	495,449	593,967	Income tax payable	19,163	73,295
Receivables from related parties (note 14)	2,499	3,193	Current portion of long-term debt (note 8)	9,200	26,300
Inventories (note 5)	578,526	607,708	Accrued expenses and other current liabilities	<u>109,855</u>	<u>218,466</u>
Prepaid expenses and other current assets (note 12)	<u>81,880</u>	<u>108,141</u>	Total current liabilities	699,402	1,262,683
Total current assets	2,214,958	2,962,037	Long-term debt, excluding current installments (note 8)	62,044	64,761
Long-term equity investments (note 6)	10,331	9,898	Other non-current liabilities:		
Property, plant and equipment (notes 5, 14 and 15):			Pension accrual (note 9)	15,697	8,298
Buildings	186,785	-	Deposits in (note 10)	<u>59,022</u>	<u>52,337</u>
Machinery and equipment	196,381	180,872	Total other non-current liabilities	<u>74,719</u>	<u>60,635</u>
Furniture and fixtures	44,682	41,212	Total liabilities	836,165	1,388,079
Other equipment	<u>15,550</u>	<u>12,664</u>	Stockholders' equity (note 11):		
	443,398	234,748	Common stock	1,533,800	1,220,000
Less: accumulated depreciation	(122,576)	(64,746)	Capital surplus	152	152
Advances for purchases of machinery and equipment	<u>-</u>	<u>4,177</u>	Legal reserve	86,393	25,267
Net property, plant and equipment	320,822	174,179	Unappropriated earnings	310,953	611,831
Other noncurrent assets:			Foreign currency translation adjustment	<u>(13,681)</u>	<u>12,993</u>
Deferred expenses (notes 7, 14 and 15)	62,708	96,548	Total stockholders' equity	1,917,617	1,870,243
Deferred income tax assets (note 12)	109,560	2,201	Commitments and contingent liabilities (notes 8 and 16)		
Other (note 15)	<u>35,403</u>	<u>13,459</u>			
Total other non-current assets	<u>207,671</u>	<u>112,208</u>			
Total assets	<u>\$ 2,753,782</u>	<u>3,258,322</u>	Total liabilities and stockholders' equity	<u>\$ 2,753,782</u>	<u>3,258,322</u>
	<u>2001</u>	<u>2000</u>			

See accompanying notes to consolidated financial statements.

HOLTEK SEMICONDUCTOR INC. AND SUBSIDIARIES

Consolidated Statements of Income

Years ended December 31, 2001 and 2000

(In thousands of New Taiwan dollars, except net income per common share)

		<u>2001</u>	<u>2000</u>
Net sales (note 14)	\$	3,330,287	4,828,664
Less: sales returns and allowances		<u>(36,216)</u>	<u>(12,224)</u>
Net sales		3,294,071	4,816,440
Cost of goods sold (note 14)		<u>2,451,623</u>	<u>3,317,406</u>
Gross profit		842,448	1,499,034
Operating expenses:			
Selling		144,202	149,375
Administrative		183,906	220,506
Research and development		<u>413,348</u>	<u>526,475</u>
		<u>741,456</u>	<u>896,356</u>
Operating income		100,992	602,678
Non-operating income:			
Interest income		17,111	30,109
Investment income		65,712	1,389
Foreign currency exchange gain, net		27,217	38,126
Other (note 16)		<u>40,612</u>	<u>14,155</u>
		150,652	83,779
Non-operating expenses:			
Interest expense		5,005	8,042
Other		<u>5,699</u>	<u>6,443</u>
		<u>10,704</u>	<u>14,485</u>
Income before income taxes		240,940	671,972
Income tax benefit (expense) (note 12)		<u>69,795</u>	<u>(60,710)</u>
Net income	\$	<u>310,735</u>	<u>611,262</u>
Net income per common share		<u>\$2.03</u>	<u>3.99</u>

See accompanying notes to consolidated financial statements.

HOLTEK SEMICONDUCTOR INC. AND SUBSIDIARIES

Consolidated Statements of Changes in Stockholders' Equity

Years ended December 31, 2001 and 2000
(In thousands of New Taiwan dollars)

