

TAIWAN SEMICONDUCTOR MANUFACTURING CO LTD

Form 6-K

April 30, 2007

1934 Act Registration No. 1-14700

**SECURITIES AND EXCHANGE COMMISSION**  
**Washington, DC 20549**

**FORM 6-K**

**REPORT OF FOREIGN PRIVATE ISSUER**  
**PURSUANT TO RULE 13a-16 OR 15d-16 OF**  
**THE SECURITIES EXCHANGE ACT OF 1934**

**For the month of April 2007**

**Taiwan Semiconductor Manufacturing Company Ltd.**

(Translation of Registrant's Name Into English)

**No. 8, Li-Hsin Rd. 6,**  
**Hsinchu Science Park,**  
**Taiwan**

(Address of Principal Executive Offices)

(Indicate by check mark whether the registrant files or will file annual reports under cover of Form 20-F or Form 40-F.)

Form 20-F ☐ Form 40-F ☐

(Indicate by check mark whether the registrant by furnishing the information contained in this form is also thereby furnishing the information to the Commission pursuant to Rule 12g3-2(b) under the Securities Exchange Act of 1934.)

Yes ☐ No ☐

(If "Yes" is marked, indicated below the file number assigned to the registrant in connection with Rule 12g3-2(b):  
82: \_\_\_\_\_.)

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**Taiwan Semiconductor Manufacturing  
Company Limited  
Financial Statements for the  
Three Months Ended March 31, 2007 and 2006 and  
Independent Accountants' Review Report**

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## **INDEPENDENT ACCOUNTANTS' REVIEW REPORT**

The Board of Directors and Shareholders

Taiwan Semiconductor Manufacturing Company Limited

We have reviewed the accompanying balance sheets of Taiwan Semiconductor Manufacturing Company Limited as of March 31, 2007 and 2006, and the related statements of income and cash flows for the three months then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to issue a report on these financial statements based on our reviews.

We conducted our reviews in accordance with Statement on Auditing Standards No. 36, "Review of Financial Statements" issued by the Auditing Standards Committee of the Accounting Research and Development Foundation of the Republic of China. A review consists principally of applying analytical procedures to financial data and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with auditing standards generally accepted in the Republic of China, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our reviews, we are not aware of any material modifications that should be made to the financial statements referred to above for them to be in conformity with the Guidelines Governing the Preparation of Financial Reports by Securities Issuers, requirements of the Business Accounting Law and Guidelines Governing Business Accounting with respect to financial accounting standards, and accounting principles generally accepted in the Republic of China. April 10, 2007

### 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 jurisdictions. The standards, procedures and practices to review such financial statements are those generally accepted and applied in the Republic of China.*

*For the convenience of readers, the accountants' review report and the accompanying financial statements have been translated into English from the original Chinese version prepared and used in the Republic of China. If there is any conflict between the English version and the original Chinese version or any difference in the interpretation of the two versions, the Chinese-language accountants' review report and financial statements shall prevail.*

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**Taiwan Semiconductor Manufacturing Company Limited****BALANCE SHEETS****MARCH 31, 2007 AND 2006****(In Thousands of New Taiwan Dollars, Except Par Value)****(Reviewed, Not Audited)**

	<b>2007</b>		<b>2006</b>	
	<b>Amount</b>	<b>%</b>	<b>Amount</b>	<b>%</b>
<b>ASSETS</b>				
<b>CURRENT ASSETS</b>				
Cash and cash equivalents (Notes 2 and 4)	\$ 119,752,168	20	\$ 109,989,790	20
Financial assets at fair value through profit or loss (Notes 2, 3 and 5)	159		58,545	
Available-for-sale financial assets (Notes 2, 3 and 6)	26,325,390	4	58,815,063	11
Held-to-maturity financial assets (Notes 2 and 7)	6,523,668	1	9,120,093	2
Receivables from related parties (Note 23)	19,157,572	3	21,248,956	4
Notes and accounts receivable	14,682,899	3	19,986,591	4
Allowance for doubtful receivables (Note 2)	(690,931)		(975,704)	
Allowance for sales returns and others (Note 2)	(2,476,287)		(4,479,954)	(1)
Other receivables from related parties (Note 23)	487,266		683,675	
Other financial assets	686,670		784,723	
Inventories, net (Notes 2 and 8)	19,933,360	3	16,901,113	3
Deferred income taxes assets (Notes 2 and 16)	9,486,631	2	7,276,728	1
Prepaid expenses and other current assets	1,362,053		1,378,283	
 Total current assets	 215,230,618	 36	 240,787,902	 44
 <b>LONG-TERM INVESTMENTS (Notes 2, 6, 7, 9 and 10)</b>				
Investments accounted for using equity method	105,135,305	18	54,047,343	10
Available-for-sale financial assets	6,466,605	1	1,900,885	
Held-to-maturity financial assets	26,697,128	5	18,677,604	4
Financial assets carried at cost	746,405		813,354	
 Total long-term investments	 139,045,443	 24	 75,439,186	 14
 <b>PROPERTY, PLANT AND EQUIPMENT (Notes 2, 11 and 23)</b>				
Cost Buildings	98,752,832	17	91,408,209	17
Machinery and equipment	538,459,403	91	468,724,647	86
Office equipment	8,722,604	1	7,978,549	2
	645,934,839	109	568,111,405	105

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Accumulated depreciation	(435,129,667)	(73)	(373,690,326)	(69)
Advance payments and construction in progress	11,740,887	2	18,101,402	3
Net property, plant and equipment	222,546,059	38	212,522,481	39
GOODWILL (Note 2)	1,567,756		1,567,756	
OTHER ASSETS				
Deferred charges, net (Notes 2 and 12)	5,593,638	1	6,179,470	1
Deferred income tax assets (Notes 2 and 16)	5,001,596	1	7,064,964	2
Refundable deposits	2,576,685		83,642	
Assets leased to others, net (Note 2)	65,712		71,446	
Others			6,789	
Total other assets	13,237,631	2	13,406,311	3
TOTAL	\$ 591,627,507	100	\$ 543,723,636	100

**LIABILITIES AND SHAREHOLDERS  
EQUITY**

**CURRENT LIABILITIES**

Financial liabilities at fair value through profit or loss (Notes 2, 3 and 5)	\$ 133,802		\$ 354,214	
Accounts payable	6,811,587	1	7,360,964	1
Payables to related parties (Note 23)	2,377,933		3,512,804	1
Income tax payable (Notes 2 and 16)	9,801,787	2	6,110,590	1
Accrued expenses and other current liabilities (Note 14)	8,497,965	1	6,886,738	1
Payables to contractors and equipment suppliers	8,694,304	2	11,621,333	2
Current portion of bonds payable (Note 13)	4,500,000	1	2,500,000	1
Total current liabilities	40,817,378	7	38,346,643	7

**LONG-TERM LIABILITIES**

Bonds payable (Note 13)	12,500,000	2	17,000,000	3
Other long-term payables (Note 14)	1,623,181		1,493,160	
Other payables to related parties (Notes 23 and 25)			1,087,410	
Total long-term liabilities	14,123,181	2	19,580,570	3

## OTHER LIABILITIES

Accrued pension cost (Notes 2 and 15)	3,546,228	1	3,437,287	1
Guarantee deposits (Note 25)	3,424,737	1	3,215,089	1
Deferred credits (Notes 2 and 23)	1,090,364		1,211,019	

Total other liabilities	8,061,329	2	7,863,395	2
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Total liabilities	63,001,888	11	65,790,608	12
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## CAPITAL STOCK \$10 PAR VALUE

Authorized: 27,050,000 thousand shares

Issued: 25,832,959 thousand shares in 2007

24,733,053 thousand shares in 2006	258,329,592	44	247,330,530	45
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CAPITAL SURPLUS (Notes 2 and 18)	54,231,465	9	57,208,367	11
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## RETAINED EARNINGS (Note 18)

Appropriated as legal capital reserve	43,705,711	7	34,348,208	6
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Appropriated as special capital reserve	640,742		2,226,427	
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Unappropriated earnings	171,616,718	29	138,803,185	26
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	215,963,171	36	175,377,820	32
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## OTHERS (Notes 2, 3 and 22)

Cumulative translation adjustments	299,332		(1,098,483)	
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Unrealized gains on financial instruments	720,134		32,869	
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	1,019,466		(1,065,614)	
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## TREASURY STOCK (AT COST, Notes 2 and 20)

33,926 thousand shares in 2007 and 32,938

thousand shares in 2006	(918,075)		(918,075)	
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Total shareholders' equity	528,625,619	89	477,933,028	88
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TOTAL	\$ 591,627,507	100	\$ 543,723,636	100
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The accompanying notes are an integral part of the financial statements.

