

MEDIATEK INCORPORATION

FINANCIAL STATEMENTS
WITH
INDEPENDENT AUDITORS' REPORT

FOR THE YEARS ENDED
DECEMBER 31, 2003 AND 2002

Notice to Readers

The reader is advised that these financial statements have been prepared originally in Chinese. In the event of a conflict between these financial statements and the original Chinese version or difference in interpretation between the two versions, the Chinese language financial statements shall prevail.

The accompanying financial statements are intended only to present the financial position and results of operations and cash flows in accordance with accounting principles and practices generally accepted in the Republic of China on Taiwan 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 on Taiwan.

English Translation of a Report Originally Issued in Chinese

Independent Auditors' Report

To the Board of Directors and Shareholders of
MediaTek Incorporation

We have audited the accompanying balance sheets of MediaTek Incorporation as of December 31, 2003 and 2002, and the related statements of income, changes in shareholders' equity, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. We did not audit the financial statements of Communication Technology Venture Capital Investment Corp. as of and for the year ended December 31, 2002, a long-term equity investee accounted for under the equity method by the Company. The financial statements of Communication Technology Venture Capital Investment Corp. were audited by other auditors. Our opinion insofar as it relates to the Company's long-term investment of approximately NT\$73,469,000 as of December 31, 2002, and the related investment loss amounting to approximately NT\$6,803,000 for the year then ended is based solely on the report of the other auditors.

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

In our opinion, based on our audits and the report of other auditors, the financial statements referred to above present fairly, in all material respects, the financial position of MediaTek Incorporation as of December 31, 2003 and 2002, and the results of its operations and its cash flows for the years then ended in conformity with generally accepted accounting principles in the Republic of China.

Diwan, Ernst & Young
January 28, 2004
Taipei, Taiwan
Republic of China

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MEDIATEK INCORPORATION
BALANCE SHEETS

As of December 31, 2003 and 2002

(Amounts in thousand New Taiwan dollars)

ASSETS	Notes	2003	2002	LIABILITIES AND SHAREHOLDERS' EQUITY	Notes	2003	2002
Current assets				Current liabilities			
Cash and cash equivalents	2, 4(1)	\$ 21,603,107	\$ 12,092,321	Long-term debts-current portion	4(7)	\$ 17,539	\$ 13,475
Short-term investments(net)	2, 4(2)	1,086,918	3,826,000	Notes and accounts payable		2,253,181	1,405,299
Notes and accounts receivable(net)	2, 4(3)	3,694,440	3,579,978	Payables to related parties	5	1,928,180	1,980,138
Receivables from related parties(net)	5	11,932	211,124	Income taxes payable	2, 4(16)	312,827	436,058
Inventories-net	2, 4(4)	2,075,508	1,667,252	Accrued expenses		1,326,411	2,608,820
Deferred tax assets-current(net)	2, 4(16)	262,733	47,952	Other current liabilities		49,129	47,166
Prepayments		126,245	238,170	Total current liabilities		<u>5,887,267</u>	<u>6,490,956</u>
Other current assets		253,960	208,413				
Restricted deposits-current	5(3),6	83,387	927,000	Long-term liabilities			
Total current assets		<u>29,198,230</u>	<u>22,798,210</u>	Long-term debts, less current portion	4(7)	<u>10,643</u>	<u>30,896</u>
Long-term investments in equity	2, 4(5)	<u>11,459,763</u>	<u>6,496,617</u>	Other liabilities			
Property, plant and equipment	2, 4(6)			Accrued pension liabilities	2, 4(8)	<u>54,319</u>	<u>36,242</u>
Buildings and facilities		734,712	75,522	Total liabilities		<u>5,952,229</u>	<u>6,558,094</u>
Machinery and equipment		100,835	146,354	Shareholders' equity			
Leased assets		-	53,998	Capital			
Leasehold improvements		7,506	64,825	Common stock	4(9)	6,415,473	4,604,654
Research and development equipment		466,837	347,890	Capital reserve			
Miscellaneous equipment		<u>21,418</u>	<u>11,850</u>	Additional paid-in capital	2, 4(11)	70,000	70,000
Total cost		<u>1,331,308</u>	<u>700,439</u>	Treasury stock transaction	2, 4(11)	41,198	10,842
Less : Accumulated depreciation		(310,004)	(231,603)	Donated assets	2, 4(11)	1,260	1,260
Add : Prepayments for equipment		27,008	34,480	Long-term investment transaction	2, 4(11)	<u>3,448</u>	<u>-</u>
Construction in progress		<u>279</u>	<u>391,660</u>	Total capital reserve		<u>115,906</u>	<u>82,102</u>
Property, plant and equipment-net		<u>1,048,591</u>	<u>894,976</u>	Retained earnings			
Intangible assets	2			Legal reserve	4(10)	2,495,315	1,271,971
Computer software		174,962	213,139	Undistributed earnings	4(12)	27,113,421	17,819,560
Others		<u>100,267</u>	<u>68</u>	Cumulative translation adjustments	2	(49,071)	125,504
Total intangible assets		<u>275,229</u>	<u>213,207</u>	Treasury stock-cost	2, 4(13)	<u>(55,970)</u>	<u>(55,970)</u>
Other assets				Total shareholders' equity		<u>36,035,074</u>	<u>23,847,821</u>
Refundable deposits		<u>5,490</u>	<u>2,905</u>				
Total assets		<u>\$ 41,987,303</u>	<u>\$ 30,405,915</u>	Total liabilities and shareholders' equity		<u>\$ 41,987,303</u>	<u>\$ 30,405,915</u>

The accompanying notes are an integral part to these financial statements.

Chairman : Ming-Kai Tsai

Chief Executive Officer : Jyh-Jer Cho

Chief Financial Officer : Ming-To Yu

English Translation of Financial Statements Originally Issued in Chinese

MEDIATEK INCORPORATION

STATEMENTS OF INCOME

For the years ended December 31, 2003 and 2002

(Amounts in thousand New Taiwan dollars, except earnings per share)

	Notes	2003	2002
Gross sales		\$ 39,778,263	\$ 30,742,443
Less : Sales returns and discounts		(1,713,844)	(1,229,294)
Net sales	2, 4(14), 5	38,064,419	29,513,149
Cost of goods sold	4.(15)	(18,409,446)	(14,840,919)
Gross profit		19,654,973	14,672,230
Operating expenses	2, 4(15),5,7(6)		
Selling expenses		(183,444)	(224,053)
Administration expenses		(440,456)	(228,513)
Research and development expenses		(3,950,293)	(1,496,327)
Total operating expenses		(4,574,193)	(1,948,893)
Operating income		15,080,780	12,723,337
Non-operating income			
Interest income		198,652	229,835
Gain on disposal of short-term investments		82,303	56,654
Reversal of accrued license fee	7(1)	1,557,540	-
Others		65,363	21,390
Total non-operating income		1,903,858	307,879
Non-operating expenses			
Interest expense		(44)	-
Net loss from equity investments	2, 4(5)	(250,105)	(131,036)
Foreign exchange loss-net		(52,631)	(49,310)
Inventory loss provision	2,4(4)	(66,833)	(16,373)
Others		(5,981)	(6,457)
Total non-operating expenses		(375,594)	(203,176)
Income before income tax		16,609,044	12,828,040
Income tax expense	2, 4(16)	(86,955)	(594,601)
Net income		\$ 16,522,089	\$ 12,233,439
Earnings Per Share (in New Taiwan dollars)	2, 4(17)		
Income before income tax		\$ 26.10	\$ 20.16
Net income		\$ 25.96	\$ 19.22
Pro-forma data: (Assuming that the Company's shares owned by its subsidiary were not treated as treasury stock)	2, 4(17)		
Earnings Per Share (in New Taiwan dollars)	2, 4(17)		
Income before income tax		\$ 25.89	\$ 20.00
Net income		\$ 25.75	\$ 19.07