	<u>Common stock</u>	<u>Capital surplus</u>	<u>Legal reserve</u>	<u>Unappro- priated earnings</u>	<u>Foreign currency translation adjustmen t</u>	<u>Total stockhold- ers' equity</u>
Balance as of January 1, 2000	\$ 1,000,000	144	-	252,673	88	1,252,905
Appropriation of earnings:						
Legal reserve	-	-	25,267	(25,267)	-	-
Stock dividends	186,000	-	-	(186,000)	-	-
Employee bonuses	34,000	-	-	(34,024)	-	(24)
Directors' and supervisors' remuneration	-	-	-	(6,805)	-	(6,805)
Gain on disposal of property and equipment transferred to capital surplus	-	8	-	(8)	-	-
Net income for 2000	-	-	-	611,262	-	611,262
Foreign currency translation adjustment	-	-	-	-	12,905	12,905
Balance as of December 31, 2000	1,220,000	152	25,267	611,831	12,993	1,870,243
Appropriation of earnings:						
Legal reserve	-	-	61,126	(61,126)	-	-
Stock dividends	231,800	-	-	(231,800)	-	-
Employee bonuses	82,000	-	-	(82,572)	-	(572)
Cash dividends	-	-	-	(219,600)	-	(219,600)
Directors' and supervisors' remuneration	-	-	-	(16,515)	-	(16,515)
Net income for 2001	-	-	-	310,735	-	310,735
Foreign currency translation adjustment	-	-	-	-	(26,674)	(26,674)
Balance as of December 31, 2001	<u>\$ 1,533,800</u>	<u>152</u>	<u>86,393</u>	<u>310,953</u>	<u>(13,681)</u>	<u>1,917,617</u>

See accompanying notes to consolidated financial statements.

HOLTEK SEMICONDUCTOR INC. AND SUBSIDIARIES

Consolidated Statements of Cash Flows

Years ended December 31, 2001 and 2000

(In thousands of New Taiwan dollars)

	2001	2000
Cash flows from operating activities:		
Net income	\$ 310,735	611,262
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	103,663	80,726
Loss from disposal of property, plant and equipment	127	2,037
Provision (reversal of provision) for inventory obsolescence and devaluation and allowance for doubtful accounts	(35,000)	10,000
Gain from disposal of long-term equity investment	(9,703)	-
Increase in net deferred income tax assets	(85,357)	(10,521)
Increase in pension accrual	7,399	5,100
Decrease in accounts receivable	160,046	108,045
Decrease (increase) in inventories	49,267	(106,640)
Decrease (increase) in prepaid expenses and other current assets	38,072	(10,423)
Increase (decrease) in accounts payable	(426,841)	33,852
Increase (decrease) in accrued expenses and other current liabilities	(196,578)	128,607
Net cash provided by (used in) operating activities	(84,170)	852,045
Cash flows from investing activities:		
Additions to property, plant and equipment	(204,922)	(69,669)
Increase in deferred expenses	(11,710)	(10,532)
Decrease (increase) in short-term investments	12,886	(853,999)
Increase in long-term equity investments	(21,419)	(9,226)
Increase in restricted bank deposits	(22,262)	(7,738)
Proceeds from disposal of long-term equity investment	33,120	-
Decrease in refundable deposits and other	762	1,994
Net cash used in investing activities	(213,545)	(949,170)
Cash flows from financing activities:		
Increase in long-term debt	-	7,958
Repayment of long-term debt	(19,817)	(9,700)
Increase in deposits in	3,536	45,954
Payments of cash dividends, directors' remuneration and employee bonuses	(236,687)	(6,829)
Net cash provided by (used in) financing activities	(252,968)	37,383
Effect of exchange rate change on cash and cash equivalents	(28,855)	11,663
Net decrease in cash and cash equivalents	(579,538)	(48,079)
Cash and cash equivalents at beginning of year	795,029	843,108
Cash and cash equivalents at end of year	\$ 215,491	795,029
Supplemental disclosures of cash flow information:		
Cash payments for interest	\$ 5,192	8,070
Cash payments for income taxes	\$ 71,678	35,961
Supplemental disclosures of non-cash financing activities:		
Current installments of long-term debt	\$ 9,200	26,300

See accompanying notes to consolidated financial statements.

HOLTEK SEMICONDUCTOR INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

December 31, 2001 and 2000

(Amounts expressed in thousands of New Taiwan dollars, except for per share information and unless otherwise noted)

(1) Organization and Principal Activities

Holtek Semiconductor Inc. (the Company) was incorporated on October 1, 1998, as a company limited by shares under the laws of the Republic of China (ROC) and the ROC Statute for the Establishment and Administration of Science-Based Industrial Park. The Company began operations on December 11, 1998. The Company established a Hong Kong branch in April 2000. The Company is engaged in the research, development, manufacture and sales of integrated circuits.

Holtek Semiconductor Holding (BVI) Ltd. (Holtek BVI) was incorporated in October 1999 in the British Virgin Islands as a holding company for the Company's overseas investments.

In December 1999, Holtek BVI invested in a 100%-owned subsidiary, Holtek Semiconductor (HK) Ltd. (Holtek (HK)). Holtek (HK) is engaged in the commerce of integrated circuits and related service for the customers located in Hong Kong.

In March 2001, Holtek BVI invested in a 100%-owned subsidiary, Holtek Semiconductor (Shanghai) Inc. (Holtek (Shanghai)). Holtek (Shanghai) is engaged in the commerce of integrated circuits and related service for the customers located in Mainland China.