**Taiwan Semiconductor Manufacturing Company Limited**  
**STATEMENTS OF INCOME**  
**FOR THE THREE MONTHS ENDED MARCH 31, 2007 AND 2006**  
(In Thousands of New Taiwan Dollars, Except Earnings Per Share)  
(Reviewed, Not Audited)

	<b>2007</b>		<b>2006</b>	
	<b>Amount</b>	<b>%</b>	<b>Amount</b>	<b>%</b>
GROSS SALES (Notes 2 and 23)	\$ 64,054,647		\$ 78,637,640	
SALES RETURNS AND ALLOWANCES (Note 2)	708,058		1,344,296	
NET SALES	63,346,589	100	77,293,344	100
COST OF SALES (Notes 17 and 23)	39,378,386	62	40,651,362	53
GROSS PROFIT	23,968,203	38	36,641,982	47
UNREALIZED GROSS PROFIT FROM AFFILIATES	198,973			
REALIZED GROSS PROFIT	23,769,230	38	36,641,982	47
OPERATING EXPENSES (Notes 17 and 23)				
Research and development	3,479,141	5	3,548,886	5
General and administrative	1,617,600	3	1,554,351	2
Marketing	310,529	1	671,400	
Total operating expenses	5,407,270	9	5,774,637	7
INCOME FROM OPERATIONS	18,361,960	29	30,867,345	40
NON-OPERATING INCOME AND GAINS				
Equity in earnings of equity method investees, net (Notes 2 and 9)	853,184	1	2,972,039	4
Interest income (Note 2)	652,231	1	902,043	1
Foreign exchange gain, net (Note 2)	440,867	1		
Technical service income (Notes 23 and 25)	161,161		142,631	
Gain on disposal of property, plant and equipment (Notes 2 and 23)	69,982		96,141	
Gain on settlement and disposal of financial instruments, net (Notes 2, 5 and 22)			1,115,518	2



Others (Note 23)	170,146		78,440	
Total non-operating income and gains	2,347,571	3	5,306,812	7
NON-OPERATING EXPENSES AND LOSSES				
Loss on settlement and disposal of financial instruments, net (Notes 2 and 5)	480,826	1		
Valuation loss on financial instruments, net (Notes 2, 5 and 22)	167,493		295,669	

(Continued)

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**Taiwan Semiconductor Manufacturing Company Limited**  
**STATEMENTS OF INCOME**  
**FOR THE THREE MONTHS ENDED MARCH 31, 2007 AND 2006**  
(In Thousands of New Taiwan Dollars, Except Earnings Per Share)  
(Reviewed, Not Audited)

	<b>2007</b>		<b>2006</b>	
	<b>Amount</b>	<b>%</b>	<b>Amount</b>	<b>%</b>
Interest expense	\$ 151,922		\$ 165,300	
Foreign exchange loss, net (Note 2)			1,032,555	2
Others (Note 2)	14,382		25,292	
 Total non-operating expenses and losses	 814,623	 1	 1,518,816	 2
 INCOME BEFORE INCOME TAX	 19,894,908	 31	 34,655,341	 45
 INCOME TAX EXPENSE (Notes 2 and 16)	 1,056,269	 1	 1,802,369	 3
 NET INCOME BEFORE CUMULATIVE EFFECT OF CHANGES IN ACCOUNTING PRINCIPLES	 18,838,639	 30	 32,852,972	 42
 CUMULATIVE EFFECT OF CHANGES IN ACCOUNTING PRINCIPLES, NET OF TAX BENEFIT OF NT\$82,062 THOUSAND (Note 3)			 (246,186)	
 NET INCOME	 \$ 18,838,639	 30	 \$ 32,606,786	 42

	<b>2007</b>		<b>2006</b>	
	<b>Before Income Tax</b>	<b>After Income Tax</b>	<b>Before Income Tax</b>	<b>After Income Tax</b>
EARNINGS PER SHARE (NT\$, Note 21)				
Basic earnings per share	\$ 0.77	\$ 0.73	\$ 1.33	\$ 1.26
Diluted earnings per share	\$ 0.77	\$ 0.73	\$ 1.33	\$ 1.26

Certain pro forma information (after income tax) is shown as follows, based on the assumption that the Company's stock held by subsidiaries is treated as an investment instead of treasury stock (Notes 2 and 20):

	<b>2007</b>	<b>2006</b>
NET INCOME BEFORE CUMULATIVE EFFECT OF CHANGES IN ACCOUNTING PRINCIPLES	\$ 18,838,639	\$ 32,852,972

NET INCOME	\$ 18,838,639	\$ 32,606,786
EARNINGS PER SHARE (NT\$)		
Basic earnings per share	\$ 0.73	\$ 1.26
Diluted earnings per share	\$ 0.73	\$ 1.26

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

(Concluded)

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**Taiwan Semiconductor Manufacturing Company Limited**  
**STATEMENTS OF CASH FLOWS**  
**FOR THE THREE MONTHS ENDED MARCH 31, 2007 AND 2006**  
**(In Thousands of New Taiwan Dollars)**  
**(Reviewed, Not Audited)**

	<b>2007</b>	<b>2006</b>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net income	\$ 18,838,639	\$ 32,606,786
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	18,488,096	15,974,533
Unrealized gross profit from affiliates	198,973	
Amortization of premium/discount of financial assets	(31,517)	(15,834)
Gain on disposal of available-for-sale financial assets, net	(29,611)	(261,300)
Equity in earnings of equity method investees, net	(853,184)	(2,972,039)
Gain on disposal of property, plant and equipment and other assets, net	(67,949)	(93,903)
Deferred income taxes	(895,100)	(568,737)
Changes in operating assets and liabilities:		
Decrease (increase) in:		
Financial assets and liabilities at fair value through profit or loss	167,493	1,442,295
Receivables from related parties	(2,288,063)	(198,352)
Notes and accounts receivable	1,595,265	605,227
Allowance for doubtful receivables		(640)
Allowance for sales returns and others	(274,778)	209,985
Other receivables from related parties	(38,000)	846,108
Other financial assets	(33,210)	321,307
Inventories	(781,146)	(643,158)
Prepaid expenses and other current assets	(140,854)	(206,510)
Increase (decrease) in:		
Accounts payable	667,908	(691,142)
Payables to related parties	(948,983)	257,542
Income tax payable	1,951,369	2,294,702
Accrued expenses and other current liabilities	343,035	(1,110,647)
Accrued pension cost	16,112	(24,105)
Deferred credits	(23,936)	(23,936)
 Net cash provided by operating activities	 35,860,559	 47,748,182