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Chairman : Ming-Kai Tsai

Chief Executive Officer : Jyh-Jer Cho

Chief Financial Officer : Ming-To Yu

English Translation of Financial Statements Originally Issued in Chinese

MEDIATEK INCORPORATION
STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

For the years ended December 31, 2003 and 2002

(Amounts in thousand New Taiwan dollars)

	Common stock	Capital reserve	Legal reserve	Undistributed earnings	Cumulative translation adjustments	Treasury stock	Total
Balance as of January 1, 2002	\$ 3,160,056	\$ 71,260	\$ 601,668	\$ 9,205,990	\$ 126,109	\$ -	\$ 13,165,083
Appropriation and distribution of 2001 earnings:							
Legal reserve	-	-	670,303	(670,303)	-	-	-
Directors' and supervisors' remuneration	-	-	-	(60,328)	-	-	(60,328)
Capitalization of employees' bonus	180,575	-	-	(361,149)	-	-	(180,574)
Stock dividends	1,264,023	-	-	(2,528,045)	-	-	(1,264,022)
Net income, 2002	-	-	-	12,233,439	-	-	12,233,439
Cumulative translation adjustments	-	-	-	-	(605)	-	(605)
Treasury stocks owned by subsidiaries	-	10,842	-	-	-	(55,970)	(45,128)
Equity adjustment due to disproportional acquisition of investees' new shares	-	-	-	(44)	-	-	(44)
Balance as of December 31, 2002	4,604,654	82,102	1,271,971	17,819,560	125,504	(55,970)	23,847,821
Appropriation and distribution of 2002 earnings:							
Legal reserve	-	-	-	-	-	-	-
Directors' and supervisors' remuneration	-	-	-	(55,050)	-	-	(55,050)
Capitalization of employees' bonus	199,190	-	-	(654,482)	-	-	(455,292)
Stock dividends	1,611,629	-	-	(5,295,352)	-	-	(3,683,723)
Net income, 2003	-	-	-	16,522,089	-	-	16,522,089
Cumulative translation adjustments	-	-	-	-	(174,575)	-	(174,575)
Treasury stocks owned by subsidiaries	-	30,356	-	-	-	-	30,356
Adjustment of capital reserve from equity investee	-	3,448	-	-	-	-	3,448
Balance as of December 31, 2003	<u>\$ 6,415,473</u>	<u>\$ 115,906</u>	<u>\$ 2,495,315</u>	<u>\$ 27,113,421</u>	<u>\$ (49,071)</u>	<u>\$ (55,970)</u>	<u>\$ 36,035,074</u>

The accompanying notes are an integral part to these financial statements.

Chairman : Ming-Kai Tsai

Chief Executive Officer : Jyh-Jer Cho

Chief Financial Officer : Ming-To Yu

MEDIATEK INCORPORATION
STATEMENTS OF CASH FLOWS
For the years ended December 31, 2003 and 2002
(Amounts in thousand New Taiwan dollars)

	2003	2002
Cash flows from operating activities :		
Net income	\$ 16,522,089	\$ 12,233,439
Adjustments to reconcile net income to net cash provided by operating activities		
Deferred income taxes	(214,781)	(14,099)
Depreciation	130,490	97,922
Amortization	179,996	100,890
Bad debt expense (reversal)	(165)	78,513
Cash dividends from investees	10,978	89,031
Inventory loss provisor	66,833	16,373
Gain on disposal of short-term investments	(82,303)	(56,654)
Net loss from equity investments	250,105	131,036
Loss (gain) on disposal of property, plant and equipment	(8,042)	287
Net changes in operating assets and liabilities		
Notes and accounts receivable	(113,427)	(854,666)
Receivables from related parties	198,322	(79,856)
Inventories	(475,089)	(1,060,703)
Prepayments	113,209	(238,170)
Other current assets	(45,547)	(174,999)
Notes payable and accounts payable	847,882	789,517
Payables to related parties	(51,958)	735,861
Income taxes payable	(123,231)	103,170
Accrued expenses	(1,282,409)	175,238
Other current liabilities	1,963	8,465
Accrued pension liabilities	18,077	12,523
Net cash provided by operating activities	15,942,992	12,093,118
Cash flows from investing activities :		
Decrease (increase) in restricted deposits	843,613	(864,000)
Decrease in short-term investments	2,821,385	740,432
Increase in long-term investments	(5,365,000)	(5,000,060)
Proceeds from disposal of long-term investments	-	186,837
Purchase of property, plant and equipment	(291,878)	(494,155)
Proceeds from disposal of property, plant and equipment	17,247	150
Increase in intangible assets	(244,734)	(155,676)
Decrease (increase) in refundable deposits	(2,585)	862,047
Net cash used in investing activities	(2,221,952)	(4,724,425)
Cash flows from financing activities :		
Increase (decrease) in long-term debts	(16,189)	11,840
Directors' and supervisors' remuneration	(55,050)	(60,328)
Employee bonus	(455,292)	(180,574)
Cash dividends	(3,683,723)	(1,264,022)
Net cash used in financing activities	(4,210,254)	(1,493,084)
Net increase in cash and cash equivalents	9,510,786	5,875,609
Cash and cash equivalents at the beginning of the year	12,092,321	6,216,712
Cash and cash equivalents at the end of the year	\$ 21,603,107	\$ 12,092,321
Supplemental disclosures of cash flow information :		
Income tax paid during the year	\$ 422,072	\$ 505,529
Interest paid during the year	\$ 44	\$ -
Purchase of property, plant and equipment	\$ 291,878	\$ 470,747
Add: net decrease in payables to equipment suppliers	-	23,408
Cash paid for the purchase of property, plant and equipment	\$ 291,878	\$ 494,155
Non-cash activities :		
Stock dividends and employee bonus capitalized	\$ 1,810,819	\$ 1,444,598
Long-term debts-current portion	\$ 17,539	\$ 13,475
Cumulative translation adjustments	\$ (174,575)	\$ (605)
Long-term equity investment adjustments	\$ 3,448	\$ -
Treasury stocks owned by subsidiaries	\$ -	\$ 55,970

The accompanying notes are an integral part to these financial statements.

Chairman : Ming-Kai Tsai

Chief Executive Officer : Jyh-Jer Cho

Chief Financial Officer : Ming-To Yu

MEDIATEK INCORPORATION
NOTES TO FINANCIAL STATEMENTS

1. Organization and Operation

MediaTek Incorporation (the "Company") was incorporated in the Hsinchu Science-Based Industrial Park ("HSIP"), Taiwan on May 28, 1997. The Company operates principally as a designer, manufacturer and supplier of integrated circuit chips and decoders of optical storage.

As of December 31, 2003 and 2002, the Company's employees totaled 639 and 438, respectively.

2. Summary of Significant Accounting Policies

The accompanying financial statements are prepared in accordance with the R.O.C.'s "Guidelines Governing the Preparation of Financial Reports by Securities Issuer" and generally accepted accounting standards. Significant accounting policies are summarized as follows:

Cash Equivalents

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

Foreign Currency Transactions

The Company maintains its accounting records in New Taiwan dollars ("NT Dollars" or "NT\$"), the national currency of Republic of China. Transactions denominated in foreign currencies are recorded in NT Dollars using the exchange rates in effect at the dates of the transactions. Assets and liabilities denominated in foreign currencies are translated into NT Dollars using the exchange rates in effect at the balance sheet date. Foreign exchange gains or losses are included in other income or losses.

The assets and liabilities of the foreign subsidiaries are translated into NT Dollars, with the local currency of each foreign subsidiary as its functional currency, at current exchange rates in effect at the balance sheet date. Revenue and expense accounts are translated using a weighted average exchange rate for the relevant period. Translation gains and losses are included as a component of shareholders' equity.

MEDIATEK INCORPORATION

NOTES TO FINANCIAL STATEMENTS – (continued)

Short-term Investments

Short-term investments are recorded at cost when acquired and are stated at the lower of aggregate cost or market value at the balance sheet date. The market value of listed equity securities or closed-end funds is determined by the average closing price during the last month of the fiscal year. The market value for open-ended funds is determined by their equity per unit at the balance sheet date. The amount by which aggregate cost exceeds market value is reported as a loss in the current year. In subsequent periods, recoveries of market value are recognized as a gain to the extent that the market value does not exceed the original aggregate cost of the investment. No revenue is recognized when stock dividends are received. Instead, the number of shares increases and the cost per share is recalculated. Gain or loss on disposal of debt securities funds is recognized using first-in-first-out method. Interest income of credit-linked structured deposits matured within a year is accrued based on the contracted interest rate.

Allowance for Doubtful Accounts

The allowance for doubtful accounts is provided based on the collectibility and aging analysis of notes and accounts receivable.

Inventories

Inventories are carried at lower of cost or market value using the weighted average cost method. Replacement cost is used to determine the market value of raw materials. Net realizable value is used to determine the market value of work in process and finished goods.

Long-term Investments in Equity

Long-term investments in which the Company holds an interest of less than 20% are accounted for under either cost method, or lower of cost or market value method. Holdings between 20% and 50% are accounted for under equity method of accounting. The difference between the investment cost and the fair value of the identifiable assets at the date of acquisition is amortized over five years using the straight-line method.

Unrealized inter-company gains and losses are eliminated under the equity method. Profit from sales of depreciable assets between the investee and the Company is amortized and recognized based on the assets' economic service lives. Profit from other types of inter-company transactions is recognized when realized.

MEDIATEK INCORPORATION

NOTES TO FINANCIAL STATEMENTS – (continued)

Consolidated financial statements are prepared if the Company owns at least 50 % of the invested company's shares. However, the financial statements of any subsidiary in which the total assets and total revenue for the current year are less than 10 % of that of the parent company may be excluded from the consolidated financial statements. If the sum of the total assets or sales of all unconsolidated subsidiaries equals to or exceeds 30% of the parent company's assets or sales, subsidiaries whose sales or assets are over or equal to 3% of the parent company's sales or assets should be consolidated.

Property, Plant and Equipment

Property, plant and equipment are stated at cost less accumulated depreciation. Depreciation is computed on a straight-line basis over the following useful lives:

Buildings and facilities	40 to 50	years
Machinery and equipment	3	years
Leased assets	50	years
Leasehold improvements	3	years
Research and development equipment	3 to 5	years
Miscellaneous equipment	3 to 5	years

Improvements and replacements are capitalized and depreciated over their estimated useful lives while ordinary repairs and maintenance are expensed as incurred.

When property, plant and equipment are disposed of, their original cost and accumulated depreciation are written off and related gains or losses are included in other income or losses.

Intangible Assets

Intangible assets are stated at cost and amortized on a straight-line basis over the following useful lives:

Computer software	1 to 3 years
Others	3 years

Capital Expenditures vs. Revenue Expenditures

If the expenditure increases the future service potential of the plant assets and the lump sum purchase price per transaction exceeds a certain criteria, the expenditure is capitalized, while the others are expensed as incurred.

Revenue Recognition

Revenue is recognized in accordance with ROC Statement of Financial Accounting Standards No. 32, "Accounting for Revenue Recognition."

MEDIATEK INCORPORATION

NOTES TO FINANCIAL STATEMENTS – (continued)

Employee Retirement Benefits

The Company has a defined benefit pension plan covering substantially all of its employees and adopts ROC Statement of Financial Accounting Standards No. 18, "Accounting for Pensions." In accordance with the Labor Standards Law of the ROC, the Company makes a monthly contribution equal to 2 % of the wages and salaries paid during the period to a pension fund maintained with the Central Trust of China. The fund is administered by the Employees' Retirement Fund Committee and is deposited in the committee's name. Therefore, the pension fund is not included in the financial statements of the Company. As of December 31, 2003 and 2002, the fund amounted to NT\$21,361 thousand and NT\$14,165 thousand, respectively.

Income Tax

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

Income tax credit is accounted for in accordance with the ROC Statement of Financial Accounting Standards No. 12, "Accounting for Income Tax Credit." Income tax credits resulting from the acquisition of equipment, research and development expenditures, employee training and investment in equity stock shall be recognized using the flow-through method.

Income taxes (10%) on undistributed earnings generated from January 1, 1998 are recorded as expense in the year when the stockholders have resolved that the earnings shall be retained.

Financial instruments

a. Foreign exchange forward contracts

A forward foreign exchange contract obligates the Company to exchange predetermined amounts of specified foreign currencies at specified exchange rates for another currency on a specified date. For contracts that are designated as hedges, discounts or premiums, being the difference between the spot exchange rate and the forward exchange rate at the inception of the contract, are accreted or amortized to the income statement over the contract lives using the straight-line method. Realized gains and losses from settlement or unrealized gains and losses resulting from changes in the spot exchange rate at the balance sheet date are recorded in the income statement as foreign exchange gains or losses in the period in which they relate. The related amounts due to or from counter parties are included in other current assets or other current liabilities.

MEDIATEK INCORPORATION**NOTES TO FINANCIAL STATEMENTS – (continued)****b. Option contracts**

At maturity the Company or the financial institution, depending upon which party has the right of the option, exercises the option to receive a said amount denominated in one currency and pay a said amount in a different currency. The conversion rate is stated in the contract.

For options, premiums are amortized over the contract lives using the straight-line method. Gains and losses are recorded in the income statement upon exercise.

Earnings Per Share

In accordance with R.O.C. Statement of Financial Accounting Standards No.24, “Earnings per Share,” the Company presents basic earnings per share if a simple capital structure exists; or both basic earnings per share and diluted earnings per share if a complex capital structure exists. Basic earnings per share is equal to the net income (loss) attributable to common stock divided by the weighted-average number of common shares. When calculating diluted earnings per share, the numerator should include or add back potential common stock dividends, interest and other conversion revenues (expenses). The denominator should include all potentially dilutive common shares.

Treasury Stock

Effective from January 1, 2002, the Company’s shares owned by its subsidiaries were treated as treasury stock according to ROC SFAS No. 30, “Accounting for Treasury Stock.” Cash dividends distributed to the Company’s subsidiaries is deducted from investment income account and credited to capital reserves-treasury stock transaction.

3. Reasons and Effects for Change in Accounting

None.

4. Contents of Significant Accounts**(1) Cash and Cash Equivalents**

<i>In thousand NTD</i>	As of December 31,	
	2003	2002
Savings and checking accounts	\$1,524,883	\$2,745,421
Time deposits	16,233,157	7,845,870
Cash equivalents	3,855,067	1,501,030
Total	<u>\$21,603,107</u>	<u>\$12,092,321</u>

MEDIATEK INCORPORATION
NOTES TO FINANCIAL STATEMENTS – (continued)

(2) Short-term Investments

<i>In thousand NTD</i>	As of December 31,			
	2003		2002	
	Cost	Market Value	Cost	Market Value
Mutual fund	\$650,000	\$653,500	\$3,756,494	\$3,813,939
Government bonds	301,006	300,093	-	-
Credit-linked structured deposits	135,912	136,422	69,506	69,763
Subtotal	1,086,918	1,090,015	3,826,000	3,883,702
Less: Allowance for market decline	-	-	-	-
Net	<u>\$1,086,918</u>	<u>\$1,090,015</u>	<u>\$3,826,000</u>	<u>\$3,883,702</u>

Please refer to Note 11 for risk disclosure of credit-linked structured deposits.

(3) Notes and Accounts Receivable

<i>In thousand NTD</i>	As of December 31,	
	2003	2002
Notes receivable	\$-	\$120,008
Accounts receivable	3,913,803	3,680,369
Subtotal	3,913,803	3,800,377
Less: Allowance for doubtful accounts	(219,363)	(220,399)
Net	<u>\$3,694,440</u>	<u>\$3,579,978</u>

(4) Inventories

<i>In thousand NTD</i>	As of December 31,	
	2003	2002
Raw materials	\$2,381	\$5,414
Work in process	1,267,715	1,155,915
Finished goods	830,473	549,495
Inventories in transit	52,240	-
Subtotal	2,152,809	1,710,824
Less: Allowance for inventory obsolescence	(77,301)	(43,572)
Net	<u>\$2,705,508</u>	<u>\$1,667,252</u>

The insurance coverage for inventories amounted to NT\$700,000 thousand and NT\$800,000 thousand as of December 31, 2003 and 2002, respectively. The insurance coverage for inventories stored at associated manufacturer is provided by processors. Processors assume damage responsibility.

MEDIATEK INCORPORATION**NOTES TO FINANCIAL STATEMENTS – (continued)****(5) Long-term Investments in Equity**

a.

As of December 31, 2003					
Investee Companies	Types	Shares	Amounts (NT\$'000)	Ownership (%)	Accounting Method
MediaTek Investment Corp.	Common share	185,000,000	\$1,487,775	100.00%	Equity
Hsu-Ta Investment Limited	Capital	-	3,478,891	100.00%	Equity
Hsu-Chia Investment Limited	Capital	-	3,234,176	100.00%	Equity
Hsu-Kang Investment Limited	Capital	-	3,234,197	100.00%	Equity
Yuantonix, Inc.	Common share	1,500,000	15,000	6.00%	Cost
Subtotal			11,450,039		
Unrealized loss on disposal of long-term equity investments			9,724		
Total			<u>\$11,459,763</u>		

As of December 31, 2002					
Investee Companies	Types	Shares	Amounts (NT\$'000)	Ownership (%)	Accounting Method
MediaTek Investment Corp.	Common share	150,000,000	\$1,458,577	100.00%	Equity
Hsu-Ta Investment Limited	Capital	-	2,000,378	100.00%	Equity
Hsu-Chia Investment Limited	Capital	-	1,513,984	100.00%	Equity
Hsu-Kang Investment Limited	Capital	-	1,513,954	100.00%	Equity
Subtotal			6,486,893		
Unrealized loss on disposal of long-term equity investments			9,724		
Total			<u>\$6,496,617</u>		

- b. For the years ended December 31, 2003 and 2002, the Company's net loss from equity investment amounted to NT\$250,105 thousand and \$131,036 thousand, respectively. Such loss was recognized based on the audited financial statements of the investees. Among the the investee companies, Communication Technology Venture Capital Investment Corp.'s (an indirect investee) 2002 financial statements were audited by other auditors. The investment loss recognized by the Company for Communication Technology Venture Capital Investment Corp. was NT\$6,803 thousand for the year ended December 31, 2002. In 2003, the Company lost its significant influence in Communication Technology Venture Capital Investment Corp. and, accordingly, accounts for it using cost method.

MEDIATEK INCORPORATION**NOTES TO FINANCIAL STATEMENTS – (continued)**

- c. In July 2002, the Company sold certain equity investments to MediaTek Capital Corp (a subsidiary) and Gaintech Co. Ltd. (a subsidiary of MediaTek Investment Corp.) at an aggregate price of NT\$186,837 thousand. The related disposal loss of NT\$9,724 thousand was deemed unrealized.

(6) Property, Plant and Equipment

- a. The insurance coverage for property, plant and equipment amounted to NT\$1,277,837 thousand and NT\$568,743 thousand as of December 31, 2003 and 2002, respectively.
- b. No interest was capitalized during the years of 2003 and 2002.

(7) Long-term Debts

The authorities of HSIP financed the Company by providing free-interest loans for certain R&D projects:

Items	Original balance (NT\$'000)	As of December 31,		Repayment
		2003 (NT\$'000)	2002 (NT\$'000)	
First project	\$17,544	\$-	\$6,579	The loan is repayable in eight quarterly installments, starting October 1, 2001, each with NT\$2,193 thousand.
Second project	17,180	6,896	13,792	The first repayment of NT\$3,388 thousand was made in May 2002. The remaining is repayable in eight quarterly installments, starting January 1, 2003, each with NT\$1,724 thousand.
Third project	24,000	21,286	24,000	The first repayment of NT\$2,715 thousand was made in August 2003. The remaining is repayable in eight quarterly installments, starting January 1, 2003, each with NT\$2,661 thousand.
Total long-term debts		28,182	44,371	
Less: Current portion		(17,539)	(13,475)	
Total		<u>\$10,643</u>	<u>\$30,896</u>	

MEDIATEK INCORPORATION**NOTES TO FINANCIAL STATEMENTS – (continued)****(8) Accrued Pension Liabilities****a. The components of net pension cost**

<i>In thousand NTD</i>	For the year ended December 31,	
	2003	2002
Service cost	\$16,782	\$11,548
Interest cost	1,773	1,285
Expected return on plan assets	(567)	(398)
Amortization	88	88
Over statement	7,145	5,201
Net pension cost	\$25,221	\$17,724

b. The funded status of the Company's pension plans

<i>In thousand NTD</i>	As of December 31,	
	2003	2002
Benefit obligations		
Vested benefit obligation	\$-	\$-
Non-vested benefit obligation	(24,743)	(17,766)
Accumulated benefit obligation	(24,743)	(17,766)
Effect of projected future salary increase	(29,902)	(26,553)
Projected benefit obligation	(54,645)	(44,319)
Fair value of plan assets	21,361	14,165
Funded status of pension plan	(33,284)	(30,154)
Unrecognized net transitional obligation	1,236	1,324
Unrecognized loss (gain)	(7,553)	369
Over-accrual	(14,718)	(7,781)
Accrued pension liabilities	\$ (54,319)	\$(36,242)

The vested benefit was nil as of December 31, 2003 and 2002.

c. The underlying actuarial assumption

	For the year ended December 31,	
	2003	2002
Discount rate	3.5%	4.0%
Rate of increase in future compensation levels	3.5%	4.0%
Expected long-term rate of return on plan assets	3.5%	4.0%

MEDIATEK INCORPORATION**NOTES TO FINANCIAL STATEMENTS – (continued)****(9) Common Stock**

Based on the resolution of the shareholders' annual general meeting on June 3, 2002, the Company issued 144,459,723 new shares, each share at par value of NT\$10, from the capitalization of retained earnings of NT\$1,264,023 thousand and employees' bonus of NT\$180,575 thousand. The capitalization had been approved by the authorities.

Following the resolution of shareholders' meeting on May 16, 2003, the Company increased its authorized capital to NT\$8,960,000 thousand, divided into 896,000 thousand shares each at par of NT\$10. Among the authorized capital, 40,000 thousand shares were reserved for the grant of options to qualified employees. The shareholders further resolved to issue 181,081,886 new shares for the capitalization of shareholders' bonus of NT\$1,611,629 thousand and employees' bonus of NT\$199,190 thousand. The capitalization had been approved by the authorities.

As of December 31, 2003, the authorized and issued common shares of the Company amounted to NT\$8,960,000 thousand and NT\$6,415,473 thousand, respectively, divided into 896,000,000 shares and 641,547,256 shares, respectively, each at par of NT\$10.

(10) Legal Reserve

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

(11) Capital Reserve

<i>In thousand NTD</i>	As of December 31,	
	2003	2002
Additional paid-in capital	\$70,000	\$70,000
Donated assets	1,260	1,260
Treasury stock transaction	41,198	10,842
Long-term investment transaction	3,448	-
Total	<u>\$115,906</u>	<u>\$82,102</u>

According to ROC Company Law, capital reserve can only be used for making up deficiencies or distributions of stock dividends. The Company shall not use capital reserve to make up its loss unless legal reserve is insufficient for making good such losses.

MEDIATEK INCORPORATION**NOTES TO FINANCIAL STATEMENTS – (continued)**

For the years ended December 31, 2003 and 2002, the cash dividends of NT\$30,356 thousand and NT\$10,842 thousand, respectively, distributed to the Company's subsidiary were credited to the Company's capital reserve account in accordance with ROC SFAS No. 30, "Accounting for Treasury Stock."

(12) Earnings Distribution

The net income for the year ended December 31, 2002 may be appropriated or distributed in the following sequences:

- (a). Income tax obligation;
- (b). Offsetting accumulated deficits, if any;
- (c). Legal reserve at 10% of net income;
- (d). Remuneration for directors and supervisors at 0.5% of the remaining of (a) through (c);
- (e). 10% to 15% of the remaining balance after the appropriations from (a) to (d) shall be distributed as employees' bonus;
- (f). The remaining balance after all the above appropriations and distributions shall be shareholders' bonus, and may be retained or distributed proportionally.

The Company's articles of incorporation, revised on May 16, 2003, provide that the net income may be appropriated or distributed proportionally as follows:

- (a). Income tax obligation;
- (b). Offsetting accumulated deficits, if any;
- (c). Legal reserve at 10% of net income;
- (d). Remuneration for directors and supervisors to a maximum of 0.5% of the remaining of (a) through (c);
- (e). 10% to 15% of the remaining balance after the appropriations from (a) to (d) shall be distributed as employees' bonus;
- (f). The remaining balance after all the above appropriations and distributions shall be shareholders' bonus, and may be retained or distributed proportionally.

(13) Treasury Stock

Effective January 1, 2002, the Company's shares owned by its subsidiaries are accounted for as treasury stock. The Company's shares owned by its subsidiary were shown as follows:

	January 1, 2003		Additions		December 31, 2003		
	Shares	Amount	Shares	Amount	Shares	Amount	Market Value
Owner		(NT\$'000)		(NT\$'000)		(NT\$'000)	(NT\$'000)
MediaTek	3,794,560	\$55,970	1,328,096	\$-	5,122,656	\$55,970	\$1,624,102
Capital Corp.			(Note)				

MEDIATEK INCORPORATION**NOTES TO FINANCIAL STATEMENTS – (continued)**

	January 1, 2002		Additions		December 31, 2002		
	Shares	Amount	Shares	Amount	Shares	Amount	Market Value
Owner		(NT\$'000)		(NT\$'000)		(NT\$'000)	(NT\$'000)
MediaTek	2,710,400	\$55,970	1,084,160	\$-	3,794,560	\$55,970	\$1,081,450
Capital Corp.			(Note)				

(Note) Stock dividend received

(14) Sales Revenues

<i>In thousand NTD</i>	For the year ended December 31,	
	2003	2002
Revenues from sales of chipsets	\$39,753,617	\$30,742,443
Others	24,646	-
Total	39,778,263	30,742,443
Less: Sales returns and sales discount	(1,713,844)	(1,229,294)
Net sales	\$38,064,419	\$29,513,149

(15) Personnel, Depreciation and Amortization Expenses

<i>In thousand NTD</i>	For the year ended December 31,					
	2003			2002		
	Recorded under cost of goods sold	Recorded under operating expense	Total	Recorded under cost of goods sold	Recorded under operating expense	Total
Personnel						
Salary expense	\$43,817	\$721,665	\$765,482	\$42,231	\$513,289	\$555,520
Insurance	1,734	28,230	29,964	1,681	19,080	20,761
Pension expense	1,496	23,725	25,221	1,369	16,355	17,724
Other	540	6,696	7,236	265	4,542	4,807
Total	\$47,587	\$780,316	\$827,903	\$45,546	\$553,266	\$598,812
Depreciation	\$26,461	\$104,029	\$130,490	\$40,875	\$57,047	\$97,922
Amortization	\$-	\$179,996	\$179,996	\$-	\$100,890	\$100,890

MEDIATEK INCORPORATION**NOTES TO FINANCIAL STATEMENTS – (continued)****(16) Income Tax**

- a. Pursuant to the “Statute for the Establishment and Administration of Science-Based Industrial Park,” the Company was granted several periods of tax holidays with respect to income derived from approved investments. The tax holidays expire on December 31, 2004.
- b. Pursuant to the “Statute for Upgrading Industries,” the Company is entitled to an income tax exemption period for five consecutive years on the income generated from qualifying high technology activities. The Company has elected the tax exemption period to be from January 1, 2002 through December 31, 2006 and January 1, 2003 through December 31, 2007.
- c. The Company’s available investment tax credits as of December 31, 2003 are as follows:

Year incurred	Nature of Expenditures	Total credit amount (NT\$'000)	Unused amount (NT\$'000)	Year expired
2000	R&D	\$208,945	\$-	2004
2001	R&D	361,488	-	2005
	Human development	4,506	-	2005
2002	R&D	534,302	-	2006
	Human development	5,345	-	2006
2003	R&D	997,743	754,261	2007
	Human development	905	-	2007
		<u>\$2,113,234</u>	<u>\$754,261</u>	

- d. The Company’s income tax returns through 1999 had been assessed by the tax authorities. The tax authorities determined that the Company should pay an additional income tax of NT\$26,947 thousand and NT\$41,290 thousand for 1998 and 1999, respectively. The Company has accrued such tax payable according to the determination while filing a re-examination.

e.

(a) Deferred tax assets and liabilities (<i>In thousand NTD</i>)	As of December 31, 2003
Total deferred tax liabilities	<u>\$309</u>
Total deferred tax assets	<u>\$778,333</u>
Valuation allowance for deferred tax assets	<u>\$515,291</u>

MEDIATEK INCORPORATION**NOTES TO FINANCIAL STATEMENTS – (continued)**

- (b) Temporary differences that generated deferred tax assets
or liabilities (*In thousand NTD*)

	As of December 31, 2003	
	Amount	Tax effect
Deductible temporary difference-Recognition of unrealized accrued expenses	\$433,730	\$6,126
Deductible temporary difference-Recognition of unrealized allowance for inventory obsolescence	\$77,301	\$1,092
Deductible temporary difference-Allowance for doubtful accounts	\$180,967	\$2,556
Deductible temporary difference-Unrealized technology license fee	\$1,012,216	\$14,298
Taxable temporary difference-Unrealized foreign exchange gain	\$21,895	\$309
Investment tax credits		\$754,261

- (c) *In thousand NTD*

	As of December 31, 2003
Deferred tax assets-current	\$776,834
Valuation allowance for deferred tax assets-current	(513,792)
Net deferred tax assets-current	263,042
Deferred tax liabilities-current	(309)
Net deferred tax assets and liabilities-current	\$262,733

- (d) *In thousand NTD*

	As of December 31, 2003
Deferred tax assets-noncurrent	\$1,499
Valuation allowance for deferred tax assets-noncurrent	(1,499)
Net deferred tax assets-noncurrent	-
Deferred tax liabilities-noncurrent	-
Net deferred tax assets and liabilities-noncurrent	\$-

MEDIATEK INCORPORATION**NOTES TO FINANCIAL STATEMENTS – (continued)**

(e)	<i>In thousand NTD</i>	For the year ended December 31, 2003
	Income tax payable-current	\$4,152,261
	10% tax on undistributed earnings generated after 1997	561,249
	Tax exemption	(3,830,782)
	Permanent difference	41,950
	Investment tax credits	(998,648)
	Net deferred income tax effect	389,767
	Effect on change in tax regulation	(273,050)
	Accruals for additional prior year income tax	41,290
	Others	2,918
	Income tax expense	\$86,955
(f) Integrated income tax information		As of December 31, 2003
	Balance of the imputation credit account (ICA)	
	(<i>In thousand NTD</i>)	\$597,381
	Expected creditable ratio	2.20%
(g) Information related to undistributed retained earnings		As of December 31, 2003
	(<i>In thousand NTD</i>)	
	Prior to 1998	\$-
	After 1998 (inclusive)	27,113,421
	Total	\$27,113,421
f.		
	(a) Deferred tax assets and liabilities (<i>In thousand NTD</i>)	As of December 31, 2002
	Total deferred tax liabilities	\$2,374
	Total deferred tax assets	\$175,850
	Valuation allowance for deferred tax assets	\$125,524

MEDIATEK INCORPORATION**NOTES TO FINANCIAL STATEMENTS – (continued)**

(b) Temporary differences that generated deferred tax assets or liabilities (<i>In thousand NTD</i>)		As of December 31, 2002	
		Amount	Tax effect
Deductible temporary difference-Recognition of unrealized accrued expenses		\$2,008,392	\$125,524
Deductible temporary difference-Recognition of unrealized allowance for inventory obsolescence		\$43,572	\$2,723
Deductible temporary difference-Allowance for doubtful accounts		\$181,568	\$11,348
Deductible temporary difference-Unrealized foreign exchange loss		\$10,022	\$626
Taxable temporary difference-Unrealized foreign exchange gain		\$37,991	\$2,374
Investment tax credits			\$35,629
(c) <i>In thousand NTD</i>		As of December 31, 2002	
Deferred tax assets-current		\$175,850	
Valuation allowance for deferred tax assets-current		(125,524)	
Net deferred tax assets-current		50,326	
Deferred tax liabilities-current		(2,374)	
Net deferred tax assets and liabilities-current		\$47,952	
(d) <i>In thousand NTD</i>		For the year ended December 31, 2002	
Income tax payable - current		\$3,207,010	
10% tax on undistributed earnings generated after 1997		319,846	
Tax exemption		(2,396,335)	
Permanent difference		19,067	
Investment tax credits		(583,527)	
Net deferred income tax effect		(452)	
Accruals for additional prior year income tax		26,947	
Others		2,045	
Income tax expense		\$594,601	

MEDIATEK INCORPORATION**NOTES TO FINANCIAL STATEMENTS – (continued)**

(e) Integrated income tax information	As of December 31, 2002
Balance of the imputation credit account (ICA)	
(In thousand NTD)	\$475,729
Actual creditable ratio	4.21%
(f) Information related to undistributed retained earnings	
(In thousand NTD)	As of December 31, 2002
Prior to 1998	\$-
After 1998 (inclusive)	17,819,560
Total	\$17,819,560

(17) Basic Earnings Per Share

The weighted average numbers of common shares outstanding were computed as follows: (in shares)

Contents	For the year ended December 31,	
	2003	2002
Common shares outstanding, beginning	460,465,370	316,005,647
Stock dividend, 40%, 2002	-	126,402,258
Stock issuance for employee bonus, 5.71%, 2002	-	18,057,465
Stock dividend, 35%, 2003	161,162,879	161,162,879
Stock issuance for employee bonus, 4.33%, 2003	19,919,007	19,919,007
Subtotal	641,547,256	641,547,256
Less: Treasury stock owned by subsidiary	(5,122,656)	(5,122,656)
Weighted average shares outstanding, ending	636,424,600	636,424,600

For the year ended December 31, 2003,

(Numerator) Income (NT\$'000)		(Denominator)	Earnings per share (NT\$)	
Before tax	After tax	(Shares)	Before tax	After tax
\$16,609,044	\$16,522,089	636,424,600	\$26.10	\$25.96

For the year ended December 31, 2002,

(Numerator) Income (NT\$'000)		(Denominator)	Earnings per share (NT\$)	
Before tax	After tax	(Shares)	Before tax	After tax
\$12,828,040	\$12,233,439	636,424,600	\$20.16	\$19.22

MEDIATEK INCORPORATION**NOTES TO FINANCIAL STATEMENTS – (continued)**

The Pro-Forma earnings per share were computed as follows assuming that the Company's shares owned by its subsidiary were not treated as treasury stock:

For the year ended December 31, 2003,

(Numerator) Income (NT\$'000)		(Denominator)	Earnings per share (NT\$)	
Before tax	After tax	(Shares)	Before tax	After tax
\$16,609,044	\$16,522,089	641,547,256	\$25.89	\$25.75

For the year ended December 31, 2002,

(Numerator) Income (NT\$'000)		(Denominator)	Earnings per share (NT\$)	
Before tax	After tax	(Shares)	Before tax	After tax
\$12,828,040	\$12,233,439	641,547,256	\$20.00	\$19.07

5. Related Party Transactions

(1) Related Parties and Relations

Related parties	Relations
United Microelectronics Corp. ("UMC")	The supervisor of the Company
King Yuan Electronics Co., Ltd. ("KING YUAN")	The chairmen of the Company and KING YUAN are close relatives.
PixArt Imaging Inc. ("PII")	Same person represents the chairman of both companies' boards.
UMC Japan ("UMCJ")	Equity investee of UMC
MediaTek Capital Corp.	Affiliated company
MediaTek Limited ("MLT")	Affiliated company
MediaTek Communications Inc. ("MTC")	Affiliated company
CrystalMedia Technology, Inc. ("CrystalMedia")	Affiliated company
Wireless ICs, Inc. ("Wireless")	Affiliated company
Gaintech Co. Ltd ("Gaintech")	Affiliated company

MEDIATEK INCORPORATION**NOTES TO FINANCIAL STATEMENTS – (continued)**

(2) Major Transactions with related parties

a. Purchases

<i>In thousand NTD</i>	For the year ended December 31,			
	2003		2002	
	Amount	% of total purchase	Amount	% of total purchase
UMC	\$8,185,626	73.04	\$7,276,842	74.23
UMCJ	1,099,645	9.81	2,290,604	23.37
Total	\$9,285,271	82.85	\$9,567,446	97.60

Prices for purchase from related parties are not comparable since UMC and UMCJ were the Company's major suppliers. Payment terms to UMC and UMCJ were month end 45 days.

b. Sales

<i>In thousand NTD</i>	For the year ended December 31,			
	2003		2002	
	Amount	% of net sales	Amount	% of net sales
MTL	\$361,659	0.95	\$1,120,219	3.80
Others	7,106	0.02	-	-
Total	\$368,765	0.97	\$1,120,219	3.80

Sales prices to the related parties were similar to those to third party customers while trade credit terms were month end 45 days.

(3) Other transactions with UMC

a.

<i>In thousand NTD</i> Transactions	For the year ended December 31,	
	2003	2002
Mask purchased and technological services	\$126	\$56,784
Rental and related expenses	-	964
Others	-	15,063
Total	\$126	\$72,811

- b. The Company entered into a manufacturing contract with UMC. Under the contract, the Company pledged a time deposit of NT\$864,000 thousand to UMC as a production deposit. Such deposit was recorded under restricted deposit account as of December 31, 2002. In August 2003, the Company cancelled the pledged time deposit.

MEDIATEK INCORPORATION

NOTES TO FINANCIAL STATEMENTS – (continued)

- (4) The Company paid NT\$647,681 thousand and NT\$652,410 thousand to KING YUAN for the years ended December 31, 2003 and 2002, respectively, for various IC testing and experimental services. In addition, the revenue from providing manufacturing technology service to KING YUAN amounted to NT\$7,539 thousand for the year 2003.
- (5) The Company sold certain equipment to KING YAUN in April 2003 at a price of NT\$7,667 thousand, resulting in a gain on disposal of the machinery and equipment of NT\$2,950 thousand.
- (6) The Company entered into a facility lease agreement with PII during in 2001. As to June 30, 2002, NT\$104,756 thousand was paid for the lease and underlying facilities and equipment were recorded under leased assets equipment and leasehold improvement. In August, 2002, the Company exercised purchase rights for the underlying facility, as permitted by the agreement and approved by HSIP. Lease facility has been transferred in March 2003 and recorded under building and facility account. In January 2003, the Company has entered into another facility purchase agreement with PII in amount of NT\$31,270 thousand. As of December 31, 2003, the Company has fully paid the purchase price.
- (7) The Company entered into a technology transfer agreement with MTC in 2002 at the price of US\$1,300 thousand. As of December 31, 2002, the Company has paid US\$650 thousand and recorded it under R&D expense. In March 2003, the agreement price has been revised for US\$650 thousand under mutual agreement of MTC and the Company.
- (8) The Company paid US\$500 thousand to MTL for commission during in 2003.
- (9) In August 2003, the Company entered into technology transfer agreements with CystalMedia and Wireless at the price of US\$4,250 thousand and US\$5,100 thousand, respectively. As of December 31, 2003, totaling US\$2,000 thousand and US\$2,150 thousand, respectively, were paid and recorded it under intangible assets.
- (10) The Company sold certain equity investments to MediaTek Capital Corp. and Gaintech in July 2002. Please refer to Note 4(5) for details.

MEDIATEK INCORPORATION**NOTES TO FINANCIAL STATEMENTS – (continued)**

(11) Receivables and payables resulting from the above transactions:

a. Receivables from related parties

<i>In thousand NTD</i>	As of December 31,			
	2003		2002	
	Amount	%	Amount	%
MTL	\$12,566	0.34	\$211,124	5.57
Others	236	0.01	-	-
Subtotal	12,802	0.35	211,124	5.57
Less: Allowance for doubtful accounts	(870)	(0.03)	-	-
Net	<u>\$11,932</u>	<u>0.32</u>	<u>\$211,124</u>	<u>5.57</u>

b. Payables to related parties

<i>In thousand NTD</i>	As of December 31,			
	2003		2002	
	Amount	%	Amount	%
UMC	\$1,716,616	41.05	\$1,432,704	42.32
KING YUAN	140,379	3.36	102,851	3.04
UMCJ	71,185	1.70	444,229	13.12
Others	-	-	354	0.01
Total	<u>\$1,928,180</u>	<u>46.11</u>	<u>\$1,980,138</u>	<u>58.49</u>

6. Assets Pledged As Collateral

(1) As of December 31, 2003

<i>In thousand NTD</i>	Net book value	Secured financial institutions	Contents
Restricted deposits	\$63,000	Farmers Bank of China	Long-term debt
Restricted deposits	20,387	Tiva	Contract executed deposits
Total	<u>\$83,387</u>		

(2) As of December 31, 2002

<i>In thousand NTD</i>	Net book value	Secured financial institutions	Contents
Restricted deposits	\$63,000	Farmers Bank of China	Long-term debt
Restricted deposits	864,000	UMC	Production deposit
Total	<u>\$927,000</u>		

MEDIATEK INCORPORATION

NOTES TO FINANCIAL STATEMENTS – (continued)

7. Commitments and Contingencies

- (1) The Company acquired its manufacturing technology of CD-ROM control chips mainly from UMC. UMC, however, was engaged in certain legal action with OAK, an U.S. company, for patents of such technology. In October 1997, OAK filed a complaint with the United States Northern District Court of California alleged that UMC breached a prior Settlement Agreement and later sought against the Company and UMC the damages, injunctive and other relief. In April 1998, OAK filed a complaint with the International Trade Committee against the Company and UMC for the infringement of the patents stated above and violation of Section 337 of the Tariff Act of 1930. In May 2001, the Court of Appeals for the Federal Circuit (“CAFC”) affirmed that there was no violation of Section 337. OAK did not appeal to Supreme Court of the United States regarding the CAFC’s decision within the legal period. In August 2003, Zoran Corporation acquire OAK and succeeded to OAK’s position in this litigation. The dispute for certain damages between the Company and Zoran in Northern District Court of California remains pending. As of December 31, 2003, the Company reversed its accrued royalty fee by NT\$ 1,557,540 thousand, and recorded it under other non-operating revenue.
- (2) On June 2001, the Company filed a complaint with the Northern District of California against VIA Technologies, Inc., (“VIA”) and AOpen, Inc. (“AOpen”), alleging that VIA and AOpen are infringing two patents related to optical disc drivers. On September 2003, the District Court granted the Company’s motion for preliminary injunction against VIA and AOpen. VIA and AOpen appealed the District Court’s decision to US Court of Appeals for the Federal Circuit, requesting for invalidity of the preliminary injunction during the appeal period. The request was denied on January 22, 2004. The Company has also named the U.S. subsidiaries of VIA and Aopen and VIA Optical Solution, Inc. as co-defendants.
- (3) On June 2003, VIA Technologies, Inc., (“VIA”) filed a complaint with the Northern District of California, naming the Company as a defendant and alleging that the Company directly or indirectly infringe its U.S. Patent No. 6459665. The Company has contracted American attorneys to defend this District Court case vigorously.
- (4) On June and July 2003, VIA Technologies, Inc., (“VIA”) filed a complaint in the Hsinchu District Court of Taiwan, naming the Company as a defendant and alleging that the Company infringed its Taiwan Patent No. 163889. VIA’s complaint alleges that the Company’s DVD-ROM and COMBI chipsets infringed the patent. The Company has contracted Taiwan attorneys to defend this case.

MEDIATEK INCORPORATION

NOTES TO FINANCIAL STATEMENTS – (continued)

- (5) In 2002, ESS Technology, Inc. (“ESS”) filed a complaint with the Northern District of California, naming the Company as a defendant and alleging that the Company infringed ESS copyrights in firmware used with ESS chipsets in DVD players. In June 2003, ESS and the Company entered into a settlement agreement resolving all of the issues in dispute between two parties. Under this settlement agreement, ESS has licensed the Company certain copyrights and the Company should pay ESS a fee of US\$45 million for usage of the rights in the past. The Company recorded such amount under R&D expense. Also the settlement agreement provides that the Company pay quarterly royalties on the total payable capped at US\$45 million within 2years starting third quarter 2004.
- (6) The Company entered into a software and assets purchase agreement with US-based Tvia Inc. (“Tvia”) in June 2003. The Company and its subsidiaries acquired on Tvia’s video related software technology, patents, associated assets and employees in US and China, in amount of US\$10,000 thousand. As of December 31, 2003, totaling US\$7,400 thousand has been paid and recorded under R&D expense. In addition, US\$600 thousand was deposited in an escrow account and recorded under restricted deposits-current.
- (7) As of December 31, 2003, totaling US\$20,722 thousand of the Company’s significant contracts remained unpaid.

8. Significant Casualty Loss

None

9. Significant Subsequent Events

None

MEDIATEK INCORPORATION**NOTES TO FINANCIAL STATEMENTS – (continued)****10. Segment Information****(1) Major Customers**

Sales to customers representing over 10% of the Company's net sales were as follows:

<i>In thousand NTD</i>	For the year ended December 31,			
	2003		2002	
	Amounts	%	Amounts	%
Customers				
A	\$5,821,199	15.29%	\$7,093,699	24.04%
B	5,668,817	14.89%	4,163,121	14.11%
C	3,631,359	9.54%	3,044,529	10.32%
Total	<u>\$15,121,375</u>	<u>39.72%</u>	<u>\$14,301,349</u>	<u>48.47%</u>

(2) Export Sales

The Company's export sales totaled NT\$33,404,609 thousand and NT\$24,254,335 thousand for the years ended December 31, 2003 and 2002, respectively, representing 87.75% and 82.18% of the Company's net sales for corresponding years.

(3) Geographic data

The Company has no significant foreign operation.

(4) Industry data

The Company operates predominantly in one industry segment, which being the designing, manufacturing, and supply of integrated circuit chips and decoders.

11. Derivative Financial Instruments**(1) Contract Amount or Nominal Amount and Credit Risk****a. As of December 31, 2003,**

Financial instruments	Type	Maturity	Contract amount (US\$'000)	Exercise rate	Credit risk
Forward exchange	Sell USD	January 2004~ February 2004	\$105,000	33.975~34.235	-
	Purchase USD	January 2004	\$1,000	34.235	-

b. As of December 31, 2002,

Financial instruments	Type	Maturity	Contract amount (US\$'000)	Exercise rate	Credit risk
Forward exchange	Sell USD	January 2003~ March 2003	\$149,000	34.409~34.983	-
Options	Call USD	March 2003~ April 2003	\$17,500	35.190~35.500	-
Swaps	Currency Swap	January 2003	\$6,022	34.870	-

MEDIATEK INCORPORATION

NOTES TO FINANCIAL STATEMENTS – (continued)

Credit risk relates to the extent to which failures by counter parties to discharge their obligations could reduce the amount of future cash flows from financial assets on hand as of the balance sheet date. The Company minimizes exposure to credit risks by only dealing with reputable banks.

(2) Price Risk

There are three types of price risk: currency risk, interest rate risk and market risk. Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates; interest rate risk is the risk that the value of a financial instrument will fluctuate due to changes in market interest rates and market risk is the risk that the value of financial instrument will fluctuate as a result of changes in market prices. The Company considers that the price risk related to the hedge transactions is minimal as gains or losses from contracts for hedging purposes are likely to be offset by gains or losses from the underlying assets and liabilities denominated in foreign currencies.

(3) Liquidity and Cash Flow Risks

Liquidity risk is the risk that the Company will encounter difficulty in raising funds to meet commitments associated with financial instruments. Liquidity risk may result from an inability to sell a financial asset quickly at close to its fair value. Cash flow risk is the risk that future cash flows associated with a monetary financial instrument will fluctuate by a significant amount.

The Company anticipates that the liquidity risk is minimal because the financial instruments entered into for hedging purposes are liquid and have binding contracts with reputable banks. The purpose of entering into forward exchange contracts and option contracts is to limit the Company's exposure to losses resulting from adverse fluctuations in assets and liabilities denominated in foreign currency. Therefore, no significant additional cash requirement is anticipated.

(4) Types of derivative financial instruments, purpose of holding the derivative financial instruments and the strategy for achieving the hedging purpose:

The Company's derivative financial instruments are not held for trading purpose. The purpose of holding forward exchange contracts is to hedge exchange rate fluctuation risk resulting from assets, liabilities or commitments denominated in foreign currency. The Company's hedging strategy is to avoid majority of market price risk. Derivative financial instruments selected for hedging are highly anti-co-related with the fluctuation of the fair value of derivatives hedged. Derivatives are evaluated periodically.

MEDIATEK INCORPORATION**NOTES TO FINANCIAL STATEMENTS – (continued)****(5) Presentation of derivative financial instruments**

Forward exchange contracts receivable and payable are reported under current assets or liability on a net basis. As of December 31, 2003, details were as follows:

In thousand NTD

Forward contract receivable	\$3,574,425
Forward contract payable	(3,567,690)
Discount	1,518
Forward exchange contracts receivable (payable)-net	<u>\$8,253</u>

Foreign exchange gain (loss) incurred from the derivatives for the years ended December 31, 2003 and 2002 amounted to NT\$13,399 thousand and NT\$(20,447) thousand, respectively.

(6) Outstanding forward exchange contract

As of December 31, 2003, the Company's outstanding forward exchange contract amounted to US\$85,000 thousand. The maturity of the contract was June 4, 2004. Under the contract, the Company may exercise US\$5,000 thousand per week. When settlement rate is lower than the contract rate, the amount that the Company can hedge is capped at the loss incurred from US\$4,000 thousand of the underlying assets or NT\$600 thousand.

(7) Disclosures of risks for investments in credit-linked notes and structured deposits**a. Contract amount (*In thousand USD*)**

<u>Underlying investments</u>	<u>As of December 31, 2003</u>
POU CHEN Credit-linked deposit	\$4,000

b. Credit Risk

Default by the issuers of underlying securities may reduce the value of credit-linked deposits to zero. The Company minimizes the credit risk by selecting counter parties who are reputable and in good financial standing.

c. Liquidity Risk

The Company is unable to have the credit-linked investments redeemed or called before maturity, which being the liquidity risk. In minimizing such risk, the Company only invests in securities whose maturities are within a year.

MEDIATEK INCORPORATION**NOTES TO FINANCIAL STATEMENTS – (continued)**

d. Market Risk

There is no market risk for the underlying investment except for the fluctuations in the exchange rate of US Dollar to NT Dollar.

e. Cash Flow Risk

No cash flow risk is involved as the entire payments of credit-liked investments were already made.

(8) Fair value of financial instruments

<i>In thousand NTD</i>	As of December 31,			
	2002		2001	
	Carrying value	Fair value	Carrying value	Fair value
<u>Non-derivative</u>				
<u>Assets</u>				
Cash, cash equivalents and restricted deposits	\$21,686,494	\$21,686,494	\$13,019,321	\$13,019,321
Short-term investments	1,086,918	1,090,015	3,826,000	3,883,702
Receivables	3,706,372	3,706,372	3,791,102	3,791,102
Long-term investments-with no market value	11,459,763	-	6,496,617	-
<u>Liabilities</u>				
Payables	4,181,361	4,181,361	3,385,437	3,385,437
Income taxes payable	312,827	312,827	436,058	436,058
Long-term debts-including current portion	28,182	28,182	44,371	44,371
<u>Derivatives</u>				
Forward exchange contracts	8,253	7262	4,028	2,533
Options	-	-	-	(9,973)
Swaps	-	-	705	705

The methods and assumptions used to estimate the fair value of derivative financial instruments are as follows:

- a. The fair value of the Company's short-term financial instruments is based on the carrying value of those instruments at reporting date due to the short maturity of those instruments. The method is applied to cash and cash equivalents, restricted deposits, receivables, payables and income taxes payable.

MEDIATEK INCORPORATION

NOTES TO FINANCIAL STATEMENTS – (continued)

- b. The fair value of the Company's marketable securities is based on market prices at reporting date if market prices are available. The fair value of the Company's long-term investments is not applicable.
- c. The fair value of long-term debts is based on the market prices at the reporting date if the market prices are available or estimated using the discounted cash flow method based on the Company's borrowing rates for similar types of borrowings.
- d. The fair value of derivative financial instruments, normally including unrealized gains or losses from outstanding forward exchange contracts, is the amount that the Company is entitled to receive or obligated to pay, assuming the Company terminated contracts at reporting date.