Sigmos Holdings Ltd. (Sigmos) was incorporated in December 2000 in the British Virgin Islands as a holding company for the Company's overseas investments.

In May 2001, Sigmos invested in a 100%-owned subsidiary, Holmate Semiconductor Inc. (Holmate). Holmate is engaged in the commerce of integrated circuits and related service for the customers located in the United States of America.

(2) Summary of Significant Accounting Policies

(a) Accounting principles and consolidation policy

The consolidated financial statements include the accounts of the Company and subsidiaries in which the Company directly or indirectly owns greater than 50 percent of the subsidiaries' voting shares and is able to exercise control over the subsidiaries' operations and financial activities.

The subsidiaries included in the accompanying consolidated financial statements as of and for the year ended December 31, 2001, are Holtek BVI, Holtek (HK), Holtek (Shanghai), Sigmos and Holmate. The subsidiaries included in the accompanying 2000 consolidated financial statements are Holtek BVI and Holtek (HK). Holtek (Shanghai) and Holmate were incorporated in 2001 and their financial statements were included in the 2001 accompanying consolidated financial statements.

All significant inter-company balances and transactions are eliminated in consolidation.

(b) Foreign currency transactions and translation

Except for Holtek BVI and Sigmos, The Company's foreign subsidiaries use their respective local currencies as their functional currencies and reporting currencies. Holtek BVI and Sigmos use New Taiwan dollars as their functional currency and reporting currency. Foreign currency transactions are recorded at the exchange rate prevailing at the transaction date. At the balance sheet date, monetary assets and liabilities denominated in foreign currency are translated using the exchange rate on that date. The resulting exchange gains or losses from settlement of such transactions or translation of monetary assets and liabilities are reflected in the accompanying consolidated statements of income.

The financial statements of foreign subsidiaries are translated into New Taiwan dollars at the exchange rates prevailing on the balance sheet date, with the exception of stockholders' equity, which is translated at historical rates, and revenues, costs and expenses, which are translated at the weighted-average exchange rates during the reporting period. Translation differences resulting from the translation of such financial statements into New Taiwan dollars are recorded as a foreign currency translation adjustment, a separate component of stockholders' equity.

(c) Cash equivalents

The Company considers all highly liquid financial instruments, such as commercial paper purchased with a maturity of three months or less, to be cash equivalents.

(d) Short-term investments

Short-term investments are stated at the lower of cost or market value. Market value is determined using the net asset value of non-listed securities on the last day of the period.

(e) Inventories

Inventories are stated at the lower of cost or market value. Cost is determined using the weighted-average method. Market value is based on estimated net realizable value for merchandise; finished goods and work in process, and on replacement cost for materials and supplies.

(f) Long-term equity investments

Long-term equity investments in which the Company directly or indirectly owns less than 20% of the investee's voting shares and is not able to exercise significant influence over the investee's operations and financial policies are accounted for by the cost method.

(g) Property, plant and equipment

Property, plant and equipment are stated at cost. Depreciation of property, plant and equipment is provided for by using the straight-line method over the estimated useful lives of the assets. Cost associated with significant additions, replacements and improvements to property, plant and equipment are capitalized. Gains on the disposal of property, plant and equipment are accounted for as non-operating income in the accompanying statements of income. Such gains which occurred before 28 December, 2001, the enacted date of the revised ROC GAAP, net of related income tax, are transferred to capital surplus in the year of disposal in accordance with the ROC Company Law.

As of December 31, 2001 and 2000, insurance coverage for property, plant and equipment amounted to \$405,622 and \$221,749, respectively.

(h) Deferred expenses

The costs of computer software, proprietary know-how and electronic power systems are recorded as deferred expenses and are amortized over periods ranging from two to five years, on a straight-line basis.

(i) Retirement plan

The Company established an employee non-contributory retirement plan (the Plan) covering all local regular employees since 1998. In accordance with the Plan, employees are eligible for retirement or are required to retire after meeting certain age or service requirements. Payments of retirement benefits are based on the years of service and the average salary for the six-month period before the employees' retirement. Each employee earns two months of salary for the first fifteen years of service, and one month of salary for each year of service thereafter. The maximum retirement benefit is 45 months of salary. The Company contributes 2 percent of wages and salaries to a pension fund maintained with the Central Trust of China on a monthly basis. Retirement benefits are paid to eligible participants on a lump-sum basis upon retirement.

Effective on December 31, 1998, the Company adopted ROC Statement of Financial Accounting Standards (SFAS) No. 18, "Accounting for Pensions." SFAS No. 18 requires the Company to perform an actuarial calculation on its pension obligation as of each fiscal year-end. Based on the actuarial calculation, the Company recognizes a minimum pension liability and net periodic pension costs.

For employees hired by the Company's Hong Kong branch, Holtek (HK) and Holtek (Shanghai), pension costs are recognized based on the actual contribution.