**CASH FLOWS FROM INVESTING ACTIVITIES**

Acquisitions of:		
Available-for-sale financial assets	(2,151,253)	(31,351,886)
Held-to-maturity financial assets		(1,379,009)
Financial assets carried at cost	(33,562)	(5,864)
Investments accounted for using equity method	(1,631,986)	(19,214)
Property, plant and equipment	(13,783,013)	(11,114,607)
		(Continued)



**Taiwan Semiconductor Manufacturing Company Limited**  
**STATEMENTS OF CASH FLOWS**  
**FOR THE THREE MONTHS ENDED MARCH 31, 2007 AND 2006**  
**(In Thousands of New Taiwan Dollars)**  
**(Reviewed, Not Audited)**

	<b>2007</b>	<b>2006</b>
Proceeds from disposal or redemption of:		
Available-for-sale financial assets	\$ 2,080,000	\$ 16,951,250
Held-to-maturity financial assets	4,282,320	2,973,000
Property, plant and equipment and other assets	1,165	461,151
Proceeds from return of capital by investee	14,068	
Increase in deferred charges	(992,173)	(96,335)
Increase in refundable deposits	(1,270,451)	
 Net cash used in investing activities	 (13,484,885)	 (23,581,514)
 <b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Repayment of long-term bonds payable	(2,500,000)	
Increase (decrease) in guarantee deposits	(385,224)	322,144
Proceeds from exercise of employee stock options	122,009	117,395
 Net cash provided by (used in) financing activities	 (2,763,215)	 439,539
 <b>NET INCREASE IN CASH AND CASH EQUIVALENTS</b>	 19,612,459	 24,606,207
 <b>CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD</b>	 100,139,709	 85,383,583
 <b>CASH AND CASH EQUIVALENTS, END OF PERIOD</b>	 \$ 119,752,168	 \$ 109,989,790
 <b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION</b>		
Interest paid	\$ 420,000	\$ 420,000
 Income tax paid	 \$ 52,670	 \$ 67,924
 <b>INVESTING ACTIVITIES AFFECTING BOTH CASH AND NON-CASH ITEMS</b>		
Acquisition of property, plant and equipment	\$ 11,807,794	\$ 13,876,710
Decrease (increase) in payables to contractors and equipment suppliers	1,975,219	(2,762,103)
 Cash paid	 \$ 13,783,013	 \$ 11,114,607

NON-CASH FINANCING ACTIVITIES

Current portion of bonds payable	\$ 4,500,000	\$ 2,500,000
Current portion of other payables to related parties (under payables to related parties)	\$	\$ 685,718
Current portion of other long-term payables (under accrued expenses and other current liabilities)	\$ 2,371,524	\$ 817,530

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

(Concluded)

**Taiwan Semiconductor Manufacturing Company Limited**

**NOTES TO FINANCIAL STATEMENTS**

**FOR THE THREE MONTHS ENDED MARCH 31, 2007 AND 2006**

**(Amounts in Thousands of New Taiwan Dollars, Unless Specified Otherwise)**

**(Reviewed, Not Audited)**

**1. GENERAL**

Taiwan Semiconductor Manufacturing Company Limited (the Company or TSMC), a Republic of China (R.O.C.) corporation, was incorporated as a venture among the Government of the R.O.C., acting through the Development Fund of the Executive Yuan; Philips Electronics N.V. and certain of its affiliates (Philips); and certain other private investors. On September 5, 1994, its shares were listed on the Taiwan Stock Exchange (TSE). On October 8, 1997, TSMC listed some of its shares of stock on the New York Stock Exchange (NYSE) in the form of American Depositary Shares (ADSs).

The Company is engaged mainly in the manufacturing, selling, packaging, testing and computer-aided designing of integrated circuits and other semiconductor devices and the manufacturing of masks.

As of March 31, 2007 and 2006, the Company had 20,222 and 20,027 employees, respectively.

**2. SIGNIFICANT ACCOUNTING POLICIES**

The financial statements are presented in conformity with the Guidelines Governing the Preparation of Financial Reports by Securities Issuers, Business Accounting Law, Guidelines Governing Business Accounting, and accounting principles generally accepted in the R.O.C.

For the convenience of readers, the accompanying financial statements have been translated into English from the original Chinese version prepared and used in the R.O.C. If there is any conflict between the English version and the original Chinese version or any difference in the interpretation of the two versions, the Chinese-language financial statements shall prevail.

Significant accounting policies are summarized as follows:

**Use of Estimates**

The preparation of financial statements in conformity with the aforementioned guidelines, law and principles requires management to make reasonable assumptions and estimates of matters that are inherently uncertain. The actual results may differ from management's estimates.

**Classification of Current and Noncurrent Assets and Liabilities**

Current assets are assets held for trading purposes and assets expected to be converted to cash, sold or consumed within one year from the balance sheet date. Current liabilities are obligations incurred for trading purposes and obligations expected to be settled within one year from the balance sheet date. Assets and liabilities that are not classified as current are noncurrent assets and liabilities, respectively.

**Cash Equivalents**

Repurchase agreements collateralized by government bonds, asset-backed commercial papers and corporate notes acquired with maturities of less than three months from the date of purchase are classified as cash equivalents. The carrying amount approximates fair value.



### **Financial Assets/Liabilities at Fair Value Through Profit or Loss**

Derivatives that do not meet the criteria for hedge accounting are initially recognized at fair value, with transaction costs expensed as incurred. The derivatives are remeasured at fair value subsequently with changes in fair value recognized in earnings. A regular way purchase or sale of financial assets is accounted for using settlement date accounting.

Fair value is estimated using valuation techniques incorporating estimates and assumptions that are consistent with prevailing market conditions. When the fair value is positive, the derivative is recognized as a financial asset; when the fair value is negative, the derivative is recognized as a financial liability.

### **Available-for-sale Financial Assets**

Investments designated as available-for-sale financial assets include debt securities and equity securities.

Available-for-sale financial assets are initially recognized at fair value plus transaction costs that are directly attributable to the acquisition. Changes in fair value from subsequent remeasurement are reported as a separate component of shareholders' equity. The corresponding accumulated gains or losses are recognized in earnings when the financial asset is derecognized from the balance sheet. A regular way purchase or sale of financial assets is accounted for using settlement date accounting.

Except structured time deposits whose fair value is estimated using valuation techniques, fair values of open-end mutual funds and publicly traded stocks are determined using the net assets value and the closing-price at the end of the period, respectively. For debt securities, fair value is determined using the average of bid and asked prices at the end of the period.

Cash dividends are recognized as investment income upon resolution of shareholders of an investee but are accounted for as a reduction to the original cost of investment if such dividends are declared on the earnings of the investee attributable to the period prior to the purchase of the investment. Stock dividends are recorded as an increase in the number of shares held and do not affect investment income. The cost per share is recalculated based on the new total number of shares. Any difference between the initial carrying amount of a debt security and the amount due at maturity is amortized using the effective interest method, with the amortization recognized in earnings.

If there is objective evidence which indicates that a financial asset is impaired, a loss is recognized. If, in a subsequent period, the amount of the impairment loss decreases, for equity securities, the previously recognized impairment loss is reversed to the extent of the decrease and recorded as an adjustment to shareholders' equity; for debt securities, the amount of the decrease is recognized in earnings, provided that the decrease is clearly attributable to an event which occurred after the impairment loss was recognized.

### **Held-to-maturity Financial Assets**

Debt securities for which the Company has a positive intention and ability to hold to maturity are categorized as held-to-maturity financial assets and are carried at amortized cost under the effective interest method. Those financial assets are initially recognized at fair value plus transaction costs that are directly attributable to the acquisition. Gains or losses are recognized at the time of derecognition, impairment or amortization. A regular way purchase or sale of financial assets is accounted for using settlement date accounting.

