

**Cathay Financial Holding Co., Ltd.**  
**Financial statements**  
**Together with**  
**Independent auditors' report**  
**December 31, 2004 and 2005**

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**English Translation of Report Originally Issued in Chinese**  
**Independent auditors' report**

To: Board of Directors  
Cathay Financial Holding Co., Ltd.

We have audited the accompanying balance sheets of Cathay Financial Holding Co., Ltd. (the "Company") as of December 31, 2004 and 2005 and the related statements of income, changes in stockholders' equity and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2004 and 2005 and the results of its operations and its cash flows for the years ended December 31, 2004 and 2005 in conformity with generally accepted accounting principles in the Republic of China, "Guidelines Governing the Preparation of Financial Reports by Securities Issuers" and "Regulations Governing the Preparation of Financial Reports by Financial Holding Companies."

Diwan, Ernst & Young  
Taipei, Taiwan  
The Republic of China  
January 27, 2006

**Notice to Readers**

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

**English Translation of Financial Statements Originally Issued in Chinese**

**Cathay Financial Holding Co., Ltd.**

**Balance sheets**

**December 31, 2004 and 2005**

**(Expressed in thousands of dollars)**

	Notes	2004		2005	
		NT \$	US \$	NT \$	US \$
<b>Assets</b>					
<b>Current assets</b>					
Cash and cash equivalents	2,4	\$20,472,483	\$645,006	\$10,448,439	\$318,550
Tax refund receivable		589,326	18,567	589,326	17,967
Interest receivable		293	9	45,557	1,389
Other receivable		584,594	18,418	2,369,120	72,229
Deferred income tax assets-current	2,12	149,698	4,717	6,368	194
Subtotal		21,796,394	686,717	13,458,810	410,329
<b>Long-term investments</b>					
Long-term investments in stocks	2,5				
Long-term investments under equity method		178,515,166	5,624,296	188,168,647	5,736,849
Long-term investments under cost method		100,000	3,151	100,000	3,049
Allowance for valuation loss on long-term investments in stocks		(110,435)	(3,479)	(68,263)	(2,081)
Subtotal		178,504,731	5,623,968	188,200,384	5,737,817
<b>Property and equipment</b>					
Transportation and communication equipment	2	3,199	101	2,550	78
Other equipment		3,880	122	4,787	146
Subtotal		7,079	223	7,337	224
Less: Accumulated depreciation		(2,258)	(71)	(2,362)	(72)
Net		4,821	152	4,975	152
<b>Other assets</b>					
Refundable deposits		-	-	2,628,000	80,122
Temporary payments and suspense accounts		1	-	21	1
Deferred income tax assets -noncurrent	2,12	-	-	194,674	5,935
Deferred charges	2	66,627	2,099	119	3
Subtotal		66,628	2,099	2,822,814	86,061
<b>Total assets</b>		<b>\$200,372,574</b>	<b>\$6,312,936</b>	<b>\$204,486,983</b>	<b>\$6,234,359</b>
<b>Liabilities &amp; stockholders' equity</b>					
<b>Current liabilities</b>					
Collections for others		\$761	\$24	\$1,151	\$35
Accrued expenses		53,546	1,687	124,268	3,789
Income taxes payable		145,714	4,591	462,698	14,106
Dividends payable		2,316	73	5,114	156
Other payable		987,900	31,125	2,746,963	83,749
Subtotal		1,190,237	37,500	3,340,194	101,835
<b>Long-term liabilities</b>					
Bonds payable	2,6,19	23,774,560	749,041	13,405,171	408,694
Accrued pension liabilities	19	8,037	253	10,965	335
Subtotal		23,782,597	749,294	13,416,136	409,029
<b>Other liabilities</b>					
Deferred income tax liabilities -noncurrent		49,794	1,569	-	-
Temporary receipts and suspense accounts		709	22	15	-
Subtotal		50,503	1,591	15	-
<b>Total liabilities</b>		<b>25,023,337</b>	<b>788,385</b>	<b>16,756,345</b>	<b>510,864</b>
<b>Stockholders' equity</b>					
Capital stock					
Common stock	7	83,167,130	2,620,262	85,242,234	2,598,849
Capital surplus	8				
Additional paid-in capital		53,524,308	1,686,336	62,592,220	1,908,299
Treasury stock transactions		5,424,265	170,897	5,491,169	167,414
Others		10,124	319	11,696	357
Retained earnings	9				
Legal reserve		3,026,715	95,360	6,009,431	183,214
Special reserve		122,653	3,864	226,579	6,908
Unappropriated retained earnings		30,640,997	965,375	28,146,255	858,117
Equity adjustments					
Unrealized valuation losses on long-term equity investments		(110,435)	(3,479)	(68,263)	(2,081)
Cumulative conversion adjustments		(96,005)	(3,025)	81,154	2,474
Net loss not yet recognized as net pension cost		(5,560)	(175)	(1,837)	(56)
Treasury stock	2,10	(354,955)	(11,183)	-	-
<b>Total stockholders' equity</b>		<b>175,349,237</b>	<b>5,524,551</b>	<b>187,730,638</b>	<b>5,723,495</b>
<b>Total liabilities and stockholders' equity</b>		<b>\$200,372,574</b>	<b>\$6,312,936</b>	<b>\$204,486,983</b>	<b>\$6,234,359</b>

(The exchange rates provided by the Federal Reserve Bank of New York on December 31, 2004 and 2005 were NT\$31.74 and NT\$32.80 to US\$1.00)

**The accompanying notes are an integral part of these financial statements.**

**English Translation of Financial Statements Originally Issued in Chinese**

**Cathay Financial Holding Co., Ltd.**

**Statements of income**

**For the years ended December 31, 2004 and 2005**

**(Expressed in thousands of dollars, except earning per share)**

	Notes	2004		2005	
		NT \$	US \$	NT \$	US \$
<b>Operating revenues</b>	2				
Interest income		\$194,076	\$6,115	\$940,097	\$28,661
Income from long-term equity investments	2,5	29,689,400	935,394	22,277,613	679,196
Other operating income		71,070	2,239	-	-
Subtotal		29,954,546	943,748	23,217,710	707,857
<b>Operating costs</b>	2				
Interest expenses		(723,072)	(22,781)	(1,227,327)	(37,419)
Provision for securities trading losses		(41,783)	(1,317)	-	-
Subtotal		(764,855)	(24,098)	(1,227,327)	(37,419)
<b>Operating gross profit</b>		29,189,691	919,650	21,990,383	670,438
<b>Operating expenses</b>					
Administrative and general expenses		(382,621)	(12,055)	(334,713)	(10,205)
<b>Operating income</b>		28,807,070	907,595	21,655,670	660,233
<b>Non-operating income</b>					
Gain on foreign exchange		956,637	30,140	300,815	9,171
Miscellaneous income		121,846	3,839	9,541	291
Subtotal		1,078,483	33,979	310,356	9,462
<b>Non-operating expenses</b>					
Loss on disposal of property and equipment		-	-	(473)	(14)
Subtotal		-	-	(473)	(14)
<b>Income from continuing operations before income taxes</b>		29,885,553	941,574	21,965,553	669,681
<b>Income taxes expense</b>	2,12	(58,398)	(1,840)	(178,500)	(5,442)
<b>Net income</b>		\$29,827,155	\$939,734	\$21,787,053	\$664,239
<b>Earnings per share (expressed in dollars)</b>					
Primary earnings per share:	13				
Income from continuing operations before income taxes		\$3.71	\$0.12	\$2.60	\$0.08
Net income		\$3.70	\$0.12	\$2.57	\$0.08
Fully-diluted earnings per share:					
Income from continuing operations before income taxes		\$3.60	\$0.11	\$2.57	\$0.08
Net income		\$3.57	\$0.11	\$2.54	\$0.08
<b>Pro-forma information as if subsidiaries' investment in the Company were not treated as treasury stock:</b>					
Income from continuing operations before income taxes		\$30,041,879	\$946,499	\$21,962,594	\$669,591
Net income		\$29,983,481	\$944,659	\$21,784,094	\$664,149
<b>Earnings per share (expressed in dollars)</b>					
Primary earnings per share:					
Income from continuing operations before income taxes		\$3.72	\$0.12	\$2.59	\$0.08
Net income		\$3.71	\$0.12	\$2.57	\$0.08
Fully-diluted earnings per share:					
Income from continuing operations before income taxes		\$3.61	\$0.11	\$2.57	\$0.08
Net income		\$3.58	\$0.11	\$2.53	\$0.08

(The exchange rates provided by the Federal Reserve Bank of New York on December 31, 2004 and 2005 were NT\$31.74 and NT\$32.80 to US\$1.00)

**The accompanying notes are an integral part of these financial statements.**

English Translation of Financial Statements Originally Issued in Chinese

**Cathay Financial Holding Co., Ltd.**  
**Statements of changes in stockholders' equity**  
**For the years ended December 31, 2004 and 2005**  
**(Expressed in thousands of dollars)**