(j) Income taxes

Income taxes are accounted for under the asset and liability method. Deferred income taxes are determined based on differences between the financial statements and tax basis of assets and liabilities using the enacted tax rates in effect during the years in which the differences are expected to reverse. The income tax effects resulting from taxable temporary differences are recognized as deferred income tax liabilities. The income tax effects resulting from deductible temporary differences, tax credits and net operating loss carryforwards are recognized as deferred income tax assets. The realization of the deferred income tax assets is evaluated and if it is considered more likely than not that the deferred income tax assets will not be realized, a valuation allowance is recognized accordingly.

Classification of the deferred income tax assets or liabilities as current or non-current is based on the classification of the related assets or liabilities. If the deferred income tax asset or liability is not directly related to a specific asset or liability, the classification is based on the asset's or liability's expected realization date.

According to the ROC Income Tax Law, the Company's unappropriated earnings are subject to an additional 10 percent corporate income surtax. The surtax is charged to income tax expense after the appropriation of earnings is resolved by the stockholders in the following year.

(k) Net income per common share

Net income per common share is computed based on the weighted-average number of common shares outstanding during the period. The effect of net income per common share from the increase in stock through the issuance of stock dividends from unappropriated earnings, capital surplus and employee bonuses is computed retroactively.

(3) Cash and Cash Equivalents

Cash and cash equivalents as of December 31, 2001 and 2000, consisted of the following:

	<u>December 31,</u>	
	<u>2001</u>	<u>2000</u>
Petty cash	\$ 190	68
Checking account	1,293	1,680
Demand deposits	106,149	27,036
Time deposits	107,859	653,425
Commercial paper	-	112,820
	<u>\$ 215,491</u>	<u>795,029</u>

(4) Short-term Investments

Short-term investments consisted of open-end mutual funds as of December 31, 2001 and 2000. The market value of these investments amounted to \$844,296 and \$877,159 as of December 31, 2001 and 2000, respectively.

(5) Inventories

Inventories as of December 31, 2001 and 2000, consisted of the following:

	<u>December 31,</u>	
	<u>2001</u>	<u>2000</u>
Finished goods	\$ 288,499	362,887
Work in process	380,275	347,752
Raw materials	25,289	35,349
Merchandise	3,206	76
Supplies	1,257	1,475
Inventory in transit	-	<u>169</u>
	<u>698,526</u>	<u>747,708</u>
Provision for inventory obsolescence and devaluation	<u>(120,000)</u>	<u>(140,000)</u>
	<u>\$ 578,526</u>	<u>607,708</u>

As of December 31, 2001 and 2000, insurance coverage for inventories amounted to \$615,510 and \$458,075, respectively.

(6) Long-term Equity Investments

Long-term equity investments as of December 31, 2001 and 2000, are summarized below:

<u>Investee</u>	<u>December 31, 2001</u>		<u>December 31, 2000</u>	
	<u>Percentage</u> <u>ownership</u>	<u>Book</u> <u>value</u>	<u>Percentage</u> <u>ownership</u>	<u>Book</u> <u>value</u>
Cost method: Tomato LSI Inc.	6.96%	\$ <u>10,331</u>	6.96%	<u>9,898</u>

(7) Deferred Expenses

Deferred expenses as of December 31, 2001 and 2000, consisted of the following:

	<u>December 31,</u>	
	<u>2001</u>	<u>2000</u>
Computer software	\$ 37,542	59,004
Proprietary know-how	23,000	35,000
Other	<u>2,166</u>	<u>2,544</u>
	<u>\$ 62,708</u>	<u>96,548</u>

(8) Long-term Debt

Long-term debt as of December 31, 2001 and 2000, consisted of the following:

	<u>December 31,</u>	
	<u>2001</u>	<u>2000</u>
Long-term loans	\$ -	62,916
Long-term commercial paper	50,000	-
Long-term payable	<u>21,244</u>	<u>28,145</u>
	71,244	91,061
Less: current portion of long-term debt	<u>(9,200)</u>	<u>(26,300)</u>
	<u>\$ 62,044</u>	<u>64,761</u>

As of December 31, 2001 and 2000, the Company had incurred long-term debt amounting to \$0 and \$62,916, respectively, from Da An Commercial Bank for purchases of machinery and equipment. The interest rate was 6.765% during both 2001 and 2000. The principal is repayable in installments from 2000 to 2004. The Company fully paid off the debt in October 2001.

In October 2001, the Company entered into a long-term revolving note facilities agreement amounting to \$100,000 with Da An Commercial Bank effective until October 11, 2004. A commitment fee of 0.2% per annum is required if the unused credit facilities exceed 50% of the granted credit line. As of December 31, 2001, The Company had issued commercial paper according to the agreement amounting to \$50,000, and the interest rate ranged 2.023~2.42%.

As of December 31, 2001 and 2000, the Company had received loans amounting to \$21,244 and \$28,145, respectively, from the Industrial Development Bureau (IDB) of the Ministry of Economic Affairs (MOEA) to develop new product (refer to note (16) (c)).