If there is objective evidence which indicates that a financial asset is impaired, a loss is recognized. If, in a subsequent period, the amount of the impairment loss decreases and the decrease is clearly attributable to an event which occurred after the impairment loss was recognized, the previously recognized impairment loss is reversed to the extent of the decrease. The reversal may not result in a carrying amount that exceeds the amortized cost that would have been determined as if no impairment loss had been recognized.

### **Allowance for Doubtful Receivables**

An allowance for doubtful receivables is provided based on a review of the collectibility of accounts receivable. The Company determines the amount of allowance for doubtful receivables by examining the aging analysis of outstanding accounts receivable and current trends in the credit quality of its customers as well as its internal credit policies.

### **Revenue Recognition and Allowance for Sales Returns and Others**

The Company recognizes revenue when evidence of an arrangement exists, shipment is made, price is fixed or determinable, and collectibility is reasonably assured. Revenues from the design and manufacture of photo masks, which are used as manufacturing tools in the fabrication process, are recognized when the photo masks are qualified by customers. Provisions for estimated sales returns and others are generally recorded in the period the related revenue is recognized based on historical experience, management's judgment, and any known factors that would significantly affect the allowance.

Sales prices are determined using fair value taking into account related sales discounts agreed to by the Company and its customers. Sales agreements typically provide that payment is due 30 days from invoice date for a majority of the customers and 30 to 45 days after the end of the month in which sales occur for some customers. Since the receivables from sales are collectible within one year and such transactions are frequent, fair value of the receivables is equivalent to the nominal amount of the cash to be received.

### **Inventories**

Inventories are stated at the lower of cost or market value. Inventories are recorded at standard cost and adjusted to the approximate weighted-average cost at the balance sheet date. Market value represents replacement cost for raw materials, supplies and spare parts and net realizable value for work in process and finished goods. The Company assesses the impact of changing technology on its inventories on hand and writes off inventories that are considered obsolete. Period-end inventories are evaluated for estimated excess quantities and obsolescence based on a demand forecast within a specific time horizon, which is generally 180 days or less. Estimated losses on scrap and slow-moving items are recognized and included in the allowance for losses.

### **Investments Accounted for Using Equity Method**

Investments in companies wherein the Company exercises significant influence over the operating and financial policy decisions are accounted for using the equity method. The Company's share of the net income or net loss of an investee is recognized in the equity in earnings/losses of equity method investees, net account. Prior to January 1, 2006, the difference, if any, between the cost of investment and the Company's proportionate share of the investee's equity was amortized by the straight-line method over five years, with the amortization recorded in the equity in earnings/losses of equity method investees, net account. Effective January 1, 2006, pursuant to the revised Statement of Financial Accounting Standards No. 5, Long-term Investments in Equity Securities (SFAS No. 5), the cost of an investment shall be analyzed and the cost of investment in excess of the fair value of identifiable net assets acquired, representing goodwill, shall not be amortized and instead shall be tested for impairment annually. If the fair value of identifiable net assets acquired is in excess of the cost of investment, the excess shall be proportionately allocated as reductions to the fair value of non-current assets. The accounting treatment for the investment premiums acquired before January 1, 2006 is the same as that for goodwill which is no longer being amortized; while investment discounts continue to be amortized over the remaining periods. When an indication of impairment is identified, the carrying amount of the investment is reduced, with the related impairment loss recognized in earnings.

When the Company subscribes for additional investee's shares at a percentage different from its existing ownership percentage, the resulting carrying amount of the investment in the investee differs from the amount of the Company's share of the investee's equity. The Company records such a difference as an adjustment to long-term investments with the corresponding amount charged or credited to capital surplus.

Gains or losses on sales from the Company to equity method investees are deferred in proportion to the Company's ownership percentage in the investees until such gains or losses are realized through transactions with third parties. The entire amount of the gains or losses on sales to investees over which the Company has a controlling interest is deferred until such gains or losses are realized through subsequent sales of the related products to third parties. Gains or losses on sales from equity method investees to the Company are deferred in proportion to the Company's ownership percentages in the investees until they are realized through transactions with third parties. Gains or losses on sales between equity method investees are deferred in proportion to the Company's weighted-average ownership percentages in the investees that record such gains or losses until they are realized through transactions with third parties.

If an investee's functional currency is a foreign currency, translation adjustments will result from the translation of the investee's financial statements into the reporting currency of the Company. Such adjustments are accumulated and reported as a separate component of shareholders' equity.

#### **Financial Assets Carried at Cost**

Investments for which the Company does not exercise significant influence and that do not have a quoted market price in an active market and whose fair value cannot be reliably measured are carried at their original cost, such as non-publicly traded stocks and mutual funds. The costs of non-publicly traded stocks and mutual funds are determined using the weighted-average method. If there is objective evidence which indicates that a financial asset is impaired, a loss is recognized. A subsequent reversal of such impairment loss is not allowed.

The accounting treatment for cash dividends and stock dividends arising from financial assets carried at cost is the same as that for cash and stock dividends arising from available-for-sale financial assets.

#### **Property, Plant and Equipment and Assets Leased to Others**

Property, plant, and equipment and assets leased to others are stated at cost less accumulated depreciation. When an indication of impairment is identified, any excess of the carrying amount of an asset over its recoverable amount is recognized as a loss. If the recoverable amount increases in a subsequent period, the amount previously recognized as impairment would be reversed and recognized as a gain. However, the adjusted amount may not exceed the carrying amount that would have been determined, net of depreciation, as if no impairment loss had been recognized.

Significant additions, renewals and betterments incurred during the construction period are capitalized. Maintenance and repairs are expensed as incurred.

Depreciation is computed using the straight-line method over the following estimated service lives: buildings 10 to 20 years; machinery and equipment 5 years; and office equipment 3 to 5 years.

Upon sale or disposal of property, plant and equipment, the related cost and accumulated depreciation are deducted from the corresponding accounts, with any gain or loss recorded as non-operating gains or losses in the period of sale or disposal.

#### **Goodwill**

Goodwill represents the excess of the consideration paid for acquisition over the fair value of identifiable net assets acquired. Prior to January 1, 2006, goodwill was amortized using the straight-line method over the estimated life of 10 years. Effective January 1, 2006, pursuant to the newly revised Statement of Financial Accounting Standards No. 25, Business Combinations Accounting Treatment under Purchase Method (SFAS No. 25), goodwill is no longer amortized and instead is tested for impairment annually. If an event occurs or circumstances change which indicated that the fair value of goodwill is more likely than not below its carrying amount, an impairment loss is recognized. A subsequent reversal of such impairment loss is not allowed.

### **Deferred Charges**

Deferred charges consist of technology license fees, software and system design costs and other charges. The amounts are amortized over the following periods: Technology license fees the shorter of the estimated life of the technology or the term of the technology transfer contract; software and system design costs and other charges 3 years. When an indication of impairment is identified, any excess of the carrying amount of an asset over its recoverable amount is recognized as a loss. If the recoverable amount increases in a subsequent period, the previously recognized impairment loss would be reversed and recognized as a gain. However, the adjusted amount may not exceed the carrying amount that would have been determined, net of amortization, as if no impairment loss had been recognized.

### **Research and Development**

Expenditures arising from research activities and those related to development activities that do not meet the criteria for capitalization are charged to expense when incurred.

### **Pension Costs**

For employees under defined contribution pension plans, pension costs are recorded based on the actual contributions made to employees individual pension accounts during their service periods. For employees under defined benefit pension plans, pension costs are recorded based on actuarial calculations.