Summary	Common stock				Capital surplus				Retained earnings				Equity adjustments				Total			
	Common stock		Capital surplus		Legal reserve		Special reserve		Unappropriated retained earnings		Unrealized valuation losses on long-term equity investments		Cumulative conversion adjustments		Net loss not yet recognized as net pension cost		Treasury stock		Total	
	NT \$	US \$	NT \$	US \$	NT \$	US \$	NT \$	US \$	NT \$	US \$	NT \$	US \$	NT \$	US \$	NT \$	US \$	NT \$	US \$	NT \$	US \$
<b>Balance on January 1, 2004</b>	\$83,074,891	\$2,617,356	\$53,651,046	\$1,690,329	\$1,335,046	\$42,062	\$1,833,255	\$57,759	\$16,916,694	\$532,977	\$(136,202)	\$(4,291)	\$176,537	\$5,562	\$(1,971)	\$(62)	\$(15,039,516)	\$(473,835)	\$141,809,780	\$4,467,857
Appropriations and distributions for 2003																				
Legal reserve					1,691,669	53,298			(1,691,669)	(53,298)									-	-
Special reserve							(1,710,602)	(53,895)	1,710,602	53,895									-	-
Cash dividends									(16,105,155)	(507,409)									(16,105,155)	(507,409)
Remuneration paid to directors and supervisors									(5,700)	(179)									(5,700)	(179)
Bonus paid to employees									(1,611)	(51)									(1,611)	(51)
Convertible notes converted into common stock	92,239	2,906	422,591	13,314															514,830	16,220
Cash dividends to subsidiaries			22,194	699															22,194	699
Capital surplus			10,124	319															10,124	319
Cumulative conversion adjustments													(272,542)	(8,587)					(272,542)	(8,587)
Gains on unrealized loss recoveries of long-term equity investments											25,767	812							25,767	812
Disposal of treasury stock			4,737,927	149,273													11,450,763	360,768	16,188,690	510,041
Treasury stock			114,815	3,618					(9,319)	(294)							3,233,798	101,884	3,339,294	105,208
Net income for the year ended December 31, 2004									29,827,155	939,734									29,827,155	939,734
Net loss not yet recognized as net pension cost															(3,589)	(113)			(3,589)	(113)
<b>Balance on December 31, 2004</b>	<b>\$83,167,130</b>	<b>\$2,620,262</b>	<b>\$58,958,697</b>	<b>\$1,857,552</b>	<b>\$3,026,715</b>	<b>\$95,360</b>	<b>\$122,653</b>	<b>\$3,864</b>	<b>\$30,640,997</b>	<b>\$965,375</b>	<b>\$(110,435)</b>	<b>\$(3,479)</b>	<b>\$(96,005)</b>	<b>\$(3,025)</b>	<b>\$(5,560)</b>	<b>\$(175)</b>	<b>\$(354,955)</b>	<b>\$(11,183)</b>	<b>\$175,349,237</b>	<b>\$5,524,551</b>
<b>Balance on January 1, 2005</b>	<b>\$83,167,130</b>	<b>\$2,535,583</b>	<b>\$58,958,697</b>	<b>\$1,797,521</b>	<b>\$3,026,715</b>	<b>\$92,278</b>	<b>\$122,653</b>	<b>\$3,739</b>	<b>\$30,640,997</b>	<b>\$934,177</b>	<b>\$(110,435)</b>	<b>\$(3,367)</b>	<b>\$(96,005)</b>	<b>\$(2,927)</b>	<b>\$(5,560)</b>	<b>\$(170)</b>	<b>\$(354,955)</b>	<b>\$(10,822)</b>	<b>\$175,349,237</b>	<b>\$5,346,012</b>
Appropriations and distributions for 2004																				
Legal reserve					2,982,716	90,936			(2,982,716)	(90,936)									-	-
Special reserve							103,926	3,169	(103,926)	(3,169)									-	-
Cash dividends									(21,187,334)	(645,955)									(21,187,334)	(645,955)
Remuneration paid to directors and supervisors									(5,700)	(174)									(5,700)	(174)
Bonus paid to employees									(2,119)	(65)									(2,119)	(65)
Convertible notes converted into common stock	2,075,104	63,266	9,067,913	276,461															11,143,017	339,727
Cash dividends to subsidiaries			8,749	267															8,749	267
Capital surplus			1,572	48															1,572	48
Cumulative conversion adjustments													177,159	5,401					177,159	5,401
Gains on unrealized loss recoveries of long-term equity investments											42,172	1,286							42,172	1,286
Treasury stock			58,154	1,773													354,955	10,822	413,109	12,595
Net income for the year ended December 31, 2005									21,787,053	664,239									21,787,053	664,239
Net loss not yet recognized as net pension cost															3,723	114			3,723	114
<b>Balance on December 31, 2005</b>	<b>\$85,242,234</b>	<b>\$2,598,849</b>	<b>\$68,095,085</b>	<b>\$2,076,070</b>	<b>\$6,009,431</b>	<b>\$183,214</b>	<b>\$226,579</b>	<b>\$6,908</b>	<b>\$28,146,255</b>	<b>\$858,117</b>	<b>\$(68,263)</b>	<b>\$(2,081)</b>	<b>\$81,154</b>	<b>\$2,474</b>	<b>\$(1,837)</b>	<b>\$(56)</b>	<b>\$-</b>	<b>\$-</b>	<b>\$187,730,638</b>	<b>\$5,723,495</b>

(The exchange rates provided by the Federal Reserve Bank of New York on December 31, 2004 and 2005 were NTS31.74 and NTS32.80 to US\$1.00)

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

**English Translation of Financial Statements Originally Issued in Chinese**

**Cathay Financial Holding Co., Ltd.**  
**Statements of cash flows**  
**For the years ended December 31, 2004 and 2005**  
**(Expressed in thousands of dollars)**

	2004		2005	
	NT \$	US \$	NT \$	US \$
<b>Cash flows from operating activities</b>				
Net income	\$29,827,155	\$939,734	\$21,787,053	\$664,239
Adjustments:				
Amortizations	146,688	4,622	59,248	1,806
Depreciation	1,055	33	1,180	36
Losses on disposal of property and equipment	-	-	473	15
Investment income recognized by equity method excess of cash dividends received	(13,212,631)	(416,277)	(4,308,166)	(131,347)
Increase in bonds payable redemption premium	716,399	22,571	569,524	17,364
Effects of exchange rate changes	571,275	17,999	(595,759)	(18,163)
Decrease in short-term investments	2,147,421	67,657	-	-
Decrease in tax refund receivable	42,621	1,343	-	-
Decrease (increase) in interest receivable	42,449	1,337	(45,264)	(1,380)
Increase in other accounts receivable	(526,142)	(16,577)	(1,784,526)	(54,406)
(Increase) decrease in deferred income tax assets-current	(127,862)	(4,028)	143,330	4,370
Decrease (increase) in deferred income tax assets-noncurrent	171,822	5,413	(194,674)	(5,935)
Decrease (Increase) in temporary payments and suspense accounts	166	5	(20)	(1)
(Decrease) increase in collections for others	(135)	(4)	391	12
Increase in accrued expenses	16,918	533	70,722	2,156
Increase in income taxes payable	145,714	4,591	316,983	9,664
Increase in dividends payable	840	26	2,799	85
Increase in other accounts payable	291,901	9,197	1,759,063	53,630
Increase in accrued pension liabilities	872	27	6,650	203
Increase (decrease) in temporary receipts and suspense accounts	14	-	(693)	(21)
Increase (decrease) in deferred income tax liabilities-noncurrent	49,794	1,569	(49,794)	(1,518)
<b>Net cash provided by operating activities</b>	<b>20,306,334</b>	<b>639,771</b>	<b>17,738,520</b>	<b>540,809</b>
<b>Cash flows from investing activities</b>				
Acquisition of long-term investments in stocks	(4,116,560)	(129,696)	(4,744,726)	(144,656)
Disposal of property and equipment	-	-	950	29
Acquisition of property and equipment	(1,207)	(38)	(2,757)	(84)
Decrease in deferred charges	18,267	576	7,259	221
Increase in refundable deposits	-	-	(2,628,000)	(80,122)
<b>Net cash used in investing activities</b>	<b>(4,099,500)</b>	<b>(129,158)</b>	<b>(7,367,274)</b>	<b>(224,612)</b>
<b>Cash flows from financing activities</b>				
(Decrease) increase in bonds payable	(1,562,099)	(49,216)	204,104	6,223
Remuneration paid to directors and supervisors	(5,700)	(179)	(5,700)	(174)
Bonus paid to employees	(1,611)	(51)	(2,119)	(65)
Cash dividends	(16,105,155)	(507,409)	(21,187,334)	(645,955)
Disposal of treasury stock	16,188,690	510,041	-	-
<b>Net cash used in financing activities</b>	<b>(1,485,875)</b>	<b>(46,814)</b>	<b>(20,991,049)</b>	<b>(639,971)</b>
<b>Effects of exchange rate changes</b>	<b>(571,275)</b>	<b>(17,999)</b>	<b>595,759</b>	<b>18,163</b>
<b>Increase (decrease) in cash and cash equivalents</b>	<b>14,149,684</b>	<b>445,800</b>	<b>(10,024,044)</b>	<b>(305,611)</b>
<b>Cash and cash equivalents at the beginning of year</b>	<b>6,322,799</b>	<b>199,206</b>	<b>20,472,483</b>	<b>624,161</b>
<b>Cash and cash equivalents at the end of year</b>	<b>\$20,472,483</b>	<b>\$645,006</b>	<b>\$10,448,439</b>	<b>\$318,550</b>
<b>Supplemental disclosure of cash flows information</b>				
Interest paid during the period	\$971	\$31	\$594,782	\$18,134
Interest paid (excluding capitalized interest)	\$971	\$31	\$594,782	\$18,134
Income tax paid	\$5,054	\$159	\$28,399	\$866
<b>Investing and financing activities with no cash flow effects</b>				
Conversion of convertible notes into common stock	\$514,830	\$16,220	\$11,143,017	\$339,726

(The exchange rates provided by the Federal Reserve Bank of New York on December 31, 2004 and 2005 were NT\$31.74 and NT\$32.80 to US\$1.00)

**The accompanying notes are an integral part of these financial statements.**

**English Translation of Financial Statements Originally Issued in Chinese**

**Cathay Financial Holding Co., Ltd.**

**Notes to financial statements**

**(Expressed in thousands of dollars**

**except for share and per share data and unless otherwise stated)**

**December 31, 2004 and 2005**

The reader is advised that these financial statements have been prepared originally in Chinese. These financial statements do not include additional disclosure information that is required for Chinese-language reports under the Regulations Governing the Preparation of Financial Reports by Financial Holding Companies. If there is any conflict between these financial statements and the Chinese version or any difference in the interpretation of the two versions, the Chinese language financial statements shall prevail.

**1. Organization and business scope**

On December 31, 2001 Cathay Life Insurance Co., Ltd. (“Cathay Life”) was reincorporated as Cathay Financial Holding Co., Ltd. (the “Company”) through stock conversion pursuant to provisions of the Republic of China (“ROC”) Financial Holding Company Act (“Financial Holding Company Act”) and its shares were listed on the Taiwan Stock Exchange Corporation (TSE) on the same day. On April 22, 2002, Cathay Century Insurance Co., Ltd. (“Cathay Century”) and Cathay United Bank Co., Ltd. (“Cathay United Bank”) were merged into the Company through stock conversion. On December 18, 2002, United World Chinese Commercial Bank Co., Ltd. (“UWCCB”) became a subsidiary of the Company by stock conversion. UWCCB and Cathay United Bank merged on October 27, 2003. UWCCB was the surviving company, and the merged bank was re-named Cathay United Bank Co., Ltd. (“Cathay United Bank (merged)”). On May 12, 2004 the Company build-up a wholly owned subsidiary of Cathay Securities Corporation (“Cathay Securities”). On June 30, 2005, an investment strategy of Lucky Bank, Inc. (“Lucky Bank”) was approved by the Financial Supervisory Commission, Executive Yuan. As of December 31, 2005 the Company had acquired its ownership interest of 81.35%. Since July 29, 2003, the Company listed a portion of its common shares on the Luxembourg Stock Exchange (LSE) in the form of Global Depositary Shares (GDSs). The Company mainly engages in financial holding business activities.

As of December 31, 2004 and 2005, the total numbers of employees were 59 and 64, respectively.



## **2. Summary of significant accounting policies**

We prepared the financial statement in accordance with generally accepted accounting principles, “Guidelines Governing the Preparation of Financial Reports by Securities Issuers” and “Regulations Governing the Preparation of Financial statements of Financial Holding Companies”. The summary of significant accounting policies is as follows:

### *(1) Distinguish assets and liabilities, current and non-current*

Current assets are assets that can be liquidated or disposed of within one year. Assets that do not belong to current assets are called non-current assets. Current liabilities are debts which must be paid-off within one year. Debts, which do not belong to current liabilities, are called non-current liabilities.

### *(2) Cash and cash equivalents*

Cash and cash equivalents includes cash on hand, unrestricted bank deposits and all highly liquid investments with a maturity of less than three months.

### *(3) Long - term investments*

#### **A. Long-term investments in stocks**

Long-term investments in listed companies in which the Company’s ownership interest is less than 20% of the voting stock, and which the Company lacks significant influence over operating and financial policies of the investee, are stated at the lower of cost or market value. Unrealized loss thereon is reflected as a reduction of shareholders’ equity. Long-term investments in unlisted companies, in which the Company’s ownership interest accounted for less than 20% of the common stock, are stated at cost. However, when there is evidence showing that a decline in market value of such investment is not temporary and is already less than cost, the market value becomes the new cost basis and the difference is accounted for as if it were a realized loss, and included in the determination of net income. Stock dividends are not recognized as investment income but are recorded as an increase in the number of shares held. Upon sales of long-term equity investments (accounted for under the cost method), any difference between the weighted-average cost and sales price is used to compute the resulting gain or loss.