As of December 31, 2001 and 2000, unused credit facilities amounted to approximately \$480,000 and \$674,146, respectively.

(9) Retirement Plan

The following table sets forth the benefit obligation and accrued pension balance related to the Company's retirement plan as of December 31, 2001 and 2000:

	<u>December 31,</u>	
	<u>2001</u>	<u>2000</u>
Vested benefit obligation	\$ -	-
Non-vested benefit obligation	<u>(18,838)</u>	<u>(7,620)</u>
Accumulated benefit obligation	(18,838)	(7,620)
Projected compensation increase	<u>(24,748)</u>	<u>(16,399)</u>
Projected benefit obligation	(43,586)	(24,019)
Fair value of plan assets	<u>13,328</u>	<u>8,999</u>
Funded status	(30,258)	(15,020)
Unrecognized pension loss	11,489	3,504
Unrecognized net assets at transition	<u>3,072</u>	<u>3,218</u>
Accrued pension	<u>\$ (15,697)</u>	<u>(8,298)</u>

The components of net periodic pension cost for the years ended December 31, 2001, and 2000, were as follows:

	<u>2001</u>	<u>2000</u>
Service cost	\$ 10,371	8,772
Interest cost	1,441	780
Actual return on plan assets	(382)	(387)
Amortization	<u>(84)</u>	<u>108</u>
Net pension cost	<u>\$ 11,346</u>	<u>9,273</u>

Significant assumptions used in the above calculation for 2001 and 2000 are summarized as follows:

	<u>December 31,</u>	
	<u>2001</u>	<u>2000</u>
Discount rate	4.50%	6.00%
Rate of increase in future compensation levels	4.50%	6.00%
Expected long-term rate of return on plan assets	4.50%	6.00%

There were no vested benefit obligations as of December 31, 2001.

The pension costs of the Company's Hong Kong Branch, Holtek (HK) and Holtek (Shanghai) which recognized base on actual contribution for the years ended December 31, 2001 and 2000, were as follows:

	<u>2001</u>	<u>2000</u>
Hong Kong branch	\$ 407	-
Holtek (HK)	2,156	381
Holtek (Shanghai)	877	-

(10) Deposits In

As of the December 31, 2001 and 2000, deposits held by Holtek (HK) from its distribution agents to secure their purchase credit lines amounted to \$59,022 and \$52,337, respectively. In 2001 and 2000, Holtek (HK) paid interest on such deposits at a rate of 5% and 6%, respectively.

(11) Stockholders' Equity

(a) Common stock

Pursuant to a stockholders' resolution on April 5, 2000, the Company increased its outstanding common stock by 22 million shares at par value of ten New Taiwan dollars per share through the transfer of unappropriated earnings and employee bonuses of \$186,000 and \$34,000, respectively. The increase in common stock was registered and approved with the governmental authorities on May 31, 2000.

Pursuant to a stockholders' resolution on March 2, 2001, the Company increased its outstanding common stock by 31.38 million shares at par value of ten New Taiwan dollars per share through the transfer of unappropriated earnings and employee bonuses of \$231,800 and \$82,000, respectively. The increase in common stock was registered with and approved by the governmental authorities on April 29, 2001. As of December 31, 2001, the Company's authorized and issued common stock amounted to \$1,800,000 and \$1,533,800, respectively.

(b) Capital surplus

Pursuant to the ROC Company Law, capital surplus can only be used to offset an accumulated deficit or to increase common stock. Capital surplus can not be used to declare cash dividends.

(c) Legal reserve and appropriation of earnings

According to the Company's articles of incorporation, 10% of the Company's net income, after offsetting any accumulated deficit, shall be set aside as a legal reserve. The remainder, if any, may be appropriated according to the proposal of the Board of Directors and the resolution of the stockholders' meeting. The percentage of such appropriation should be as follows:

- 82% as dividends to stockholders;
- 15% as bonuses to employees; and
- 3% as remuneration to directors and supervisors

Regarding the above-mentioned dividends to stockholders, the cash dividends to stockholders should not less than 10% of total cash and stock dividends. But the amount of earnings distribution and the ratio of cash dividends could be adjusted according to the resolution of the stockholders' meeting based on the estimation of the current year's operation results and cash flows expectation.

(12) Income Taxes

The Company qualifies as a "scientific industry" as prescribed by the Statute for the Establishment and Administration of the Science-Based Industrial Park (the SBIP Statute) and an "Important Technology Industry" as prescribed by the ROC Statute for Upgrading Industries (SUI). In accordance with the ROC SUI, the Company or its stockholders are entitled to either a corporate income tax exemption period of five years or to a tax credit equal to 20% of their investment in the Company. Pursuant to a stockholders' resolution, the Company's stockholders have resolved to receive the tax credits.