### **Income Tax**

The Company applies intra-period and inter-period allocations for its income tax, whereby (1) a portion of current period's income tax expense is allocated to the cumulative effect of changes in accounting principles; and (2) deferred income tax assets and liabilities are recognized for the tax effects of temporary differences and unused tax credits. Valuation allowances are provided to the extent, if any, that it is more likely than not that deferred income tax assets will not be realized. A deferred tax asset or liability is classified as current or noncurrent in accordance with the classification of its related asset or liability. However, if a deferred tax asset or liability does not relate to an asset or liability in the financial statements, then it is classified as either current or noncurrent based on the expected length of time before it is realized or settled.

Any tax credits arising from purchases of machinery, equipment and technology, research and development expenditures, personnel training expenditures, and investments in important technology-based enterprises are recognized using the flow-through method.

Adjustments of prior years' tax liabilities are added to or deducted from the current period's tax provision.

Income tax on unappropriated earnings at a rate of 10% is expensed in the year of shareholder approval which is the year subsequent to the year the earnings are generated.

The R.O.C. government enacted the Alternative Minimum Tax Act (the AMT Act), which became effective on January 1, 2006. The alternative minimum tax (AMT) imposed under the AMT Act is a supplemental tax levied at a rate of 10% which is payable if the income tax payable determined pursuant to the Income Tax Law is below the minimum amount prescribed under the AMT Act. The taxable income for calculating the AMT includes most of the income that is exempted from income tax under various laws and statutes. The Company has considered the impact of the AMT Act in the determination of its tax liabilities.

**Stock-based Compensation**

Employee stock option plans that are amended or have options granted on or after January 1, 2004 are accounted for by the interpretations issued by the Accounting Research and Development Foundation. The Company adopted the intrinsic value method and any compensation cost determined using this method is recognized in earnings over the employee vesting period.

**Treasury Stock**

The Company's stock held by subsidiaries is treated as treasury stock and reclassified from investments accounted for using equity method to treasury stock. The gains resulted from disposal of the treasury stock held by subsidiaries and cash dividends received by subsidiaries from the Company are recorded under capital surplus treasury stock transactions.

**Foreign-currency Transactions**

Foreign-currency transactions are recorded in New Taiwan dollars at the rates of exchange in effect when the transactions occur. Exchange gains or losses derived from foreign-currency transactions or monetary assets and liabilities denominated in foreign currencies are recognized in earnings. At the balance sheet date, monetary assets and liabilities denominated in foreign currencies are revalued at prevailing exchange rates with the resulting gains or losses recognized in earnings.

**3. ACCOUNTING CHANGES**

On January 1, 2006, the Company adopted the newly released Statements of Financial Accounting Standards No. 34, Financial Instruments: Recognition and Measurement (SFAS No. 34) and No. 36, Financial Instruments: Disclosure and Presentation.

The Company had categorized its financial assets and liabilities upon initial adoption of the newly released SFASs. The adjustments made to the carrying amounts of the financial instruments categorized as financial assets or financial liabilities at fair value through profit or loss were included in the cumulative effect of changes in accounting principles; the adjustments made to the carrying amounts of those categorized as available-for-sale financial assets were recognized as adjustments to shareholders' equity.

The effect of adopting the newly released SFASs is summarized as follows:

	<b>Recognized as Cumulative  Effect of Changes in  Accounting Principles (Net of Tax)</b>	<b>Recognized as a Separate Component of Shareholders Equity</b>
Financial assets or liabilities at fair value through profit or loss	\$ (246,186)	\$
Available-for-sale financial assets		
	\$ (246,186)	\$

The adoption of the newly released SFASs resulted in a decrease in net income before cumulative effect of changes in accounting principles of NT\$295,669 thousand, a decrease in net income of NT\$541,855 thousand, and a decrease in basic earnings per share (after income tax) of NT\$0.02, for the three months ended March 31, 2006.

Effective January 1, 2006, the Company adopted the newly revised SFAS No. 5 and SFAS No. 25, which prescribe that investment premiums, representing goodwill, be assessed for impairment at least on an annual basis instead of being amortized. Such a change in accounting principle did not have a material effect on the Company's financial statements as of and for the three months ended March 31, 2006.

#### 4. CASH AND CASH EQUIVALENTS

	March 31	
	2007	2006
Cash and deposits in banks	\$ 77,169,400	\$ 48,126,259
Repurchase agreements collateralized by government bonds	41,985,407	61,427,311
Asset-backed commercial papers	597,361	
Corporate notes		436,220
	\$ 119,752,168	\$ 109,989,790

#### 5. FINANCIAL ASSETS AND LIABILITIES AT FAIR VALUE THROUGH PROFIT OR LOSS

	March 31	
	2007	2006
Derivatives – financial assets		
Forward exchange contracts	\$	\$ 2,254
Cross currency swap contracts	159	56,291
	\$ 159	\$ 58,545
Derivatives – financial liabilities		
Forward exchange contracts	\$ 18,717	\$ 6,597
Cross currency swap contracts	115,085	347,617
	\$ 133,802	\$ 354,214

The Company entered into derivative contracts during the three months ended March 31, 2007 and 2006 to manage exposures due to fluctuations of foreign exchange rates. The derivative contracts entered into by the Company did not meet the criteria for hedge accounting prescribed by SFAS No. 34. Therefore, the Company discontinued applying hedge accounting treatment for its derivative contracts.

Outstanding forward exchange contracts as of March 31, 2007 and 2006:

	Maturity Date	Contract Amount (in Thousands)
March 31, 2007		
Sell EUR/Buy US\$	April 2007	EUR 23,000

March 31, 2006

Sell EUR/Buy US\$

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April 2006

EUR 30,500

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Outstanding cross currency swap contracts as of March 31, 2007 and 2006:

<b>Maturity Date</b>	<b>Contract Amount (in Thousands)</b>	<b>Range of Interest Rates Paid</b>	<b>Range of Interest Rates Received</b>
March 31, 2007			
April 2007 to June 2007	US\$835,000	2.65%-5.35%	1.65%-5.16%
March 31, 2006			
April 2006 to June 2006	US\$2,311,000	2.91%-5.65%	0.10%-2.04%

For the three months ended March 31, 2007 and 2006, net losses and net gains arising from derivative financial instruments were NT\$677,929 thousand (including realized settlement losses of NT\$510,436 thousand and valuation losses of NT\$167,493 thousand) and NT\$558,549 thousand (including realized settlement gains of NT\$854,218 thousand and valuation losses of NT\$295,669 thousand), respectively.

#### **6. AVAILABLE-FOR-SALE FINANCIAL ASSETS**

	<b>March 31</b>	
	<b>2007</b>	<b>2006</b>
Open-end mutual funds	\$ 23,976,854	\$ 19,085,320
Corporate bonds	4,163,115	11,961,405
Government bonds	4,152,738	4,884,533
Structured time deposits	499,288	499,091
Agency bonds		13,154,575
Corporate issued asset-backed securities		10,936,373
Corporate notes		97,863
Money market funds		90,509
Publicly-traded stocks		6,279
	32,791,995	60,715,948
Current portion	(26,325,390)	(58,815,063)
	\$ 6,466,605	\$ 1,900,885

In 2004, the Company entered into investment management agreements with three well-known financial institutions (fund managers) to manage its investment portfolios. In accordance with the investment guidelines and terms specified in these agreements, the securities invested by the fund managers cannot be below a pre-defined credit rating. In the second half year of 2006, the Company transferred investment portfolios managed by the fund managers of US\$1,277,789 thousand to TSMC Global Ltd. (TSMC-Global), a subsidiary of TSMC. The transferred investment portfolios held by TSMC Global are still being managed by the same fund managers in accordance with the aforementioned investment guidelines and terms.