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Investments in equity securities are accounted for under the equity method where the Company's ownership interest is 20% or more of the voting shares and the Company have significant influence.

If the investee company issues new shares and original shareholders do not purchase or acquire new shares proportionately, then the investment percentage and the equity in net assets for the investment that the investor company has invested will be changed. Such difference shall be used to adjust the additional paid-in capital and the long-term investment under the equity method accounts.

If the adjustment stated above is to debit the additional paid-in capital account and the book balance of additional paid-in capital from long-term investments is not enough to be offset, the difference shall be debited to the retained earnings account.

The cost of the disposal of an investment is determined by the weighted-average method.

### **B. Transactions with affiliated companies**

Unrealized intercompany gains or losses are eliminated under the equity method. Gains or losses from sales of depreciable assets between the Company and its subsidiaries are amortized to income over the economic service life of the asset. Gains or losses from other types of intercompany transactions are recognized when realized.

#### *(4) Property and equipment*

Property and equipment are stated at cost or cost plus appreciation. Major improvements, additions, and renewals are capitalized, while repairs and maintenance are expensed when incurred.

Upon the sale or disposal of properties and equipment, their cost, related accumulated depreciation and accumulated impairment are removed from the respective accounts. Gain or loss resulting from such sale or disposal is accounted for as non-operating gain or loss.

Depreciation is calculated using the straight-line method over the estimated service

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lives prescribed by the “Estimated Useful Life of Fixed Assets Table” published by the Executive Yuan of the ROC. Property and equipment that are still in use after their useful lives are depreciated based on the residual value and the newly estimated remaining useful lives.

### *(5) Deferred charges*

Deferred charges are expenses where the associated economic benefit extends more than one year. Deferred charges are amortized over the economic useful life by the straight-line method.

### *(6) Impairment of assets*

Pursuant to SFAS No. 35, the Company assesses indicators for impairment for all its assets within the scope of SFAS No. 35 on each balance sheet date. If impairment indicators exist, the Company shall then compare the carrying amount with the recoverable amount of the assets or the cash-generating unit (“CGU”) and write down the carrying amount to the recoverable amount where applicable. Recoverable amount is defined as the higher of fair values less costs to sell and the values in use.

For previously recognized losses, the Company shall assess, at each balance sheet date, whether there is any indication that the impairment loss may no longer exist or may have decreased. If there is any such indication, the Company has to recalculate the recoverable amount of the asset. If the recoverable amount increases as a result of the increase in the estimated service potential of the assets, the Company shall reverse the impairment loss to the extent that the carrying amount after the reversal would not exceed the carrying amount that would have been determined (net of amortization or depreciation) had no impairment loss been recognized for the assets in prior years.

In addition, a goodwill-allocated CGU or group of CGUs is tested for impairment annually, or more frequently if events or changes in circumstance indicate goodwill impairment. Any impairment loss is recognized to reduce the carrying amount of the assets of the CGU or the group of CGUs in the following order:

- A. first, to reduce the carrying amount of any goodwill allocated to the CGU or group of CGUs; and
- B. if the goodwill has been written off, to reduce the other assets of the CGU or group of CGUs pro rata to their carrying amount.

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Thus, reversal of impairment loss on goodwill is prohibited.

Impairment loss (reversal) is classified as non-operating losses/ (income).

### *(7) Convertible notes*

The excess of the redemption price over the par value of a convertible notes are credited to redemption premium payable and amortized using the interest method. This amortization is recorded as interest expense.

The book value approach is used when the conversion privilege of a convertible bond is exercised. In addition, the accounts of convertible notes and reserve amount for bonds redemption are transferred to the accounts of capital stock and capital surplus accordingly. No gain or loss is recognized upon conversion.

### *(8) Foreign currency transactions*

Foreign currency transactions are recorded in NT dollars at the spot rate when the conversion occurs. Gains or losses resulting from adjustments or settlements of foreign currency assets and liabilities are credited or charged to income in the period of actual conversion or settlement. Long-term investment in foreign currency is accounted for as cumulative conversion adjustments and is treated as adjustments of stockholders' equity. Assets and liabilities denominated in foreign currencies are restated at the balance sheet date exchange rates, and resulting gains or losses are credited or charged to current income.

### *(9) Derivative financial instruments*

Interest rate swap ("IRS") transactions may involve the exchange of fixed-rate interest payment for the market floating-rate interest payment obligation based on a notional principal amount. For IRS transactions undertaken for hedging purposes, income and expenses arising upon settlement are netted off and recognized in the statement of income and expenditure.

For cross-currency swap contracts undertaken for non-trading purposes, amounts to be exchanged on settlement dates are recorded at the contracted forward rate. The

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interest, which may involve the exchange of fixed-rate interest payments for floating-rate interest payments based on a notional principal amount, on each settlement date, is recorded as gain or loss.

For option contracts, only memo entries of notional principal amounts are made on the contract date. Premiums paid or received are recorded as assets or liabilities. As of the balance sheet date, outstanding option contracts are marked-to-market and the gains and losses are recognized in the current statement of income. Gains or losses on the exercise of options are recognized in the current period.

### *(10) Income taxes*

The Company adopted SFAS No. 22, “Accounting for Income Taxes”, which requires inter-period and intra-period tax allocations in addition to computing current period income tax payable. Furthermore, it requires recognition of temporary differences between deferred income tax liabilities, deferred income tax assets, prior year’s loss carry forwards and investment tax credits. An allowance is provided under assessment of the realizability of deferred tax asset. Adjustments of prior years’ income tax payable are included in current income tax expense.

In accordance with Article 49 of the Financial Holding Company Act, the Company and its subsidiaries adopt the linked-tax system for tax filings and pay a 10% surcharge on their undistributed retained earnings under the consolidated income tax return. If there are any tax effects due to the adoption of the linked-tax system, the Company can proportionately allocate the effects on tax expense (benefit), deferred income tax and tax payable (tax refund receivable) among the Company and its subsidiaries.

Deferred income tax assets or liabilities are classified as current or non-current on the basis of the classification of the related assets or liabilities for financial reporting. A deferred income tax asset or liability not related to an asset or liability for financial reporting is classified based on the expected realization date of the temporary difference.

The additional 10% income tax imposed on the undistributed earnings is recognized as an expense on the date of the earnings distribution resolution of the stockholders’ meeting.

*(11) Capital expenditure expenses*

Capital expenditure is capitalized and amortized over its useful life if the amount is significant and may generate revenues in future periods. Otherwise, it is expensed in the year as incurred.

*(12) Treasury stock*

The stock that the Company repurchases is recorded in the “treasury stock account”. The book value of the treasury stock is determined based on the reason of purchase and stock type (common or preferred stock) using the weighted average method. When treasury stock is retired, capital surplus-premium of common shares and common stock are debited according to the ratio of retired treasury stock to total issued stock. When the book value of the retired treasury stock is higher than the sum of its par value and capital surplus-premium of common shares, the difference is debited to other capital surplus. If other capital surplus is insufficient to cover the difference, retained earnings are debited. When the book value of the retired treasury stock is lower than the sum of its par value and capital surplus-premium of common shares, the difference is credited to capital surplus-treasury stock.

According to the Ministry of Finance-Securities and Futures Commission (91) article 108164:

In accordance with Article 38 of the Financial Holding Company Act which provides strict prohibitions on cross-holdings, all the prior share buybacks conducted by listed or over-the-counter traded financial institutions (in accordance with Article 28-2 of Securities and Exchange Law), upon the conversion of such institutions into wholly-owned subsidiaries of a financial holding company, must be converted into treasury shares of the financial holding company to be held by such subsidiaries for a period of no more than three years. If such subsidiaries fail to dispose such treasury shares within this period, those shares will be deemed as un-issued share capital of the financial holding company and shall be cancelled accordingly. Treasury shares of a financial holding company held by its subsidiaries as described above are also treated as their own treasury shares and therefore such subsidiaries may not exercise shareholders rights with respect to those stocks in accordance with Article 28-2 of the Securities and Exchange Law.

According to the Securities and Futures Commission (91) article 111467, shares

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previously bought back by listed or over-the-counter traded financial institutions (in accordance with Article 28-2 of Securities and Exchange Law), upon conversion of the institutions into wholly-owned subsidiaries of a financial holding company and the conversion of such shares into treasury shares of the financial holding company, must be treated by such subsidiaries as their own treasury shares and a deduction of shareholders' equity and must be treated as treasury shares of the financial holding company. If the financial institutions hold shares of other financial institutions whose shares are also converted into the shares of the same financial holding company, the principle of equity investment shall apply. The Company follows SFAS NO.30 "Treasury Stock Accounting Principle" and treats shares held by its subsidiaries as treasury stock in its income statements.

### *(13) Pension plan*

The Company has established a pension plan for all employees. Pension plan benefits are based primarily on participants' compensation and the number of years of credited service.

The Labor Pension Act of ROC ("the Act"), which adopts a defined contribution scheme, takes effect from July 1, 2005. In accordance with the Act, employees of the Company may elect to be subject to either the Act, and maintain their seniority before the enforcement of the Act, or the pension mechanism of the Labor Standards Law. For employees subject to the Act, the Company shall make monthly contributions to the employees' individual pension accounts on a basis no less than 6% of the employees' monthly wages.

In compliance with SFC regulations, the Company and its subsidiaries follow the ROC SFAS No. 18, "Accounting for Pensions". When providing defined benefit plans, an actuarial valuation of pension liability is performed on the balance sheet date, and a minimum pension liability is recorded in the financial statements based on the difference between the accumulated benefit obligation and the fair value of plan assets; when providing defined contribution plans, an enterprise should recognize the amounts to be contributed as current expense for the employee's employment period.

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### (14) Conversion to U.S. dollars

The financial statements are stated in NT dollars. The converted U.S. dollars amounts from NT dollars as of December 31, 2004 and 2005 are for information only. The U.S. dollar/NT dollars noon buying rates of NT\$31.74 and NT\$32.80 provided by Federal Reserve Bank of New York of December 31, 2004 and 2005 are used for the conversion.