According to the SBIP Statute, the Company was entitled to a tax-exemption for income resulting from the expanded operations generated by its capital increase in 2000 for four consecutive years. The period of tax-exemption is not decided yet by the Company.

The statutory tax rate of the Company's revenue generated from "Scientific Industry" - related business was 20%, while the tax rate of other revenue was 25% according to the SBIP Statute. Commencing from January 20, 2001, the statutory tax rate of the Company is 25% due to the revision of the SBIP Statute. In 2001 and 2000, the tax rate of Holtek (HK) was 16% and 16.5%, respectively, based on Hong Kong tax law.

The components of income tax expense (benefit) for the years ended December 31, 2001 and 2000, are summarized as follows:

	<u>2001</u>	<u>2000</u>
Current	\$ 15,562	71,232
Deferred	<u>(85,357)</u>	<u>(10,522)</u>
Income tax expense (benefit)	<u>\$ (69,795)</u>	<u>60,710</u>

A reconciliation of the expected income tax expense at the statutory tax rate and the actual income tax expense (benefit) for the years ended December 31, 2001 and 2000, was as follows:

	<u>2001</u>	<u>2000</u>
Income tax expense computed at the statutory tax rate	\$ 60,745	134,343
Tax effect of exempted income	(15,200)	(347)
Investment tax credits	(124,723)	(74,717)
Changes in valuation allowance of deferred income tax assets	29,000	(3,671)
Effect of tax rate change	(8,914)	-
Additional 10% income surtax on unappropriated earnings	-	5,132
Over-accrual in prior years	(2,634)	(4,304)
Other	<u>(8,069)</u>	<u>4,274</u>
Actual income tax expense (benefit)	<u>\$ (69,795)</u>	<u>60,710</u>

The components of deferred income tax assets (liabilities) as of December 31, 2001 and 2000, were as follows:

	December 31,			
	2001		2000	
	Amount	Tax	Amount	Tax
	t	effect	t	effect
Current:				
Allowance for doubtful accounts	\$ 10,228	2,557	28,000	5,600
Provision for inventory obsolescence and devaluation	120,000	30,000	140,000	28,000
Loss carryforward of foreign branch and subsidiaries	23,037	3,684	-	-
Investment tax credits	33,000	33,000	56,730	56,730
Other	4,408	799	(718)	(144)
	\$ <u>70,040</u>		<u>90,186</u>	
Noncurrent:				
Investment loss (income) accounted for by the equity method	\$ 11,650	2,912	(3,292)	(659)
Pension accrual	13,698	3,425	8,298	1,660
Investment tax credits	129,922	129,922	-	-
Other	2,000	500	6,000	1,200
	136,759		2,201	
Less: valuation allowance	(29,000)		-	
	\$ <u>107,759</u>		<u>2,201</u>	
Total deferred income tax assets	\$ <u>206,799</u>		<u>93,190</u>	
Total deferred income tax liabilities	\$ <u>356</u>		<u>803</u>	
Total valuation allowance	\$ <u>29,000</u>		<u>-</u>	

According to the ROC SUI, the total amount of investment tax credits that can be utilized per year is limited to 50 percent of the year's current income tax expense. However, the foregoing limit does not apply to the last year of the investment tax credits' expiration period. As of December 31, 2001, the estimated unused investment tax credits and related expiration dates were as follows:

<u>Unused investment tax credits</u>	<u>Expiration date</u>
\$ 34,783	December 31, 2002
29,873	December 31, 2003
54,797	December 31, 2004
<u>43,469</u>	December 31, 2005
\$ <u>162,922</u>	

The Company's income tax returns after 1998 have not been assessed by the tax authorities.

Pursuant to the Hong Kong Inland Revenue Ordinance, net losses as assessed by the Inland Revenue Department can be carried forward to set off future years' assessable profits. As of December 31, 2001, the unused loss carryforwards of the Company's Hong Kong branch and Holtek (HK) were \$15,157 and \$7,880, respectively.

Beginning in 1998, an integrated income tax system was implemented in the ROC. Under the new tax system, the income tax paid at the corporate level can be used to offset the ROC resident stockholders' individual income tax. The Company is required to establish an Imputation Credit Account (ICA) to maintain a record of the corporate income taxes paid and imputation credit that can be allocated to each stockholder. The credit available to each ROC resident stockholder is calculated by multiplying the dividend by the creditable ratio. The creditable ratio is calculated as the balance of the ICA divided by earnings retained since January 1, 1998.