Structured time deposits categorized as available-for-sale financial assets consisted of the following:

	<b>Principal Amount</b>	<b>Carrying Amount</b>	<b>Interest Rate</b>	<b>Maturity Date</b>
March 31, 2007				
Step-up callable deposits				
Domestic deposits	\$ 500,000	\$ 499,288	1.76%	March 2008

March 31, 2006

Step-up callable deposits				
Domestic deposits	\$ 500,000	\$ 499,091	1.76%	March 2008

The interest rate of the step-up callable deposits was pre-determined by the Company and the banks.

## 7. HELD-TO-MATURITY FINANCIAL ASSETS

	<b>March 31</b>	
	<b>2007</b>	<b>2006</b>
Corporate bonds	\$ 13,426,614	\$ 9,288,167
Structured time deposits	11,117,800	10,641,200
Government bonds	8,676,382	7,868,330
	33,220,796	27,797,697
Current portion	(6,523,668)	(9,120,093)
	\$ 26,697,128	\$ 18,677,604

Structured time deposits categorized as held-to-maturity financial assets consisted of the following:

	<b>Principal Amount</b>	<b>Interest Receivable</b>	<b>Range of Interest Rates</b>	<b>Maturity Date</b>
March 31, 2007				
Step-up callable deposits				
Domestic deposits	\$ 4,500,000	\$ 13,593	1.50%-1.83%	June 2007 to October 2008
Callable range accrual deposits				
Domestic deposits	3,970,680	14,752	(See below)	September 2009 to December 2009
Foreign deposits	2,647,120	7,390	(See below)	October 2009 to December 2009

\$ 11,117,800      \$ 35,735

(Continued)

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	<b>Principal Amount</b>	<b>Interest Receivable</b>	<b>Range of Interest Rates</b>	<b>Maturity Date</b>
March 31, 2006				
Step-up callable deposits				
Domestic deposits	\$ 3,500,000	\$ 16,881	1.40%-2.01%	June 2007 to March 2009
Callable range accrual deposits				
Domestic deposits	3,895,200	14,553	(See below)	September 2009 to December 2009
Foreign deposits	3,246,000	12,433	(See below)	October 2009 to January 2010
	\$ 10,641,200	\$ 43,867		

(Concluded)

The amount of interest earned by the Company for the callable range accrual deposits is based on a pre-defined range as determined by the 3-month or 6-month LIBOR plus an agreed upon rate ranging between 2.10% and 3.45%. Based on the terms of the contracts, if the 3-month or 6-month LIBOR moves outside of the pre-defined range, the interest paid to the Company is at a fixed rate between zero and 1.5%. Under the terms of the contracts, the bank has the right to cancel the contracts prior to the maturity date.

As of March 31, 2007 and 2006, the principal of the deposits that resided in banks located in Hong Kong amounted to US\$60,000 thousand and US\$80,000 thousand, respectively; those resided in banks located in Singapore amounted to US\$20,000 thousand.

**8. INVENTORIES, NET**

	<b>March 31</b>	
	<b>2007</b>	<b>2006</b>
Finished goods	\$ 3,477,094	\$ 3,075,200
Work in process	15,567,178	12,192,651
Raw materials	1,197,164	1,899,428
Supplies and spare parts	449,237	795,070
	20,690,673	17,962,349
Allowance for losses	(757,313)	(1,061,236)
	\$ 19,933,360	\$ 16,901,113

**9. INVESTMENTS ACCOUNTED FOR USING EQUITY METHOD**

	<b>March 31</b>			
	<b>2007</b>		<b>2006</b>	
	<b>Carrying Amount</b>	<b>% of Owner- ship</b>	<b>Carrying Amount</b>	<b>% of Owner- ship</b>
TSMC Global (Note 6)	\$ 43,771,405	100	\$	
TSMC International Investment Ltd. (TSMC International)	26,934,392	100	25,985,340	100
TSMC (Shanghai) Company Limited (TSMC-Shanghai)	9,127,747	100	9,352,101	100
Systems on Silicon Manufacturing Company Pte Ltd. (SSMC)	8,134,439	39	4,629,413	32
Vanguard International Semiconductor Corporation (VIS)	5,999,943	27	5,541,044	27
TSMC Partners, Ltd. (TSMC Partners)	4,572,167	100	4,106,947	100
TSMC North America (TSMC-North America)	2,107,864	100	1,826,618	100
Xintec Inc. (Xintec)	1,370,453	43		
VentureTech Alliance Fund II, L.P. (VTAF II)	801,222	98	630,569	98
Emerging Alliance Fund, L.P. (Emerging Alliance)	779,280	99	1,250,283	99
Global UniChip Corporation (GUC)	692,434	38	451,841	45
VentureTech Alliance Fund III, L.P. (VTAF III)	438,480	98		
Chi Cherng Investment Co., Ltd. (Chi Cherng)	118,167	36	78,197	36
Hsin Ruey Investment Co., Ltd. (Hsin Ruey)	116,793	36	77,470	36
TSMC Japan Limited (TSMC-Japan)	98,799	100	94,218	100
Taiwan Semiconductor Manufacturing Company Europe B.V. (TSMC-Europe)	56,633	100	23,302	100
TSMC Korea Limited (TSMC-Korea)	15,087	100		
	\$ 105,135,305		\$ 54,047,343	

In November 2006, the Company acquired 81 thousand shares in SSMC from EDB Investments Pte Ltd. under a Shareholders Agreement. After the acquisition, the number of SSMC shares owned by the Company increased from 382 thousand to 463 thousand; the percentage of ownership increased from 32% to 39%.

In January 2007, the Company acquired 90,526 thousand shares in Xintec, representing 43% of the total common shares, for NT\$1,357,890 thousand.

For the three months ended March 31, 2007 and 2006, net equity in earnings of NT\$853,184 thousand and NT\$2,972,039 thousand was recognized, respectively. The carrying amounts of the investments accounted for using the equity method and the related equity in earnings or losses of equity method investees were determined based on the reviewed financial statements of the investees as of and for the same periods ended as the Company.

**10. FINANCIAL ASSETS CARRIED AT COST**

	<b>March 31</b>	
	<b>2007</b>	<b>2006</b>
Non-publicly traded stocks	\$ 364,913	\$ 472,500
Mutual funds	381,492	340,854
	\$ 746,405	\$ 813,354

**11. PROPERTY, PLANT AND EQUIPMENT**

Accumulated depreciation consisted of the following:

	<b>March 31</b>	
	<b>2007</b>	<b>2006</b>
Buildings	\$ 51,483,606	\$ 44,728,744
Machinery and equipment	377,026,674	323,087,400
Office equipment	6,619,387	5,874,182
	\$ 435,129,667	\$ 373,690,326

No interest was capitalized during the three months ended March 31, 2007 and 2006.