### 3. Accounting changes: None

### 4. Cash and cash equivalents

	December 31,			
	2004(NT\$)	2004(US\$)	2005(NT\$)	2005(US\$)
Petty cash	\$60	\$2	\$60	\$2
Cash in banks	15,707,437	494,878	5,557,619	169,439
Time deposits	2,673,595	84,234	4,376,042	133,416
Cash equivalents	2,091,391	65,892	514,718	15,693
Total	\$20,472,483	\$645,006	\$10,448,439	\$318,550

### 5. Long-term investments in stocks

Name of investee	December 31,			
	2004(NT\$)	2004(US\$)	2005(NT\$)	2005(US\$)
Under the equity method:				
Cathay Life	\$90,571,820	\$2,853,555	\$97,592,064	\$2,975,368
Cathay United Bank (merged)	80,149,348	2,525,184	77,928,075	2,375,856
Cathay Century	2,966,117	93,450	3,194,216	97,385
Cathay Securities	3,458,434	108,961	4,015,333	122,419
Cathay Pacific Venture Capital Co., Ltd.	583,715	18,391	568,960	17,346
Cathay Venture Capital Co., Ltd.	69,538	2,191	224,835	6,855
Cathay II Venture Capital Co., Ltd.	586,314	18,472	605,369	18,456
Cathay Capital Management Inc.	19,445	613	40,077	1,222
Lucky Bank	-	-	3,931,455	119,861
Subtotal	178,404,731	5,620,817	188,100,384	5,734,768
Under the cost method:				
Debt Instrument Depository and Clearing				
Co., Ltd. Taiwan	100,000	3,151	100,000	3,049
Total	\$178,504,731	\$5,623,968	\$188,200,384	\$5,737,817



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(1) Changes in long-term investments under the equity method are summarized as follows:

	For the years ended December 31,			
	2004(NT\$)	2004(US\$)	2005(NT\$)	2005(US\$)
Balance on January 1	\$157,950,702	\$4,976,393	\$178,404,731	\$5,439,168
Add: Investment gains under equity method recognized	29,689,400	935,394	22,277,613	679,196
Add: Increment of investment	4,116,560	129,696	4,744,726	144,656
Add: Cash dividends to subsidiaries	22,194	699	8,749	267
Add: Capital surplus under equity method recognized	10,124	319	1,572	48
(Less) add :Cumulative conversion adjustments under equity method recognized	(272,542)	(8,587)	177,159	5,401
Add: Disposal of the Company stocks that the subsidiaries held as investments were treated as treasury stocks	3,339,295	105,208	413,109	12,595
Add: Gains on unrealized value recoveries of long-term equity investments under equity method recognized	25,767	812	42,173	1,286
Less: Cash dividends received	(16,476,769)	(519,117)	(17,969,448)	(547,849)
Balance on December 31	<u>\$178,404,731</u>	<u>\$5,620,817</u>	<u>\$188,100,384</u>	<u>\$5,734,768</u>

(2) The investment gains (losses) account for by the equity method for the years ended December 31, 2004 and 2005 are listed below:

Name of Investee	For the years ended December 31,			
	2004(NT\$)	2004(US\$)	2005(NT\$)	2005(US\$)
Cathay Life	\$15,386,051	\$484,753	\$17,846,968	\$544,115
Cathay United Bank (merged)	13,767,747	433,766	3,831,829	116,824
Cathay Century	587,903	18,522	607,838	18,532
Cathay Securities	(41,566)	(1,309)	56,899	1,735
Cathay Pacific Venture Capital Co., Ltd.	(8,372)	(264)	(15,547)	(474)
Cathay Venture Capital Co., Ltd.	(3,744)	(118)	5,538	169
Cathay II Venture Capital Co., Ltd.	(7,904)	(249)	13,273	405
Cathay Capital Management Inc.	9,285	293	36,131	1,101
Lucky Bank	-	-	(105,316)	(3,211)
Total	<u>\$29,689,400</u>	<u>\$935,394</u>	<u>\$22,277,613</u>	<u>\$679,196</u>

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- A. Combined with the voting rights of its subsidiaries, the Company had significant influence on Cathay Venture Capital Co., Ltd. Thus the investment losses/gains of Cathay Venture Capital Co., Ltd. for the years ended December 31, 2004 and 2005 were recognized under equity method based on the audited financial statements in the-respective period.
- B. The financial statements of Cathay Pacific Venture Capital Co., Ltd. for the years ended December 31, 2004 and 2005 were audited by another auditor and unqualified opinions were expressed by the auditor. The Company recognized the losses on investments in Cathay Pacific Venture Capital Co., Ltd. based on the aforementioned audited reports.
- (3) Effective from January 1, 2005, the Company adopted SFAS No. 7 “Consolidated Financial Statements” which was revised on December 9, 2004. The revised SFAS No. 7 no longer allows excluding subsidiaries which the total assets and operating revenues are less than 10% of the parent company respectively from the consolidated financial statements. In addition, restating prior periods consolidated financial statements is not required in the year of adoption. The consolidated financial statements of the Company as of and for the year ended December 31, 2004 exclude Cathay Pacific Venture Capital Co., Ltd., Cathay II Venture Capital Co., Ltd., Cathay Venture Capital Co., Ltd., Cathay Life Insurance Ltd. (Shanghai), Lin Yuan Property Management Co., Ltd., Symphox Information Co., Ltd., Cathay Futures Corp., Seaward Leasing Ltd., Indovina Bank, Cathay Capital Management Inc. Cathay Bank Life Insurance Agency of Association, Seaward Card Co., Ltd., Cathay Insurance (Bermuda) Co., Ltd., Cathay Securities Investment Co., Ltd., Cathay Pacific Partners Co., Ltd., Cathay Bank Property Agency of Association and China England Co., Ltd. because its total assets and operating revenues were less than 10% of the total assets and operating revenues of the Company. In addition the others subsidiaries were recorded in the consolidated financial statements.
- (4) The consolidated financial statements of the Company as of and for the year ended December 31, 2005 excluded Cathay Capital Management Inc., Cathay Bank Life Insurance Agency of Association, Seaward Card Co., Ltd., Cathay Insurance (Bermuda) Co., Ltd., Cathay Securities Investment Co., Ltd., Cathay Pacific Partners Co., Ltd., Cathay Bank Property Agency of Association and China England Co., Ltd. due to their respective total assets and operating revenues were insignificant to the Company. All other subsidiaries were included in the consolidated financial statements.
- (5) There was no collateralized or pledged long-term investments of the Company as of December 31, 2004 and 2005.

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### 6. Bonds payable

	December 31,			
	2004(NT\$)	2004(US\$)	2005(NT\$)	2005(US\$)
Zero coupon convertible notes	\$21,759,548	\$685,556	\$11,865,321	\$361,747
Redemption premium payable	2,015,012	63,485	1,539,850	46,947
Total	\$23,774,560	\$749,041	\$13,405,171	\$408,694

Please see note 19(3), “Zero coupon convertible notes related information” for details.

### 7. Common stock

As of December 31, 2004 and 2005, the numbers of common with a par value of NT\$10 (US\$0.3) shares issued, were 8,316,713 thousand shares and 8,524,223 thousand shares, respectively.

On December 31, 2001, the Company listed its shares of stock on Taiwan Stock Exchange (TSE) in accordance with relevant regulations. Since July 29, 2003, the Company listed a portion of its common shares on the Luxembourg Stock Exchange in the form of Global Depositary Shares (GDSs).

### 8. Capital surplus

- (1) The capital surplus of the Company consists of premium of stock conversion from consolidation, equity method adjustments from investee companies and transactions of treasury stocks. Capital surplus as of December 31, 2004 and 2005 were NT\$58,958,697 (US\$1,857,552) and NT\$68,095,085 (US\$2,076,070), respectively and both were inclusive of NT\$267,215 (US\$8,147) the undistributed retained earnings of subsidiaries before the stock conversion. Before conversion into a financial holding company, NT\$267,215 (US\$8,147) constituted retained earnings of certain subsidiaries of the Company.
- (2) The additional paid-in capital from the conversion of shares was generated from the conversion of the shares between the subsidiaries and the Company. In compliance with Item 4 of Article 47 of the Financial Holding Company Act, the portion of additional paid-in capital from the share conversion which comes from the original financial institution’s undistributed retained earnings is allowed to be distributed as cash dividends.
- (3) In addition, pursuant to the Company Law, capital surplus can only be used to offset

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the deficit or to increase the share capital. Capital surplus cannot be distributed as cash dividends. Issuance of new stocks funded by capital surplus can be made only once per year. In addition, the amount to be capitalized should not exceed the specific percentage of capital surplus set by the SFC.

### **9. Retained earnings**

#### (1) Legal reserve

Pursuant to the Company Law, 10% of the Company's after-tax net income in the current year must be appropriated as legal reserve until the total amount of the legal reserve equals the issued share capital. This legal reserve can be used to offset deficits but cannot be used for the purpose of cash dividend distributions. However, if the total legal reserve is greater than 50% of the issued share capital, up to 50% of such excess can be capitalized if agreed by its stockholders.

#### (2) Unappropriated retained earnings

- A. According to the Company Law and the Company's articles of incorporation, 10% of the Company's annual earnings, after paying tax and offsetting deductions, if any, shall be appropriated as legal reserve and 0.01%~0.05% for employees' bonus. The remainder must be appropriated in accordance with the resolutions passed at the stockholders' meeting.
- B. The distribution of the 2003 earnings was approved in the shareholders' meeting on June 3, 2004. The distribution resulted from retained earnings of NT\$20,588,763 (US\$648,669) in 2003, amounts from special reserve which were converted into undistributed retained earnings totaling NT\$887,442 (US\$27,960) and the disposition of fixed assets from subsidiaries which amounted to NT\$57,683 (US\$1,817), respectively. The Company declared cash dividends of NT2 dollars (US0.06 dollars) on each common share and such dividends were paid on July 9, 2004.
- C. On June 3, 2005, the stockholders' meeting resolved the appropriation of earnings for the year ended December 31, 2004. The Company declared cash dividends and cash bonus of NT2.5 dollars (US0.08 dollars) per common share and such dividends were paid on July 11, 2005.
- D. Cathay Life originally held 156,927 thousand shares of the Company. After

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conversion into a financial holding company, Cathay Life's treasury stock has been treated as the Company's treasury stock without any stockholder rights. As of December 31, 2005, Cathay Life had transferred all such treasury shares to employees.

- E. The Company is required to pay an extra 10% income tax on all undistributed retained earnings generated during the year.
- F. In accordance with SFC regulations, in addition to the legal reserve retained, the Company is required to provide a special reserve in the amount equal to current year's contra account in shareholders' equity from current year's earnings after tax or prior years' undistributed earnings. However, contra accounts in prior years' accumulated shareholders' equity should only be provided from prior years' undistributed earnings. If a reversal of shareholders equity contra account occurs, the reversed portion of the special reserve could be distributed as dividends.
- G. In accordance with SFC regulations, posterior to 2002 subsidiaries of financial holding companies that hold shares of their parent company should treat those shares as treasury stock as of January 1, 2002. The cost of these shares are exempted from distributing as special reserve.

### H. Dividends policy

The Company's dividends policy is to distribute dividends in stock in order to retain sufficient cash for operations with excess cash from retained earnings distributed in cash, but cash dividends must be a minimum of 10% of the total dividends declared.

- I. In 2005, pursuant to SFC, the information regarding the appropriation of employees, directors and supervisors, and estimate earnings per share will be available on the website of "Market Observation Post System" immediately after the meeting of directors.

In accordance with SFC regulations, the Company should assume that the dividends of year 2004 would be appropriated to the employees, directors and supervisors, and pro forma earnings per share for the current year.

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Name of Investee	For the year ended December 31,	
	2004(NT\$)	2004(US\$)
a. Distributions		
Bonus paid to employees-cash	\$2,119	\$67
Bonus paid to employees-stock	-	-
Remuneration paid to directors and supervisors	5,700	180
b. After income taxes earnings per share:		
(expressed in dollars)	\$3.70	\$0.12
Pro forma earnings per share:		
(expressed in dollars)	\$3.70	\$0.12
Pro forma earnings per share =	$\frac{\text{Net income-Bonus paid to employees-Remuneration paid to directors and supervisors}}{\text{Weighted average outstanding number of shares}}$	

### 10. Treasury stock

(1) The following is a summary of the movement of treasury stock for the year ended December 31, 2005.