Information relating to the Company's ICA as of December 31, 2001 and 2000, is summarized as follows:

	December 31,	
	<u>2001</u>	<u>2000</u>
Unappropriated retained earnings:		
Earned after December 31, 1997	\$ <u>310,953</u>	<u>611,831</u>
Imputation credit account balance	\$ <u> 32</u>	<u> 3,556</u>
	<u>2001</u>	<u>2000</u>
Expected creditable ratio for earnings distribution to resident stockholders	<u>5.97%</u> (expected)	<u>12.04%</u> (actual)

(13) Financial Instruments

(a) Derivative financial instruments

The Company entered into several forward foreign currency exchange contracts and foreign currency exchange option contracts to hedge exposures on foreign currency accounts receivable and payable. The counter-parties of the derivative contracts are reputable domestic financial institutions. Therefore, management believes that the risk of default by the counter-parties is remote. The Company and Subsidiaries did not hold any derivative financial contracts as of December 31, 2001 and 2000.

(b) Non-derivative financial instruments

The Company and subsidiaries' non-derivative financial assets include cash and cash equivalents, short-term investment, notes and accounts receivable, and receivables from related parties and long-term investments. The Company and Subsidiaries' non-derivative financial liabilities consist of notes and accounts payable, payables to related parties, and long-term debts.

The following methods and assumptions are used to estimate the fair value for each class of non-derivative financial instruments:

1. The carrying amounts of cash and cash equivalents, accounts receivable and accounts payable approximate their fair value due to the short-term nature of these items.
2. The fair value of short-term investments is based on publicly quoted market prices. Refer to note 4 for information on market value of short-term investments.
3. It is not practicable to determine the fair value of long-term equity investments since these investments are not publicly traded. Please refer to note 6 for information on book value of long-term equity investments.
4. The book value of the loans from the IDB of the MOEA amounted to \$21,244. Their fair value based on the present value of the expected future cash flows was \$19,852. The discount rate was based on the bank rate for similar loans that the Company would be able to obtain. Except for the above-mentioned loans from IDB, the Company's long-term debts bear floating interest rates; therefore, the principal amounts of long-term debts approximate their fair value.

(14) Transactions with Related Parties

(a) Names and relationships

<u>Name of related party</u>	<u>Relationship</u>
United Microelectronics Corp. (iUMC)	The Company's major shareholder
Applied Component Technology Corp. (iACTC)	Investee accounted for under the equity method by UMC
Novatek Microelectronics Corp. (iNMC)	Investee accounted for under the equity method by UMC
Faraday Electronics Manufacture Corp. (iFEMC)	Investee accounted for under the equity method by UMC

(b) Significant transactions and balances with related parties as of and for the years ended December 31, 2001 and 2000, are summarized below:

Sales

	<u>2001</u>		<u>2000</u>	
	<u>Amount</u>	<u>Percentage of net sales</u>	<u>Amount</u>	<u>Percentage of net sales</u>
ACTC	\$ 23,424	1	90,926	2
NMC	-	-	9,545	-
	<u>\$ 23,424</u>	<u>1</u>	<u>100,471</u>	<u>2</u>

There were no significant differences in credit terms between related parties and third party customers.

Purchases

	<u>2001</u>		<u>2000</u>	
	<u>Amount</u>	<u>Percentage of total purchases</u>	<u>Amount</u>	<u>Percentage of total purchases</u>
UMC	\$ 546,614	23	1,028,992	32
FEMC	-	-	6,001	-
ACTC	-	-	85	-
	<u>\$ 546,614</u>	<u>23</u>	<u>1,035,078</u>	<u>32</u>

There were no significant differences in purchasing terms between related parties and third party suppliers.

Accounts receivable/payable

- Accounts receivable

	<u>December 31,</u>			
	<u>2001</u>		<u>2000</u>	
	<u>Amount</u>	<u>Percentag e of total accounts receivable</u>	<u>Amount</u>	<u>Percentag e of total accounts receivable</u>
ACTC	\$ <u>2,499</u>	<u>1</u>	<u>3,193</u>	<u>1</u>

- Accounts payable

	<u>December 31,</u>			
	<u>2001</u>		<u>2000</u>	
	<u>Amount</u>	<u>Percentag e of total accounts payable</u>	<u>Amount</u>	<u>Percentag e of total accounts payable</u>
UMC	\$ <u>121,124</u>	<u>22</u>	<u>312,834</u>	<u>33</u>

Purchase of property and equipment

The Company purchased a building located in the Hsin Chu Science-Based Industrial Park and related improvements amounting to \$165,000 from UMC in March 2001. There were no outstanding balances as of December 31, 2001, related to the purchase.

The Company purchased equipment and computer software from UMC in 2000 amounting to \$533. There were no outstanding balances as of December 31, 2000, related to these purchases.

Operating leases

The Company leased its office, dormitory and parking lots from UMC in 2001 and 2000. In 2001 and 2000, total rental expense amounted to \$3,318 and \$15,003, respectively. The related payable balance as of December 31, 2001 and 2000, amounted to \$0 and \$3,110, respectively.

Other

The service fee for IC design which the Company outsourced to FEMC in 2001 amounted to \$4,386. The related payable balance as of December 31, 2001, was \$1,622.

UMC paid certain expenses on behalf of the Company amounting to \$4,801 in 2001. The related payable balance as of December 31, 2001, was \$232.

(15) Pledged Assets

Assets pledged as collateral as of December 31, 2001 and 2000, are summarized as follows:

<u>Assets</u>	<u>Pledged for</u>	<u>Carrying amount as of December 31,</u>	
		<u>2001</u>	<u>2000</u>
Machinery and equipment	Long-term loans	\$ -	51,717
Computer software	Long-term loans	-	20,190
Time deposits	Long-term payable	30,000	7,738
Buildings and structures	Long-term loans	<u>120,000</u>	-
		<u>\$ 150,000</u>	<u>79,645</u>

(16) Commitments and Contingent Liabilities

- (a) The Company entered into certain lease agreements for its office and parking lots. As of December 31, 2001, the minimum future rental payments under existing rental agreements were as follows:

<u>Year ending</u>	<u>Amount</u>
2002	\$ 11,019
2003	<u>2,150</u>
	<u>\$ 13,169</u>

- (b) The Company leases land for the site of its building from the Industrial Park Administration Bureau. The lease term for the current agreement is effective for 20 years, starting from March 15, 2001. In accordance with the lease agreement, rental payment is subject to adjustment as the government reappraises the land value. The current rental is \$3,102 per year.
- (c) Under a research and development agreement with the IDB of the MOEA, the Company was entitled to receive both a grant and a loan amounting to \$29,210 during the period from August 1, 1998, to April 30, 2000. The agreement was completed on April 30, 2000. Total revenue related to this agreement amounted to \$7,958 for the year ended December 31, 2000. The Company can not apply for the patent to produce project products outside Taiwan until the loan and compensation required under the agreement are fully paid to the Development Funds of the Executive Yuan, or until the Company obtains approval from the IDB. In accordance with the agreement, the Company has issued promissory notes amounting to \$29,210 to Chiao Tung Bank and will repay the loan in twelve quarterly installments beginning from May 2001. Beginning from the date that sales of the project's products commence, the Company must make quarterly payments to a governmental institution in an amount equal to 2% of sales for three consecutive years. The aggregate amount shall not exceed 40% of the above loan. There were no sales of the project's products incurred as of December 31, 2001.
- (d) The Company and subsidiaries entered into several agreements to purchase equipment and for the transfer of technology. As of December 31, 2001 and 2000, the unpaid balance under these agreements amounted to \$8,479 and \$16,398, respectively.

(17) Segment Information

(a) Industry information

The Company and subsidiaries operate predominantly in one industry segment, integrated circuits.

(b) Geographic information

	2001							Eliminations	Consolidated
	Taiwan	HK Branch	Holtek BVI	Holtek (HK)	Holtek (Shanghai)	Sigmos	Holmate		
Area revenue:									
Customers	\$ 1,791,844	251,992	-	1,236,407	10,997	-	2,831	-	3,294,071
Inter-company								(2,487,995)	
	<u>1,267,876</u>	<u>1,220,119</u>							
	<u>\$ 3,059,720</u>	<u>1,472,111</u>		<u>1,236,407</u>	<u>10,997</u>		<u>2,831</u>	<u>5</u>	<u>3,294,071</u>
Net income	\$ <u>274,029</u>	<u>(12,541)</u>	<u>1,057</u>	<u>(9,013)</u>	<u>(6,538)</u>		<u>(568)</u>	<u>64,309</u>	<u>310,735</u>
Area identifiable assets	\$ <u>2,671,748</u>	<u>385,031</u>	<u>83,214</u>	<u>217,172</u>	<u>62,212</u>	<u>6,898</u>	<u>9,410</u>	<u>(681,903)</u>	<u>2,753,782</u>
	2000								
	Taiwan	HK Branch	Holtek BVI	Holtek (HK)	Eliminations		Consolidated		
Area revenue:									
Customers	\$ 3,104,609	25,937	-	1,685,894		-		4,816,440	
Inter-company	<u>1,524,860</u>	<u>161,109</u>				<u>(1,685,969)</u>			
	<u>\$ 4,629,469</u>	<u>187,046</u>		<u>1,685,894</u>		<u>(1,685,969)</u>		<u>4,816,440</u>	
Net income	\$ <u>608,399</u>	<u>2,863</u>	<u>4,134</u>	<u>3,549</u>		<u>(7,683)</u>		<u>611,262</u>	
Area identifiable assets	\$ <u>3,190,337</u>	<u>424,424</u>	<u>85,497</u>	<u>278,925</u>		<u>(720,861)</u>		<u>3,258,322</u>	

(c) Significant customers

Sales to major customers for the years ended December 31, 2001 and 2000, are summarized as follows:

	2001		2000	
	Amount	% of total sales	Amount	% of total sales
Customer A	\$ <u>507,623</u>	<u>15</u>	<u>510,529</u>	<u>11</u>