**12. DEFERRED CHARGES, NET**

	<b>March 31</b>	
	<b>2007</b>	<b>2006</b>
Technology license fees	\$ 4,425,854	\$ 4,670,054
Software and system design costs	1,137,467	1,446,346
Others	30,317	63,070
	\$ 5,593,638	\$ 6,179,470

**13. BONDS PAYABLE**

	<b>March 31</b>	
	<b>2007</b>	<b>2006</b>
Domestic unsecured bonds:		
Issued in December 2000 and repayable in December 2007, 5.36% interest payable annually	\$ 4,500,000	\$ 4,500,000
Issued in January 2002 and repayable in January 2007, 2009 and 2012 in three installments, 2.60%, 2.75% and 3.00% interest payable annually, respectively	12,500,000	15,000,000
	17,000,000	19,500,000
Current portion	(4,500,000)	(2,500,000)
	\$ 12,500,000	\$ 17,000,000



As of March 31, 2007, future principal repayments for the Company's bonds were as follows:

<b>Year of Repayment</b>	<b>Amount</b>
2007 4 <sup>th</sup> quarter	\$ 4,500,000
2009	8,000,000
2012	4,500,000
	\$ 17,000,000

#### **14. OTHER LONG-TERM PAYABLES**

Most of the payables resulted from license agreements for certain semiconductor-related patents. As of March 31, 2007, future payments for other long-term payables were as follows:

<b>Year of Payment</b>	<b>Amount</b>
2007 (2 <sup>nd</sup> to 4 <sup>th</sup> quarter)	\$ 2,294,096
2008	751,617
2009	342,140
2010	342,140
2011	264,712
	3,994,705
Current portion (classified under accrued expenses and other current liabilities)	(2,371,524)
	\$ 1,623,181

#### **15. PENSION PLANS**

The Labor Pension Act (the Act) became effective on July 1, 2005. The employees who were subject to the Labor Standards Law prior to July 1, 2005 were allowed to choose to be subject to the pension mechanism under the Act with their seniority as of July 1, 2005 retained or continue to be subject to the pension mechanism under the Labor Standards Law. Employees who joined the Company after July 1, 2005 can only be subject to the pension mechanism under the Act.

The pension mechanism under the Act is deemed a defined contribution plan. Pursuant to the Act, the Company has made monthly contributions equal to 6% of each employee's monthly salary to employees' pension accounts starting from July 1, 2005, and recognized pension cost of NT\$148,533 thousand and NT\$155,461 thousand for the three months ended March, 2007 and 2006, respectively.

The Company has a defined benefit plan under the Labor Standards Law that provides benefits based on an employee's length of service and average monthly salary for the six-month period prior to retirement. The Company contributes an amount equal to 2% of salaries paid each month to a pension fund (the Fund), which is administered by the pension fund monitoring committee (the Committee) and deposited in the Committee's name in the Central Trust of China. The Company recognized pension cost of NT\$81,154 thousand and NT\$53,834 thousand for the three months ended March, 2007 and 2006, respectively.

Changes in the Fund under the defined benefit plan are summarized as follows:

	<b>Three Months Ended March 31</b>	
	<b>2007</b>	<b>2006</b>
Balance, beginning of period	\$ 1,913,002	\$ 1,658,864
Contributions	68,155	79,041
Interest	46,279	34,384
Payments		(4,678)
Balance, end of period	\$ 2,027,436	\$ 1,767,611

# 16. INCOME TAX

- a. A reconciliation of income tax expense based on income before income tax at statutory rate and income tax currently payable was as follows:

	<b>Three Months Ended March 31</b>	
	<b>2007</b>	<b>2006</b>
Income tax expense based on income before income tax at statutory rate (25%)	\$ 4,973,727	\$ 8,663,835
Tax effect of the following:		
Tax-exempt income	(991,862)	(3,772,846)
Temporary and permanent differences	(79,127)	(84,382)
Cumulative effect of changes in accounting principles		(82,062)
Income tax credits	(1,951,369)	(2,362,272)
Income tax currently payable	\$ 1,951,369	\$ 2,362,273

- b. Income tax expense consisted of the following:

Income tax currently payable	\$ 1,951,369	\$ 2,362,273
Other income tax adjustments		8,833
Net change in deferred income tax assets		
Investment tax credits	509,910	503,405
Temporary differences	(708,401)	(1,327,214)
Valuation allowance	(696,609)	255,072
Income tax expense	\$ 1,056,269	\$ 1,802,369

- c. Net deferred income tax assets consisted of the following:

	<b>March 31</b>	
	<b>2007</b>	<b>2006</b>
Current deferred income tax assets		
Investment tax credits	\$ 9,486,631	\$ 7,276,728



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Noncurrent deferred income tax assets, net		
Investment tax credits	\$ 9,960,351	\$ 16,085,638
Temporary differences	1,548,865	644,944
Valuation allowance	(6,507,620)	(9,665,618)
	\$ 5,001,596	\$ 7,064,964

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## d. Integrated income tax information:

The balance of the imputation credit account as of March 31, 2007 and 2006 was NT\$828,612 thousand and NT\$80,472 thousand, respectively.

The estimated and actual creditable ratio for distribution of earnings of 2006 and 2005 was 0.54 % and 2.88 %, respectively.

The imputation credit allocated to shareholders is based on its balance as of the date of dividend distribution. The estimated creditable ratio may change when the actual distribution of the imputation credit is made.

## e. All earnings generated prior to December 31, 1997 have been appropriated.

## f. As of March 31, 2007, investment tax credits consisted of the following:

<b>Regulation</b>	<b>Item</b>	<b>Total Creditable Amount</b>	<b>Remaining Creditable Amount</b>	<b>Expiry Year</b>
Statute for Upgrading Industries	Purchase of machinery and equipment	\$ 3,955,454	\$ 2,004,085	2008
		6,030,087	6,030,087	2009
		5,971,768	5,971,768	2010
		144,422	144,422	2011
		\$ 16,101,731	\$ 14,150,362	
Statute for Upgrading Industries	Research and development expenditures	\$ 1,627,095	\$ 1,627,095	2008
		1,534,230	1,534,230	2009
		1,534,050	1,534,050	2010
		440,265	440,265	2011
		\$ 5,135,640	\$ 5,135,640	
Statute for Upgrading Industries	Personnel training expenditures	\$ 40,734	\$ 40,734	2008
		40,442	40,442	2009
		\$ 81,176	\$ 81,176	
Statute for Upgrading Industries	Investments in important	\$ 79,804	\$ 79,804	2010

technology-based  
enterprises

- g. The profits generated from the following expansion and construction projects are exempt from income tax for a four-year or five-year period:

	<b>Tax-Exemption Period</b>
Expansion of Fab 2 to Fab 6	2003 to 2006
Construction of Fab 12 Module A	2004 to 2007
Construction of Fab 14 Module A	2006 to 2010

- h. The tax authorities have examined income tax returns of the Company through 2003.

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## 17. LABOR COST, DEPRECIATION AND AMORTIZATION

	Three Months Ended March 31, 2007		
	Classified		
	as		
	Classified	Operating	
	as		
	Cost of	Expenses	Total
	Sales		
Labor cost			
Salary	\$ 2,219,384	\$ 1,048,077	\$ 3,267,461
Labor and health insurance	160,974	86,039	247,013
Pension	149,674	80,013	229,687
Meal	104,780	38,199	142,979
Welfare	55,674	31,019	86,693
Others	30,552	1,171	31,723
	\$ 2,721,038	\$ 1,284,518	\$ 4,005,556
Depreciation	\$ 16,857,622	\$ 957,405	\$ 17,815,027
Amortization	\$ 458,751	\$ 206,968	\$ 665,719

Three Months Ended March 31, 2006				
		Classified		
		as		
		Classified	Operating	
		as		
		Cost of	Expenses	
		Sales	Total	
Labor cost				
Salary		\$ 2,585,763	\$ 1,029,808	\$ 3,615,571
Labor and health insurance		168,406	81,425	249,831
Pension		141,112	68,183	209,295
Meal		115,836	39,662	155,498
Welfare		48,480	24,345	72,825
Others		51,769	3,614	55,383
		\$ 3,111,366	\$ 1,247,037	\$ 4,358,403
Depreciation		\$ 14,548,962	\$ 818,442	\$ 15,367,404
Amortization		\$ 364,266	\$ 237,773	\$ 602,039

## **18. SHAREHOLDERS EQUITY**

As of March 31, 2007, 888,740 thousand ADSs of the Company were traded on the NYSE. The number of common shares represented by the ADSs was 4,443,698 thousand (one ADS represents five common shares).