(Unit: in thousands of shares)

Reason for acquisition	January 1,			December 31, 2005			Per share Book value (in NT dollars)	Per share Book value (in US dollars)	Per share Market value (in NT dollars)	Per share Market value (in US dollars)
	2005	Increase	Decrease	Book value (NT\$)	Book value (US\$)	Book value (in NT dollars)	Book value (in US dollars)	Market value (in NT dollars)	Market value (in US dollars)	
Shares held by subsidiaries	6,897	-	6,897	-	\$-	\$-	\$-	\$-	\$-	\$-

(2) The following is a summary of the movement of treasury stock for the year ended December 31, 2004.

(Unit: in thousands of shares)

Reason for acquisition	January 1,			December 31, 2004			Per share Book value (in NT dollars)	Per share Book value (in US dollars)	Per share Market value (in NT dollars)	Per share Market value (in US dollars)
	2004	Increase	Decrease	Book value (NT\$)	Book value (US\$)	Book value (in NT dollars)	Book value (in US dollars)	Market value (in NT dollars)	Market value (in US dollars)	
Subsidiaries										
transferred shares to employees	51,551	-	51,551	-	\$-	\$-	\$-	\$-	\$-	\$-
The Company that the subsidiaries held were treated as treasury stock										
	11,705	-	4,808	6,897	354,955	11,183	51.47	1.62	63.00	1.98
Subsidiaries' stocks held by the Company after conversion which are treated as treasury stock										
	254,911	-	254,911	-	-	-	-	-	-	-
Total	318,167	-	311,270	6,897	\$354,955	\$11,183				

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(3) As of December 31, 2004, the Companies' stocks held by subsidiaries are illustrated as follows:

(Unit: in thousands of shares)

Name	Holding share	Amount	Amount	Cause	About retained earnings limit	Legal time limit	Pro forma way
		(NT\$)	(US\$)				determined by the board of directors
							determine
Cathay United Bank (merged)	3,500	\$210,810	\$6,642	Holding other subsidiaries stock by conversion	None	Within three years	None
Cathay Century	3,397	214,007	6,742	"	None	Within three years	None
Total	6,897	\$424,817	\$13,384				

**11. Personnel, depreciation, depletion and amortization expenses**

Item	For the year ended December 31, 2004			For the year ended December 31, 2005		
	(NT\$)			(NT\$)		
	Operating costs	Operating expenses	Total	Operating costs	Operating expenses	Total
Personnel Expenses						
Salary and wages	\$-	\$131,548	\$131,548	\$-	\$161,797	\$161,797
Labor & health Insurance expenses	-	3,008	3,008	-	3,989	3,989
Pension expenses	-	3,687	3,687	-	7,640	7,640
Other expenses	-	1,826	1,826	-	1,460	1,460
Depreciation	-	1,055	1,055	-	1,180	1,180
Depletion	-	-	-	-	-	-
Amortizations	-	146,688	146,688	-	59,248	59,248

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Item	For the year ended December 31,2004 (US\$)			For the year ended December 31,2005 (US\$)		
	Operating costs	Operating expenses	Total	Operating costs	Operating expenses	Total
Personnel Expenses						
Salary and wages	\$-	\$4,145	\$4,145	\$-	\$4,933	\$4,933
Labor & health Insurance expenses	-	95	95	-	122	122
Pension expenses	-	116	116	-	233	233
Other expenses	-	58	58	-	45	45
Depreciation	-	33	33	-	36	36
Depletion	-	-	-	-	-	-
Amortizations	-	4,622	4,622	-	1,806	1,806

**12. Estimated income taxes**

(1) Income tax expenses for the years ended December 31, 2004 and 2005 are estimated as follows:

	For the years ended December 31,			
	2004(NT\$)	2004(US\$)	2005(NT\$)	2005(US\$)
Income before income taxes	\$29,885,553	\$941,574	\$21,965,553	\$669,681
Adjustments:				
Interest income of tax on a separate basis	(19,636)	(619)	(52,289)	(1,594)
Investment gains recognized by equity method	(29,689,400)	(935,394)	(22,277,613)	(679,196)
Unrealized bonds payable redemption premium	716,399	22,571	561,179	17,109
Unrealized exchange (gain) loss	(1,652,397)	(52,060)	304,140	9,273
Realized exchange gain	687,352	21,656	585,200	17,842
Unrealized loss on market price recovery of short-term investment	(71,070)	(2,239)	-	-
Others	(15,067)	(475)	(9,507)	(290)
Taxable income	(158,266)	(4,986)	1,076,663	32,825
Times: Taxes rate	25%-10	25%	25%-10	25%
Subtotal	(39,576)	(1,247)	269,156	8,206
Add: Tax on a separate basis	3,927	124	10,457	319
Deferred income tax expense (benefit)	93,755	2,954	(101,138)	(3,084)
Dissimilitude on estimate tax after time	292	9	25	1
Income taxes expense	\$58,398	\$1,840	\$178,500	\$5,442



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(2) Deferred income tax assets and liabilities are as follows:

	December 31,			
	2004(NT\$)	2004(US\$)	2005(NT\$)	2005(US\$)
A. Total deferred income tax assets	\$658,632	\$20,751	\$395,185	\$12,048
B. Total deferred income tax liabilities	\$558,728	\$17,603	\$194,143	\$5,919
	December 31,			
	2004(NT\$)	2004(US\$)	2005(NT\$)	2005(US\$)
C. Temporary differences from resulting deferred tax assets or liabilities:				
a. Deductible temporary difference from unrealized redemption premium payable of convertible notes	\$2,015,012	\$63,485	\$1,539,850	\$46,947
b. Deductible temporary difference from organization costs amortization into 5 years	32,551	1,025	16,275	496
c. Deductible temporary difference from pension expenses	4,449	140	11,099	338
d. Taxable temporary difference from unrealized gain on foreign exchange	(2,234,913)	(70,413)	(776,574)	(23,676)
e. Deductible temporary difference from unrealized loss on foreign exchange	582,515	18,353	13,517	412
Total	\$399,614	\$12,590	\$804,167	\$24,517
D. Deferred income tax assets-current	\$149,698	\$4,716	\$6,368	\$194
Deferred income tax liabilities-current	-	-	-	-
Net offset balance of deferred income tax assets (liabilities)-current	\$149,698	\$4,716	\$6,368	\$194
E. Deferred income tax assets-noncurrent	\$508,934	\$16,034	\$388,817	\$11,854
Deferred income tax liabilities- noncurrent	(558,728)	(17,603)	(194,143)	(5,919)
Net offset balance of deferred income tax assets (liabilities)-noncurrent	\$(49,794)	\$(1,569)	\$194,674	\$5,935

(3) The tax authorities have examined and cleared income tax returns of the Company through 2001.

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(4) Under a Article 49 of the Financial Holding Company Act, a financial holding company and its subsidiaries that are owned by the financial holding company for 12 months within the same tax year, may choose to file the consolidated income tax return.

(5) Information related tax imputation:

	December 31,			
	2004(NT\$)	2004(US\$)	2005(NT\$)	2005(US\$)
Balance of imputation credit account	\$362,239	\$11,413	\$1,681,979	\$51,280

  

	For the years ended December 31,	
	2004 (Actual)	2005 (Estimate)
Imputation credit account ratio	7.58%	7.62%

(6) Information relating of undistributed earnings:

Year	December 31,			
	2004(NT\$)	2004(US\$)	2005(NT\$)	2005(US\$)
Prior to 1997	\$267,215	\$8,419	\$267,215	\$8,147
After 1998	30,640,997	965,375	28,146,255	858,117
Total	\$30,908,212	\$973,794	\$28,413,470	\$866,264

The undistributed earnings prior to 1997 which derived from the undistributed retained earnings of the subsidiaries were included in the Company's capital surplus and were allowed to be distributed as cash dividends by the regulations.

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### 13. Earnings per share

For the year ended December 31, 2004									
	Amount (Numerator)				Shares (in thousands of shares) (denominator)	EPS			
	Before income taxes		After income taxes			Before income taxes		After income taxes	
	EPS (in dollars)		EPS (in dollars)			EPS (in dollars)		EPS (in dollars)	
	NT\$	US\$	NT\$	US\$		NT\$	US\$	NT\$	US\$
Net Income	<u>\$29,885,553</u>	<u>\$941,574</u>	<u>\$29,827,155</u>	<u>\$939,734</u>					
<b>Primary earnings per share</b>									
Net income for common stock holder	\$29,885,553	\$941,574	\$29,827,155	\$939,734	8,064,662	<u>\$3.71</u>	<u>\$0.12</u>	<u>\$3.70</u>	<u>\$0.12</u>
<b>Effect of potentially dilutive common stock</b>									
Convertible notes payable	<u>716,398</u>	<u>22,571</u>	<u>537,299</u>	<u>16,928</u>	<u>446,119</u>				
<b>Fully-diluted earnings per share</b>									
Net income for common stock holder & effect of potentially common stock	<u>\$30,601,951</u>	<u>\$964,145</u>	<u>\$30,364,454</u>	<u>\$956,662</u>	<u>\$8,510,781</u>	<u>\$3.60</u>	<u>\$0.11</u>	<u>\$3.57</u>	<u>\$0.11</u>
For the year ended December 31, 2005									
	Amount (Numerator)				Shares (in thousands of shares) (denominator)	EPS			
	Before income taxes		After income taxes			Before income taxes		After income taxes	
	EPS (in dollars)		EPS (in dollars)			EPS (in dollars)		EPS (in dollars)	
	NT\$	US\$	NT\$	US\$		NT\$	US\$	NT\$	US\$
Net Income	<u>\$21,965,553</u>	<u>\$669,681</u>	<u>\$21,787,053</u>	<u>\$664,239</u>					
<b>Primary earnings per share</b>									
Net income for common stock holder	\$21,965,553	\$669,681	\$21,787,053	\$664,239	8,462,518	<u>\$2.60</u>	<u>\$0.08</u>	<u>\$2.57</u>	<u>\$0.08</u>
<b>Effect of potentially dilutive common stock</b>									
Convertible notes payable	<u>569,524</u>	<u>17,364</u>	<u>427,143</u>	<u>13,023</u>	<u>299,010</u>				
<b>Fully-diluted earnings per share</b>									
Net income for common	<u>\$22,535,077</u>	<u>\$687,045</u>	<u>\$22,214,196</u>	<u>\$677,262</u>	<u>8,761,528</u>	<u>\$2.57</u>	<u>\$0.08</u>	<u>\$2.54</u>	<u>\$0.08</u>

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stock holder & effect of  
potentially common stock

The changes of the above weighted-average outstanding number of shares are shown below:

(in thousands of shares)	For the years end December 31,	
	2004	2005
Shares at the beginning of year	8,307,489	8,316,713
Add: The subsidiaries were sold The Company's stock	(243,725)	(3,169)
Convertible notes conversion	898	148,974
Total	8,064,662	8,462,518

The pro forma earnings per shares of Company that the subsidiaries held as short-term investments were not treated as treasury stock:

	For the years ended December 31,			
	2004(NT\$)	2004(US\$)	2005(NT\$)	2005(US\$)
Income before income taxes	\$30,041,879	\$946,499	\$21,962,594	\$669,591
Net income after income taxes	\$29,983,481	\$944,659	\$21,784,094	\$664,149
Before income taxes primary earnings per share (expressed in dollars)	\$3.72	\$0.12	\$2.59	\$0.08
After income taxes primary earnings per share (expressed in dollars)	\$3.71	\$0.12	\$2.57	\$0.08
Before income taxes fully – diluted earnings per share (expressed in dollars)	\$3.61	\$0.11	\$2.57	\$0.08
After income taxes fully – diluted earnings per shares (expressed in dollars)	\$3.58	\$0.11	\$2.53	\$0.08

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**14. Related party transactions**

*(1) Related parties*

Name	Relationship
Cathay Life	Subsidiary of the Company
Cathay United Bank (merged)	Subsidiary of the Company
Cathay Century	Subsidiary of the Company
Cathay Securities	Subsidiary of the Company
Cathay Pacific Venture Capital Co., Ltd.	Subsidiary of the Company
Cathay II Venture Capital Co., Ltd.	Subsidiary of the Company
Cathay Capital Management Inc.	Subsidiary of the Company
Lucky Bank	Subsidiary of the Company
Cathay Venture Capital Co., Ltd.	The investee is accounted for using the equity method
Lin Yuan Property Management Co., Ltd.	Subsidiaries' investee is accounted for using the equity method
Cathay Insurance (Bermuda) Co., Ltd.	Subsidiaries' investee is accounted for using the equity method
Cathay Life Insurance Ltd. (Shanghai)	Subsidiaries' investee is accounted for using the equity method
Symphox Information Co., Ltd.	Subsidiaries' investee is accounted for using the equity method
Cathay Securities Investment Co., Ltd.	Subsidiaries' investee is accounted for using the equity method
Cathay Bank Life Insurance Agency of Association (merged with Seaward Insurance Agent Corp. on February 5, 2004, Cathay Bank Life Insurance Agency of Association was the surviving company)	Subsidiaries' investee is accounted for using the equity method
Cathay Futures Corp.	Subsidiaries' investee is accounted for using the equity method
Cathay General Hospital	Their chairman is the Company's chairman
Seaward Leasing Ltd.	Subsidiaries' investee is accounted for using the equity method
Seaward Card Co., Ltd.	Subsidiaries' investee is accounted for using the equity method
Indovina Bank	Subsidiaries' investee is accounted for using the equity method
Cathay Bank Property Agency of Association	Subsidiaries' investee is accounted for using the equity method
Cathay Pacific Partners Co.,Ltd.	Subsidiaries' investee is accounted for using the equity method
China England Co., Ltd.	Investee company of Seaward Leasing Ltd.
Pao Shin Securities	Subsidiaries' investee is accounted for using the equity method
Culture and Charity Foundation of the CUB	Cathay United Bank (merged) is the major sponsor of the foundation
Cathay Charity Foundation	Cathay Life is the major sponsor of the foundation
Lin Yuan Investment Co.,Ltd.	Their chairman is a second immediate family member of the Company's chairman
Cathay Real Estate Development Co., Ltd.	Affiliate

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(2) *Significant transactions with related parties:*

A. Cash in bank

		As of and for the year ended December 31, 2004		
Name	Item	Ending balance (NT\$)	Rate	Interest income (NT\$)
Cathay United Bank (merged)	Time deposits	\$41,462	1.00%	\$5,824
	Cash in bank	5,767	0.10%	524
	Total	<u>\$47,229</u>		<u>\$6,348</u>

		As of and for the year ended December 31, 2004		
Name	Item	Ending balance (US\$)	Rate	Interest income (US\$)
Cathay United Bank (merged)	Time deposits	\$1,306	1.00%	\$183
	Cash in bank	182	0.10%	17
	Total	<u>\$1,488</u>		<u>\$200</u>

		As of and for the year ended December 31, 2005		
Name	Item	Ending balance (NT\$)	Rate	Interest income (NT\$)
Cathay United Bank (merged)	Time deposits	\$3,585,383	1.15%-4.375%	\$182,861
	Cash in bank	1,982	0.10%	67
	Total	<u>\$3,587,365</u>		<u>\$182,928</u>

		As of and for the year ended December 31, 2005		
Name	Item	Ending balance (US\$)	Rate	Interest income (US\$)
Cathay United Bank (merged)	Time deposits	\$109,311	1.15%-4.375%	\$5,575
	Cash in bank	60	0.10%	2
	Total	<u>\$109,371</u>		<u>\$5,577</u>

B. Interest receivable

Name	December 31,			
	2004(NT\$)	2004(US\$)	2005(NT\$)	2005(US\$)
Cathay United Bank (merged)	<u>\$50</u>	<u>\$2</u>	<u>\$6,972</u>	<u>\$213</u>

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C. Other accounts receivable

Name	December 31,			
	2004(NT\$)	2004(US\$)	2005(NT\$)	2005(US\$)
Cathay United Bank (merged)	\$508,186	\$16,011	\$2,245,837	\$68,471
Cathay Century	76,408	2,407	100,943	3,077
Cathay Capital Management Inc.	-	-	7,782	237
Cathay Securities	-	-	14,558	444
<b>Total</b>	<b>\$584,594</b>	<b>\$18,418</b>	<b>\$2,369,120</b>	<b>\$72,229</b>

D. Acquisition of property and equipment information:

Name	Item	December 31,			
		2004(NT\$)	2004(US\$)	2005(NT\$)	2005(US\$)
Cathay Real Estate Development Co., Ltd.	Transportion and communication equipment	\$-	\$-	\$1,850	\$56

E. Disposal of property and equipment information:

For the year ended December 31, 2004: None.

Name	Item	For the year ended December 31, 2005			
		Amount		Loss	
		NT\$	US\$	NT\$	US\$
Cathey Real Estate Development Co., Ltd.	Transportation and communication equipment	\$950	\$29	\$(473)	\$(14)

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F. Other accounts payable

Name	December 31,			
	2004(NT\$)	2004(US\$)	2005(NT\$)	2005(US\$)
Cathay Life	\$409,990	\$12,917	\$2,171,620	\$66,208
Cathay United Bank (merged)	571,606	18,009	571,606	17,427
Cathay Pacific Venture Capital Co., Ltd.	5,906	186	665	20
Cathay II Venture Capital Co., Ltd.	-	-	3,072	94
Total	<u>\$987,502</u>	<u>\$31,112</u>	<u>\$2,746,963</u>	<u>\$83,749</u>

G. Operating expense

Name	For the years ended December 31,			
	2004(NT\$)	2004(US\$)	2005(NT\$)	2005(US\$)
Cathay Life	\$8,718	\$275	\$10,138	\$309
Symphox Information Co., Ltd.	223	7	412	13
Seaward Leasing Ltd.	204	6	902	27
Seaward Card Co., Ltd.	853	27	382	12
Lucky Bank	-	-	1,900	58
Total	<u>\$9,998</u>	<u>\$315</u>	<u>\$13,734</u>	<u>\$419</u>

**15. Pledged assets: None.**

**16. Other important matters and contingent liabilities: None.**

**17. Serious damages: None.**

**18. Subsequent events: None.**



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**19. Other important events**

(1) Pension related information

According to the ROC SFAS No.18 “Accounting for Pensions”, the actuarial report disclosure of pension information for the years ended December 31, 2004 and 2005 was as follows:

A. Pension funded status

	December 31,			
	2004(NT\$)	2004(US\$)	2005(NT\$)	2005(US\$)
a. Vested benefit obligation	\$ (3,668)	\$ (116)	\$ (5,350)	\$ (163)
b. Non-vested benefit obligation	(4,785)	(151)	(6,726)	(205)
c. Accumulated benefit obligation	(8,453)	(267)	(12,076)	(368)
d. Additions benefits based on future salaries	(4,548)	(143)	(6,095)	(186)
e. Projected benefit obligation	(13,001)	(410)	(18,171)	(554)
f. Fair value of plan assets	416	13	1,112	34
g. Funded status=e+f	(12,585)	(397)	(17,059)	(520)
h. Unrecognized pension loss	10,108	319	7,931	242
i. Additional accrued pension liability	(5,560)	(175)	(1,837)	(56)
j. Accrued pension liability=g+h+i	<u>\$ (8,037)</u>	<u>\$ (253)</u>	<u>\$ (10,965)</u>	<u>\$ (334)</u>
k. Vested benefit	<u>\$ 9,173</u>	<u>\$ 289</u>	<u>\$ 14,041</u>	<u>\$ 428</u>

B. Actuarial assumptions

	For the years ended December 31,	
	2004	2005
a. Discount rate	3.00%	3.00%
b. Expected rate of increase in salaries	3.00%	3.00%
c. Expected long-term rate of return on plan assets	3.00%	3.00%

(2) Financial instruments related information

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### A. Derivative financial instruments related information:

#### a. Purpose

As of December 31, 2004 and 2005, the Company held the following derivative financial instruments: interest rate swaps, cross-currency swaps and foreign currency options. The primary objective of interest rate swaps, cross-currency swaps, and foreign currency options is to limit interest rate and exchange rate exposures related to assets and liabilities denominated in foreign currencies and foreign currency commitments, and bearing fixed interest rates. None of them was for trading purposes.

#### b. Credit and market risks

The counterparties for all of the Company's interest rate swaps, cross-currency swaps and foreign currency options are international financial organization with superior credit ratings. In addition, the Company worked with several other financial institutions to diversify its risks. The Company believes that the possibility of a breach of contract was quite low. Moreover, if there is a breach, the Company believes that it would not encounter major loss due to the nature of the investments. Further, the Company was exposed to various exchange rate risks but the possible loss can be balanced out by gain/loss from hedging transactions.

#### c. Cash flow and demand

As cash inflow and cash outflow will be automatically offset against each other on the expiration date of a forward contract, no demand for substantial cash flow is expected in connection with such transactions.

#### d. Interest rate swaps (IRS)

(a) IRS transactions may involve the exchange of fixed-rate interest payments for a market floating-rate interest payment obligation based on a notional principal amount. For IRS transactions undertaken for hedging purposes, income and expenses that arise upon settlement are netted off and recognized in the statement of income.

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(b) As of December 31, 2004:

<u>Counterpart</u>	<u>Effective</u>	<u>Period</u>	<u>Contract amount</u>	<u>Contract value</u>
Goldman Sachs International	2002.5.20	2002.5.20-2005.5.20	<u>USD700,000</u>	<u>USD700,000</u>

As of December 31, 2005: None.

e. Cross-currency swaps (CCS)

(a) For CCS contracts undertaken for non-trading purposes, amounts to be exchanged on settlement dates are recorded at the contracted forward rate. The interest, which may involve the exchange of fixed-rate interest payments for floating-rate interest payments based on a notional principal amount, is recorded as revenue or expense on each settlement date.

(b) As of December 31, 2004: None.

(c) As of December 31, 2005:

<u>Counterpart</u>	<u>Effective</u>	<u>Period</u>	<u>Contract amount</u>	<u>Contract value</u>	<u>Fair value</u>
Goldman Sachs International	2005.3.3	2005.3.7- 2010.3.7	<u>USD500,000</u>	<u>USD500,000</u>	<u>USD450,342</u>

f. Foreign currency options

(a) The Company uses foreign currency option contract to manage currency exposures.

(b) As of December 31, 2004: None.

As of December 31, 2005:

<u>Counterpart</u>	<u>Effective</u>	<u>Period</u>	<u>Contract amount</u>	<u>Contract value</u>	<u>Fair value</u>
Goldman Sachs International	2005.3.3	2005.3.7- 2010.3.7	<u>USD500,000</u>	<u>USD500,000</u>	<u>USD514,800</u>

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B. Non-derivative financial instruments related information

	December 31, 2004			
	NT\$		US\$	
	Carrying amount	Fair value	Carrying amount	Fair value
<u>Assets</u>				
Cash and cash equivalents	\$20,472,483	\$20,472,483	\$645,006	\$645,006
Other receivable	584,594	584,594	18,418	18,418
Long-term investments in stocks	178,504,731	178,504,731	5,623,968	5,623,968
Deferred charges	66,627	66,627	2,099	2,099
<u>Liabilities</u>				
Other payable	987,900	987,900	31,125	31,125
Bonds payable	23,774,560	23,774,560	749,041	749,041

	December 31, 2005			
	NT\$		US\$	
	Carrying amount	Fair value	Carrying amount	Fair value
<u>Assets</u>				
Cash and cash equivalents	\$10,448,439	\$10,448,439	\$318,550	\$318,550
Other receivable	2,369,120	2,369,120	72,229	72,229
Long-term investment in stocks	188,200,384	188,200,384	5,737,817	5,737,817
Refundable deposits	2,628,000	2,628,000	80,122	80,122
Deferred charges	119	119	3	3
<u>Liabilities</u>				
Other payable	2,746,963	2,746,963	83,749	83,749
Bonds payable	13,405,171	13,405,171	408,694	408,694

Methods and assumptions applied in estimating the fair value of non-derivative financial instruments are as follows:

- a. Short-term financial instruments are stated at carrying amount on the balance sheet date. The carrying amounts of the accounts such as cash and cash equivalents, and receivables approximate their fair value because of the short maturities of these instruments.

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- b. The market prices are used to determine the values of long-term investments in stocks if the market prices are available. Otherwise, carrying values or other financial information are used to estimate the fair values.
- c. The guarantee deposits paid are stated of the carrying amounts due to the fair values approximated to the carrying amounts.

(3) Zero coupon convertible notes related information:

Issuer: Cathay Financial Holding Co., Ltd.

Issue amount: US\$700 million.

Issue price: 100%.

Maturity date: May 20, 2007.

Interest: The notes do not bear interest except in the limited circumstances.

Conversion rights:

Subject to certain conditions, each holder of the notes (the “Holder”) has the right during the conversion period to convert its notes (or any portion thereof being US\$1,000 dollars in principal amount or an integral multiple thereof) into common shares and, upon conversion may, subject to compliance with the terms and conditions of the applicable deposit agreement, direct that the common shares deliverable upon conversion be deposited with the depository for issuance of GDSs, provided, however, that the conversion right during any closed period shall be suspended and the conversion period shall not include any such closed period.

Repurchase at the option of the holder:

Unless the notes have been previously redeemed, repurchased and cancelled, or converted, each Holder shall have the right, at such Holder's option, to require the Company to repurchase all (or any portion of the principal amount thereof which is US\$1,000 dollars or any integral multiple thereof) of such Holder's Notes, on May 20, 2005 at a price equal to 100% of the outstanding principal amount thereof plus the redemption premium. The redemption premium is the amount payable at the issue price on the original issue date, plus a compound yield rate of 2.75% per annum (computed on a semi-annual note equivalent basis).

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### Repurchase in the event of desisting:

Unless the notes have been previously redeemed, repurchased and cancelled, or converted, in the event that the Company's common shares cease to be listed or admitted to trading on the Taiwan Stock Exchange, each Holder shall have the right, at such Holder's option, to require the Company to repurchase all (or any portion of the principal amount thereof which is US\$1,000 dollars or any integral multiple thereof) of such Holder's notes at a price equal to 100% of the outstanding principal amount thereof plus the redemption premium.

### Repurchase in the event of change of control:

Unless the notes have been previously redeemed, repurchased and cancelled, or converted, each Holder shall have the right, at such Holder's option, to require the Company to repurchase all (or any portion of the principal amount thereof which is US\$1,000 dollars or any integral multiple thereof) of such Holder's notes at a price equal to 100% of the outstanding principal amount thereof plus the redemption premium, upon the occurrence of a change of control.

### Redemption at the option of the Company:

The notes may be redeemed at the option of the Company, in whole but not in part, at any time on or after May 20, 2005 at a price equal to 100% of the outstanding principal amount thereof plus the redemption premium on the redemption date; provided that (a) the closing price (translated into US dollars at the prevailing rate) of the common shares for a period of 30 consecutive trading days (including trading days that fall within a closed period), the last of which occurs not more than five days prior to the date on which notice of such redemption is given, is at least 130% of the conversion price (translated into US dollars at the exchange rate, as defined in the indenture for the notes) and (b) the applicable redemption date does not fall within a closed period. Notwithstanding the foregoing, the Company may redeem, in whole but not in part, the notes at any time, on not less than 30 nor more than 60 days' notice, if at least 90% in principal amount of the notes originally outstanding have been redeemed, repurchased and cancelled, or converted, at a redemption price equal to 100% of the outstanding principal amount thereof plus the redemption premium on the redemption date; provided that the applicable redemption date does not fall within a closed period.

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### Tax redemption:

If, as a result of certain changes relating to the ROC tax laws or such other jurisdiction in which the Company is then organized, the Company becomes obligated to pay certain additional amounts, the notes may be redeemed at the option of the Company, in whole but not in part, at a price equal to 100% of the outstanding principal amount thereof plus the redemption premium on such redemption date.

### Redemption amount at maturity:

Unless the notes have been previously redeemed, repurchased and cancelled, or converted, the Company will redeem the notes on the maturity date at a price equal to 100% of the outstanding principal amount thereof plus the redemption premium.

### Negative pledge:

Subject to certain exceptions, the Company will not, and will procure that none of its principal subsidiaries will, create or permit to subsist any lien to secure for the benefit of the holders of any international investment securities any sum owing in respect thereof or any guarantee or indemnity thereof without making effective provision to secure the notes (a) equally and ratably with such international investment securities with a similar lien or (b) with such other security as shall be approved by Holders of not less than a majority in aggregate principal amount of the outstanding notes.

### Further issues:

The Company may create and issue further securities with the same terms and conditions from time to time without the consent of the Holders of the notes so that such further issuance shall be consolidated and form a single series with the notes.

### Governing law:

The indenture, notes and deposit agreements are governed by, and construed in accordance with, the laws of the State of New York.

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Status quo:

As of December 31, 2005, the Company has converted US\$336,303 convertible notes at conversion price of NT\$54.15 dollars (US\$1.65 dollars) or NT\$51.94 dollars (US\$1.58 dollars) per share, into 216,734 thousand common stocks. The redemption premiums payable and additional paid-in capital of this conversion amounted to NT\$9,490,504 (US\$299,008), which are recognized as capital surplus. As of December 31, 2005 the Holder had exercised the repurchase right with US\$2,500 by par value, the Company had repurchased such Holder's notes at par value plus the redemption premium with US\$214.

### **(4) Capital adequacy ratio on a consolidated basis**

As of December 31, 2004 and 2005 the consolidated capital adequacy ratios were 153.89% and 162.88%, respectively.

### **(5) Material contract: None.**

### **(6) Presentation of financial statements:**

Certain accounts in financial statements for the year ended December 31, 2004 have been reclassified in order to be comparable with those in the financial statements for the year ended December 31, 2005.

## **20. Information for investment in Mainland China:**

On December 25, 2002 and July 24, 2003, the Investment Commission of the Ministry of Economic Affairs (MOEAIC) authorized Cathay Life to remit US\$22,850 and US\$27,150, respectively, as the registered capital to establish a China-based company named Cathay Life Insurance Co., Ltd. (Guangzhou). On September 25, 2003, MOEAIC authorized Cathay Life Insurance Co., Ltd. (Guangzhou) to change its location from Guangzhou to Shanghai. Cathay Life's subsidiary, Cathay Life Insurance Ltd. (Shanghai) has acquired a business license of an enterprise as legal person on December 29, 2004. As of December 31, 2005, Cathay Life's remittances to this new company totaled approximately US\$48,330.

## **21. Segment information: None.**



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22. The major subsidiaries' concise balance sheets and statements of income

(1) Concise balance sheets :

Items/Period	Cathay Life		Cathay United Bank		Cathay Century		Cathay Securities		Lucky Bank		Pao Shin Securities		Indovina Bank		Cathay Life Insurance Ltd. (Shanghai)	
	December 31, 2004	December 31, 2005	December 31, 2004	December 31, 2005	December 31, 2004	December 31, 2005	December 31, 2004	December 31, 2005	December 31, 2004	December 31, 2005	December 31, 2004	December 31, 2005	December 31, 2004	December 31, 2005	December 31, 2004	December 31, 2005
	NTS	NTS	NTS	NTS	NTS	NTS	NTS	NTS	NTS	NTS	NTS	NTS	NTS	NTS	NTS	NTS
Current assets	\$571,371,303	\$655,206,150	\$371,856,922	\$364,114,078	\$7,725,799	\$7,178,916	\$4,199,265	\$3,721,177	\$23,114,986	\$32,110,553	\$176,138	\$169,378	\$1,402,266	\$1,680,284	\$3,033,242	\$1,756,393
Bills and loans-net	450,828,752	442,686,793	585,618,279	616,026,087	788,350	1,321,212	-	-	62,805,013	58,895,205	-	-	5,993,705	6,117,367	-	-
Funds and long-term investments	537,449,975	648,434,334	37,399,221	63,450,216	2,579,776	3,572,477	18	18	477,021	406,807	9,150	9,150	-	-	-	1,122,021
Fixed assets	14,924,869	14,134,371	24,794,199	24,743,550	80,022	69,034	37,551	107,180	2,077,376	1,691,124	100,337	59,687	38,210	85,013	23,719	26,731
Other assets	50,146,644	107,326,473	4,696,134	5,727,092	485,382	550,967	243,472	306,041	995,913	859,345	101,035	100,548	26,466	38,921	13,000	885,204
Current liabilities	8,191,707	9,980,160	893,869,496	960,672,183	1,201,945	1,291,528	1,018,191	107,344	84,971,458	90,037,348	13,287	6,291	5,951,177	6,661,394	16,655	21,039
Long-term liabilities	1,431,436	1,631,044	-	-	9,209	6,869	1,810	2,586	292,006	276,907	9,590	11,013	-	-	-	-
Other liabilities	1,524,526,580	1,758,584,852	50,135,101	35,460,765	7,268,050	8,199,992	1,871	9,153	3,471	3,675	40,149	40,686	115,515	184,889	-	697,235
Capital stocks	50,686,158	50,686,158	43,182,407	46,420,518	2,317,006	2,317,006	3,500,000	3,700,000	3,146,000	3,146,000	312,000	312,000	795,625	820,500	3,092,240	3,256,400
Capital surplus	12,591	13,153	13,463,074	13,464,276	1,909	2,021	-	258,434	463,482	463,482	-	-	106,857	131,578	-	-
Retained earnings	39,956,516	46,896,873	23,830,886	17,968,156	861,358	875,348	(41,566)	56,899	610,999	106,866	11,634	(31,227)	91,473	123,224	(38,934)	(184,325)
Equity adjustments	(83,445)	(4,119)	(116,209)	75,125	(148)	(158)	-	-	(17,107)	(71,244)	-	-	-	-	-	-
Total assets	\$1,624,721,543	\$1,867,788,121	\$1,024,364,755	\$1,074,061,023	\$11,659,329	\$12,692,606	\$4,480,306	\$4,134,416	\$89,470,309	\$93,963,034	\$386,660	\$338,763	\$7,060,647	\$7,921,585	\$3,069,961	\$3,790,349
Total liabilities	\$1,534,149,723	\$1,770,196,056	\$944,004,597	\$996,132,948	\$8,479,204	\$9,498,389	\$1,021,872	\$119,083	\$85,266,935	\$90,317,930	\$63,026	\$57,990	\$6,066,692	\$6,846,283	\$16,655	\$718,274
Total stockholders' equity	\$90,571,820	\$97,592,065	\$80,360,158	\$77,928,075	\$3,180,125	\$3,194,217	\$3,458,434	\$4,015,333	\$4,203,374	\$3,645,104	\$323,634	\$280,773	\$993,955	\$1,075,302	\$3,053,306	\$3,072,075

Items/Period	Cathay Life		Cathay United Bank		Cathay Century		Cathay Securities		Lucky Bank		Pao Shin Securities		Indovina Bank		Cathay Life Insurance Ltd. (Shanghai)	
	December 31, 2004	December 31, 2005	December 31, 2004	December 31, 2005	December 31, 2004	December 31, 2005	December 31, 2004	December 31, 2005	December 31, 2004	December 31, 2005	December 31, 2004	December 31, 2005	December 31, 2004	December 31, 2005	December 31, 2004	December 31, 2005
	US\$	US\$	US\$	US\$	US\$	US\$	US\$	US\$	US\$	US\$	US\$	US\$	US\$	US\$	US\$	US\$
Current assets	\$18,001,616	\$19,975,797	\$11,715,719	\$11,101,039	\$243,409	\$218,869	\$132,302	\$113,451	\$728,260	\$978,980	\$5,550	\$5,164	\$44,062	\$51,197	\$95,565	\$53,548
Bills and loans-net	14,203,804	13,496,549	18,450,481	18,781,283	24,838	40,281	-	-	1,978,734	1,795,585	-	-	175,764	186,392	-	-
Funds and long-term investments	16,932,892	19,769,339	1,178,300	1,934,458	81,278	108,917	1	1	15,029	12,403	288	279	-	-	-	34,208
Fixed assets	470,222	430,926	781,166	754,377	2,521	2,105	1,183	3,267	65,450	51,559	3,161	1,820	1,201	2,590	747	815
Other assets	1,579,920	3,272,149	147,956	174,606	15,293	16,798	7,670	9,330	31,377	26,200	3,183	3,065	832	1,186	410	26,988
Current liabilities	258,088	304,273	28,162,240	29,288,786	37,869	39,376	32,079	3,272	2,677,110	2,745,041	419	192	186,997	202,968	525	641
Long-term liabilities	45,099	49,727	-	-	290	209	57	79	9,200	8,442	302	336	-	-	-	-
Other liabilities	48,031,713	53,615,392	1,579,556	1,081,121	228,987	250,000	59	279	109	112	1,265	1,240	3,630	5,633	-	21,257
Capital stocks	1,596,917	1,545,310	1,360,504	1,415,260	73,000	70,640	110,271	112,805	99,118	95,915	9,830	9,512	25,000	25,000	97,424	99,281
Capital surplus	397	401	424,168	410,496	60	62	-	7,879	14,602	14,131	-	-	3,358	4,009	-	-
Retained earnings	1,258,869	1,429,783	750,815	547,810	27,138	26,688	(1,310)	1,735	19,250	3,258	366	(952)	2,874	3,755	(1,227)	(5,620)
Equity adjustments	(2,629)	(126)	(3,661)	2,290	(5)	(5)	-	-	(539)	(2,172)	-	-	-	-	-	-
Total assets	\$51,188,454	\$56,944,760	\$32,273,622	\$32,745,763	\$367,339	\$386,970	\$141,156	\$126,049	\$2,818,850	\$2,864,727	\$12,182	\$10,328	\$221,859	\$241,365	\$96,722	\$115,559
Total liabilities	\$48,334,900	\$53,969,392	\$29,741,796	\$30,369,907	\$267,146	\$289,585	\$32,195	\$3,630	\$2,686,419	\$2,753,595	\$1,986	\$1,768	\$190,627	\$208,601	\$525	\$21,898
Total stockholders' equity	\$2,853,554	\$2,975,368	\$2,531,826	\$2,375,856	\$100,193	\$97,385	\$108,961	\$122,419	\$132,431	\$111,132	\$10,196	\$8,560	\$31,232	\$32,764	\$96,197	\$93,661

English Translation of Financial Statements Originally Issued in Chinese

(2) Concise income statement :

Items/Period	Cathay Life		Cathay United Bank		Cathay Century		Cathay Securities		Lucky Bank		Pao Shin Securities		Indovina Bank		Cathay Life Insurance Ltd. (Shanghai)	
	For the year ended Dec. 31, 2004	For the year ended Dec. 31, 2005	For the year ended Dec. 31, 2004	For the year ended Dec. 31, 2005	For the year ended Dec. 31, 2004	For the year ended Dec. 31, 2005	For the year ended Dec. 31, 2004	For the year ended Dec. 31, 2005	For the year ended Dec. 31, 2004	For the year ended Dec. 31, 2005	For the year ended Dec. 31, 2004	For the year ended Dec. 31, 2005	For the year ended Dec. 31, 2004	For the year ended Dec. 31, 2005	For the year ended Dec. 31, 2004	For the year ended Dec. 31, 2005
	NTS	NTS	NTS	NTS	NTS	NTS	NTS	NTS	NTS	NTS	NTS	NTS	NTS	NTS	NTS	NTS
Operating revenues	\$528,792,877	\$554,243,919	\$41,851,027	\$48,885,722	\$13,892,595	\$17,229,348	\$60,335	\$352,533	\$2,275,011	\$2,124,037	\$38,773	\$26,131	\$481,149	\$572,597	\$748	\$792,351
Operating costs & expenses	(512,880,225)	(539,357,918)	(25,322,607)	(43,437,703)	(13,083,064)	(16,429,956)	(125,627)	(307,529)	(1,849,323)	(1,943,351)	(69,741)	(56,144)	(333,086)	(398,036)	(39,612)	(920,990)
Operating income	15,912,652	14,886,001	16,528,420	5,448,019	809,531	799,392	(65,292)	45,004	425,688	180,686	(30,968)	(30,013)	148,063	174,561	(38,864)	(128,639)
Non-operating revenues	2,106,927	2,297,854	1,287,486	151,693	37,466	16,035	16,186	43,006	16,799	24,240	33,102	23,618	3,575	10,938	-	6,983
Non-operating expenses	(2,757,105)	(478,601)	(147,659)	(486,969)	(27,414)	(64,106)	(107)	(2,229)	(7,131)	(36,438)	-	-	(1,624)	(3,417)	(29)	(16,619)
Operating income before taxes	15,262,474	16,705,254	17,668,247	5,112,743	819,583	751,321	(49,213)	85,781	435,356	(162,853)	2,134	(42,833)	150,014	182,082	(38,893)	(138,275)
Net income (loss)	15,618,806	17,922,656	13,879,247	3,852,743	640,617	590,545	(41,566)	56,899	481,809	(166,788)	2,134	(42,861)	118,483	145,917	(38,893)	(138,275)
Earning per share before taxes (in dollars)	\$3.02	\$3.30	\$3.81	\$1.10	\$3.54	\$3.24	\$(0.14)	\$0.24	\$1.38	\$(0.52)	\$0.07	\$(1.37)	\$-	\$-	\$-	\$-
Earning per share (in dollars)	\$3.09	\$3.54	\$2.99	\$0.83	\$2.76	\$2.55	\$(0.12)	\$0.16	\$1.53	\$(0.53)	\$0.07	\$(1.37)	\$-	\$-	\$-	\$-

  

Items/Period	Cathay Life		Cathay United Bank		Cathay Century		Cathay Securities		Lucky Bank		Pao Shin Securities		Indovina Bank		Cathay Life Insurance Ltd. (Shanghai)	
	For the year ended Dec. 31, 2004	For the year ended Dec. 31, 2005	For the year ended Dec. 31, 2004	For the year ended Dec. 31, 2005	For the year ended Dec. 31, 2004	For the year ended Dec. 31, 2005	For the year ended Dec. 31, 2004	For the year ended Dec. 31, 2005	For the year ended Dec. 31, 2004	For the year ended Dec. 31, 2005	For the year ended Dec. 31, 2004	For the year ended Dec. 31, 2005	For the year ended Dec. 31, 2004	For the year ended Dec. 31, 2005	For the year ended Dec. 31, 2004	For the year ended Dec. 31, 2005
	US\$	US\$	US\$	US\$	US\$	US\$	US\$	US\$	US\$	US\$	US\$	US\$	US\$	US\$	US\$	US\$
Operating revenues	\$16,660,141	\$16,897,681	\$1,318,558	\$1,490,418	\$437,700	\$525,285	\$1,901	\$10,748	\$71,677	\$64,757	\$1,221	\$797	\$14,409	\$17,783	\$24	\$24,157
Operating costs & expenses	(16,158,797)	(16,443,839)	(797,814)	(1,324,320)	(412,195)	(500,913)	(3,958)	(9,375)	(58,265)	(59,248)	(2,197)	(1,712)	(9,975)	(12,362)	(1,248)	(28,079)
Operating income	501,344	453,842	520,744	166,098	25,505	24,372	(2,057)	1,373	13,412	5,509	(976)	(915)	4,434	5,421	(1,224)	(3,922)
Non-operating revenues	66,381	70,056	40,563	4,625	1,180	489	510	1,311	529	739	1,043	720	107	340	-	213
Non-operating expenses	(86,866)	(14,592)	(4,652)	(14,847)	(864)	(1,954)	(3)	(68)	(225)	(11,207)	-	(1,111)	(48)	(106)	(1)	(507)
Operating income before taxes	480,859	509,306	556,655	155,876	25,821	22,907	(1,550)	2,616	13,716	(4,959)	67	(1,306)	4,493	5,655	(1,225)	(4,216)
Net income (loss)	492,086	546,422	437,279	117,462	20,183	18,005	(1,310)	1,735	15,180	(5,085)	67	(1,307)	3,548	4,532	(1,225)	(4,216)
Earning per share before taxes (in dollars)	\$0.10	\$0.10	\$0.12	\$0.03	\$0.11	\$0.10	\$-	\$0.01	\$0.04	\$(0.02)	\$-	\$(0.04)	\$-	\$-	\$-	\$-
Earning per share (in dollars)	\$0.10	\$0.11	\$0.09	\$0.03	\$0.09	\$0.08	\$-	\$-	\$0.05	\$(0.02)	\$-	\$(0.04)	\$-	\$-	\$-	\$-