Capital surplus can only be used to offset a deficit under the Company Law. However, the capital surplus generated from donations and the excess of the issuance price over the par value of capital stock (including the stock issued for new capital, mergers, convertible bonds and the surplus from treasury stock transactions) may be appropriated as stock dividends, which are limited to a certain percentage of the Company's paid-in capital.

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Capital surplus consisted of the following:

	<b>March 31</b>	
	<b>2007</b>	<b>2006</b>
From merger	\$ 24,003,546	\$ 24,003,546
Additional paid-in capital	20,063,728	23,341,345
From convertible bonds	9,360,424	9,360,424
From long-term investments	414,524	196,129
From treasury stock transactions	389,188	306,868
Donations	55	55
	<b>\$ 54,231,465</b>	<b>\$ 57,208,367</b>

The Company's Articles of Incorporation provide that, when allocating the net profits for each fiscal year, the Company shall first offset its losses in previous years and then set aside the following items accordingly:

- a. Legal capital reserve at 10% of the profits left over, until the accumulated legal capital reserve has equaled the Company's paid-in capital;
- b. Special capital reserve in accordance with relevant laws or regulations or as requested by the authorities in charge;
- c. Bonus to directors and supervisors and bonus to employees of the Company of not more than 0.3% and not less than 1% of the remainder, respectively. Directors who also serve as executive officers of the Company are not entitled to receive the bonus to directors and supervisors. The Company may issue stock bonus to employees of an affiliated company meeting the conditions set by the Board of Directors or, by the person duly authorized by the Board of Directors;

- d. Any balance left over shall be allocated according to the resolution of the shareholders' meeting.

The Company's Articles of Incorporation also provide that profits of the Company may be distributed by way of cash dividend and/or stock dividend. However, distribution of profits shall be made preferably by way of cash dividend. Distribution of profits may also be made by way of stock dividend; provided that the ratio for stock dividend shall not exceed 50% of the total distribution.

Any appropriations of the profits are recorded in the year of shareholder approval and given effect to in the financial statements of that year.

The appropriation for legal capital reserve shall be made until the reserve equals the Company's paid-in capital. The reserve may be used to offset a deficit, or be distributed as dividends and bonuses for the portion in excess of 50% of the paid-in capital if the Company has no unappropriated earnings and the reserve balance has exceeded 50% of the Company's paid-in capital. The Company Law also prescribes that, when the reserve has reached 50% of the Company's paid-in capital, up to 50% of the reserve may be transferred to capital.

A special capital reserve equivalent to the net debit balance of the other components of shareholders' equity (for example, cumulative translation adjustments and unrealized loss on financial instruments, but excluding treasury stock) shall be made from unappropriated earnings pursuant to existing regulations promulgated by the Securities and Futures Bureau (SFB). Any special reserve appropriated may be reversed to the extent that the net debit balance reverses.

The appropriations of earnings for 2006 and 2005 had been approved in a Board of Directors meeting held on February 6, 2007 and a shareholders meeting held on May 16, 2006, respectively. The appropriations and dividends per share were as follows:

	Appropriations of Earnings		Dividends Per Share (NT\$)	
	For Fiscal	For Fiscal	For	For
	Year 2006	Year 2005	Fiscal Year 2006	Fiscal Year 2005
Legal capital reserve	\$ 12,700,973	\$ 9,357,503		
Special capital reserve	(11,192)	(1,585,685)		
Bonus to employees in cash	4,572,798	3,432,129		
Bonus to employees in stock	4,572,798	3,432,129		
Cash dividends to shareholders	77,489,064	61,825,061	\$ 3.00	\$ 2.50
Stock dividends to shareholders	516,594	3,709,504	0.02	0.15
Bonus to directors and supervisors	285,800	257,410		
	\$ 100,126,835	\$ 80,428,051		

The Board of Directors meeting held on February 6, 2007 also resolved to distribute stock dividends out of capital surplus in the amount of NT\$774,891 thousand.

The amounts of the appropriations of earnings for 2005 are consistent with the resolutions of the meeting of the Board of Directors held on February 14, 2006. The amounts of the appropriations of earnings for 2006 and the stock dividends to be distributed out of capital surplus have not yet been resolved by the shareholders. If the above bonus to employees, directors and supervisors had been paid entirely in cash and charged to earnings of 2006 and 2005, the basic earnings per share (after income tax) for the years ended December 31, 2006 and 2005 shown in the respective financial statements would have decreased from NT\$4.93 to NT\$4.56 and NT\$3.79 to NT\$3.50, respectively. The shares distributed as a bonus to employees represented 1.77% and 1.39% of the Company's total outstanding common shares as of December 31, 2006 and 2005, respectively.

The information about the appropriations of bonus to employees, directors and supervisors is available at the Market Observation Post System website.

Under the Integrated Income Tax System that became effective on January 1, 1998, R.O.C. resident shareholders are allowed a tax credit for their proportionate share of the income tax paid by the Company on earnings generated since January 1, 1998.

#### 19. STOCK-BASED COMPENSATION PLANS

The Company's Employee Stock Option Plans under the 2004 Plan, 2003 Plan and 2002 Plan were approved by the SFB on January 6, 2005, October 29, 2003 and June 25, 2002, respectively. The maximum number of options authorized to be granted under the 2004 Plan, 2003 Plan and 2002 Plan was 11,000 thousand, 120,000 thousand and 100,000 thousand, respectively, with each option eligible to subscribe for one common share when exercisable. The options may be granted to qualified employees of the Company or any of its domestic or foreign subsidiaries, in which the Company's shareholding with voting rights, directly or indirectly, is more than fifty percent (50%). The options of all the plans are valid for ten years and exercisable at certain percentages subsequent to the second anniversary of the grant date. Under the terms of the plans, the options are granted at an exercise price equal to the closing price of the Company's common shares listed on the TSE on the grant date.

Options of the aforementioned plans that had never been granted or had been granted but subsequently cancelled had expired as of March 31, 2007.





Information about outstanding options for the three months ended March 31, 2007 and 2006 was as follows:

	<b>Number of Options (in Thousands)</b>	<b>Weighted- Average Exercise Price (NT\$)</b>
Three months ended March 31, 2007		
Balance, beginning of period	52,814	39.6
Options exercised	(3,271)	37.3
Options cancelled	(252)	47.2
Balance, end of period	49,291	39.7
Three months ended March 31, 2006		
Balance, beginning of period	67,758	42.1
Options exercised	(3,028)	38.8
Options cancelled	(1,117)	46.6
Balance, end of period	63,613	42.2

The number of outstanding options and exercise prices have been adjusted to reflect the distribution of dividends in accordance with the plans.

As of March 31, 2007, information about outstanding and exercisable options was as follows:

<b>Range of Exercise Price (NT\$)</b>	<b>Options Outstanding</b>			<b>Options Exercisable</b>	
	<b>Number of Options (in Thousands)</b>	<b>Weighted- average Remaining Contractual Life (Years)</b>	<b>Weighted- average Exercise Price (NT\$)</b>	<b>Number of Options (in Thousands)</b>	<b>Weighted- average Exercise Price (NT\$)</b>
\$27.6-\$39.7	31,782	3.92	\$ 35.5	27,625	\$ 34.9
\$45.1-\$52.3	17,509	5.65	47.5	6,495	47.0
	49,291			34,120	

No compensation cost was recognized under the intrinsic value method for the three months ended March 31, 2007 and 2006. Had the Company used the fair value based method (based on the Black-Scholes model) to evaluate the options granted after January 1, 2004, the assumptions and pro forma results of the Company for the three months

ended March 31, 2007 and 2006 would have been as follows: