

# 2005 ANNUAL REPORT



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## HIGHLIGHT

	The Bank			HNFHC (Consolidated)
	31.12.2004	31.12.2005	31.12.2005	31.12.2005
WORLDWIDE RANKING:				
The banker - by Tier 1 Capital (July)	222	237	-	-
The banker - by Total Assets (July)	192	191	-	-
CAPITAL ADEQUACY RATIO (%)	12.29	12.77		

	Millions of N.T. Dollar		Millions of U.S. Dollar 31.12.2005	Millions of N.T. Dollar 31.12.2005
	31.12.2004	31.12.2005		
FINANCIAL ITEMS:				
BALANCE SHEET ITEMS:				
Total Assets	1,508,428	1,584,445	50,854	1,671,049
Total Deposits and Remittances Payable	1,217,326	1,292,091	39,031	1,282,563
Total Loans, Discounts and Bills Purchased	885,730	945,415	28,685	942,600
Stockholders' Equity	65,040	71,735	2,726	89,566
INCOME STATEMENT ITEMS:				
Interest Revenues	31,870	36,526	1,158	38,047
Total Operating Revenues	47,894	53,813	2,070	68,031
Income (Loss) before Income Tax	13,000	11,906	340	11,187
Net Income (Loss)	9,963	9,403	290	9,528

PROFITABILITY:				
Earning (Loss) Per Share	2.69	2.54	0.05	1.60
ADDITIONAL DATA:				
Employees	7,322	7,738	-	10,014
Domestic Branches	182	182	-	264
Domestic Sub-branches	13	13	-	17
Overseas Branches	5	5	-	5
Overseas Representative Offices	2	2	-	2

Note : The Exchange Rate as of December 31, 2005 was NT\$32.86 to US\$1.

# Honesty

We provide professional and trustworthy services with honesty and integrity.



## MESSAGE TO OUR SHAREHOLDERS



Chairman Ming-cheng Lin

The continued rise in international crude oil and raw materials prices over the past year caused the global economic expansion to lose steam, which in turn impacted Taiwan's economy. In order to ward off the threat of inflation, major economies gradually hiked interest rates. The slowing global economy also impacted Taiwan's exports, causing momentum here to wane. In the first quarter, domestic industrial production and manufacturing output contracted 0.62% and 1.19% compared with the year earlier period. Economic growth in the first and second quarters slowed to 2.49% and 2.97%, respectively, compared with 5.51% growth in the third quarter of 2004. Taiwan's economic growth for the first six months of 2005 was only 2.73%. Starting in August and September, however, growth began to accelerate in Taiwan's two main export markets, namely the United States and China. In addition, international demand for information and electronics products rose. This, coupled with the traditional Christmas season and Chinese Lunar New Year demand, helped spark Taiwan's economy. Industrial production and manufacturing output rebounded handsomely. By the fourth quarter, annual growth returned to about 10%. The composite economic indicator flashed green in August, indicating stable growth, and continued to do so for the remaining months of the year. Economic growth in the third quarter rebounded to 4.38%, compared with 2.97% in the second quarter. Growth further gained steam to 6.40% in the fourth quarter. Despite the challenges presented by the economic situation, Hua Nan Commercial Bank was able to put in an impressive performance for the year, whether it be in terms of profitability or improvement in operational structure.



The Bank last year posted after tax profit of NT\$9.428 billion, reaching 97.24% of its internal target. In addition, in light of the Bank's prudent policies in writing off large amounts of bad loans in recent years, Hua Nan's overdue loan ratio fell to 2.12% in 2005 from 2.27% in the previous year. Sales of collateral associated with bad debts that had been written off helped bring in income of over NT\$5.7 billion last year. This outstanding performance confirms that the Bank has one of the highest levels of asset quality among its local counterparts and has an excellent level of financial transparency.

The Bank has undertaken organizational restructuring to better meet the rapid changes in the banking environment. Last year, it contracted Watson Wyatt to draw up a plan to bolster organizational performance. The plan included organizational diagnosis, performance management systems, performance-based remuneration, and change management. The organizational restructuring plan was approved in August, after which a management and planning task force was established to oversee and ensure smooth implementation of the plan.

In the first half of 2005, growth in the international economy began to weaken due to continued rises in international crude and raw materials prices. Central banks throughout the world gradually raised interest rates in an attempt to keep inflationary pressure in check. This, along with weak exports, triggered an economic slowdown on Taiwan. In the first quarter, industrial production and manufacturing output staged rare contractions, by 0.62% and 1.19%, respectively. In light of the export slowdown, Taiwan posted trade deficits of between US\$100 million and US\$400

million in January, March and June. Meanwhile, the composite economic indicator, which signals the state of the economy, fell into the yellow-blue level for five months starting in March, indicating weak growth. At one point, the composite index fell to 18, which is the lowest score in the yellow-blue level. Economic growth in the first and second quarters stood at only 2.49% and 2.97%, respectively, compared with a peak of 5.51% in the third quarter of 2004. Growth in the first half of 2005 was only 2.73%.

Starting in August and September, an economic upturn in the United States and China, which are Taiwan's two largest export markets, and increased international demand for information and electronics products, helped spark industrial production and manufacturing output here. Christmas-and Chinese Lunar New Year-related demand also boosted demand, enabling Taiwan's external trade situation to rebound. The composite economic indicator flashed green in each month from August to December, signifying stable growth. According to preliminary data from the Directorate General of Budget, Accounting and Statistics, economic growth in the third quarter accelerated to 4.38%, compared with a pace of 2.97% in the second quarter. Growth further hastened to 6.40% in the fourth quarter. For 2005 as a whole, economic growth stood at 4.09%.

On the domestic monetary front, growth in bank lending waned in the first half of 2005 in reflection of the slowing economy. Average annual growth in the M2 money supply fell from 6.20% in January to a low of 5.57% in April. For the first half of the year, annual growth in the M2 was 6.03%. Bank lending and investment growth staged a short rebound early in the second half of the year. This caused M2 growth to accelerate to peaks of 6.51% and 6.52% in July and August, respectively. M2 growth then began to wane, easing to 6.14% in November. For 2005 as a whole, M2 growth was 6.22%, which fell within the central bank's target range of 3.5-7.5%. Generally speaking, the money supply was flush in 2005. Interest rates, however, began to rebound. In light of the high level of liquidity in the banking system in 2004, the interbank overnight lending rate traded at levels below 1.2%. Starting early in 2005, however, interest rates began to head north as central banks throughout the world hiked rates. The interbank overnight rate, which stood at 1.202% in January, rose to 1.406% in December. Furthermore, in an effort to maintain price stability, prevent expectations of higher inflation, reduce domestic and overseas interest rate differentials and rectify the situation in which real interest rates here were negative, the board of governors of Taiwan's Central Bank of China hiked the bank's rediscount rate, accommodations rate against secured loans, and interest rate on accommodation without collateral four times. Interest rates rose from 1.75%, 2.125% and 4.0%, to 2.25%, 2.625% and 4.5%, respectively. In the currency market, the twin deficits of the United States continued to put a drag on the US dollar in the beginning of the year. In addition, Europe and the US continued to put pressure on the Chinese government to quickly implement a more flexible currency system for the yuan. These factors caused the New Taiwan dollar to rise sharply in the first quarter. In the second quarter, the US dollar rebounded from its big drop. In addition, economic fundamentals in the US were quite strong, causing the US dollar to regain ground against the NT dollar. In the third and fourth quarters, the US Federal Reserve continued hiking interest rates, causing the interest rate differential between the US and Taiwan to widen. This caused further pressure on the NT dollar to depreciate. At the end of 2005, the NT dollar had depreciated 2.84% against the US dollar in comparison with the end of 2004. The local currency, however,

appreciated 11.21% against the yen and 11.61% against the euro.

Hua Nan faced considerable challenges last year amid this complex, unpredictable and rapidly changing environment. Thanks to the efforts and contributions of the board, supervisors and shareholders, the Bank was able to maintain steady growth. Taiwan Ratings Corp. in its latest ratings (July 13, 2005) of the Bank assigned Hua Nan twAA- and twA-1, with a stable outlook. In addition, Moody's in September 2005 assigned ratings to the Bank of A3/P-1, with a stable outlook. Hua Nan has great expectations for 2006. Described below are introductions into the bank's performance last year, including operations, research and development, the results of business projects, the state of budget execution, income and expenditures, and profitability.

## 1. Key Operational Measures and the State of R&D

Hua Nan's main operational measures in 2005 included : 1) Amending account opening procedures for the visually impaired, in line with a directive by the Banking Bureau of the Financial Supervisory Commission. In addition to the current system of having a court notary, the prospective customer can appoint a witness to provide assistance or another bank employee not involved in the account opening process to serve as a third witness ; 2) Introducing home banking operations ; 3) Providing the ability to pay premiums for compulsory vehicle insurance via Internet banking and Internet ATMs ; 4) Strengthening Internet banking and Internet ATM networks, and offering comprehensive travel insurance services through the Internet ; 5) Simplifying operational procedures and reducing waiting times for customers with regards to time deposits ; 6) Introducing corporate issuance or check cashing and financing services for Level 1-5 companies based on TCRI ratings ; 7) Introducing SME credit guarantee fund tranche guarantee services, which helps to expand SME loan operations and raise the Bank's BIS ratio ; 8) Introducing electronic domestic letters of credit and negotiations with China Steel being the beneficiary. This meets the needs of China Steel in computerizing all of its domestic LC/negotiation business ; 9) Introducing labor pension loans to provide capital needed to make monthly labor pension contributions or contributions to labor pension reserve funds ; 10) Introducing domestic private sector patent litigation loans. These loans are being offered in conjunction with plans by the Ministry of Economic Affairs to assist local private sector firms in international patent lawsuits or judgments, and helping the local corporate sector in raising its foreign competitiveness ; 11) Introducing new consumer loan screening guidelines to centralize and standardize the review of loan applications ; 12) Serving as an agent to collect and pay public utility fees, parking fees and tuition, helping to boost credit card handling fee income and efficiency ; 13) In order to broaden the payment network for cardholders, the Bank in 2005 contracted Family Mart, OK, and Life convenience stores to serve as agents so that cardholders can pay credit card bills at these outlets. This brings to five convenience store chains (contracts were previously signed with Nikomart and President) where cardholders can pay their bills ; 14) The Bank is cooperating with VIA Cord Blood Stem Foundation to issue a VIA card. This cooperation with Taiwan's first public service cord blood storage institution will attract pregnant women to store blood at the foundation and enable them to be Bank cardholders ; 15) The Bank has introduced credit card cash advance installment plans to raise credit card



handling fee income and boost the utilization of Bank funds. In 2005, a total of NT\$381.99 million of funds were approved, providing handling fee income of NT\$18.35 million ; 16) The Bank has established a credit card loyalty management system (LMS) in conjunction with the issuance of IC cards and the needs of contracted vendors. The LMS system included in the chip enables the Bank to implement various loyalty point or promotional activities ; 17) The Bank has introduced services through its Internet banking facility to transfer passbook foreign currency deposits into time deposits ; 18) Hua Nan has introduced partial credit and risk guarantee services in line with the Asian Development Bank's Trade Finance Facilitation Program, helping Taiwan companies to expand into Asian markets and to strengthen its cooperation relationship with the ADB ; 19) The Bank has introduction swaptions, which satisfy the needs of customers in terms of managing interest rate risk and helping to provide an array of financial services ; 20) Hua Nan applied to the State Bank of Vietnam on August 10, 2005 to upgrade its representative office in Ho Chi Minh City to a branch ; 21) Began offering foreign currency investment products and interest rate options at its Hong Kong branch to broaden its array of services ; 22) Continued to strengthen its range of domestic and foreign investment options, such as mutual funds, structured bonds, bonds of foreign governments and institutions, and other securities worthy of investment for financial trusts and personal trusts ; 23) Continued to expand its custodian operations to increase handling fee income, and also developed custodian services for private placement funds and other new financial products ; 24) Continued to promote children's education, insurance, and pension personal trusts, as well as equity trusts, inheritance trusts, and real estate trusts ; 25) Developed an electronic platform for domestic LC and negotiations, enabling customers to engage in such services via the CDS platform. This provides customers an electronic means to complete, amend or nullify LCs or apply for negotiations. The CDS platform encrypts information and then forwards it to the bank or appropriate business units, which then use an Intranet system to screen the applications ; 26) Developed a wealth management VIP system that provides information on the amount of business generated by customers, management, sales and marketing assistance, business and investment analysis, and personal finance planning, enabling the Bank to strengthen operations in the area and provide services to its best customers ; 27) The Bank enables customers using an IC banking card from any bank to access its eATM system using a special card reader. Customers can check balances, carry out fund transfers, pay taxes and bills, and pay insurance premiums online ; 28) The Bank continued to create central operations centers. After completing the establishment of its Taipei central operations center and its Greater Taipei branch check clearing center, it has set up a central operations center in Kaohsiung and check clearing centers in Taoyuan, Hsinchu, Kaohsiung and for other areas ; 29) Establishment of an e-TABS (NT dollar) system. This system helps to raise teller service quality and provide comprehensive customer services. Utilizing Windows as an operating platform, the system integrates the NT dollar system, as well as foreign exchange import, export and OBU operations in a single workstation.

The Bank continued to encourage employees to express their ideas in research and development work. During the year, staff produced 300 R&D proposals, with the bank adopting 92 of these. A total of NT\$86,800 in bonuses were granted to those responsible for the ideas.

## 2. Results of Operational Plans and Budget Execution

All areas of the Bank's business performed well in 2005 thanks to the efforts of employees. Average total deposits (not including interbank deposits) stood at NT\$1.174 trillion, which was three percent higher than the Bank's target of NT\$1.142 trillion. Average outstanding loans amounted to NT\$868.4 billion, which was only 0.5 percent short of the Bank's target of NT\$873.0 billion. The Bank handled foreign exchange business of US\$181.0 billion, a growth of 6.89%.

## 3. Income, Expenditures and Profitability

After tax profit in 2005 came to NT\$9.43 billion, which was 97.24% of the Bank's internal target. Total income was NT\$54.50 billion. Operating income accounted for 98.75% of that amount (interest income 67.03%, recovery of bad loans 10.54%, profit associated with bills trading 10.08%, commission fee income 7.96%, and other revenue 3.14%). Meanwhile, non-operating income accounted for 1.25% of total income. Total expenditures came to NT\$42.59 billion, which was 78.15% of total income. Operating expenses accounted for 77.67% (interest expenditure 35.29%, business and management expense 24.90%, provisioning 14.87%, and other expense 2.61%). Non-operating expenditures and losses accounted for 0.48%. Tax expense stood at 4.59% of the total and after tax profit 17.26%.

In summary, in 2005 Hua Nan faced a number of challenges associated with the economic situation at home and abroad, as well as keen competition from counterparts. Still, the Bank put in an outstanding performance. In the future, the Bank will continue to work in conjunction with the directions set by Hua Nan Financial Holdings, and will operate according to its long-held tenets of trust, sincerity and innovation. The Bank will continue to pursue diversified businesses, automated operations and providing services to the public at large. We hope that directors, supervisors and shareholders will continue to provide us with direction, enabling the Bank to scale to greater heights in the future.

Chairman Lir



President Lee



# Efficiency

We provide We respond to customer's need with swift actions and trustworthy services with honesty and integrity.



## BRIEF HISTORY

### 1. Brief History

Hua Nan Bank was founded in 1919 with capital of 10 million yen. Founders included the prominent local entrepreneur, Mr. Lin Hsiung-cheng, and several Southeast Asian overseas Chinese investors. The founding ceremony was held on January 29, 1919 and Mr. Lin Hsiung-cheng served as Chairman. The Bank was established for the purpose of promoting both domestic and international investment, and maintained a head office in Taipei. The Bank started business in March 1919. Subsequently, the Bank set up branches in Canton, Haiphong, Saigon, Rangoon, Singapore, Tokyo and other cities throughout Asia, helping to contribute to the development of trade between Taiwan and Southeast Asia. Private banks in Taiwan ran into operational difficulties during the 1930's Depression, and the government engineered some to merge. Thanks to the efforts of Mr. Lin Hsiung-cheng and his partners, the Bank avoided being merged. Mr. Lin Hsiung-cheng served as Chairman from 1919 to 1944. In 1944, Bank of Taiwan used its majority ownership in the bank to reassign Mr. Akekula as Chairman, and Mr. Lin Hsiung-cheng became Chairman Emeritus.

Following the retrocession of Taiwan to China on October 25, 1945, Mr. Lin Hsiung-cheng, as Chairman of the Commercial Association of Taiwan, was selected as Taiwan Province representative to participate in the ceremony that reinstated the R.O.C. capital. He also carried out the important mission of seeking support from the R.O.C. authorities to ensure the continued viability of Hua Nan Commercial Bank. He passed away on November 27, 1946. On February 22, 1947, the Bank held a shareholders' meeting, during which Mr. Liu Chi-kuang was nominated by the board to become Chairman. Upon its inception, the Bank mainly focused on business activities within Taiwan Province, serving with other banks to help finance the construction of a new Taiwan. On May 3, 1947, the Bank merged with Taiwan Trust Company, the latter becoming the Bank's newly-formed Trust Department, and increased capital to 25 million Old Taiwan dollars to enlarge the Bank's scope of business and build a solid capital base. By June 1948 more than 60 branches staffed with high caliber employees had been established throughout Taiwan. Hua Nan Commercial Bank thus became well-known and highly regarded as a sound and solid financial institution.

In 1948 when Taiwan's economy began to be seriously impacted by the economic slump in mainland China, the Bank revised its business focus, reducing low yield business while promoting more profitable business. During this time, the Bank again increased capital to 1 billion Old Taiwan dollars. In the period since monetary reform on June 15, 1949 through May 18, 2001, the Bank increased capital a number of times to reach the present amount of NT\$37,091,000,000, positioning it as one of the soundest and largest banks in Taiwan.

A large number of government-owned shares was released on January 22, 1998, enabling the Bank to complete privatization and embark upon a new era. In order to adapt to government financial reforms and changes in the financial environment, to achieve synergy through diversification, and to meet long-term development needs, the Bank and Entrust Securities Co. each convened extraordinary shareholders' meetings on November 14, 2001 and passed a proposal to establish Hua Nan Financial Holdings Co., Ltd. (HNFHC) via a 100% stock conversion. Mr. Lin, Ming-cheng was elected as the Chairman of the board. On December 19, 2001 HNFHC started business and its shares listed on the Taiwan Stock Exchange. HNFHC, with registered capital of NT \$100 billion, maintains its head office in Taipei. The Bank accordingly became a subsidiary of HNFHC.

## 2. ORGANIZATION

The Shareholders' Meeting serves as the highest decision-making body of the important matters in the Bank's organizational structure. All matters including appointment of directors and supervisors, establishment and amendment of internal rules and regulations, increase of capital, appropriation of earnings and dividends, and other matters, are decided upon during Shareholders' Meetings of which there are two types --- Ordinary and Extraordinary. The Ordinary Meeting is held once a year, while the latter type is held when necessary as called for by the Directors or Supervisors.

The Board of Directors and Board of Supervisors serve to formulate strategy, carry out bank policies, and execute and supervise business activities. The Directors and Supervisors, who number fifteen and five, are separately appointed by the shareholders through the Shareholders' Meeting.

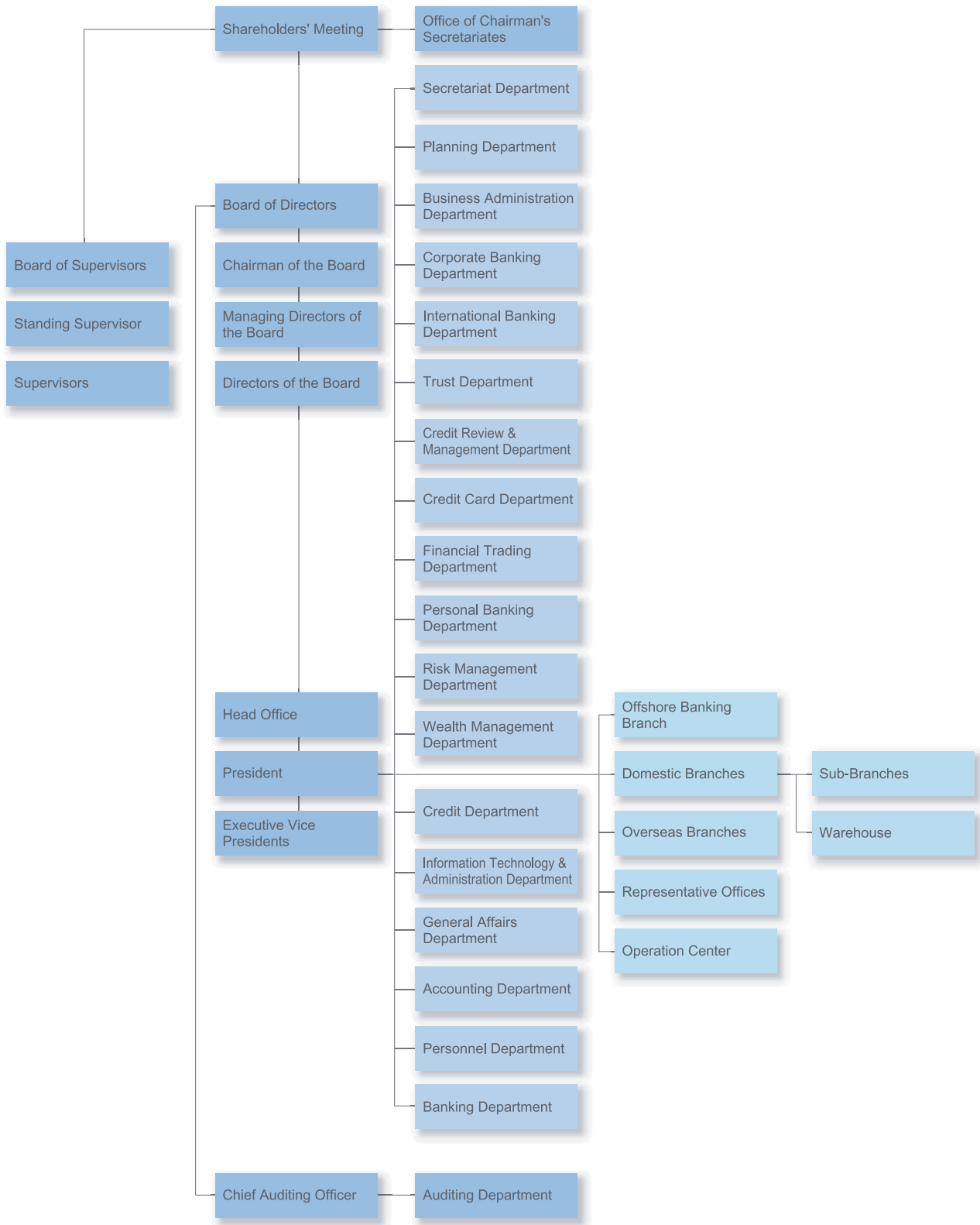
The Directors among themselves elect five Managing Directors, who elect a Chairman one another. Internally, the Chairman is the head of the Shareholders' Meeting, Board of Directors and Board of Managing Directors, while, externally, the Chairman represents the Bank.

A Board of Directors meeting is held once every three months. In case of emergency or if more than half of the Directors so request, an Extraordinary Meeting may be held. The Managing Directors reside in the Bank acting on behalf of shareholders, and may assist in carrying out business activities. Under the Board of Directors, we established the Auditing Department with chief auditor being the department head responsible for all auditing related business.

The Board of Supervisors is formed by five Supervisors, who elect a Standing Supervisor one another. The Standing Supervisor is resident in the Bank, where he or she is charged with execution of supervisory duties.

The Bank was established as a company limited by shares in accordance with the regulations set forth in the Banking Laws. The head office is located in Taipei City. In terms of management, the Bank has one president who is responsible for all business activities and who acts in accordance with resolutions passed at the Board of Directors meetings. Three Executive Vice Presidents are appointed to assist the President. As of December 2005, in accordance with internal regulations governing organizational structure, the Bank maintained eighteen departments at the head office: Secretariat Department, Planning Department, Business Administration Department, Corporate Banking Department, International Banking Department, Trust Department, Credit Review & Management Department, Credit Card Department, Financial Trading Department, Personal Banking Department, Risk Management Department, Wealth Management Department, Credit Department, Information Technology & Administration Department, General Affairs Department, Accounting Department, Personnel Department and Banking Department. The Bank further maintains 182 branches within Taiwan, and 13 sub-branches around the island. The Bank also operates one warehouse. Overseas branches are located in Los Angeles, New York, Hong Kong, Singapore and London, with two representative offices in Shenzhen and Ho Chi Minh City. As of 31 December 2005 the Bank's manpower resources totaled 7,738 personnel.

## ORGANIZATION CHART FOR HUA NAN BANK



## BOARD OF DIRECTORS AND SUPERVISORS

2006.6.9

NAME	CURRENT POSITION	EXPERIENCE	EDUCATION
Ming-cheng Lin	Chairman, Hua Nan Commercial Bank, Ltd. Director, The Central Bank of China. Chairman, Memorial Scholarship Foundation to Mr. Lin Hsiung-Chen	Vice Chairman, Hua Nan Commercial Bank, Ltd. President, Ta-Yung Shing Yeh Corp.	Master of Laws, Keio University, Japan.
Lee, Jeng-Yih	Managing Director & President, Hua Nan Commercial Bank, Ltd.	Executive Vice President, Hua Nan Commercial Bank, Ltd.	Dept. of Economics, National Taiwan University.
Yun Lin	Managing Director, Hua Nan Commercial Bank, Ltd. Professor, Dept. of Finance, National Taiwan University.	Chairman of Finance Dept., National Taiwan University.	Ph.D. Univ. of Illinois Urbana Champaign, U.S.A.
Hsien-Hsien Hsu	Managing Director, Hua Nan Commercial Bank, Ltd. Director, Prince Motors Co., Ltd. Assistant to the Chairman of Shin-Kong Wu Ho-Su Memorial Hospital	Director & Supervisor, Shin-Kong Life Insurance Co., Ltd.	Department of Economics, Meiji University, Japan.
Hsieh Chuan Chuan	Director, Hua Nan Commercial Bank, Ltd. S.V.P. & General Manager, Loans & Discounts Dept., Bank of Taiwan.	Vice President & Deputy General Manager, Loans & Discounts Dept., Bank of Taiwan.	Business Dept., National Taiwan University.
Ya-hwei Yang	Director, Hua Nan Commercial Bank, Ltd. Research Fellow, Chung-Hua Institution for Economic Research.	Director, Division of Taiwan Economy.	Ph.D. of Economics, National Taiwan University.
Chen, Chan-Sheng	Director, Hua Nan Commercial Bank, Ltd. President, Central Deposit Insurance Corp.	Manager, Bank Examination Dept., The Central Bank of China. President, Central Deposit Insurance Corp.	Tamkang University Accounting Dept.
Shu-shai Yen Chen	Director, Hua Nan Commercial Bank, Ltd. Manager, Wellin Investment Co., Ltd.	Director, Taipei Business Bank	Shih Chien University.
Tommy Lin	Director, Hua Nan Commercial Bank, Ltd. Special Assistant To The Chairman, Yong Da Construction Co., Ltd.	Fund Manager, Mercury Asset management Co., Ltd. (Japan)	J.D. Law, Univ. of California Los Angeles, U.S.A

NAME	CURRENT POSITION	EXPERIENCE	EDUCATION
Hsu Chen, An-Lan	Director, Hua Nan Commercial Bank, Ltd. Director, Hua Nan Securities Co., Ltd.	Chairman, Yuan Ding Investment Co., Ltd Chairman, En Trust Securities Co., Ltd.	Western Culture & Literature, Tung Hai University
Hsu, Po-Wei	Director, Hua Nan Commercial Bank, Ltd. Chairman, Hua Nan Securities Co., Ltd.	President & CEO, En Trust Securities Co., Ltd.	Master of Chemical Engineer, University of South California, U.S.A.
Chiang Chia Chun	Director, Hua Nan Commercial Bank, Ltd.	Pricewater House Co.Operators.	Fu Jen Catholic University.
Chen, Chin-Yi	President, Hua Nan Financial Holdings Co., Ltd. Workers' Union.	Vice President; Assistant Vice President & Deputy Vice President, Hua Nan Commercial Bank, Ltd.	Chen kuo College of Business.
Sou-shan Wu	Standing Supervisor, Hua Nan Commercial Bank, Ltd. Dean & Professor, College of management, Chang Gung University.	Chairman of Management Science Dept., Director of Management Science Institute, National Chiao-Tung University. Academic Advisor to Ministry of Education.	Ph.D. in Finance, Insurance & Real Estate, University of Florida, U.S.A.
Wen-yuh Tsai	Supervisor, Hua Nan Commercial Bank, Ltd. Chairman of Sin-Jang CPAS office.	CPA, Audit, Tax- Planning, Business Management etc. Instructor of University.	M.B.A. Cheng Chi National University.
Yen Fuei-Liang	Supervisor, Hua Nan Commercial Bank, Ltd. Chairman, Te Ho Co., Ltd.	Senior Vice President, Hua Nan commercial Bank, Ltd.	Kai Nan commercial & Technical Senior High School.
Yen Hui-Wei	Supervisor, Hua Nan Commercial Bank, Ltd. Chairman, Taiwan Mineral Resources & Industry Co., Ltd. Supervisor, Evergreen Realestate & Construction Corp.	Director, Chang Hwa Commercial Bank, Ltd. Instructor of University.	Ph. D. Hawaii Pacific University, U.S.A.



## TOP MANAGEMENT AND DEPARTMENT MANAGERS IN HEAD OFFICE

**David, J.Y.Lee**

President

**York, M.Y. Lai**

Executive Vice President

**Donald, W.H. Hsu**

Executive Vice President

**Yun-peng Chang**

Executive Vice President

**Johnson C.S. Chen**

Chief Auditing Officer

**Fuh-ji Chang**

Senior Vice President & General Manager of Auditing Department

**Young-tzew Hsu**

Senior Vice President & Chief Secretary of Secretariat Department

**Mon-shung Chung**

Senior Vice President & General Manager of Planning Department

**Tony Jang**

Senior Vice President & General Manager of Business Administration Department

**Chin-nan Ku**

Senior Vice President & General Manager of Corporate Banking Department

**Ching-yuh Wu**

Senior Vice President & General Manager of Accounting Department

**Tsao-sin Liu**

Senior Vice President & General Manager of Personnel Department

**Dong-lee Hong**

Senior Vice President & General Manager of Credit Department

**Kou-an Lee**

Senior Vice President & General Manager of General Affairs Department

**Casey Lo**

Senior Vice President & General Manager of Information Technology & Administration Department

**Ching-hsing Chen**

Senior Vice President & General Manager of Trust Department

**Ming-Chu Liao**

Senior Vice President & General Manager of Credit Card Department

**Jou-Che Kau**

Senior Vice President & General Manager of Credit Review & Management Department

**Jeng-fang Geeng**

Vice President & General Manager of Financial Trading Department

**Jung-Cheng Kao**

Senior Vice President & General Manager of Personal Banking Department

**Betty Y.F. Hsu**

Senior Vice President & General Manager of Wealth Management Department

**Robert Li**

Vice President & General Manager of Risk Management Department

**Pao-yen Lee**

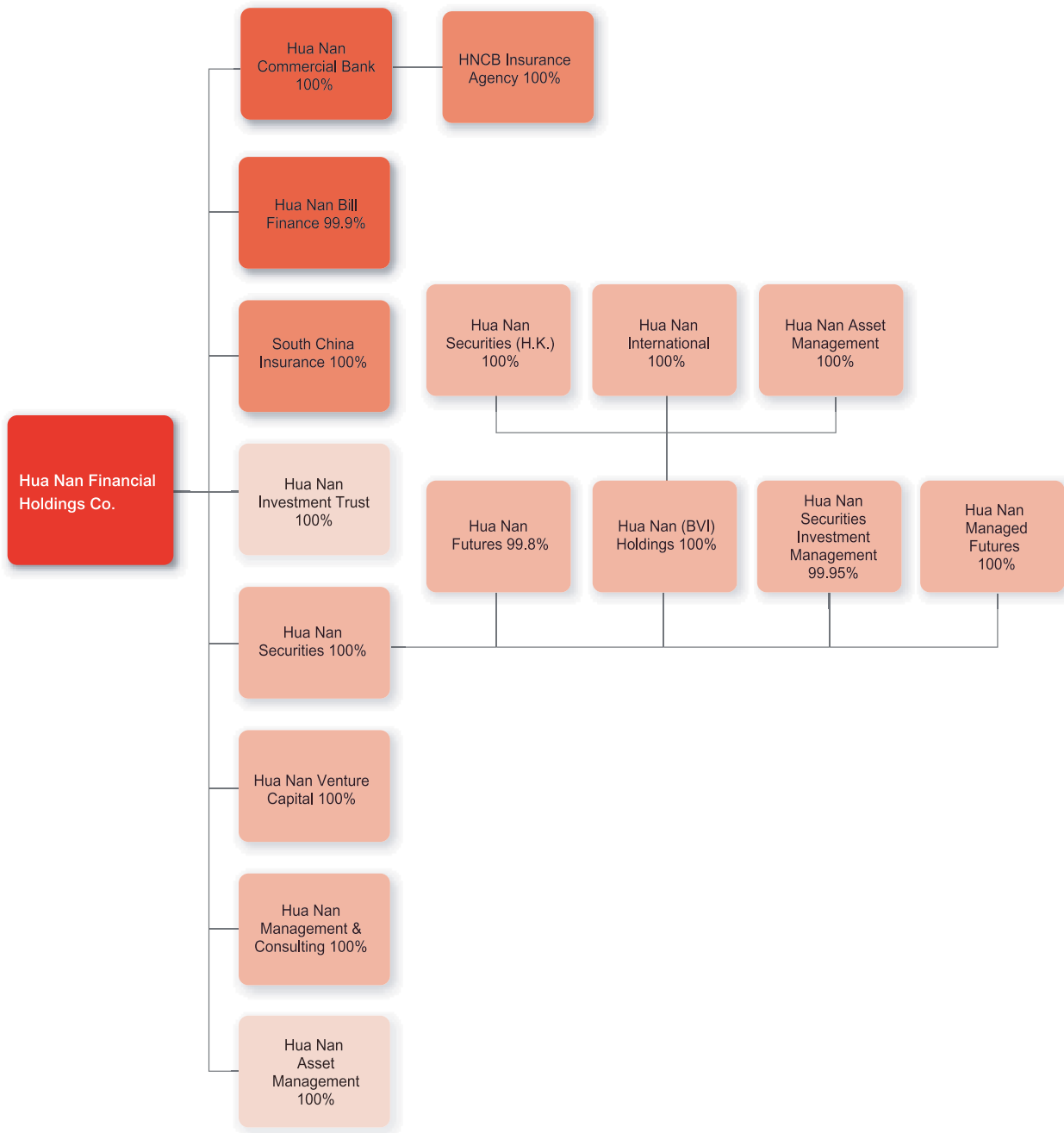
Senior Vice President & General Manager of Banking Department

**Carl, S.M.Huang**

Senior Vice President & General Manager of International Banking Department

## ORGANIZATION CHART FOR HUA NAN FINANCIAL HOLDINGS GROUP

Dec.31,2005



### Divided by Line of Business

- Commercial Bank
- Securities / Investment banking
- Insurance
- Asset Management

## MANAGEMENT OF THE HNFHC GROUP

### BOARD OF DIRECTORS

Chairman of the Board	
Ming-cheng Lin	
Managing Directors	
David J.Y. Lee Rong-chu Liu Chan-sheng Chen Shiu-hsiung Chen Chuan-chuan Hsieh Ya-hwei Yang Yun Lin	Chih-yang Lin Hsien-hsien Hsu Hsu Hsueh Chang Tommy Lin An-lan Hsu Chen Po-wei Hsu
Supervisors	
Sou-shan Wu Wen-yuh Tsai Li-yen Yang	James Hui-jan Yen Chia-ying Shen
Executive Officers	
David J.Y. Lee President	Chen-fang Chang General Manager of Marketing Department
Mao-hsien Liu Executive Vice President & General Manager of General Administration Department	Ching-yuh Wu General Manager of Treasury & Investment Department
James H. J. Liu Executive Vice President & General Manager of Risk Management	Casey Lo General Manager of Information Technology & Administration Department
Jeffrey C. F. Lee Executive Vice President & Chief Auditor	

# Activeness

We pro-actively listen more, think more and do more with passion.

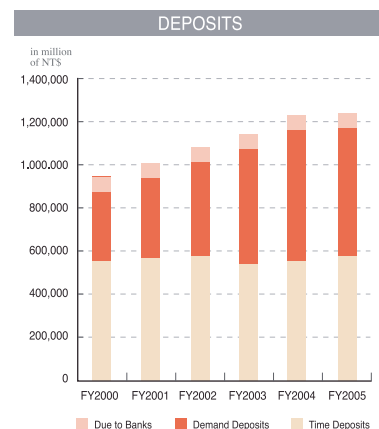


## REVIEW OF OPERATIONS IN FISCAL YEAR 2005

The Bank's main operations over the past year are as follows:

### 1. Deposits

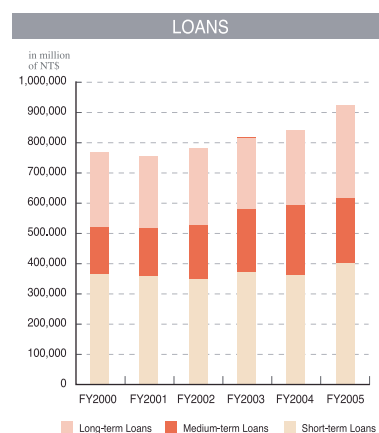
As of December 31, 2005, total deposits stood at NT\$1.295 trillion, an increase of NT\$77.7 billion from the end of 2004, and equivalent to growth of 6.38%. After deducting deposits by other financial institutions, deposits stood at NT\$1.250 trillion, a growth of NT\$80.6 billion, or 6.89%, on the year. In terms of deposits by category, demand deposits stood at NT\$636.50 billion, a rise of 3.09%, or NT\$19.06 billion from the end of the previous year, time deposits increased 11.15% to NT\$613.57 billion, and deposits by other financial institutions declined 6%, or NT\$2.90 billion, to NT\$45.39 billion.



Demand deposits comprised 49.13% of all deposits, time deposits 47.36% and interbank deposits 3.51%.

### 2. Loans

Global economic growth waned in 2005. In addition, international raw materials prices remained at high levels and inflationary pressure showed signs of emerging. Interest rates rose and the threat of avian flu was a foremost concern. Furthermore, local elections at the end of the year as well as cross-strait relations also caused uncertainty. Bank staff worked to their utmost, resulting in a growth in loans during the year despite these various factors. Outstanding loans in 2005 stood at NT\$868.4 billion, which was a rise of NT\$32.2 billion, or 3.85%, from 2004, and reached 99.47% of the Bank's target of NT\$873.0 billion.



Total loans as of December 31, 2005 (not including loans to other financial institutions or overdrafts) stood at NT\$935.35 billion. Of this, foreign exchange purchases and import/export negotiations stood at NT\$14.97 billion, or 1.60% of the total; discounts and overdrafts NT\$1.96 billion, or 0.21% of the total; short-term loans NT\$411.06 billion, or 43.95% of the total; medium-term loans NT\$218.01 billion, or 23.31% of the total; and long-term loans NT\$289.35 billion, or 30.93% of the total.

Outstanding loans as of the end of 2005 increased NT\$61.17 billion, or 7%, from the end of 2004. Of this, foreign exchange purchases and import/export negotiations rose NT\$1.27 billion, or 9.23%, from the end of 2004; discounts and overdrafts fell NT\$1.47 billion, or 42.76%; short-term loans increased NT\$59.72 billion, or 17%; medium-term loans fell NT\$15.60 billion, or 6.68%; and long-term loans rose NT\$17.24 billion, or 6.34%.

### 3. Personal Banking Operations

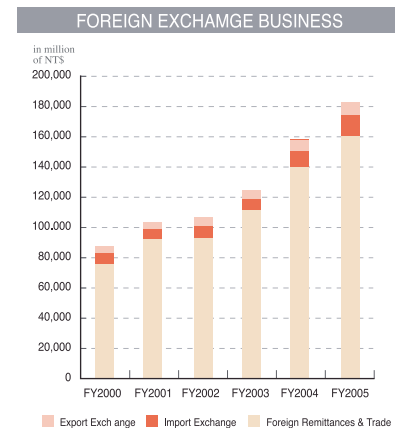
As of the end of December, the amount of credit extended (not including cash cards) stood at NT\$281.1 billion, which was a rise of NT\$17.5 billion or 6.64% from the end of 2004. Of this, home mortgage amounted to NT\$210.7 billion, a rise of NT\$12.4 billion or 6.25% from 2004; consumer loans (including revolving loans) were NT\$21.0 billion, a rise of 11% or NT\$2.1 billion from the end of 2004; and turnover loans amounted to NT\$49.4 billion, a rise of about NT\$3.0 billion or 6.46% from the end of the previous year.

The Bank's total fee income from home mortgage loans in 2005 was NT\$37.38 million, which was equivalent to 86.5% of its target and fee income was NT\$24.98 million, equal to 78% of its target. The outstanding level of personal installment loans (including cash cards) in 2005 was NT\$279.1 billion, which was slightly above the Bank's target of NT\$278.8 billion. NT dollar-denominated credit as of December comprised 36.45%, which was a slight decline of 0.17 percentage point from December 2004. Interest income as of December comprised 44.5% of total income in this area, which was a rise of 1.38 percentage points from December 2004.

According to statistics compiled by the Financial Supervisory Commission, the total number of cash cards in issuance on Taiwan at the end of 2005 stood at 5.37 million cards. Of these, 60.9%, or 3.27 million cards were in use. The amount of funds mobilized (including funds under collection) stood at NT\$298.4 billion. On average, NT\$91,300 was borrowed on each card. The overall overdue ratio stood at 1.835%. Hua Nan commenced cash card operations on February 27, 2004. As of the end of 2004, cash card counters had been set up at 133 branches and the Bank had issued 234,000 cards, with 161,000 cards, or 68.8%, in use. The amount of funds withdrawn using cash cards was NT\$10.76 billion, equivalent to NT\$67,000 per card.

### 4. Foreign Exchange and International Operations

The number of foreign exchange transactions and amounts handled rose for the Bank in 2005, sparked by the gradual rebound in the global economy. In 2005, the Bank's domestic and overseas offices handled 1.898 million foreign exchange transactions, which was a rise of 8.73% from 2004. Foreign exchange business amounted to US\$180.97 billion, a rise of 14.50% from the previous year. The Bank handled 77,149 import letters of credit and collections, a slight fall of 2.31% from the previous year, with the area of business valued at US\$10.32 billion, a fall of 5.29% from 2004. Meanwhile, a total of 109,123 export negotiations and collections were handled, a drop of 5.57% on the year, while the amount of this business was US\$9.26 billion, arose of 9.41% from 2004. The Bank also handled 1.71 million foreign exchange remittances (including inward and outward remittance, purchase or collection of clean bills), which was a growth of 10.35% from the previous year. The amount of this business stood at US\$161.39 billion, a rise of 16.37% from 2004.



#### Business at Overseas Units

Pre-tax profits from Hua Nan's five overseas branches and OBU in 2005 stood at US\$73.94 million, which was a 36.05% rise from 2004's pre-tax profit of US\$54.35 million. Of this amount, pre-tax profits at OBU and the Hong Kong branch rose US\$6.90 million and US\$6.51 million, respectively, which contributed 12.69% and 11.97% growth, respectively.

Deposits at these units in 2005 stood at US\$1.96 billion, a rise of 13.54% from 2004. Loans from these units in 2005 declined 8.99% to US\$1.46 billion.

### 5. Securities Underwriting

In 2005, Hua Nan served as lead underwriter for Cathay High Dividend Balanced Fund Underwriting income came to NT\$13.85 million. The Bank also had unrealized losses of NT\$10.53 million from its subscription to underwriting securities.

### 6. Trust

#### (1) Investment in Local and Foreign Securities by Discretionary Trusts

- a. Foreign Currency Trust Funds: These are invested in foreign mutual funds, indexed bonds and government bonds. At the end of 2005, the amount of foreign currency trust funds stood at US\$685.28 million, with the increase in funds under management in 2005 at US\$471.30 million. Handling fee income for the year was NT\$485.58 million.
- b. NT Dollar Trust Funds: These are invested in domestic and overseas mutual funds, and local structured products.  
At the end of 2005, the amount of trust funds under management stood at NT\$54.11 billion, with the amount of funds handled in 2005 standing at NT\$98.88 billion. These operations generated handling fee income of NT\$108.66 million.
- c. Composite Account Trust Funds: The amount of these trust funds at the end of 2005 was zero. During the year, handling fee income stood at NT\$200,000.

#### (2) Custodial Services

As of the end of 2005, Hua Nan provided custodial services for 58 mutual funds. Presently, 95 customers have contracted Hua Nan Bank for custodial services, with the commissioned custodial amount at NT\$149.33 billion. Handling fee income in 2005 was NT\$172.99 million.

#### (3) Securities Certification

Certification was handled for shares and bonds of 728 companies in 2005, with the amount certified totaling

NT\$97.59 billion. Certification was handled for beneficiary certificates in 31 instances in 2005, with the total certified amount reaching NT\$42.57 billion. Handling fee income in 2005 was NT\$11.03 million.

#### (4) Personal Trusts

As of the end of 2005, the Bank had 668 trust clients (616 individual accounts and 52 corporate employee savings trusts). Assets stood at NT\$44.92 billion. On March 7, 2005, the Bank began handling collective investment accounts. By the end of 2005, the number of these accounts stood at 10,563, with net asset value at NT\$1.87 billion. Handling fee income (including collective investment accounts) stood at NT\$52.93 million.

#### (5) Corporate Bond Issuance

The Bank issued corporate bonds on behalf of four clients in 2005, with the amount of bonds issued totaling NT\$14.5 billion. This generated handling fee income of NT\$1.25 million.

## 7. Domestic Remittance and Agency Services

In 2005, the Bank processed NT\$8.36 trillion of outward remittances, a decline of 1.86% from the previous year. Hua Nan served as an agent in the collection of 11.42 million bills, which was a rise of 14.71% from the year earlier. The Bank served as an agent for the following:

- (1) Collection of tax payments for the National Treasury;
- (2) Collection of payment for insurance premiums, taxes, telecom fees, utility bills, tuition, labor insurance premiums, national health insurance premiums, subscriptions for corporate rights issues, payment of principal and interest on bonds, issuance of cash dividends, and payment of winnings in the public welfare lottery;
- (3) Bidding for government bonds;
- (4) Sales of gold and silver coins, and sales of public welfare lottery tickets.

## 8. Financial Products

#### (1) Foreign Currency:

In 2005, the Bank handled trading of interest rate options, foreign currency structured investment products, cross currency swaps, and interest rate swaps amounting to US\$2.66 billion, which was a rise of 9.97% compared with 2004.

#### (2) New Taiwan Dollar:

In 2005, the Bank handled trades of interest rate swaps and structured investment products of NT\$20.13 billion, generating income of NT\$47.34 million.



## 9. Credit Cards

### (1) State of Credit Card Operations:

Hua Nan commenced international credit card business in 1995. In November 1996, it initiated international credit card collection operations. In April 1997, it began international banking card services and started collection services in June of that year. In September 2002, it issued its first EMV chip credit card (the national travel card), and on June 1, 2004 inaugurated combo card services. In December 2004, it cooperated with Jaeger Le-Coultrre in issuing a joint branded card. In January 2005, it issued the JCBMomo card and in March of that year began credit card installment cash advance operations. In August, it launched a new national travel card called the "Let's Go National Travel Card." In September, it issued the VIA Cord Blood Card, which is the world's first cord blood recognition card. In November it issued the Platinum Volkswagen co-branded card. The status of operations as of the end of 2005 is as follows:

### (2) Credit Card Issuance:

As of the end of 2005, the number of cards in issuance stood at 756,831, an increase of 102,404 cards from the previous year. The total amount of spending from these cards in 2005 was NT\$15.71 billion, a rise of 49.97% from 2004. As of the end of December, the amount of revolving credit extended stood at NT\$2.19 billion, a rise of 73.03% from the previous year. Handling fee income during the year amounted to NT\$275.96 million, an increase of NT\$192.04 million from the previous year.

In terms of acquiring, Hua Nan had 4,619 contracted stores in 2005, a decline of 171 from 2004. The total amount transacted at these outlets was NT\$28.56 billion, a decrease of 6.03% from the year earlier. Total handling fee income stood at NT\$547.33 million, a rise of 90.51% from 2004.

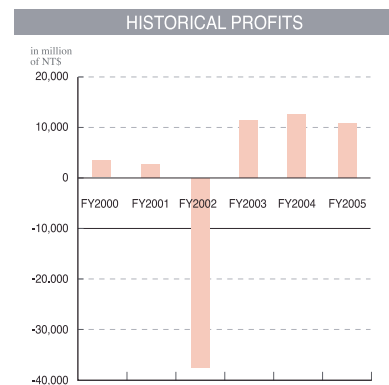
## 10. Wealth Management

(1) The Bank started wealth management operations on December 19, 2005, following approval by the Financial Supervisory Commission to engage in this business. At present, the Bank is employing 162 wealth management sales representatives ("sales representatives") throughout 151 branches to provide wealth management services to customers with high net worth. These sales representatives also provide assistance in financial planning and asset allocation, utilizing financial products and services offered by the Bank.

(2) It will work toward providing customers more professional financial services and developing the training incentive program of sales representatives. It will also integrate sales and marketing efforts with the rest of the Bank's network. Products will be designed with customer financial planning and asset allocation in need. Customers will have a wide range of product to choose, including trusts (domestic and overseas funds, structured notes and collective investment accounts), life insurance, and etc.

## 11. Operational Performance

In summary, the Bank registered an outstanding performance in 2005 despite various domestic and international political and economic uncertainties, as well as heated competition from counterparts. Pre-tax profit in 2005 stood at NT\$9.43 billion, which was 97.24% of the Bank's internal goal. Total income for the year was NT\$54.50 billion, with operating income comprising 98.75% (including interest income 67.03%, bad loan recoveries 10.54%, bills trading income 10.08%, handling fee income 7.96%, and other income 3.14%) and non-operating income 1.25%. Total expenditures stood at NT\$42.59 billion, which amounted to 78.15% of total income. Operating expense accounted for 77.67% (including interest expense 35.29%, business and management expense, 24.90%, provisioning 14.87%, and other expense 2.61%) and non-operating expenses and losses amounted to 0.48%. Income tax comprised 4.59%. After-tax profit amounted to 17.26%.



## MARKET ANALYSIS

A review of Taiwan's economic and monetary situation over the past year follows:

### 1. The Economy in General

The continued rise in international crude oil and raw materials prices over the past year caused the global economic expansion to lose steam, which in turn impacted Taiwan's economy. In order to ward off the threat of inflation, major economies gradually hiked interest rates. The slowing global economy also impacted Taiwan's exports, causing momentum here to wane. In the first quarter, domestic industrial production and manufacturing output contracted 0.62% and 1.19% compared with the year earlier period. In light of the export slowdown, Taiwan posted trade deficits of between US\$100 million and US\$400 million in January, March and June. Meanwhile, the composite economic indicator, which signals the state of the economy, fell into the yellow-blue level for five months starting in March, indicating weak growth. At one point, the composite index fell to 18, which is the lowest score in the yellow-blue level. Economic growth in the first and second quarters stood at only 2.49% and 2.97%, respectively, compared with a peak of 5.51% in the third quarter of 2004. Growth in the first half of 2005 was only 2.73%.

Starting in August and September, an economic upturn in the United States and China, which are Taiwan's two largest export markets, and increased international demand for information and electronics products, helped spark industrial production and manufacturing output here. Christmas- and Chinese Lunar New Year-related demand also boosted demand, enabling industrial production and manufacturing output to return to 10% annualized growth levels in November and December. The external trade situation gradually improved, helping to expand Taiwan's trade surplus. For the year, Taiwan's trade surplus was US\$7.788 billion, which was a rise of US\$1.663 billion, or 27.2% from 2004. The composite economic indicator flashed green in each month from August to December, signifying stable growth. According to preliminary data from the Directorate General of Budget, Accounting and Statistics, economic growth in the third quarter accelerated to 4.38%, compared with a pace of 2.97% in the second quarter. Growth further hastened to 6.40% in the fourth quarter. For 2005 as a whole, economic growth stood at 4.09%.

### 2. Industrial Production

Industrial production in 2004 was impacted by a slowdown in the global economy, which reduced demand for exports. In addition, data was also influenced by the relocation of many factories overseas. Industrial production in the first and second quarters was little changed from the year earlier, contracting 0.62% and rising 0.18%, respectively. Manufacturing output contracted 1.19% and 0.29% during those quarters. Historically speaking, this situation in which growth turned negative has been seldom seen. Export orders, however, hit new highs, with orders in the first and second quarters tallied at US\$55.51 billion and US\$60.69 billion, which were rises of 20.13% and 15.12% compared with the corresponding quarters in 2004. This situation indicated that local firms

received orders here, but many of the goods were produced in their factories overseas.

In the second half of the year, global economic growth gained steam. In addition, demand picked up for information, communications and consumer electronics products. As a result, Taiwan's industrial production gradually emerged from the weakness exhibited in the first half of the year and returned to steady growth. Of the four major manufacturing sectors, growth in the information and electronics sector was the strongest due to demand for consumer electronics and 3G telecommunications products. Industrial production growth hit 4.97% in the third quarter on an annualized basis, which was sharply higher than the 2.50% and 1.86% growth levels seen in the first and second quarters. Manufacturing output vaulted to double digit growth in November and December in reflection of continued strong export orders and overtime put in ahead of the Chinese Lunar New Year. For the year as a whole, industrial production grew 3.37% from 2004. Manufacturing sector output posted annualized growth of 3.18%, utilities output increased 3.79% and housing construction rose 11.43%.

Export orders posted double digit growth in the first half of the year despite the slowing international economic expansion. In the second half of the year as the global economy rebounded, growth in export orders gained further steam. For the year as a whole, growth in export orders reached 19.20%. Orders from the Asian region increased US\$23.97 billion, or 22.62%, during the year, making the biggest contribution to growth. In 2005, export orders amounted to US\$256.39 billion, an increase of US\$41.31 billion from the previous year. If tabulated in NT dollars, growth for the year stood at 15.18%. Electronics products and information/communications goods continued to hold the title of being Taiwan's two most important export industries. Orders for electronics products were impressive due to demand for consumer electronics and semiconductor products. Orders in this category reached US\$57.19 billion in 2005, a rise of US\$10.16 billion or 21.60%, on the year. Demand for information and telecommunications products was sparked by strength in the cellular phone market and orders for notebook computers. This category also benefited from contract manufacturing orders placed by major overseas electronics companies. For the year, orders for information and telecommunications products hit US\$50.17 billion, a rise of 24.52% from the year earlier.

### 3. Foreign Trade

The rise in imports in the first half of the year exceeded that of exports. This was the result of the global economic slowdown, record-setting crude and raw materials prices, and the placing of orders here but production being carried out overseas. Exports in the first and second quarters of 2005 stood at US\$42.85 billion and US\$46.83 billion, rises of 7.8% and 6.0%, respectively. Imports for the two quarters rose 12.6% and 10.6% to stand at US\$42.56 billion and US\$46.69 billion, respectively. Taiwan's trade surplus shrank considerably to just US\$283 million and US\$131 million in the two quarters, plunging 85.0% and 92.8% from the year earlier periods. The island even posted trade deficits ranging between US\$100 million and US\$400 million in January, March and June.

Seasonable demand for personal computers, Internet communications and consumer electronics products in the second half of the year, combined with Christmas-related demand at the end of the year, pushed exports up to

US\$47.48 billion in the third quarter (up 7.12% on the year), while imports stood at US\$45.96 billion (up 9.78% on the year). The trade surplus for the quarter jumped dramatically in comparison to the first two quarters to US\$1.52 billion. Nonetheless, this figure was still a drop of 38.76% from the third quarter of 2004. For the year, exports rose 8.8% to US\$189.39 billion, and imports grew 8.2% to US\$181.61 billion, resulting in a trade surplus of US\$7.79 billion, which itself was a rise of 27.2% from the previous year.

#### 4. Inflation

Soaring prices for imports of crude and international raw materials pushed the consumer price index (CPI) up 1.57% in the first quarter compared with a year earlier. Merchandise prices rose 2.61%, while service sector prices rose a more modest 0.42%. Core inflation in the quarter, which excludes fresh produce and energy prices, rose 0.85%. Wholesale prices in the quarter rose 2.87% compared with the year earlier. The CPI continued to be impacted in the second quarter by high crude and raw materials prices. The CPI for that quarter rose 2.10% on the year. However, core inflation for the quarter stood at 0.58%. The wholesale price index (WPI) in the second quarter rose 0.14% on an annualized basis.

In the third quarter, the CPI rose by 3.03% due to the impact of typhoons hitting the island and hikes in fuel prices. In September alone, the CPI rose an annualized 3.12%. Rises in the WPI waned in the third quarter due to falling prices for electronics spare parts, computers, and communications and media products. The WPI in September declined 0.16% from the year earlier.

For the year as a whole, the CPI increased 2.30%. Merchandise prices rose 3.78% largely on the rise in food prices caused by typhoons. Service sector prices rose 0.61%, which was attributed mainly to a hike in registration fees at hospitals and Western medicine clinics. If fruit and vegetable prices are subtracted from the equation, the rise for the year was 0.98%. Furthermore, if fish prices and energy prices were deducted, core inflation for the year stood at 0.65%. Last year's WPI rose 0.60% compared with 2004. Of this, domestically produced items rose 1.47% and import prices 2.42%. The price of exported items dropped 2.46%. The price of domestically sold products (including the sale of locally produced items and imports) rose 1.90%, while the price of locally produced products (including the sale of locally produced items and exports) fell 0.26%.

#### 5. Money Supply

Currency gradually returned to the banking system after the Chinese Lunar New Year. In addition, inflows of foreign stock investment funds waned in the quarter. In the first quarter, average annual growth in the M1A, M1B and M2 money supplies stood at 10.35%, 9.11%, and 6.21%, respectively, all of which were lowered compared with the previous quarter. In the second quarter, growth in the money supplies slowed to 6.65%, 6.38% and 5.85% due to a further downturn in the inflow of foreign investment funds and ebbing bank loan and investment growth. In the third quarter, growth in the M2 and M1B money supplies initially picked up, before slowing again. Growth in the M2 and M1B in September stood at 6.35% and 6.31%, declines of 0.17 and 1.28 percentage points

from August. This was attributed to the outflow of foreign investment funds as well as capital outflows by locals. For 2005 as a whole, average growth in the M1A, M1B and M2 money supplies stood at 7.65%, 7.10% and 6.22%. In sum, growth in the M1A and M1B money supplies gradually slowed to around the 7% level, while growth in the M2 money supply fluctuated around 6%, which was within Taiwan's Central Bank of China's target range for the M2 money supply of 3.5%-7.5%.

## 6. Domestic and Overseas Operations Network

As of the end of 2005, 56 of Hua Nan's branches had been authorized by Taiwan's Central Bank of China to engage in foreign exchange operations. In 2005, branches that were newly authorized to handle foreign exchange business included the South Yungho and Tataocheng branches. Meanwhile, a total of 64 branches were authorized to buy and sell foreign currency notes and travelers checks. Other branches offered services to arrange import/export and foreign exchange business.

Meanwhile, Hua Nan maintains five overseas branches, in Los Angeles, New York, Hong Kong, Singapore and London. It also has representative offices in Shenzhen and Ho Chi Minh City. At the end of 2005, the Bank was able to carry out foreign exchange transactions with 2,315 local and foreign banks covering five continents, including 32 in Africa, 906 in Asia and the Middle East, 875 in Europe, 78 in Latin America, 333 in North America and 91 in Oceania, providing convenient services to its customers.

## 7. Outlook

Looking ahead to 2006, Hua Nan has many reasons to be optimistic. Amid the highly competitive local banking market, the Bank has an outstanding reputation and boasts a high level of innovation. The Bank also enjoys a stable client base. In addition, Hua Nan has a sizeable market share, especially with regards to corporate banking and finance. In light of this, the Bank has a competitive advantage against most of its industry counterparts and has further room to expand its bottom line. On the other hand, factors not advantageous to the Bank include the high level of competition in the market. This establishes obstacles in the expansion of business and profit growth. From a macro-economic perspective, buoyant global consumption and investment will continue to propel domestic and international economic growth. Furthermore, up to the beginning of this year, the international economic environment remains generally steady, and major research institutions on Taiwan and overseas remain optimistic on the prospects for global economic growth this year. International growth is generally seen exceeding 3.0%. Stable international growth will benefit Taiwan's industrial output and exports, providing an opportunity for local economic growth to continue to gain steam. Taiwan's Directorate General of Budget, Accounting and Statistics forecasts growth to reach 4.31% this year and GNP to hit NT\$11.85 trillion, equivalent to US\$373.60 billion. DGBAS forecasts per capital GNP at US\$16,423, while predicting rises in the CPI and WPI of 1.76% and 1.4%, respectively. This steady outlook will provide a strong foundation for operations in the banking sector. Nonetheless, there are threats to the global economy, including high oil prices, global current account imbalances, the re-emergence of trade protectionism, rising inflationary pressure, and the possibility of the spread of avian flu.

## RISK MANAGEMENT

### 1. Bank Risk Management Framework and Policies

Hua Nan established a risk management department in September 2005 responsible for planning, assessment and establishment of systems addressing credit risk, market risk, operational risk, and integrated risk. The division works in conjunction with the Hua Nan Bank Basel II Supervisory Committee and seeks to implement risk control concepts according to Basel II throughout all business units.

In addition to abiding by guidelines set by regulatory authorities, Hua Nan seeks to implement professional management to all types of risk faced by the Bank to ensure sound operations and enhance capital utilization. These will enable Hua Nan to meet its goals of rationalizing risk and return.

### 2. Methods of Measuring and Controlling Risk and Quantifying Exposure

#### 1. Credit Risk

##### (1) Definition of Credit Risk:

Credit risk refers to the possibility that a borrower or counterparty may not be able to fulfill contractual duties due to the deterioration of a company's financial structure or disputes with the party to the deal, which results in losses.

##### (2) Plans to Manage Credit Risk:

In order to prepare for the implementation of Basel II, Hua Nan has carried out the calculation of risk-weighted assets and regulatory capital based on proposed amendments by local regulator. In the process of carrying out the trial tabulations, the Bank is re-examining the suitability of its credit database and engaging in gap analysis. The Bank is also improving efficiency of credit management process and establishing a bank-wide risk management culture.

##### (3) Development of Models (Internal Rating Based Approach):

The goal of the development of a credit rating model is to better assess the credit risk of each customer and assign an appropriate interest rate to each client. The model also offers a reference tool in the approval or rejection of credit applications, helping to achieve the goal of risk management.

The Bank has contracted consultants to provide assistance and engage in technical transfers. The Bank is presently developing application and behavior scorecards to be used when small- and medium-sized enterprises apply for loans. Since loans continue to serve as the primary source of income for the Bank, Hua Nan's long-term goal is to develop credit models suitable for a variety of business, including credit-card, mortgage, etc. It will amend these models based on any changes in the regulatory environment or to better reflect various trends.

## 2. Market Risk

### (1) Definition of Market Risk:

Market risk refers to any potential losses, both to the bank on-balance sheet and off-balance sheet, resulting from fluctuations in market prices in an undesired direction. Market price risk includes changes in interest rates, exchange rates, equities and commodities prices, and volatilities.

### (2) Planning a Market Risk Management Framework:

Hua Nan already has systems in place to recognize market risk in the trading of financial instruments and to measure the fair value of financial instruments. It also monitors market risk and requires the disclosure of risk reports. The Bank is planning to introduce a system that better monitors risk adopted by the international banks, hoping to conform to internal and external standards and strengthen its present market risk control mechanism.

Hua Nan presently utilizes standard approach for market risk capital calculation. However, regulatory authorities are in the process of amending regulations to conform to Basel II requirements. The Bank will amend its capital calculation method appropriately to meet the requirements of regulators and Basel II.

### (3) Development of Internal Models:

Hua Nan is developing internal models for capital calculation in line with new regulations, hoping to strengthen its ability to control market risk and enhance the utilization of capital. It also plans to establish a Value at Risk control system. It will assess external systems in helping to develop its own internal system.

## 3. Operational Risk Management

### (1) Definition of Operational Risk:

Operational risk management and related capital calculation are new ideas and standards introduced from Basel II. This indicates that international financial institutions have already begun to pay increasing attention to operational risk. Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems, or from external events.

### (2) Planning of Operational Risk Management Framework:

In order to enhance operational risk management quality, an organization needs to first establish operational risk management goals and strategy, build the risk management culture, make appropriate adjustments to the organizational structure, generate management policies, establish proper reporting mechanism, formulate management procedures, and establish corporate loss databases. Of these, building risk management culture and adjusting to the organizational structure are the foundation of efficient risk management framework to be established.

### (3) Goal of Operational Risk Management:

Hua Nan will continue to carry out employee training program, build risk management culture within the organization. In the future, it will make adjustment to its organizational structure and will establish an operational risk management system that is efficient for identifying, assessing, monitoring, and controlling operational risk. With the efficient operational risk management system, Hua Nan hopes to not only meet cost-benefit principle, but also enhance the utilization of capital, more effectively.



# Responsibility

We continuously improve, pursue excellence and take full ownership.



## BUSINESS PLAN FOR 2006

### 1. Development of New Financial Products

- (1) The Bank plans to combine various derivatives products in an effort to provide a wider selection of structured investment tools. Presently, the Bank not only provides NT dollar interest rate products. This will be expanded to include equities products and index-linked products. As for foreign currency products, the Bank is planning to introduce guaranteed return foreign exchange products. Expansion of this business is expected to boost performance and non-interest income, in addition to meeting the personal finance needs of customers.
- (2) Hua Nan is working aggressively to serve as custodian for new mutual funds and existing funds.
- (3) In order to bolster its asset management ability and take advantage of its strong brand name in the area of trust investment, and also in preparation to seek to engage in proprietary trading for the Labor Retirement Fund, Hua Nan in 2006 will introduce its second collective investment account. Investment targets will primarily be global bond funds and emerging market equities funds.
- (4) Hua Nan is promoting corporate employee savings trust operations in light of the introduction of the new labor pension system. This will provide assistance to companies facing a shortage of manpower and strengthen interaction with outstanding companies.
- (5) Hua Nan will seek to act as the lead in domestic and overseas syndicated loans.
- (6) Hua Nan will work in conjunction with the sales and marketing systems of other Hua Nan Financial Holdings subsidiaries in promoting loan operations.
- (7) The Bank will adopt different pricing strategies for different segments of customers. It will integrate its various home loan and consumer loans products, creating a comprehensive product line. This will provide customers with a wider range of selections and will also increase income.
- (8) Hua Nan will expand its strategic alliances and direct marketing networks to boost sources of income.
- (9) The Bank will continue to increase the number of domestic and foreign investment targets, such as funds, index-linked funds, sovereign and institutional bonds, and other securities worthy of investment, used in special purpose trusts.
- (10) The Bank will promote personal trusts, including children's education, insurance fund, and retirement trusts.
- (11) Hua Nan will continue to meet the needs of customers in foreign currency structured products.
- (12) The Bank will further strengthen the functions of its Shenzhen and Ho Chi Minh representative offices, preparing the units to upgrade into branches.

- (13) The Bank is working to establish FTP and ALM asset and liability management systems in line with policies set by the financial holding company. The Bank is setting guidelines with regards to reasonable cost in order to boost competitiveness and increase returns. It will also regularly examine the risk of all of its investments and strengthen its risk control mechanisms.
- (14) Hua Nan will issue subordinated debentures at an appropriate time to further strengthen its fiscal structure and raise its capital adequacy ratio.
- (15) The Bank is integrating its existing products and will introduce new financial products based on market and economic trends in order to provide customers with a broader range of options in financial planning and asset allocation.

## 2. Future R&D Projects

- (1) iCP: 1) Integrate the data of the customers, accounts and products of all financial holding company subsidiaries in order to provide a single sign-on for customers, single view and one-stop shopping; 2) Establish different platforms for different customer segments, providing the various products offered under the financial holding company umbrella and achieving the benefits of cross-marketing; 3) Share customer bases, operational resources and systems information to avoid overlapping investment by holding company subsidiaries; 4) After integration of systems software and modularization, the Bank will be able to provide rapid development of portfolios and make necessary changes. This will reduce development costs and the need for a sizeable maintenance staff; 5) Hua Nan currently offers time deposit balance, demand deposit balance, loan balance and mutual fund investment balance as part of its wealth management system. As soon as the needs of the call center, SFA and e-Portal are made clear, Hua Nan will establish means for common access of these items.
- (2) Risk Management System: 1) Hua Nan is working with an AMN AMRO consulting team in addressing the Basel II risk controls (personal banking, credit risk, corporate banking credit risk, market risk and operational risk). The bank is following the advice of the consultants in drafting timetables and carrying out information-related operations; 2) Hua Nan is developing risk-weighted asset and capital cost software platforms. This software tabulates capital charges based on Basel II specifications and produces risk evaluation reports, alleviating the need to allocate manpower to undertake this work and guaranteeing the timeliness and accuracy of data; 3) The risk management division has implemented a system to report losses. In line with Basel II guidelines, all risk-related information will be collected and employees can then use their workstations to file loss reports online. These reports are provided to all branches (including overseas branches) for use by branch auditors, managers and the risk management department.
- (3) Financial Systems: Hua Nan is establishing several financial systems that are expected to be ready in about 14 months. These systems will provide an integrated pricing and trading platform for a wide variety of products in many currencies throughout many markets. They will also strengthen risk management related to these new products and provide real-time management of outstanding positions. The systems will conform to

the Basel II capital accord and will also provide tight-knit links between front and back offices, helping to achieve automated and flexible operations management. These systems will have the following benefits: 1) Provide the opportunity to expand business through trading of new financial products; 2) Simplify management procedures and reduce risk via specialized software systems; 3) Bolster market risk controls; 4) Flexibly adapt to rapid changes in market trends; 5) Raise decision-making quality.

(4) Electronic System for Domestic Letters of Credit and Negotiations: This will provide computerized operations for letters of credit, negotiations, acceptances and repayment, payment of maturing drafts and offer the option to tailor services to each customer. In the past, computers were used to process this business only after bank staff initiated the draft. The new system will simplify the complex operations related to opening LCs. Once operational, the new system will be able to be used for all Hua Nan customers. Hua Nan's Internet bank will offer LC services, which will be integrated with back-counter accounts systems. In future, the system will provide a single window via which to apply and obtain LC.

(5) Sales Force Automation

Hua Nan is establishing a sales force automation system to boost customer satisfaction, sales performance and achieve synergy via cross-sales with other holding company subsidiaries. The system also assists sales personnel in managing sales activities. 1) Stage 1 Basic SFA: This includes providing a comprehensive list of clients, real-time billing lists, introduction to products, and comprehensive pre-sales (investment recommendation) and after-sales (stop loss or profit-taking) services. 2) Stage 2 Advanced SFA: This includes customers related to other customers, customer recommendations of other customers, recommendation of tailored investment portfolios, and tracing of services provided. 3) Stage 3 Complete SFA: This assists cross sales and marketing in personal banking and corporate banking.

(6) Transformation of Hong Kong branch computer system: Hua Nan has completed development of its overseas branch computer system and has completed installation of this system in its New York, Singapore, Los Angeles and London branches. Next, the bank will install the new system in its Hong Kong branch, which has the highest level of trading volume and business of all of its branches. Hua Nan is presently making amendments to the system to make it applicable to the Hong Kong branch, given its scale of operations. Additions to the system include FSC risk control reports, RTGS interface, reports on questionable transactions, deposit insurance, yuan deposits, limits on related accounts, purchase of clean bills, NDFs, factoring, structured deposits, options, analysis of contribution by each customer, and pre-purchases and pre-sales.

(7) Raising the single portal function of the Hong Kong branch's Internet banking system: Hua Nan intends to strengthen its Internet banking platform at its Hong Kong branch in conjunction the introduction of a new computer system there. The platform will provide customers with comprehensive Internet banking services. Expanded functions to be introduced in 2006 include an English-language version, information on foreign exchange import and export, lending, interest rates, and the application for checks. This will attract a larger number of Hong Kong customers to use the system and will replace the branch's present independently

operated system, enabling the branch's system to be fully integrated with the rest of Hua Nan's portals. This initiative will also reduce costs and manpower related to system maintenance.

- (8) Raising the single portal function of the Singapore branch's Internet banking system: After completing the single portal initiative in Hong Kong, Hua Nan intends to expand the scope of Internet banking at its other overseas branches. It will also create an overseas branch Internet banking standardized platform in order to reduce the time needed to implement the systems. Upon completion, the system will not only increase the competitiveness of overseas branches, raise service quality and reduce costs and the time needed to carry out business, but also will provide real-time account management for customers throughout the world, multiple accounts and in different currencies. In 2006, Hua Nan will develop an Internet banking system for its Singapore branch, which will go online in three phases. In Phase I, customers will be able to check their savings balance, review all transactions, and retrieve data on foreign currency import and export. In Phase II, the system will enable customers to check import/export, credit limits and foreign exchange rates. In the final phase, an English-language version will be introduced and account-related transactions (including single, multiple, real-time, and fixed remittances, cross-strait remittances, and outward remittances) will be possible.
- (9) Central Operations Centers: 1) Hua Nan is establishing a central foreign exchange remittance operations system to centralize its operations in this area. This center will need to employ only a limited number of highly trained staff, but will ensure the same high level of customer service and efficiency. 2) Hua Nan will also centralize the processing of its domestic remittance operations. This will simplify operational procedures at branches throughout Taiwan.
- (10) Employee Savings Trusts: Hua Nan will introduce such trusts in wake of the change in the local labor pension system, enabling employees to carry their pensions with them when they change jobs. These trusts will provide more options for employees when they change workplaces. Companies seeking to bolster employee loyalty can also consider using employee savings trusts, with contributions made by the employer and employee on a monthly basis. The trusts will invest in mutual funds, helping workers to accumulate savings for retirement.
- (11) Real Estate Automated Valuation Model: The AVM model will help in pricing assets, reducing the human factor and negotiation costs, cut credit screening costs, largely reduce the time needed for credit screening, boost real estate market competitiveness, provide for real-time monitoring of real estate collateral adequacy, reduce default risk, help in developing outstanding customers, and raise risk management associated with real estate collateralized loans. The model will also provide decision-making support and conform to capital adequacy provisioning as required under the Basel II capital accord.
- (12) Consumer Loan and Cash Card Central Collection Operations Systems: Hua Nan is developing these systems to provide centralized screening of consumer loans and centralized collection of cash card debt. These systems included the following: 1) an electronic collection system; 2) a legal collector operations system; 3)

an overdue loan reporting system; 4) a system to write-off bad loans; 5) a system to manage outsourced collection activities.

- (13) Personal Consumer Loan Screening System - Stage 2 (Message queue check credibility information system, home loans, auto loans): This will help to further simplify credit screening procedures with regards to personal loans, reduce the time needed in the credit screening process, and raise operational efficiency.
- (14) Development of System to Control Limits on Derivatives Products: Hua Nan will establish this system to effectively put limits on risk associated with trading and investment in derivatives products. This database will indicate limits and the amount of funds mobilized under those limits, and will enable real-time changes if needed. Limits will be amended only upon approval by business units. The platform will also indicate the amount of funds mobilized, and this will change immediately upon any trades. The system will update limits upon the closure of various trades or the maturity of various products.
- (15) Development of Syndicated Loan Collateral (fixed and non-fixed assets) System: Since Hua Nan sometimes participates in syndicated loans in which it does not serve as lead manager, it is unable to obtain comprehensive information on collateral, which would be keyed in to its collateral system. The inability to include this data into its system creates a gap in information. The establishment of a new collateral system will enhance disclosure of collateral information associated with syndicated loans.
- (16) Hua Nan will provide comprehensive training for financial-related staff, enabling them to provide personal finance investment, financial planning, asset allocation and tax planning services.
- (17) Hua Nan will develop new financial products and asset allocation technology to meet customer needs and market trends.
- (18) The Bank will utilize domestic and overseas strategic alliances to expand the scope of its asset management and raise its competitiveness.
- (19) Wealth Management System - Stage 2: The second stage of this system is being developed to provide overall performance and business management, sales representatives' to-do-list management, sales analysis, district management and sales representatives management reports. The goal is to maintain an eye on performance in wealth management operations and analyze the results of the products recommended.

# Teamwork

We support each other to maximize team synergy.



## FINANCIAL STATEMENT

### FIVE-YEARS FINANCIAL SUMMARY

In thousands of NT \$

	31.12.2001	31.12.2002	31.12.2003	31.12.2004	31.12.2005
Operating revenues	69,727,159	49,927,752	49,834,137	47,893,818	53,813,396
Operating expenses	64,427,091	89,604,770	38,550,260	35,321,055	42,329,833
Operating income (Loss)	5,300,068	( 39,677,018)	2,397,118	12,572,763	11,483,563
Non-operating income(Loss)	( 752,522)	2,861,823	342,850	427,715	422,746
Income (Loss) before income tax	4,547,546	( 36,815,195)	11,626,727	13,000,478	11,906,309
Net income (Loss)	3,974,104	( 27,187,822)	9,006,874	9,962,622	9,402,773
Earning (Loss) per share(by NT Dollar)	1.07	( 7.33)	2.43	2.69	2.54
Current assets	386,604,137	450,494,232	512,245,480	528,147,242	528,921,349
Loans, discounts and bills Purchased	822,150,101	807,047,059	858,999,364	885,729,850	945,414,558
Funds and long-term equity investment	9,094,996	13,557,933	11,369,148	51,794,768	67,993,599
Fixed assets	21,519,774	21,813,458	21,512,376	22,468,741	22,226,385
Other assets	14,435,861	22,570,384	20,330,511	20,388,161	19,889,361
Total assets	1,253,804,869	1,315,483,366	1,424,456,879	1,508,528,762	1,584,445,252
Current liabilities	135,943,864	150,438,458	170,099,139	133,051,071	129,581,108
Deposits and remittances	1,008,879,725	1,075,342,184	1,132,561,859	1,217,326,432	1,292,091,422
Bank debenture payable	13,500,700	25,000,000	50,670,000	60,670,000	63,033,000
Other liabilities	15,821,771	15,007,361	12,477,063	32,440,968	28,004,551
Capital stock	37,091,000	37,901,000	37,091,000	37,091,000	37,091,000
Capital surplus	18,405,586	18,405,586	12,618,838	15,388,081	18,776,827
Retained earnings (accumulated deficit)	24,183,443	( 5,786,748)	9,006,874	12,664,684	15,945,900
Equities adjustment	( 21,220)	( 14,475)	( 37,894)	( 103,474)	( 78,556)
Total liabilities and shareholders'equity	1,253,804,869	1,315,483,366	1,424,456,879	1,508,528,762	1,584,445,252



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English Translation of a Report Originally Issued in Chinese

INDEPENDENT AUDITORS' REPORT

The Board of Directors and the Stockholders  
Hua Nan Commercial Bank, Ltd.

We have audited the accompanying balance sheets of Hua Nan Commercial Bank, Ltd. (the "Bank," a wholly owned subsidiary of Hua Nan Financial Holdings Co. Ltd.) as of December 31, 2005 and 2004, and the related statements of income, changes in stockholder's equity and cash flows for the years then ended. These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the Rules Governing the Auditing and Certification of Financial Statements of Financial Institutions by Certified Public Accountants and auditing standards generally accepted in the Republic of China. Those rules and 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 Hua Nan Commercial Bank, Ltd. as of December 31, 2005 and 2004 and the results of its operations and its cash flows for the years then ended, in conformity with the Guidelines Governing the Preparation of Financial Reports by Public Banks, Guidelines Governing the Preparation of Financial Reports by Securities Issuers and accounting principles generally accepted in the Republic of China.



January 24, 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 jurisdictions. The standards, procedures and practices to audit such financial statements are those generally accepted and applied in the Republic of China.

For the convenience of readers, the auditors' 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 auditors' report and financial statements shall prevail. Also, as stated in Note 2 to the financial statements, the additional footnote disclosures that are not required under generally accepted accounting principles were not translated into English.

**HUA NAN COMMERCIAL BANK, LTD.  
BALANCE SHEETS**

**DECEMBER 31, 2005 AND 2004**

(In Thousands of New Taiwan Dollars, Except Par Value)

(The Exchange Rates as of December 31, 2005 and 2004 were NT\$32.860 and NT\$31.768)

ASSETS	2005		2004	
	Amount	%	Amount	%
CASH AND CASH EQUIVALENTS (Note 4)	\$ 34,462,360	2	\$ 27,898,980	2
DUE FROM THE CENTRAL BANK AND OTHER BANKS (Note 5)	145,054,012	9	127,204,364	8
SECURITIES PURCHASED, NET (Notes 2, 6 and 12)	322,613,391	20	347,202,148	23
RECEIVABLES, NET (Notes 2 and 7)	26,791,586	2	25,740,996	2
PREPAYMENTS	4,101,546	-	3,072,749	-
BILLS PURCHASED, DISCOUNTS AND LOANS, NET (Notes 2 and 8)	945,414,558	60	885,729,850	59
LONG-TERM INVESTMENTS (Notes 2 and 9)				
Long-term stock investments	7,215,850	-	9,313,767	-
Others	60,777,749	4	42,481,001	3
Total long-term investments	67,993,599	4	51,794,768	3
PROPERTIES (Notes 2 and 10)				
Land (including revaluation increments)	11,670,104	1	11,812,156	1
Buildings (including revaluation increments)	11,379,563	1	11,091,141	1
Office equipment	4,533,511	-	4,396,056	-
Transportation equipment	970,462	-	952,061	-
Other equipment	2,249,150	-	2,082,266	-
Leasehold improvements	454,705	-	447,222	-
Cost and revaluation increments	31,257,495	2	30,780,902	2
Less accumulated depreciation	9,104,318	-	8,532,621	-
Net properties	22,153,177	2	22,248,281	2
Construction in progress and advances on acquisitions of equipment	73,208	-	220,460	-
Net properties	22,226,385	2	22,468,741	2
OTHER ASSETS (Notes 2, 11 and 20)				
Deferred income tax asset, net (Notes 2, 11 and 20)	4,334,433	-	6,085,115	-
Others, net (Notes 2 and 11)	11,453,382	1	11,230,297	1
Total other assets	15,787,815	1	17,315,412	1
<b>TOTAL</b>	<b>\$ 1,584,445,252</b>	<b>100</b>	<b>\$ 1,508,428,008</b>	<b>100</b>
LIABILITIES AND STOCKHOLDER'S EQUITY	2005		2004	
	Amount	%	Amount	%
LIABILITIES				
Due to the Central Bank and other banks (Note 13)	\$ 80,540,499	5	\$ 90,967,349	6
Bonds sold under repurchase agreements (Note 2)	19,487,465	1	19,050,464	1
Payables (Note 14)	49,040,609	3	41,982,968	3
Advance collections	597,974	-	615,628	-
Deposits and remittances (Note 15)	1,292,091,422	82	1,217,326,432	81
Bank debenture payable (Note 16)	63,033,000	4	60,670,000	4
Other liabilities (Notes 2 and 17)	7,919,112	-	12,774,876	1
Total liabilities	1,512,710,081	95	1,443,387,717	96
STOCKHOLDER'S EQUITY (Note 18)				
Capital stock, authorized and issued 3,709,100,000 shares at \$10 par value	37,091,000	3	37,091,000	2
Capital surplus	18,776,827	1	15,388,081	1
Retained earnings				
Legal reserve	5,690,849	-	2,702,062	-
Unappropriated earnings	10,255,051	1	9,962,622	1
Cumulative translation adjustments	( 78,556)	-	( 103,474)	-
Total stockholder's equity	71,735,171	5	65,040,291	4
<b>TOTAL</b>	<b>\$ 1,584,445,252</b>	<b>100</b>	<b>\$ 1,508,428,008</b>	<b>100</b>

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

## HUA NAN COMMERCIAL BANK, LTD. STATEMENTS OF INCOME

YEARS ENDED DECEMBER 31, 2005 AND 2004

(In Thousands of New Taiwan Dollars, Except Earnings Per Share)

(The Exchange Rates as of December 31, 2005 and 2004 were NT\$32.860 and NT\$31.768)

	2005		2004	
	Amount	%	Amount	%
<b>OPERATING REVENUES AND GAINS</b>				
Interest (Notes 2 and 27)	\$ 36,526,350	68	\$ 31,870,544	66
Service fees (Note 2)	4,337,301	8	4,112,953	9
Income from securities, net (Notes 2 and 27)	5,491,006	10	3,629,092	8
Income from long-term equity investments under the equity method, net (Notes 2 and 9)	71,213	-	105,329	-
Foreign exchange gain, net (Notes 2 and 27)	914,616	2	676,776	1
Others	6,472,910	12	7,499,124	16
Total operating revenues and gains	53,813,396	100	47,893,818	100
<b>OPERATING EXPENSES</b>				
Interest	19,231,942	36	15,015,817	31
Service charges	879,194	2	793,575	2
Provision for reserves, bad debts and losses from decline in market value of securities purchased and investments (Notes 2 and 31)	8,103,499	15	6,327,182	13
General and administrative (Note 19)	13,571,917	25	12,958,665	27
Others	543,281	1	225,816	1
Total operating expenses	42,329,833	79	35,321,055	74
<b>OPERATING INCOME</b>	11,483,563	21	12,572,763	26
<b>NONOPERATING INCOME</b>	682,287	1	638,233	1
<b>NONOPERATING EXPENSES</b>	259,541	-	210,518	-
<b>INCOME BEFORE INCOME TAX</b>	11,906,309	22	13,000,478	27
<b>INCOME TAX (Notes 2 and 20)</b>	2,503,536	5	3,037,856	6
<b>NET INCOME</b>	\$ 9,402,773	17	\$ 9,962,622	21
	<b>Before Income Tax</b>	<b>After Income Tax</b>	<b>Before Income Tax</b>	<b>After Income Tax</b>
<b>BASIC EARNINGS PER SHARE (Note 21)</b>	\$ 3.21	\$ 2.54	\$ 3.51	\$ 2.69

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

**HUA NAN COMMERCIAL BANK, LTD.**  
**STATEMENTS OF CHANGES IN STOCKHOLDER'S EQUITY**  
**YEARS ENDED DECEMBER 31, 2005 AND 2004**

(In Thousands of New Taiwan Dollars)

(The Exchange Rates as of December 31, 2005 and 2004 were NT\$32.860 and NT\$31.768)

	Capital Stock		Capital Surplus (Notes 2 and 18)	
	Shares	Amount	Additional Paid-in Capital	Revaluation Increments on Properties
BALANCE, JANUARY 1, 2004	3,709,100,000	\$ 37,091,000	\$ 12,616,761	\$ -
Appropriation of 2003 earnings				
Legal reserve	-	-	-	-
Cash dividends	-	-	-	-
Bonuses to employees - cash	-	-	-	-
Return of additional paid-in capital used to offset 2002 deficit	-	-	-	2,769,243
Net income in 2004	-	-	-	-
Cumulative translation adjustments	-	-	-	-
BALANCE, DECEMBER 31, 2004	3,709,100,000	37,091,000	12,616,761	2,769,243
Appropriation of 2004 earnings				
Legal reserve	-	-	-	-
Cash dividends	-	-	-	-
Bonuses to employees - cash	-	-	-	-
Reserve for land revaluation increment tax	-	-	-	3,389,498
Capital surplus from equity-method investees	-	-	-	-
Net income in 2005	-	-	-	-
Cumulative translation adjustments	-	-	-	-
BALANCE, DECEMBER 31, 2005	<u>3,709,100,000</u>	<u>\$ 37,091,000</u>	<u>\$ 12,616,761</u>	<u>\$ 6,158,741</u>

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

## HUA NAN COMMERCIAL BANK, LTD. STATEMENTS OF CHANGES IN STOCKHOLDER'S EQUITY YEARS ENDED DECEMBER 31, 2005 AND 2004

(In Thousands of New Taiwan Dollars)

(The Exchange Rates as of December 31, 2005 and 2004 were NT\$32.860 and NT\$31.768)

Capital Surplus (Notes 2 and 18)		Retained Earnings (Note 18)			Cumulative Translation Adjustments (Note 2)	Total Stockholder's Equity
Others	Total	Legal Reserve	Revaluation Increments on Properties	Revaluation Increments on Properties		
\$ 2,077	\$ 12,618,838	\$ -	\$ 9,006,874	\$ 9,006,874	\$ ( 37,894)	\$ 58,678,818
-	-	2,702,062	( 2,702,062)	-	-	-
-	-	-	( 3,031,184)	( 3,031,184)	-	( 3,031,184)
-	-	-	(504,385)	( 504,385)	-	( 504,385)
-	2,769,243	-	( 2,769,243)	( 2,769,243)	-	-
-	-	-	9,962,622	9,962,622	-	9,962,622
-	-	-	-	-	( 65,580)	( 65,580)
2,077	15,388,081	2,702,062	9,962,622	12,664,684	( 103,474)	65,040,291
-	-	2,988,787	( 2,988,787)	-	-	-
-	-	-	( 5,563,650)	( 5,563,650)	-	( 5,563,650)
-	-	-	( 557,907)	( 557,907)	-	( 557,907)
-	3,389,498	-	-	-	-	3,389,498
( 752)	( 752)	-	-	-	-	( 752)
-	-	-	9,402,773	9,402,773	-	9,402,773
-	-	-	-	-	24,918	24,918
<u>\$ 1,325</u>	<u>\$ 18,776,827</u>	<u>\$ 5,690,849</u>	<u>\$ 10,255,051</u>	<u>\$ 15,945,900</u>	<u>\$ ( 78,556)</u>	<u>\$ 71,735,171</u>

**HUA NAN COMMERCIAL BANK, LTD.  
STATEMENTS OF CASH FLOWS**

**YEARS ENDED DECEMBER 31, 2005 AND 2004**

(In Thousands of New Taiwan Dollars)

(The Exchange Rates as of December 31, 2005 and 2004 were NT\$32.860 and NT\$31.768)

	2005	2004
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net income	\$ 9,402,773	\$ 9,962,622
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation and amortization	984,449	877,665
Amortization of premium on long-term bond investments	943,005	334,313
Gain on disposal of properties, net	( 173,300)	( 326,978)
(Gain) loss from disposal of long-term investments	( 105,162)	69,477
Valuation losses on long-term equity investment	310,745	-
Cash dividends from equity-method investees	81,908	81,930
Gain from equity investments under the equity method	( 71,213)	( 105,329)
Provision for reserves, bad debts and losses from decline in market value of securities purchased and investments	8,103,499	7,223,383
Deferred income tax	1,750,682	3,071,439
Net changes in operating assets and liabilities		
Accrued pension cost	104,192	165,254
Receivables and prepayments	( 2,015,499)	( 5,985,624)
Payables and advance collections	7,040,587	5,956,254
Others	( 449,622)	( 382,125)
Net cash provided by operating activities	<u>25,907,044</u>	<u>20,942,281</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
(Increase) decrease in due from the Central Bank and other banks	( 17,849,648)	15,185,111
Decrease in investment in bonds under resale agreement	375,595	230,000
Increase in bills purchased, discounts and loans	( 67,666,603)	( 34,084,988)
Decrease (increase) in securities purchase	25,969,622	( 26,072,749)
Proceeds from sale of long-term investments	664,137	10,160
Increase in long-term investments	( 19,239,753)	( 40,815,314)
Acquisition of properties	( 899,455)	( 1,339,979)
Proceeds from sale of properties	-	459,338
Increase in other assets	( 223,085)	( 810,612)
Net cash used in investing activities	<u>( 78,869,190)</u>	<u>( 87,239,033)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Decrease in due to the Central Bank and other banks	( 10,426,850)	( 23,378,655)
Increase (decrease) in bonds sold under agreements to repurchase	437,001	( 147,646)
Increase in deposits and remittances	74,764,990	84,764,573
Increase in bank debenture payable	2,363,000	10,000,000
(Decrease) increase in other liabilities	( 1,490,457)	410,509
Cash dividends paid	( 5,564,347)	( 3,031,184)
Bonuses paid to employees	( 557,811)	( 504,385)
Net cash provided by financing activities	<u>59,525,526</u>	<u>68,113,212</u>
<b>INCREASE IN CASH</b>	\$ 6,563,380	\$ 1,816,460
<b>CASH, BEGINNING OF YEAR</b>	<u>27,898,980</u>	<u>26,082,520</u>
<b>CASH, END OF YEAR</b>	<u>\$ 34,462,360</u>	<u>\$ 27,898,980</u>
<b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION</b>		
Interest paid	\$ 18,759,298	\$ 14,681,072
Income tax paid	\$ 903,390	\$ 741,292
<b>NONCASH INVESTING ACTIVITIES</b>		
Reduction of land revaluation increment tax recorded incapital surplus	\$ 3,389,498	\$ -
Long-term investments reclassified as securities purchased	\$ 1,216,750	\$ -

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

**HUA NAN COMMERCIAL BANK, LTD.  
NOTES TO FINANCIAL STATEMENTS  
YEARS ENDED DECEMBER 31, 2005 AND 2004**

(In Thousands of New Taiwan Dollars, Unless Stated Otherwise)

## 1. ORGANIZATION AND OPERATIONS

Hua Nan Commercial Bank, Ltd. (the “Bank” ) was established on March 1, 1947 through the restructuring of the China and Southern Bank, which was founded in 1919. The Bank engages in (a) all commercial banking operations allowed by the Banking Law; (b) international banking operations; (c) overseas branch operations authorized by the respective foreign governments; and (d) other operations as authorized by the central authorities.

The Bank maintains its head office in Taipei. As of December 31, 2004, the Bank had Banking, Financing, International Banking and Trust Departments as well as 196 domestic branches and representative offices, an offshore banking unit (OBU), 5 overseas branches, and 2 overseas representative offices.

The operations of the Bank's Trust Department are (1) trust business planning, managing and operating and (2) custody of nondiscretionary trust funds in domestic and overseas securities and mutual funds. These operations are regulated under the Banking Law and the Trust Law.

Under the Financial Holding Company Law, the Bank and EnTrust Securities Co., Ltd. ( “EnTrust” ) established Hua Nan Financial Holdings Co., Ltd. (HNFH), a financial holding company, through stock conversion on December 19, 2001. The parties established the holding company to maximize the benefit of their combined capital, pool their business channels, and fully harness the synergy of the diversified business operations. The Bank and EnTrust exchanged issued shares with HNFH at ratios of 1:1 and 1.2821:1 ( “1” refers to HNFH), respectively, and the stockholders approved this share swap on November 14, 2001. The board of directors resolved the effective date of stock conversion as December 19, 2001. Thus, on December 19, 2001, the shares of the Bank, HNFH, and HNFH's wholly owned subsidiary (the subsidiary's shares have no quoted market price) became listed on the Taiwan Stock Exchange (TSE). EnTrust was renamed Hua Nan Securities Co., Ltd. (HNSC) in June 2003. The Bank and HNSC became wholly owned subsidiaries of HNFH.

As of December 31, 2005 and 2004, the Bank had 7,738 and 7,322 employees, respectively.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### Basis of Presentation

The accompanying financial statements include the accounts of the Head Office, OBU, all domestic and overseas branches and representative offices. All interoffice account balances and transactions have been eliminated.



The Bank's financial statements were prepared in conformity with Guidelines Governing the Preparation of Financial Reports by Public Banks (amended on January 1, 2004), Guidelines Governing the Preparation of Financial Reports by Securities Issuers (amended in 2003) and accounting principles generally accepted in the Republic of China (ROC). In preparing financial statements in conformity with these guidelines and principles, the Bank is required to make certain estimates and assumptions that could affect the amounts of allowance for doubtful accounts, allowance for credit losses and pension. Actual results could differ from these estimates.

Since the length of the operating cycle in the banking industry could not be reasonably identified, accounts included in the Bank's financial statements were not classified as current or noncurrent. Nevertheless, accounts were properly categorized according to the nature of each account and sequenced by their liquidity. The maturity analysis of the Bank's assets and liabilities is shown in Note 25.

For the convenience of readers, 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 financial statements shall prevail. However, the accompanying financial statements do not include English translation of the additional footnote disclosures that are not required under generally accepted accounting principles but are required by the Securities and Futures Bureau (SFB, formerly the "Securities and Futures Commission" before July 1, 2004) for their oversight purposes.

The Bank's significant accounting policies are summarized as follows:

#### **Securities Purchased**

Securities purchased, which consist of government bonds, corporate bonds, financial bonds, short-term negotiable instruments, foreign securities, listed and over-the-counter stocks and beneficiary certificates of mutual funds, are stated at the lower of aggregate cost or market on the balance sheet dates, taking into account country risk on foreign securities. However, preferred stocks are stated at cost. When the market value of securities purchased declines carrying value, an allowance is provided. If the market value recovers, the allowance will be reversed to the extent of the original carrying value.

Cost of securities sold is determined on the basis of the specific identification method, but the moving-average method is used for stocks and beneficiary certificates.

Under the "Guidelines Governing the Preparation of Financial Reports by Public Banks," amended on January 1, 2004, bond transactions under repurchase/resale agreements are treated as financing transactions.

## Nonperforming Loans

Under relevant regulations, the balance of overdue loans and other credits extended by the Bank and the related accrued interest are classified as nonperforming loans.

## Allowance for Credit Losses and Provision for Losses on Guarantees

The Bank determines the allowance for credit losses and provision for losses on guarantees by evaluating the losses on particular loans and overall credit portfolio and considering the balances of bills purchased, discounts and loans, interest receivables, other receivables and nonperforming loans, as well as guarantees and acceptances on the balance sheet date.

Under the “Rules for Bank Asset Evaluation, Loss Reserve Provision, and Disposal of Overdue Loans and Bad Debts” , promulgated by the Ministry of Finance (MOF), the Bank evaluates credit losses on the basis of its borrowers'/clients' financial position, the Bank's prior lending experience, principal and interest payment record borrowers'/clients, collaterals provided, and estimated collectibility of the loans.

The Bank assesses losses on nonperforming loans (NPLs) in accordance with the above MOF rules. It also complies with the MOF requirements that the loan amount percentages shown below be used in setting up NPL provisions and that the minimum amount of provision for credit losses should be equal to 50% of the aggregate doubtful credits and 100% of the uncollectible credits.

Starting from July 1, 2005, the Bank's policy of provision for loans and non-performing loans is described as follows:

- (a) Class two (special mention credits): 2%
- (b) Class three (likely to be paid in full): 10%
- (c) Class four (doubtful collectibility): 50%
- (d) Class five (Entirely uncollectible): 100%

Under MOF guidelines, NPLs may be written off upon approval by the board of directors.

## Long-Term Investments

Long-term equity investments are accounted for by the equity method if the Bank has significant influence over the investees; otherwise, the Bank uses the cost method.

Investments accounted for by the equity method are stated at cost plus (or minus) a proportionate share in the investees' net earnings (losses) or changes in net worth. Shares in net earnings (net losses) are recognized as investment income (loss), and cash dividends received are accounted for as a reduction of the carrying value of the investments.

Investments accounted for by the cost method are carried at cost. Cash dividends received a year or more after the acquisition date are recognized as investment income. On the balance sheet dates, if the aggregate market value of listed stocks or over-the-counter stocks falls below cost, this unrealized decline in market value is debited to stockholder's equity. If a decline in the value of unlisted stocks is considered irreversible, the reduced market value becomes the new carrying value of the investment, and the realized loss is charged to current income.

For both equity-method and cost-method investments, stock dividends received result only in an increase in number of shares and are not recognized as investment income. Cost of long-term equity investments sold is determined by the weighted-average method.

Long-term bond investments are stated at cost. The premium or discount on acquisition is amortized using the straight-line method over the residual period of the bond, which is stated as an adjustment to interest revenue. Cost of bond investments matured or sold is determined by the specific identification method.

For securities purchased reclassified as the long-term investments or long-term investments reclassified as securities purchased, when the market value is lower than the carrying amount, a realized loss for market value decline is recognized, and the reduced market value becomes the new carrying value.

### **Properties**

Properties are stated at cost, or cost plus revaluation increments, less accumulated depreciation. Major renewals, additions and improvements are capitalized, while repairs and maintenance are expensed as incurred.

Depreciation is calculated using the straight-line method over the estimated useful lives of assets. Leasehold improvements are depreciated over the lease periods or five years, whichever is shorter. Revaluation increments are depreciated over the remaining useful lives on the revaluation dates. For assets still in use beyond their originally estimated service lives, further depreciation is calculated over the reestimated useful lives.

Upon disposal or other sale of properties, their cost and related accumulated depreciation are removed from the respective accounts. Any resulting gain (loss) is credited (charged) to current income. Up to December 31, 2000, gain on disposal of properties was recorded as nonoperating income and then transferred to capital surplus after deducting applicable income tax.

Impairment loss is recognized immediately for any significant decline in the value of property and equipment. If the loss is reversed, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, such that the increased carrying amount should not exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset in prior years. A reversal of an impairment loss is immediately recognized as gain.

### **Collaterals Assumed**

Collaterals assumed are recorded at cost (included in other assets) and revalued at the lower of cost or net realizable value on the balance sheet date.

### **Pension Costs**

According to the Regulations for Labor Retirement Fund, effective on July 1, 2005, employer should contribute amounts equal to not less than 6% of salary per month for each employee who chooses to apply for the “defined contribution plan” (the “DCP” ). The amounts contributed to the DCP are charged to expense when paid and deposited to specific reserved account of the Council of Labor Affairs.

Since its privatization on January 22, 1998, employee retirement benefits have been based on the Labor Standards Law, with the year of service restarted from January 22, 1998. Based on the Statement of Financial Accounting Standards No.18, “Accounting for Pensions” , pension costs of the defined benefit pension plan are recognized actuarially.

### **Recognition of Revenue**

Interest revenue on loans is recorded using the accrual basis. No interest revenue is recognized in the accompanying financial statements on loans and other credits extended by the Bank that are classified as nonperforming loans. The interest revenue on those loans/credits is recognized upon collection. Under Ministry of Finance regulations, the interest revenue on credits for which agreements have been reached to extend their maturities is recognized upon collection.

Service fees are recorded as income upon receipt or substantial completion of activities involved in the earnings process.

Preferred dividend is accrued according to issuance terms.

### **Income Tax**

Inter-period income tax allocation is applied, in which tax effects of loss carryforward, deductible temporary differences and unused investment tax credits are recognized as deferred income tax assets, and those of taxable temporary differences are recognized as deferred income tax liabilities. A valuation allowance is provided for deferred income tax assets that are not certain to be realized.

Tax credits for certain acquisitions of equipment or technology, research and development expenditures, personnel training expenditure and equity investments, are accounted for by the flow-through method.

Adjustments of prior year's tax liabilities are included in the current year's tax expense.

Income tax (10%) on unappropriated earnings after July 1, 1998 is recorded as income tax in the year when the stockholder resolves the appropriation of the earnings.

The Bank, HNHF, and HNHF's subsidiaries chose to adopt the linked-tax system in the filing of their returns. Under a directive issued by the Accounting Research and Development Foundation of the ROC, the linked-tax system requires a reasonable and systematic method for tax allocation. The tax allocation is recorded as receivables or payables.

#### Contingencies

A loss is recognized when it is probable that an asset has been impaired or a liability has been incurred and the amount of loss can be reasonably estimated. If loss is possible but the amount of the loss cannot be reasonably estimated, the information on the circumstances that might give rise to the loss should be disclosed in the notes to the financial statements.

#### Foreign-Currency Transactions

The Bank records foreign-currency transactions (except derivative transactions) in the respective currencies in which these are denominated at rates in effect when the transactions occur. Foreign-currency income and expenses are translated into New Taiwan dollars at the exchange rates announced by the Central Bank of China (CBC) at each month end. Foreign-currency assets and liabilities except those resulting from forward contracts, are translated into New Taiwan dollars on the balance sheet dates at closing rates published by the CBC. Realized and unrealized foreign exchange gains or losses resulting from these translations are credited or charged to current income. Retained earnings or accumulated deficits of overseas branches are translated into New Taiwan dollars at historical rates, and the resulting unrealized gains or losses are recorded as “cumulative translation adjustments” under stockholder's equity.

#### Derivative Financial Instruments

##### a. Forward exchange contracts

Foreign-currency assets and liabilities on forward exchange contracts, which are mainly for accommodating customers' needs or managing the Bank's currency positions, are recorded at the contracted forward rates. Gains or losses arising from the differences between the contracted forward rates and spot rates at settlement are credited or charged to current income. For contracts open as of the balance sheet dates, the gains or losses arising from the differences between the contracted forward rates and the forward rates available for the remaining maturities of the contracts are credited or charged to current income. Receivables and payables on the forward contracts are netted out on the balance sheet dates.

Non-deliverable forward contracts do not involve exchanges of principals upon settlement. The gains or losses

on the differences between the contracted forward rate and the spot rate at on settlement are recognized as foreign exchange gain or loss.

**b. Interest rate swap**

Interest rate swaps, which are used for nontrading purposes, do not involve exchanges of the contractual (notional) principals, which are recorded on the contract dates using memorandum entries. The net interest on each settlement is recorded as an adjustment to interest revenue or expense associated with the hedged item.

**c. Cross-currency swap**

Cross-currency swap contracts, which are for hedging purposes, are recorded at rates prevailing on the contract dates. The net interest on each settlement is recorded as an adjustment to interest revenue or expense associated with the hedged item.

Cross-currency swap contracts, which are for the purposes of accommodating customers' needs or managing the Bank's exposures, are marked to market as of the balance sheet dates.

The interest received or paid on the settlement date or balance sheet date is recognized as interest income or expense, which is credited or charged to current income.

**d. Currency swap contracts**

Foreign-currency spot-position assets or liabilities on currency swap contracts are recorded at spot rates when the transactions occur, while the corresponding forward-position assets or liabilities are recorded at the contracted forward rates. The difference between spot rate on the contract date and contracted forward rate is amortized by the straight-line method over the term of the contract and recorded as interest income or expense. On the balance sheet date, the receivables and payables contracts are netted out.

**e. Options**

Premiums paid or received for options are recorded as assets or liabilities, respectively, and are recognized as revenue or expense upon each settlement. Gains or losses on the exercise of these options are credited or charged to current income. Options outstanding on the balance sheet dates are marked to market, and the resulting gains or losses are recognized currently.

**3. CHANGE IN ACCOUNTING PRINCIPLE**

The Bank adopted Statement of Financial Accounting Standards ( "SFAS" ) No. 35, "Accounting for Impairment of Assets" , effective on January 1, 2005. This did not have material effect on the Bank's financial statements.

#### 4. CASH AND CASH EQUIVALENTS

	2005	2004
Notes and checks for clearing	\$ 21,995,932	\$ 12,324,635
Cash	8,133,300	7,990,477
Foreign currencies	615,163	609,170
Due from other banks	3,717,965	6,974,698
	<u>\$ 34,462,360</u>	<u>\$ 27,898,980</u>

#### 5. DUE FROM THE CENTRAL BANK

	2005	2004
Call loans to other banks	\$ 101,018,432	\$ 73,021,657
Reserve - checking accounts	11,426,982	23,054,986
Reserve - demand accounts	32,389,216	31,016,123
Reserve - foreign-currency deposit	115,010	3,177
Others	104,372	108,421
	<u>\$ 145,054,012</u>	<u>\$ 127,204,364</u>

Under the relevant regulations, the Bank maintains a certain amount of deposit at a prescribed rate based on the daily average of clients' deposits in the reserve-demand account. The reserve is subject to withdrawal restrictions and adjusted monthly. The reserve-demand account carries interest at a rate announced by the Central Bank.

Reserve - checking accounts and reserve - foreign-currency deposit are not interest bearing and may be withdrawn anytime.

#### 6. SECURITIES PURCHASED

	2005	2004
Certificate of deposit purchased	\$ 234,429,697	\$ 260,140,703
Foreign securities	45,539,859	43,165,564
Securities - dealing	15,238,323	19,368,734
Listed and over-the-counter stocks and beneficiary certificates	7,466,619	6,935,622
Treasury bills	-	990,302
Bonds	16,870,523	14,881,656
Securities purchased under resale agreements	344,404	720,000
Bank acceptances	-	3,693
Commercial paper	2,111,120	2,108,028
Securities - underwriting	612,846	644,308
	<u>322,613,391</u>	<u>348,958,610</u>
Less allowance for decline in market value	-	1,756,462
	<u>\$ 322,613,391</u>	<u>\$ 347,202,148</u>

As of December 31, 2005 and 2004, securities purchased that had been pledged as guarantee deposits or reserves are described in Note 12.

## 7. RECEIVABLES

	2005	2004
Acceptances receivable	\$ 9,220,438	\$ 8,826,798
Interest receivable	4,929,565	5,006,808
Accrued revenue	850,684	1,450,368
Receivables from lending to employees	194,853	208,617
Accounts receivable	8,025,487	5,539,639
Allocation receivables from related party on the linked-tax system	114,298	273,901
Receivable for advances on letters of credit	411,860	445,213
Receivable from clearing	173,890	163,291
Refundable tax	1,154,954	851,694
Others	<u>2,721,142</u>	<u>3,892,025</u>
	27,797,171	26,658,354
Less allowance for bad debts	<u>1,005,585</u>	<u>917,358</u>
	<u>\$ 26,791,586</u>	<u>\$ 25,740,996</u>

## 8. BILLS PURCHASED, DISCOUNTS AND LOANS

	2005	2004
Short-term loans		
Unsecured	\$ 296,017,392	\$ 239,706,406
Secured	115,044,650	111,633,843
Medium-term loans		
Unsecured	133,391,221	156,158,332
Secured	84,613,594	77,441,951
Long-term loans		
Unsecured	28,916,201	29,946,782
Secured	260,432,741	242,161,699
Bills discounted	29,637	20,617
Overdraft		
Unsecured	256,719	1,560,723
Secured	1,677,557	1,849,230
Bills purchased and import and outward bills	14,967,954	13,702,647
Nonperforming loans	<u>19,674,383</u>	<u>20,141,930</u>
	955,022,049	894,324,160
Less allowance for bad debts	<u>9,607,491</u>	<u>8,594,310</u>
	<u>\$ 945,414,558</u>	<u>\$ 885,729,850</u>

The unrecognized interest revenue on nonperforming loans was \$986,342 thousand in 2005 and \$1,232,151 thousand in 2004.

In 2005 and 2004, the Bank wrote off credits only after completing the required legal procedures.



The changes in the allowance for bad debts on loans, discounts and bills purchased in 2005 and 2004 are summarized below:

	2005			2004		
	Specific Risk	General Risk	Total	Specific Risk	General Risk	Total
Balance, January 1	\$ 6,450,644	\$ 2,143,666	\$ 8,594,310	\$ 7,216,495	\$ 3,098,912	\$ 10,315,407
Provision	7,843,675	331,383	8,175,058	7,102,24	( 898,961)	6,203,288
Write-off	( 7,105,151)	( 79,009)	( 7,184,160)	( 7,855,354)	( 21,214)	( 7,876,568)
Effects of exchange rate changes	4,389	17,894	22,283	( 12,746)	( 35,071)	( 47,817)
Balance, December 31	<u>\$ 7,193,557</u>	<u>\$ 2,413,934</u>	<u>\$ 9,607,491</u>	<u>\$ 6,450,644</u>	<u>\$ 2,143,666</u>	<u>\$ 8,594,310</u>

## 9. LONG-TERM INVESTMENTS

As of December 31, 2005 and 2004, long-term stock investments are summarized as follows:

	2005		2004	
	Amount	%	Amount	%
<b>Equity method</b>				
Stocks with no quoted market prices				
Hua Nan Bills Finance Co.	\$ 1,703,683	42.41	\$ 1,701,792	42.41
HNCB Insurance Agency Co., Ltd.	137,454	100.00	150,803	100.00
Chung-Hua Real Estate Management Co.	80,806	30.00	80,796	30.00
Total long-term equity investments under equity method	<u>1,921,943</u>		<u>1,933,391</u>	
<b>Cost method</b>				
Listed and over-the-counter stocks				
First Financial Holdings	-	-	1,216,750	2.97
Taiwan Business Bank	558,968	1.83	1,117,942	4.26
Taiwan Development Corporation	114,060	5.70	114,060	5.70
Chang Hwa Commercial Bank	143,395	0.38	143,395	0.38
Taiwan Navigation Co., Ltd.	42,979	1.88	42,979	1.88
Bank of Overseas Chinese	17,021	0.28	17,021	0.28
	<u>876,423</u>		<u>2,652,147</u>	
Stocks with no quoted market prices				
Taiwan Asset Management Corporation	2,000,000	11.35	2,000,000	11.35
Taiwan Power Co., Ltd.	1,184,504	0.45	1,184,504	0.45
Tang Eng Iron Works Co., Ltd.	310,745	8.88	621,490	8.88
CDIB & Partners Investment Holding Corp.	500,000	4.95	500,000	4.95
Taiwan Television Enterprise	81,570	7.25	81,570	7.25
Taiwan Stock Exchange Co.	72,000	3.00	72,000	3.00
Fuyu Venture Capital Investment Co.	60,000	4.44	60,000	4.44
Taiwan Financial Asset Service Corporation	50,000	2.94	50,000	2.94
Financial Information Service Co., Ltd.	46,358	1.15	46,358	1.15
Capital Venture Management Co.	30,000	5.00	30,000	5.00
Taiwan Sugar Corp.	28,029	0.14	28,029	0.14
Others	54,278	-	54,278	-
	<u>4,417,484</u>		<u>4,728,229</u>	
	<u>5,293,907</u>		<u>7,380,376</u>	
Total long-term stock investments	<u>\$ 7,215,850</u>		<u>\$ 9,313,767</u>	

As of December 31, 2005 and 2004, other long-term investments are summarized as follows:

	2005	2004
<b>Preferred stock</b>		
Taiwan High Speed Rail Corporation	\$ 2,000,000	\$ 2,000,000
Taishin Financial Holding Co., Ltd.	300,000	-
Chinatrust Financial Holding Co., Ltd.	280,000	-
	<u>2,580,000</u>	<u>2,000,000</u>
<b>Government Bonds</b>		
Government Bond A93-7	5,661,320	-
Government Bond A90-1	4,482,627	4,586,440
Government Construction 89-8	3,770,375	3,922,050
Government Construction 89-5	3,598,560	3,700,862
Government Construction 87-1	2,310,903	2,415,712
Government Construction 86-2	2,082,540	2,191,221
Others	4,816,310	13,394,471
	<u>26,722,635</u>	<u>30,210,756</u>
<b>Corporate Bonds</b>		
91 Taiwan Power 4B07	607,286	303,496
91 Yuan Ding 1B01	509,815	516,293
91 Yuan Ding 1A02	509,373	-
93 Uni-President 2A	505,101	-
91 Union Textile 0418	504,343	507,701
93 Eternal 1A	504,196	-
93 Taiwan Power 3A07	503,457	-
94 AU Optronics 1A03	500,545	-
94 AU Optronics 1A02	500,545	-
94 AU Optronics 1B03	500,377	-
93 Uni-President 2D	500,000	-
93 Uni-President 2E	500,000	-
93 Uni-President 2F	500,000	-
93 Uni-President 2G	500,000	-
94 AU Optronics 1B06	499,805	-
94 Taiwan Power 2A01	499,130	-
94 Taiwan Power 2B03	498,933	-
94 Taiwan Power 2B04	498,282	-
93 Taiwan Power 2B02	496,504	-
Test Rite 881A	441,741	460,426
90 Taiwan Power 1A02	403,919	413,650
90 Far Eastern Textile 1A03	402,231	404,625
Others	12,479,484	6,452,987
	<u>23,365,067</u>	<u>9,059,178</u>
<b>Financial Bonds</b>		
91 Chiao Tung Bank 1630	706,599	712,123
94 E. Sun Bank 1H	532,018	-
94 E. Sun Bank 1J	532,016	-
94 E. Sun Bank 1G	532,013	-
94 E. Sun Bank 1I	532,013	-
94 Cathay United Bank 1A	503,474	-
91 Taipei Fubon Bank 3A	499,328	498,944
92 Council of Europe Development Bank 1H	459,440	-
Others	3,813,146	-
	<u>8,110,047</u>	<u>1,211,067</u>
	<u>\$ 60,777,749</u>	<u>\$ 42,481,001</u>

As of December 31, 2005 and 2004, the aggregate market values of listed and over-the-counter stocks, government bonds, corporate bonds, and financial bonds totaled \$59,680,910 thousand and \$47,556,302 thousand, respectively.

The Bank recognized \$71,213 thousand and \$105,329 thousand income from long-term equity investments under the equity method in 2005 and 2004, respectively. The calculation of the carrying amounts of the equity-method investments as of December 31, 2005 and 2004 and the related investment income for the years then ended was based on the investees' audited financial statements.

## 10.PROPERTIES

	2005	2004
Land		
Cost	\$ 2,759,038	\$ 2,832,320
Revaluation increments	<u>8,911,066</u>	<u>8,979,836</u>
	<u>\$ 11,670,104</u>	<u>\$ 11,812,156</u>
Buildings		
Cost	\$ 11,337,497	\$ 11,049,040
Revaluation increments	<u>42,066</u>	<u>42,101</u>
	<u>\$ 11,379,563</u>	<u>\$ 11,091,141</u>
Accumulated depreciation		
Buildings		
Cost	\$ 3,254,207	\$ 3,000,797
Revaluation increments	<u>12,074</u>	<u>11,434</u>
	<u>3,266,281</u>	<u>3,012,231</u>
Office equipment	3,555,052	3,379,221
Transportation equipment	702,256	695,779
Other equipment	1,265,215	1,174,996
Lease improvements	<u>315,514</u>	<u>270,394</u>
	<u>\$ 9,104,318</u>	<u>\$ 8,532,621</u>

The Bank revalued its land and buildings several times in prior years. As of December 31, 2005, land and building revaluation increments (for both operating and nonoperating assets) amounted to \$14,712,342 thousand; reserve for land value increment tax (included in long-term liabilities) amounted to \$4,807,252 thousand. The law on land tax was amended on January 1, 2005, and announced on February 1, 2005. According to this law, the Bank reduced by \$3,389,498 thousand the reserve for land revaluation increment tax. The reduction was recorded in capital surplus.

No properties had been pledged as collateral as of December 31, 2004.

## 11. OTHER ASSETS

	2005	2004
Deferred income tax assets, net	\$ 4,334,433	\$ 6,085,115
Nonoperating assets, net	8,215,844	8,416,430
Refundable deposits	1,126,038	1,510,995
Collaterals assumed, net	2,103,183	1,189,663
Other assets to be settled	88	91,241
Other	<u>8,229</u>	<u>21,968</u>
	<u>\$ 15,787,815</u>	<u>\$ 17,315,412</u>

Nonoperating assets consisted of:

	2005	2004
Land		
Cost	\$ 1,779,301	\$ 1,849,596
Revaluation increments	<u>5,746,738</u>	<u>5,864,121</u>
	<u>7,526,039</u>	<u>7,713,717</u>
Buildings		
Cost	955,037	952,220
Revaluation increments	<u>12,472</u>	<u>12,500</u>
	<u>967,509</u>	<u>964,720</u>
Total cost and revaluation increments	8,493,548	8,678,437
Less accumulated depreciations	<u>277,704</u>	<u>262,007</u>
	<u>\$ 8,215,844</u>	<u>\$ 8,416,430</u>

Buildings and part of the land included in nonoperating assets had been leased to other entities.

## 12. PLEDGED ASSETS

	2005	2004
Certificates of deposit purchased	\$ 10,000,000	\$ 9,000,000
Bonds - par value	<u>1,371,400</u>	<u>977,400</u>
	<u>\$ 11,371,400</u>	<u>\$ 9,977,400</u>

Information on pledged bonds is as follows:

	2005	2004
Guarantee deposit for provisional seizure of collaterals due to loan defaults and others	\$ 1,130,800	\$ 733,700
Guarantee deposit for clearing reserve	90,000	90,000
Guarantee deposit for securities trading operations	50,000	50,000
Guarantee deposit for trust business compensation reserve	50,000	50,000
Guarantee deposits for bills trading operations	50,000	50,000
Others	<u>600</u>	<u>3,700</u>
	<u>\$ 1,371,400</u>	<u>\$ 977,400</u>

### 13. DUE TO THE CENTRAL BANK AND OTHER BANKS

	2005	2004
Deposits from the Central Bank	\$ 303,792	\$ 273,938
Call loans from other banks	69,922,960	85,232,762
Overdraft	6,624,129	4,975,851
Deposits from other banks	<u>3,689,618</u>	<u>484,798</u>
	<u>\$ 80,540,499</u>	<u>\$ 90,967,349</u>

### 14. PAYABLES

	2005	2004
Notes and checks in clearing	\$ 21,995,932	\$ 12,324,635
Bank acceptances payable	9,619,222	9,345,976
Interest payable	4,469,624	3,997,446
Accrued expenses	2,058,330	1,950,349
Collections for others	2,723,531	1,815,179
Tax payable	492,165	417,221
Dividend payable	300,376	300,977
Others	<u>7,381,429</u>	<u>11,831,185</u>
	<u>\$ 49,040,609</u>	<u>\$ 41,982,968</u>

### 15. DEPOSITS AND REMITTANCES

	2005	2004
Savings deposits	\$ 665,728,816	\$ 640,279,536
Time deposits	312,765,984	260,301,819
Demand deposits	247,809,805	257,876,073
Checking account deposits	57,293,309	50,155,020
Negotiable certificates of deposits	7,592,000	7,884,300
Remittances	<u>901,508</u>	<u>829,684</u>
	<u>\$ 1,292,091,422</u>	<u>\$ 1,217,326,432</u>

## 16. BANK DEBENTURES PAYABLE

	2005	2004
90-1 term 10-year subordinated debentures; 4.20% fixed rate; maturity on August 30, 2011; the rate will become floating if the Bank cannot redeem the debenture by August 30, 2006	\$ 6,200,000	\$ 6,200,000
90-2 term seven-year subordinated debenture; 3.80% fixed rate; maturity on October 22, 2008	3,800,000	3,800,000
91-1 term five-year subordinated debenture; 4.10% fixed rate; maturity on April 29, 2007	4,250,000	4,250,000
91-2 term five-year subordinated debenture; 4.10% fixed rate; maturity on April 29, 2007	700,000	700,000
91-3 term five-year subordinated debenture; 4.10% fixed rate; maturity on May 20, 2007	880,000	880,000
91-4 term five-year subordinated debenture; 4.10% fixed rate; maturity on May 20, 2007	1,070,000	1,070,000
91-5 term five-year subordinated debenture; 3.75% simple interest rate in first three years and floating rate in last two years; maturity on May 20, 2007	300,000	300,000
91-6 term five-year subordinated debenture; floating rate; maturity on May 20, 2007	300,000	300,000
91-7 term seven-year subordinated debenture; floating rate; maturity on May 20, 2009	5,000,000	5,000,000
91-8 term seven-year subordinated debenture; floating rate; maturity on June 18, 2009	2,500,000	2,500,000
92-1 term eight-year debenture; floating interest rate in the first five years, 1.5% in the sixth year and 0.5% in the seventh and eighth years; maturity on February 24, 2011	2,480,000	2,480,000
92-2 term seven-year debenture; floating interest rate; maturity on February 27, 2010	1,500,000	1,500,000
92-3 term eight year debenture; floating interest rate; maturity on February 27, 2011	500,000	500,000
92-4 term eight-year debenture; floating interest rate; maturity on February 27, 2011	490,000	490,000
92-5 term five-year debenture; floating interest rate; maturity on September 10, 2008	1,200,000	1,200,000
92-6 term five-year debenture; floating interest rate; maturity on October 7, 2008	1,000,000	1,000,000
92-7 term five-year debenture; floating interest rate; maturity on October 7, 2008	300,000	300,000
92-8-1 term two-year subordinated debenture; fixed interest rate; maturity on October 16, 2005	-	2,937,000
92-8-2 term three-year subordinated debenture; fixed interest rate; maturity on October 16, 2006	1,563,000	1,563,000
92-9 term five-year debenture; floating interest rate; maturity on November 7, 2008	2,100,000	2,100,000
92-10 term five-year subordinated debenture; fixed rate; maturity on May 7, 2009	3,000,000	3,000,000
92-11 term seven-year subordinated debenture; floating interest rate; maturity on November 27, 2010	2,600,000	2,600,000
92-12 term seven-year debenture; floating interest rate; maturity on November 27, 2010	-	1,000,000
92-13 term seven-year debenture; floating interest rate; maturity on November 27, 2010	1,000,000	1,000,000
92-14 term five-year debenture; floating interest rate; maturity on December 16, 2008	4,000,000	4,000,000
93-1 term seven-year debenture; floating interest rate; maturity on March 15, 2011	3,000,000	3,000,000
93-2 term five-year and six-month subordinated debentures; floating interest rate; maturity on September 25, 2010	2,000,000	2,000,000
93-2 term five-year and six-month subordinated debentures; fixed rate; maturity on September 25, 2010	2,000,000	2,000,000
93-3 term seven-year debentures; floating interest rate; maturity on May 14, 2011	1,000,000	1,000,000
93-3 term five-year and six-month debenture; floating interest rate; maturity on November 14, 2009	1,000,000	1,000,000
93-3 term five-year and six-month debentures; floating interest rate; maturity on November 14, 2009	1,000,000	1,000,000
94-1 term seven-year subordinated debenture; fixed interest rate; maturity on January 28, 2012	3,300,000	-
94-2 term seven-year subordinated debentures; fixed interest rate; maturity on February 2, 2012	3,000,000	-
	<u>\$ 63,033,000</u>	<u>\$ 60,670,000</u>

## 17. OTHER LIABILITIES

	2005	2004
Reserve for land value increment tax (Note 11)	\$ 4,807,252	\$ 8,372,351
Funds received for sub-loans	506,953	791,490
Accrued pension costs (Note 23)	424,022	319,829
Guarantee deposits received	1,379,239	2,353,122
Reserve for losses on guarantees	184,315	504,305
Deferred revenue	127,575	220,485
Reserve for securities trading losses	200,000	200,000
Others	289,756	13,294
	<u>\$ 7,919,112</u>	<u>\$ 12,774,876</u>

## 18. STOCKHOLDER'S EQUITY

### Capital Surplus

Under the Company Law, capital surplus from the issuance of shares in excess of par value and donation may be appropriated to common stock with the approval of stockholders.

Under the regulations issued by the Securities and Futures Bureau, capital surplus from the issue of shares in excess of par value may, except in the year the surplus arises, be distributed as stock dividends. This distribution may be made only once a year and within other specified limits.

Capital surplus from equity-method long-term equity investments may not be distributed for any purpose.

### Dividend Policy and Appropriation of Retained Earnings

The Articles of Incorporation stipulates that from annual net income net of any accumulated deficit, 30% should be appropriated as legal reserve until the reserve equals the Bank's paid-in capital. A special reserve based on business needs may then be appropriated. Any remainder should be appropriated as follows:

- a. 1% to 8% as bonuses to employees. The board of directors (BOD) is authorized to resolve the bonus percentage.
- b. Dividends. The BOD is authorized to appropriate dividends according to the economic environment and the Bank's development needs. The cash dividend should be at least one third of total dividends and approved by the stockholders' annual meeting.

In contrast to the Company Law, the Financial Holding Company Law provides that the board of directors are authorized to execute the rights and functions of stockholders' meetings.

Under the Company Law, legal reserve should only be used to offset deficit. When the reserve reaches 50% of paid-in capital, up to 50% thereof may be capitalized. In addition, the Banking Law provides that, when the legal reserve reaches the amount of paid-in capital, annual cash dividends should not exceed 15% of capital.

The appropriation of the 2004 earnings approved by the BOD on April 25, 2004 was as follows:

Bonuses to employees	\$557,907
Cash dividends	<u>5,563,650</u>
	<u>\$ 6,121,557</u>

## 19. OPERATING AND ADMINISTRATIVE EXPENSES

	2005			2004		
	Operating Expenses	Administrative Expenses	Total	Operating Expenses	Administrative Expenses	Total
Personnel expenses						
Salaries and wages	\$ 4,715,234	\$ 819,787	\$ 5,535,021	\$ 4,641,991	\$ 677,920	\$ 5,319,911
Labor insurance and national health insurance expenses	271,799	46,735	318,534	268,025	33,765	301,790
Pension	665,896	84,742	750,638	600,017	81,750	681,767
Others	1,746,208	322,233	2,068,441	1,697,836	235,405	1,933,241
Depreciation	778,116	38,780	816,896	713,672	32,404	746,076
Amortization	101,466	-	101,466	63,851	-	63,851
Tax other than income tax	1,127,783	3,746	1,131,529	1,014,631	3,017	1,017,648
Rental	963,844	2,903	966,747	950,768	3,097	953,865
Other	1,830,406	52,239	1,882,645	1,895,279	45,237	1,940,516
	<u>\$ 12,200,752</u>	<u>\$ 1,371,165</u>	<u>\$ 13,571,917</u>	<u>\$ 11,846,070</u>	<u>\$ 1,112,595</u>	<u>\$ 12,958,665</u>

## 20. INCOME TAX

Under a Ministry of Finance directive, a financial holding company and its domestic subsidiaries that hold over 90% of issued shares of the financial holding company for 12 months within the same taxation year may adopt the linked-tax system for income tax filing. In 2002, Hua Nan Financial Holdings Co., Ltd. (HNFH) and its qualified subsidiaries, including the Bank and Hua Nan Securities Co., Ltd. (HNSC), adopted the linked tax system for income tax filings.

The principle adopted by the Bank, HNFH, HNSC, SCIC and HNIT (collectively, the “Group”) under the linked-tax system is to reduce the income tax liabilities of the Group and to consider the fairness of the tax borne by all the three companies in order to maximize the synergy of the Group.

Tax on pretax income at statutory rate and current income tax expense are reconciled as follows:

	2005	2004
Tax on pretax income at statutory rate (25%)	\$ 2,976,567	\$ 3,250,109
Permanent differences	( 782,390)	( 314,852)
Temporary differences	-	( 225,679)
Income tax payable, current	<u>2,194,177</u>	<u>2,709,578</u>
Tax on unappropriated earnings (10%)	280,893	201,507
Deferred income tax	28,466	126,771
Income tax expense	<u>\$ 2,503,536</u>	<u>\$ 3,037,856</u>



Deferred income tax assets (included in other assets) as of December 31, 2005 and 2004 are summarized as follows:

	2005	2004
Deferred income tax assets		
Loss carryforwards	\$ 4,410,069	\$ 6,358,208
Tax credits	-	2,367
Provision for bad debts and losses on guarantees	48,328	46,722
Interest revenue	7,825	7,565
Other	95,883	44,907
	4,562,105	6,459,769
Effect of the adoption of the linked tax system	( 227,672)	( 374,654)
	\$ 4,334,433	\$ 6,085,115

The loss carryforwards and tax credits as of December 31, 2005 can be used to reduce the Bank's taxable income up to 2007.

The receivable and payable on the adoption of the linked tax system were as follows:

	December 31, 2005
Refundable tax receivable from the parent company	\$ 376,386
Tax payable to the parent company	( 262,088)
	\$ 114,298

The balances of imputation credit account as of December 31, 2005 and 2004 were \$194,251 and \$139,797 respectively.

The actual creditable tax ratio for the 2004 earnings was 1.27%.

The Bank's income tax returns through 2001 had been examined by the tax authorities as of December 31, 2005.

## 21. EARNINGS PER SHARE

The numerator and denominator used in computing earnings per share are summarized as follows:

	2005				
	Net Income		Denominator (Shares in Thousands)	Earnings Per Share (Dollars)	
	Pretax	After Tax		Pretax	After Tax
Basic earnings per share					
Net earnings of common stockholder	\$ 11,906,309	\$ 9,402,773	3,709,100	\$ 3.21	\$ 2.54
	2004				
	Net Income		Denominator (Shares in Thousands)	Earnings Per Share (Dollars)	
	Pretax	After Tax		Pretax	After Tax
Basic earnings per share					
Net earnings of common stockholder	\$ 13,000,478	\$ 9,962,622	3,709,100	\$ 3.51	\$ 2.69

## 22. PENSION

According to the Regulations for Labor Retirement Fund, effective on July 1, 2005, the Bank contributed amounts equal to 6% of salary per month for each employee. The contributed amount totaled \$35,846 thousand for the six-month ended December 31, 2005.

For employees eligible for pension, service years were restarted on January 22, 1998 and calculation of pension benefits began to be based on the Labor Standards Law. The Bank's current contributions of amounts equal to 12% of salaries and wages to a pension fund, a rate approved by the government, are deposited in the Central Trust of China.

a. Net pension costs in 2005 and 2004 are summarized below:

	2005	2004
Service cost	\$ 651,682	\$ 636,072
Interest cost	122,599	102,704
Actual return on plan assets	( 47,126)	( 33,754)
Loss on plan assets	( 46,698)	( 53,341)
Amortization	26,702	14,428
Net pension cost	<u>\$ 707,159</u>	<u>\$ 666,109</u>

b. The reconciliations of the fund status of the plan and accrued pension cost as of December 31, 2005 and 2004 are as follows:

	2005	2004
Benefit obligation		
Vested benefit obligation	\$ 2,235,464	\$ 1,824,744
Non-vested benefit obligation	1,497,575	1,307,819
Accumulated benefit obligation	3,733,039	3,132,563
Additional benefits based on future salaries	1,260,296	1,158,278
Projected benefit obligation	4,993,335	4,290,841
Fair value of plan assets	( 3,449,977)	( 3,165,853)
Fund status	1,543,358	1,124,988
Unrecognized pension loss	( 1,119,336)	( 805,159)
Accrued pension cost	<u>\$ 424,022</u>	<u>\$ 319,829</u>
c. Vested benefits - undiscounted	<u>\$ 2,700,416</u>	<u>\$ 2,257,831</u>
d. Actuarial assumptions		
Discount rate used in determining present values	2.50%	3.00%
Future salary increase rate	2.50%	2.75%
Expected rate of return on plan assets	2.50%	3.00%

The changes in the pension fund are summarized below:

	2005	2004
Balance, January 1	\$ 3,165,853	\$ 2,688,182
Contributions	441,785	484,298
Interest income	47,126	33,754
Benefits paid	( 204,787)	( 40,381)
Balance, December 31	<u>\$ 3,449,977</u>	<u>\$ 3,165,853</u>

## 23. RELATED-PARTY TRANSACTIONS

The Bank's related parties are as follows:

Related Party	Relationship with the Bank
Hua Nan Financial Holdings Co., Ltd. (HNFH)	Parent company
Bank of Taiwan Co., Ltd. (BOT)	Majority stockholder of parent company
Hua Nan Bills Finance Corporation (HNBF)	Parent company's subsidiary
HNCB Insurance Agency Co., Ltd. (HNCB Insurance Agency)	Bank subsidiary
Hua Nan Securities Corp. (HNSC)	Subsidiary of the Parent Company
Hua Nan Investment Trust Corporation (HNIT)	Subsidiary of the Parent Company
South China Insurance Co., Ltd. (SCIC)	Subsidiary of the Parent Company
Hua Nan Asset Management Corp. (HNAMEC)	Subsidiary of the Parent Company
Hua Nan Futures Co., Ltd. (HNFC)	Substantial related party
Hua Nan Holdings Corp.[formerly EnTrust (BVI) Holdings Corp.]	Substantial related party
Hua Nan International Limited [formerly EnTrust International (Cayman) Limited]	Substantial related party
Hua Nan Asset Management Corp. [formerly EnTrust Global Management (Cayman) Limited]	Substantial related party
Hua Nan Securities (HK) Limited [formerly EnTrust Securities (HK) Limited] ( "Hua Nan Securities HK" )	Substantial related party
Hua Nan Investment Management Co., Ltd (HNIM)	Substantial related party
Hua Nan Venture Capital Co., Ltd. (HNVC)	Subsidiary of the Parent Company
Hua Nan Management & Consulting Co., Ltd. (HNMC)	Subsidiary of the Parent Company
Yung-Da Real Estate & Construction Co., Ltd. ( "Yung-Da Real Estate & Construction" )	Its chairperson is the wife of the Bank's chairman
Others	Directors, supervisors, managers, their relatives, companies under their control, and other related parties in substance

Significant related-party transactions were as follows:

### Due from Other Banks

	2005		2004	
	Amount	%	Amount	%
BOT	\$ 166,135	0.11	\$ 331,246	1.19

### Due to Other Banks

	2005		2004	
	Amount	%	Amount	%
BOT	\$ 6,457	-	\$ 6,250	-

### Call Loans to Other Banks

	2005				2004			
	Highest Balance	Ending Balance	Interest Income	Interest Rate (%)	Highest Balance	Ending Balance	Interest Income	Interest Rate (%)
BOT	\$ 13,080,036	\$ 3,258,002	\$ 64,091	1.20~4.63	\$ 15,649,730	\$ 2,367,820	\$ 38,258	0~2.44
HNBF	1,500,000	-	908	1.21~1.45	3,780,000	-	5,795	0.935~1.185
		\$ 3,258,002	\$ 64,999			\$ 2,367,820	\$ 44,053	

### Call Loans from Other Banks

	2005				2004			
	Highest Balance	Ending Balance	Interest Income	Interest Rate (%)	Highest Balance	Ending Balance	Interest Income	Interest Rate (%)
BOT	\$ 8,600,400	\$ 1,971,600	\$ 51,785	1.19~4.37	\$ 12,488,960	\$ 1,906,080	\$ 42,528	0.94~2.55
HNBF	500,000	-	52	1.27				
		<u>\$ 1,971,600</u>	<u>\$ 51,837</u>					

### Loans and Advances

	2005				2004			
	Highest Balance	Ending Balance	Interest Income	Interest Rate (%)	Highest Balance	Ending Balance	Interest Income	Interest Rate (%)
Others	\$ 2,315,481	\$ 1,675,373	\$ 29,249	1.50~5.32	\$ 1,891,891	\$ 1,649,071	\$ 29,461	1.55~6.749

In compliance with Banking Law, except for customer loans, credits extended by the Bank to any related party should be 100% secured, and the terms of credits extended to related parties should be similar to those extended to third parties.

### Deposits

	2005		2004	
	Amount	Interest Rate (%)	Amount	Interest Rate (%)
HNFB	\$ 6,057,564	0~0.80	\$ 4,601,436	0~0.70
HNFC	192,165	0~1.74	1,101,578	0~1.425
Hua Nan Securities (HK)	447,041	0.01~0.25	489,475	0.01
HNCB Insurance Agency	1,700,082	0~1.525	598,473	0~1.425
HNSC	338,725	0~1.645	296,613	0~1.425
HNIM	20,495	0~1.645	48,695	0~1.425
SCIC	119,253	0~1.85	228,032	0~1.425
HNBF	355,765	0~0.55	96,043	0~0.25
HNVC	220,027	0.10~1.525	96,676	0~0.10
HNAMC	11,841	0~1.31	-	-
HNIT	14,302	0~0.50	4,993	0~0.20
Others	11,693,009	0~13.00	7,187,185	0~13.00
	<u>\$ 21,170,269</u>		<u>\$ 14,749,199</u>	

### Guarantee Deposits Paid

	2005		2004	
	Amount	%	Amount	%
HNFC	\$ 134,596	-	\$ -	-

### Securities (Accumulated Face Amounts)

		2005	2004
HNBF	Outright purchase	\$ 12,041,000	\$ 1,958,000
	Outright sale	16,659,000	3,900,000
	Short-term bills and bonds purchased under resell agreements	150,000	-
HNSC	Outright purchase	6,750,000	6,120,000
	Outright sale	1,426,100	800,500
	Short-term bills and bonds purchased under resell agreements	-	468,000

Interest Expense

	2005		2004	
	Amount	%	Amount	%
HNFH	\$ 38,887	0.20	\$ 19,256	0.13

Service Charges

	2005		2004	
	Amount	%	Amount	%
HNSC	\$ 6,636	0.15	\$ 7,696	0.19
SCIC	24,232	0.56	17,093	0.42
HNIT	9,664	0.22	6,792	0.18
	\$ 40,532		\$ 31,581	

Service charges are the premium of synergy business from HNSC, SCIC and HNIT.

There is no the same kind of trade can be compared.

Lease

The Bank rents out office to HNCB Insurance Agency, with rentals payable monthly under an operating lease agreement expiring in February 2006. Rentals received in 2005 and 2004 amounted to \$2,498 thousand each.

The Bank rents out office space to HNSC, with rentals payable monthly under an operating lease agreement expiring in November 2007. Guarantee deposits received amounted to \$809 thousand, and rentals received amounted to \$18,176 thousand in 2005 and \$14,714 in 2004.

The Bank rents office space from Yung-Da Real Estate & Construction, with refundable deposits of \$158,400 thousand replacing rentals, under an operating lease agreement ending in November 2006. The rentals amounted to \$3,041 thousand in 2005 and \$2,257 thousand in 2004.

The Bank rents out office space to HNFH, with rentals payable monthly under an operating lease agreement expiring in September 2008. Rentals received in 2005 and 2004 amounted to \$2,888 thousand each.

The Bank rents out office space to HNBF, with rentals payable monthly under an operating lease agreement expiring in February 2006. Guarantee deposits received amounted to \$176 thousand, and rentals received in 2005 and 2004 amounted to \$704 thousand each.

The Bank rents out office space to HNIT, with rentals payable monthly under an operating lease agreement expiring in June 2006. Rentals received amounted to \$256 thousand in 2005 and 2004.

The Bank rents out office space to SCIC, with rentals payable monthly under an operating lease agreement expiring in February 2007. Rentals received amounted to \$2,958 thousand in 2005 and \$2,728 thousand in 2004.

The Bank rents out office space to HNFC, with rentals payable monthly under an operating lease agreement expiring in May 2006. Rentals received amounted to \$324 thousand in 2005 and 2004.

Service Fee

	2005		2004	
	Amount	%	Amount	%
HNSC	\$ 3,454	0.39	\$ 3,776	0.48

For synergy business, the Bank paid the premium to HNSC, and there is no the same kind of trade can be compared.

Operating Expense - Apportionment of Other Expense

	2005		2004	
	Amount	%	Amount	%
HNSC	\$ 44,144	0.36	\$ 46,645	0.39
HNFC	5,846	0.05	9,353	0.08
	<u>\$ 49,990</u>		<u>\$ 55,998</u>	

For integrated marketing purposes, the Bank shared operating space and facilities with HNSC and HNFC. The related expense is stated as operating expense - apportionment of other expense.

Operating Expense - Insurance Expense

	2005		2004	
	Amount	%	Amount	%
SCIC	\$ 33,646	0.28	\$ 46,809	0.40

Nonoperating Income - Consulting Fee

	2005		2004	
	Amount	%	Amount	%
HNCB Insurance Agency	\$ 221,733	1.82	\$ 174,562	2.74

Derivative Financial Instrument

	2005		2004	
	Amount	Interest	Amount	Interest
HNSC - Interest rate swap	\$ 70,000	\$ 1,680	\$ 196,100	\$ 4,523
HNBF - Interest rate swap	\$ 2,600,000	\$ 57,951	\$ -	\$ -

Receivable (Payable) from (to) Related Party for Allocation under the Linked-Tax System

	2005		2004	
	Amount	%	Amount	%
HNFH	\$ 114,298	0.43	\$ 273,901	1.44

Research and Development Expense

	2005		2004	
	Amount	%	Amount	%
HNIM	\$ -	-	\$ 4,890	-

The terms of transactions with related parties were similar to those for third parties.

## 24. AVERAGE AMOUNT AND AVERAGE INTEREST RATE OF INTEREST-EARNING ASSETS AND INTEREST-BEARING LIABILITIES

Average balance is calculated by the daily average balance of interest-earning assets and interest-bearing liabilities.

	2005		2004	
	Average Balance	Interest Rate (%)	Average Balance	Interest Rate (%)
<b>Interest-earning assets</b>				
Certificates of deposit purchased	\$ 262,721,747	1.34	\$ 258,265,635	1.22
Due from other banks	5,830,351	0.97	6,836,906	0.54
Call loans to other banks	117,161,122	3.04	95,004,099	1.58
Due from the Central Bank	48,797,866	0.98	46,163,308	1.01
Redeposits in the Central Bank	74,485,096	2.64	7,879,060	1.23
Securities purchased	834,666	1.08	92,037,359	3.39
Bonds and securities purchased under resale agreements	874,431,018	3.25	914,333	1.20
Bills purchased, discounts and loans	46,593,624	1.92	842,290,804	2.94
Long-term investments - bonds	2,080,384	4.94	12,561,415	1.81
<b>Interest bearing liabilities</b>				
Due to the Central Bank	44,184	-	369,393	-
Due to other banks	163,450,564	2.51	176,731,274	1.49
Bonds and securities sold under repurchase agreements	19,733,536	0.97	20,293,902	0.77
Demand deposits	276,889,242	0.32	262,557,363	0.14
Savings deposits	318,447,726	0.53	293,598,412	0.52
Time deposits	238,053,475	1.77	202,906,858	1.10
Savings-time deposits	332,291,674	1.80	332,679,103	1.61
Negotiable certificates of deposit	8,427,487	1.04	8,746,213	0.96
Funds borrowed from the Central Bank and other banks	8,630,691	2.63	15,452,317	1.42
Bank debentures payable	65,786,529	2.40	58,047,049	3.15

## 25. MATURITY ANALYSIS OF ASSETS AND LIABILITIES

The maturity of assets and liabilities of the Bank is based on the remaining period from balance sheet date. The remaining period to maturity is based on maturity dates specified under agreements, and, if there are no specified maturity dates, on the expected dates of collection.

	December 31, 2005			December 31, 2004		
	Due in One Year	Due after One Year	Total	Due in One Year	Due after One Year	Total
<b>Assets</b>						
Cash and cash equivalents	\$ 34,462,360	\$ -	\$ 34,462,360	\$ 27,898,980	\$ -	\$ 27,898,980
Due from the Central Bank and other banks	145,054,012	-	145,054,012	127,204,364	-	127,204,364
Securities purchased	312,483,546	10,129,845	322,613,391	302,986,382	44,215,766	347,202,148
Receivables	26,791,586	-	26,791,586	25,740,996	-	25,740,996
Bills purchased, discounts and loans	437,759,100	507,655,458	945,414,558	379,167,700	506,562,150	885,729,850
	<u>\$ 956,550,604</u>	<u>\$ 517,785,303</u>	<u>\$ 1,474,335,907</u>	<u>\$ 862,998,422</u>	<u>\$ 550,777,916</u>	<u>\$ 1,413,776,338</u>
<b>Liabilities</b>						
Due to the Central Bank and other banks	\$ 80,540,499	\$ -	\$ 80,540,499	\$ 90,967,349	\$ -	\$ 90,967,349
Bonds sold under repurchase agreements	19,487,465	-	19,487,465	19,050,464	-	19,050,464
Payables	49,040,609	-	49,040,609	41,982,968	-	41,982,968
Deposits and remittances	1,242,428,700	49,662,722	1,292,091,422	1,114,528,100	102,798,332	1,217,326,432
Bank debentures payable	1,563,000	61,470,000	63,033,000	2,937,000	57,733,000	60,670,000
	<u>\$ 1,393,060,273</u>	<u>\$ 111,132,722</u>	<u>\$ 1,504,192,995</u>	<u>\$ 1,269,465,881</u>	<u>\$ 160,531,332</u>	<u>\$ 1,429,997,213</u>

## 26. COMMITMENTS AND CONTINGENT LIABILITIES

In addition to those disclosed in Note 27, financial instruments, contingencies and commitments of the Bank are summarized as follows:

The Bank's use of certain office spaces is covered by operating lease agreements. As of December 31, 2005, total rental deposits amounted to \$601,367 thousand, including \$580,100 thousand refundable deposits in lieu of rentals. Minimum rentals payable in the next five years are as follows:

Year	Amount
2006	\$ 398,235
2007	328,301
2008	239,095
2009	142,270
2010	92,064

Rentals for the years beyond 2011 amount to \$122,062 thousand, the present value of which is about \$117,552 thousand as discounted at 1.92%, the Bank's one-year time deposit interest rate as of December 31, 2005.



A depositor sued the Bank to recover his \$222,267 deposit, which was allegedly embezzled by the depositor's employee. Believing the depositor's claim is without merit, the Bank retained an attorney in August 1996 to handle the case. As of December 31, 2005, the case was being reviewed by the Supreme Court, and the final outcome of this case was uncertain.

The Bank took over land, buildings and shares from Farmer's Association of Guanyin of Toayuan county, Siaogang of Kaohsiung city, Zhutian of Pingdong county and Jiadong of Pingdong county. In September 2001, according to the thirtieth meeting resolution of Financial Restructuring Fund, the Council of Agriculture's letter of Nong-Jin No. 0945070440, and the Bureau of Agricultural Finance's letter of Council of Agriculture's letter of Nong-Jin-two No. 0945070476, the Bank should return the controversial assets to the Farmer's Association. On August 1, 2005, the Council of Agriculture paid the Bank for the assets which included \$87,492 thousand of land, \$22,392 thousand of buildings, and \$91,169 thousand of shares or a total of \$201,053 thousand.

The balance sheet and trust property of trust accounts were as follows:

**Balance Sheet of Trust Accounts**  
(In Thousands of New Taiwan Dollars)

December 31, 2005		December 31, 2004	
Trust Assets	Amount	Trust Assets	Amount
Bank deposits	\$ 1,612,666	Bank deposits	\$ 1,044,451
Investments		Investments	
Bonds	16,033,412	Bonds	8,742,867
Common stocks	38,774,515	Common stocks	25,284,452
Mutual funds	60,644,719	Mutual funds	58,759,309
Real estate	2,872,631	Real estate	1,305,280
Uncompleted mutual fund	470		<u>\$ 95,136,359</u>
Credit right receivable	260,000		
Collective investment trust fund account net assets	1,874,948		
	<u>\$ 122,073,361</u>		
Trust Liabilities and Equities	Amount	Trust Liabilities and Equities	Amount
Trust liabilities	\$ 186	Trust liabilities	\$ 186
Trust capital		Trust capital	
Monetary trust	79,227,791	Monetary trust	69,180,635
Securities trust	37,828,081	Securities trust	24,196,640
Real estate trust	3,240,333	Real estate trust	1,601,570
Credit right trust	262,160	Retained earnings	157,328
Collective investment trust fund account net liability	1,874,948		<u>\$ 95,136,359</u>
Retained earnings	( 360,138)		
	<u>\$ 122,073,361</u>		

Note: Trust account included foreign currencies mutual funds invested in foreign securities, transactions of OBU, totaled \$967,286 thousand.

**Trust Property of Trust Accounts**  
(In Thousands of New Taiwan Dollars)

December 31, 2005		December 31, 2004	
Investment Portfolio	Amount	Investment Portfolio	Amount
Demand deposits	\$ 797,799	Demand deposits	\$ 404,073
Time deposits	814,867	Time deposits	640,378
Bond investments	16,033,412	Bond investments	8,742,867
Common stock investments	38,774,515	Common stock investments	25,284,452
Domestic mutual funds	29,205,371	Domestic mutual funds	33,187,639
Overseas mutual funds	31,439,348	Overseas mutual funds	25,571,670
Collective investment trust fund account net assets	1,874,948	Land	1,159,769
Uncompleted mutual fund	470	Buildings	5,126
Credit right receivable	260,000	Construction in progress	140,385
Land	2,467,316		<u>\$ 95,136,359</u>
Buildings	7,242		
Construction in progress	398,073		
	<u>\$ 122,073,361</u>		

## 27. DISCLOSURE OF FINANCIAL INSTRUMENTS

### Derivative Financial Instruments

The Bank entered into derivative transactions mainly to accommodate customers' needs and to manage its exposures. The interest rate swap (IRS) and cross-currency swap (CCS) contracts, which are entered into for nontrading purposes, are used to hedge the effects of foreign exchange or interest rate fluctuations on foreign-currency assets or liabilities. The Bank's strategy is to hedge the market risk by matching the exposure between floating-rate U.S. dollar borrowings and (a) fixed-rate U.S. dollar lendings; or (b) fixed-income securities denominated in foreign currencies. These IRS and CCS agreements serve to hedge the Bank's interest rates and foreign currency exposures to stabilize (or "lock in") the yields on the loans or investments.

As of December 31, 2005 and 2004, the contract (notional) amounts, credit risk and market values of outstanding contracts were as follows:

Financial Instruments	December 31, 2005			December 31, 2004		
	Contract (Notional) Amount	Credit Risk	Fair Value	Contract (Notional) Amount	Credit Risk	Fair Value
For accommodating customers' needs and managing the Bank's exposures						
Forward contracts	\$ 48,009,464	\$ 997,765	\$ 194,591	\$ 40,922,422	\$ 658,740	\$ 137,914
Currency swap contracts	23,952,111	137,656	( 139,945)	7,168,746	113,089	( 167,305)
Interest rate swap contracts	32,185,930	135,883	( 2,967)	-	-	-
Cross-currency swap	1,889,647	81,530	( 20,520)	1,826,850	-	123,981
For nontrading purposes						
Interest rate swap contracts	52,360,148	792,375	( 525,619)	66,002,224	533,029	( 531,705)
Cross-currency swap contracts	13,165,326	13,788	13,580	12,897,808	213	-
For accommodating customers' needs and managing the Bank's exposures						
Options						
Buy	6,369,822	64,787	116,841	22,599,648	320,393	777,434
Sell	6,369,822	-	116,841	22,599,648	-	777,434

The Bank is exposed to credit risk from counter-parties' default on contracts. To manage this risk, the Bank enters into forward contracts with customers that have satisfied its credit approval process and have provided the necessary collaterals. Transactions are made within each customer's credit lines. All forward contracts the Bank entered into as of December 31, 2005 were with customers engaging in import and export activities. Guarantee deposits may be required depending on the customers' credit standing. Transactions with other banks are made within the trading limit prescribed for each bank based on the Bank's credit rating and its worldwide ranking. Thus, no significant losses on counter-parties' defaults are anticipated. The forward positions have been offset by the opposite spot or forward positions, so no significant gains or losses would result from exchange rate and interest rate fluctuations, and there is no significant demand for cash on these contracts.

All counter-parties to the IRS or CCS agreements are banks with long-term credit rating of "invest" or higher given by a credit rating organization which is approved by the authority in charge. Thus, the related credit risk is deemed very limited. Because the Bank enters into IRS and CCS agreements for hedging purposes, no significant gains or losses would result from interest rate and exchange rate fluctuations, and there is no significant demand for cash on these contracts. These IRS and CCS are settled at the interest differentials between specified financial indices.

Fair value of each forward exchange contract is determined at the forward rate for the remaining contract term quoted by the Reuters or Telerate Information System. The Bank estimates the fair value of individual IRS or CCS contract using the quotations from the Bloomberg Information System.

The gains or losses on derivative financial instruments in 2005 and 2004 were as follows:

	2005	2004
For accommodating customers' needs and managing the Bank's exposures		
Forward contracts and currency swap contracts		
Foreign-exchange gain and interest revenue	\$ ( 928,199)	\$ ( 313,579)
Cross-currency swap contracts	( 46,544)	18,345
Option	59,727	-
For nontrading purposes		
Interest rate swap contracts	( 41,595)	90,872
Cross-currency swap contracts	2,671	( 5,583)
	<u>\$ ( 953,940)</u>	<u>\$ ( 209,945)</u>

#### Fair Values of Nonderivative Financial Instruments

	2005		2004	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Assets				
Financial assets - fair values approximate carrying values	\$ 1,475,461,946	\$ 1,475,461,946	\$ 1,415,287,333	\$ 1,415,287,333
Long-term equity investments	67,993,599	70,732,146	51,794,768	58,751,409
Liabilities				
Financial liabilities - fair values approximate carrying values	1,506,206,762	1,506,206,762	1,433,362,310	1,433,362,310

The Bank adopts the following methods and assumptions in estimating fair values of its financial instruments:

- (a) Fair values of short-term financial instruments, except securities purchased, are based on carrying values because these instruments have short maturities. These instruments include cash and cash equivalents, due to/from the Central Bank and other banks, receivables, bonds sold under repurchase agreements, payables, deferred revenue and remittances.
- (b) Bills purchased, discounts and loans are financial assets that carry floating interest rates. The carrying values of these assets approximate their fair values because the carrying value of nonperforming loans, which is net of allowance for bad debts, represents the estimated collectible amount.
- (c) Deposits, funds borrowed from the Central Bank and other banks, bank debentures payable and funds received for sub-loans are interest-bearing financial liabilities. Thus, the carrying values approximate their fair values.
- (d) Fair values of refundable deposits in the form of certificate of deposits and fair values of guarantee deposits received are estimated at their carrying values because they do not have maturity dates.
- (e) Fair values for securities purchased and long-term investments are estimated at the available market prices. If market price is not available, securities purchased and long-term bond investments are valued at carrying value.

**Off-Balance-Sheet Credit Risks**

The Bank has commitments to extend loans and issue credit cards. The interest rates for the loans ranged from 1.31% to 5.63% in 2005 and from 1.83% to 8.94% in 2004. The highest interest rates for credit cards were 18%. Starting from February 2004, the Bank issued cash cards, for which interest rates reached as high as 18.25%. The Bank also provided guarantees and letters of credit to help ensure customers' compliance with contract. The terms of these guarantees and letters of credit are usually one year, and their maturity dates are not concentrated in one period.

The amounts of financial contracts with off-balance-sheet credit risks as of December 31, 2005 and 2004 as follows:

	2005	2004
Guarantees and issuance of letters of credit	\$ 106,799,780	\$ 116,342,944
Credit commitments for credit cards	51,808,069	87,991,638
Irrevocable loan commitments	25,909,042	25,479,400

Since most of the commitments are expected to expire without being fully used, the total commitment amounts do not necessarily represent future cash requirements. The total potential loss on counter-parties' default is equal to the above contractual amounts, if fully used, without considering the value of any collateral.

The Bank evaluates the creditworthiness of each credit application case by case, taking into account the credit history, credit rating and financial condition of the applicant. Collaterals, mostly in the form of real estate, cash, inventories, securities and other assets, may be required depending on the result of the above evaluation. About 49% and 50% of the total loans were secured by collaterals as of December 31, 2005 and 2004, respectively. For credit card facilities, no collateral is required but the credit status of each credit cardholder is closely monitored. Appropriate measures are adopted depending on the results of the credit status monitoring, which include amending the credit limit and, if necessary, canceling the facility.

## 28. CONCENTRATION OF CREDIT RISK

The Bank does not have concentrations of credit risk on an individual counter-party, region or industry (no particular industry accounts for at least 10% of the outstanding loans). However, the parties accounting for at least 10% of the outstanding loans are summarized as follows:

	2005	2004
Private enterprises	\$ 480,710,669	\$ 444,360,449
Natural persons	292,668,752	273,518,861
Government	75,990,332	107,142,762

As of December 31, 2005 and 2004, no significant net positions on foreign-currency transactions needed to be disclosed.

## 29. LOAN ASSET QUALITY

	2005	2004
Reported past-due loans (including reported nonperforming loans) (Note a)	\$ 20,226,231	\$ 20,342,991
Nonperforming loans	19,674,383	20,141,930
Past-due loan ratio (Note b)	2.12	2.27
Surveillance loans (Note c)	-	2,819,912
Surveillance loan ratio	-	0.32
Allowance for loans and nonperforming loans	9,607,491	8,594,310
Bad debts written off (Note d)	7,184,160	7,876,568

Note a: Reported past-due loans did not include past-due loans allowed to be exempted, as stipulated by the Bureau of Monetary Authority (BOMA).

Note b: Past-due loans ratio = Reported past-due loans (including reported nonperforming loans) ÷ (Loans + nonperforming loans)

Note c: Surveillance loans included (i) long-term installment loans, which are overdue for more than three months but less than six months, (ii) principal of other loans overdue for less than six months, (iii) past-due loans allowed to be exempted from reporting, as stipulated by BOMA.

Note d: The amounts of bad debts written off were cumulative from January 1 to December 31 of 2005 and 2004.

### 30. CONCENTRATION OF CREDIT EXTENSIONS

Bank contracts with credit extensions as of December 31 2005 and 2004 were as follows:

	2005		2004	
Loans to parties with common interests	\$	54,591,512	\$	31,170,474
Ratio to total loans		5.41%		3.27%
Stock pledged ratio		1.63%		1.80%
	<b>Industry</b>	<b>%</b>	<b>Industry</b>	<b>%</b>
Credit concentration (Top 3)	Private parties	29.02	Private parties	28.70
	Manufacturing	24.82	Manufacturing	24.62
	Wholesale, retailing and restaurant	9.74	Wholesale, retailing and restaurant	9.94

### 31. MARKET RISK SENSITIVITY

Market risk sensitivity as of December 31, 2005 and 2004 was as follows:

	2005	2004
Ratio of interest-sensitive assets to liabilities	101.15%	100.28%
Ratio of interest-sensitive gap to net assets	18.97%	4.97%

Note a: Ratio of interest-sensitive assets to interest-sensitive liabilities =  $\frac{\text{Interest-sensitive assets}}{\text{Interest-sensitive liabilities}}$   
 (Assets and liabilities will be due within one year)

Note b: Interest sensitive gap = Interest sensitive assets - Interest sensitive liabilities

### 32. MAJOR NET POSITIONS ON FOREIGN CURRENCY TRANSACTIONS

The Bank's major net positions on foreign-currency transactions as of December 31, 2005 and 2004 were as follow:

2005				2004			
Currency		Amount in NTD		Currency		Amount in NTD	
USD	28,428	\$	934,141	USD	23,002	\$	730,737
HKD	27,389		116,080	JPY	964,042		297,985
JPY	354,138		98,663	EUR	1,562		67,491
EUR	1,589		61,819	HKD	7,226		29,517
NZD	1,022		22,940	AUD	1,506		26,151

### 33. PROFITABILITY

	2005	2004
Return on assets (Note a)	0.77%	0.89%
Return on equity (Note b)	17.41%	21.02%
Profit margin (Note c)	17.47%	20.80%

$$\text{Note a: Return on assets} = \frac{\text{Income before income tax}}{\text{Average assets}}$$

$$\text{Note b: Return on assets} = \frac{\text{Income before income tax}}{\text{Average equities}}$$

$$\text{Note c: Profit margin} = \frac{\text{Net income}}{\text{Operating revenues}}$$

### 34. ANALYSIS OF DUE DATES OF ASSETS AND LIABILITIES

Amounts of due dates of assets and liabilities for New Taiwan dollar transactions arising from the Bank's Head Office and domestic branches (excluding foreign-currency transactions) as of December 31, 2005 are as follows:

	Total	Periods Due				
		0 30 Days	31 90 Days	91 180 Days	181 Days 1 Year	Above 1 Year
Assets	\$ 1,306,043,000	\$ 343,484,000	\$ 107,904,000	\$ 170,135,000	\$ 122,323,000	\$ 562,197,000
Liabilities	1,237,527,000	138,723,000	121,226,000	641,293,000	199,865,000	136,420,000
Gap	68,516,000	204,761,000	( 13,322,000)	( 471,158,000)	( 77,542,000)	425,777,000
Accumulated gap	68,516,000	204,761,000	191,439,000	( 279,719,000)	( 357,261,000)	68,516,000

### 35. SPECIAL RECORDED ITEMS

Description	Reason and Amount
Within the past year, the director or any employee, in the course of business, violated the law, resulting in an indictment by a prosecutor.	None
Within the past year, a fine was levied on the Bank for violations of regulations promulgated by the Ministry of Finance (MOF).	None
Within the past year, misconduct occurred that resulted in the Ministry of Finance imposing strict corrective measures on the Bank.	None
Within the past year, the Bank incurred a loss exceeding \$50,000 thousand due to employee fraud or work-place accidents.	None
Others	None

### 36. CAPITAL ADEQUACY RATIO

The Banking Act and related regulations require that the Bank maintain a capital adequacy ratio (CAR) of at least 8%. Thus, if the Bank's CAR falls below 8%, the MOF may prohibit the Bank from paying dividends and/or take other necessary actions. As of December 31, 2005 and 2004, the Bank's stand-alone CARs were 12.13% and 11.91%, respectively, and the consolidated CARs were 12.10% and 12.08%, respectively.

The Bank's capital adequacy as of December 31, 2005 and 2004 is broken down as follows:

	2005	2004
a. Tier I Capital	\$ 65,576,429	\$ 62,271,048
b. Tier II Capital	40,154,872	37,705,991
c. Tier III Capital	1,563,000	2,452,025
d. Deduction items	8,235,849	10,590,899
Equity Capital, net (a+b+c-d)	99,058,452	91,838,165
Risk assets	816,398,082	770,924,724
Capital adequacy ratio	12.13%	11.91%
Liability to equity ratio	2,108.74%	2,219.22%

### 37. KEY RATIOS OF DEPOSITS TO TOTAL DEPOSITS

	2005	2004
Demand deposits	\$ 650,662,473	\$ 630,854,003
Demand deposit ratio	52.05%	53.94%
Time deposits	599,403,579	538,613,558
Time deposit ratio	47.95%	46.06%
Foreign exchange accounts	172,896,949	135,264,755
Foreign exchange account ratio	13.83%	11.57%

### 38. AMOUNTS OF SMALL ENTERPRISE LOANS AND CONSUMER LOANS AND THEIR RATIOS TO TOTAL LOANS

	2005	2004
Small enterprise loans	\$ 216,095,225	\$ 197,611,491
Small enterprise loans ratio	22.63%	22.10%
Consumer loans	242,162,262	225,396,452
Consumer loans ratio	25.36%	25.20%



### 39. COMMON INTEREST PARTY TRANSACTIONS

Common interest party transactions as of December 31, 2005 are summarized as follows:

Description	No. of Customers	Ending Balance	Estimated Loss
Consumer loans	2,165	\$ 1,009,553	\$ -
Employees' mortgage loans	1,820	5,485,576	32
Loans to other common interest parties	873	48,119,111	2,267
Loans with common interest parties as guarantors	1,981	11,288,799	1,729
Loans with common interest parties as collateral providers	1,546	3,872,346	-

### 40. SYNERGY AGREEMENTS WITH OTHER SUBSIDIARIES OF HNFH

After the establishment of the Hua Nan Financial Holdings Co., Ltd. (Note 1), the Bank, HNSC, SCIC, HNBF, and HNIT became subsidiaries of HNFH. These subsidiaries entered into a synergy agreement to share with each other their workplaces, manpower, and business information. The period of the agreement was from June 21, 2005 to June 20, 2006.

In addition, the Bank also entered into a commission agreement with HNCB Insurance Agency and SCIC.

### 41. ADDITIONAL DISCLOSURES

The additional disclosures required by the Securities and Futures Bureau are shown in Tables 1 and 2 (attached). Disclosures on derivative transactions are shown in Note 27 to the financial statements. The Bank has no investment in Mainland China.

### 42. SEGMENT INFORMATION

The Bank engages only in banking activities as prescribed by the Banking Act. No single customer or overseas units account for at least 10% of the Bank's operating revenue or total assets. Thus, no customer and geographical information is required to be disclosed.

## HUA NAN COMMERCIAL BANK, LTD.

TABLE 1 Information of investees for the year ended December 31, 2005

(In Thousands of New Taiwan Dollars)

Investor Company	Investor Company	Location	Main Businesses and Products	Investment Amount		Balance as of December 31, 2005			Net Income (Loss) of the Investee	Investment Gain (Loss)	Note
				Dec. 31, 2005	Dec. 31, 2004	Shares	Percentage of Ownership	Carrying Value			
Hua Nan Commercial Bank, Ltd.	Hua Nan Bills Finance Corporation	10F, No.188, Nanjing E. Rd. Sec.5, Taipei, Taiwan, R.O.C.	Bills and bonds business	\$ 1,696,843	\$ 1,696,843	169,684,282	42.41	\$ 1,703,683	\$ 4,459	\$ 1,891	Note
	Chung-Hua Real Estate Management Co.	12F, No.396, Jilung Rd., Sec.1, Taipei, Taiwan, R.O.C.	Construction plan review and consulting, evaluating real estate, reviewing construction and managing construction	49,940	49,940	4,994,000	100.00	137,454	69,292	68,560	Note
	HNCB Insurance Agency Co., Ltd.	2F, No. 96, Yanping N. Rd., Sec. 2, Taipei, Taiwan, R.O.C.	Insurance agency	19,264	19,264	7,670,160	30.00	80,806	31	762	Note
Chung-Hua Real Estate Management Co.	Feng Hua Development Corp.	12F., No. 396, Jilung Rd., Sec. 1, Taipei, Taiwan, R.O.C.	Real estate construction and sales	93,735	93,735	8,910,000	45.00	150,926	69,422	31,240	Note

Note: The investment gains (losses) recognized by the Bank in 2005 were based on audited financial statements as of and for the year ended December 31, 2005.

**HUA NAN COMMERCIAL BANK, LTD.**

TABLE 2 Investment by the Bank's investees as of December 31, 2005

(In Thousands of New Taiwan Dollars)

Held Company Name	Marketable Securities Type and Name	Relationship with the Company	Financial Statement Account	December 31, 2005				Note
				Shares	Carrying Value	Percentage of Ownership	Market Value or Net Equity	
Chung-Hua Real Estate Management Co.	Stock							
	Feng Hua Development Corp.	Equity-method investee	Long-term equity investments	8,910,000	\$150,926	45.00	\$150,926	Note 1
	Everterminal Co., Ltd.	-	Long-term equity investments	1,030,336	10,000	0.84	10,000	Note 1
	Twinhead International Corp.	Same president	Short-term investments	1,217,542	5,442	-	5,442	Note 2
	Pan-International Industrial Corp.	-	Short-term investments	77,962	3,652	-	3,652	Note 2
	Fubon Financial Holding Co., Ltd.	-	Short-term investments	61,682	1,712	-	1,712	Note 2
	Chung Hsin Electric & Machinery Mfg. Corp. Ltd.	-	Short-term investments	55,649	1,188	-	1,188	Note 2
	Yulon Motor Co., Ltd.	-	Short-term investments	48,553	1,741	-	1,741	Note 2
	Yuanta Core Pacific Securities Co., Ltd.	-	Short-term investments	45,668	1,012	-	1,012	Note 2
	Taiwan Rubber Co., Ltd.	-	Short-term investments	48,903	865	-	865	Note 2
	Cathay Financial Holdings Co., Ltd.	-	Short-term investments	25,879	1,559	-	1,559	Note 2
	BES Engineering Corp.	-	Short-term investments	35,468	156	-	156	Note 2
	China Development Financial Holding Corporation	-	Short-term investments	14,279	172	-	172	Note 2
	E.Sun Financial Holdings Co., Ltd.	-	Short-term investments	1,530	32	-	32	Note 2
	HSBC Fund	-	Short-term investments	528,700.9	3,511	-	3,511	Note 2
HNCB Insurance Agency Co., Ltd.	Government Construction Bond 89-7	-	Guarantee deposits	7,500	8,531	-	11,238	Note 2

Note 1: The net asset value is based on the investee's unaudited financial statements.

Note 2: The market value of the beneficiary certificates is determined at the net asset value as of December 31, 2005. The market values of bonds are based on the reference prices of the over-the-counter securities exchange as of December 31, 2005. The market values of the listed and over-the-counter stocks of cost-method investees are based on the average closing price in the last month of the accounting period.

## HUA NAN FINANCIAL HOLDINGS CO., LTD. AND SUBSIDIARIES CONSOLIDATED BALANCE SHEETS

DECEMBER 31, 2005 AND 2004

(In Thousands of New Taiwan Dollars, Except Par Value)

(The Exchange Rates as of December 31, 2005 and 2004 were NT\$32.860 and NT\$31.768)

ASSETS	2005		2004	
	Amount	%	Amount	%
CASH AND CASH EQUIVALENTS	\$ 44,359,983	3	\$ 30,236,716	2
DUE FROM THE CENTRAL BANK AND OTHER BANKS	145,254,012	9	127,364,364	8
SECURITIES PURCHASED, NET	373,313,759	22	396,538,808	25
RECEIVABLES, NET	38,729,262	2	37,204,559	2
CUSTOMERS' MARGIN DEPOSITS	1,182,644	-	1,936,879	-
PREPAYMENTS	4,120,106	-	3,093,922	-
BILLS PURCHASED, DISCOUNTS AND LOANS, NET	942,599,507	56	885,797,852	56
LONG-TERM INVESTMENTS				
Stock under the equity method	80,806	-	2,520,279	-
Stock under the cost method	6,363,205	-	8,057,738	-
Bonds	58,877,554	4	41,001,966	3
Real-estate	124,560	-	115,913	-
Others	2,864,437	-	2,247,085	-
Total long-term investments	<u>68,310,562</u>	<u>4</u>	<u>53,942,981</u>	<u>3</u>
PROPERTIES				
Cost				
Land (including revaluation increments)	13,687,176	1	13,719,624	1
Buildings (including revaluation increments)	12,446,201	1	12,111,167	1
Office equipment	5,417,562	-	5,230,887	-
Transportation equipment	982,562	-	960,488	-
Other equipment	2,500,337	-	2,284,472	-
Leasehold improvements	512,259	-	492,286	-
Cost and revaluation increments	35,546,097	2	34,798,924	2
Less accumulated depreciation	10,261,471	-	9,540,030	-
	<u>25,284,626</u>	<u>2</u>	<u>25,258,894</u>	<u>2</u>
Prepayments and construction in progress	91,786	-	231,034	-
Net properties	<u>25,376,412</u>	<u>2</u>	<u>25,489,928</u>	<u>2</u>
INTANGIBLE ASSETS	<u>61,034</u>	<u>-</u>	<u>148,030</u>	<u>-</u>
OTHER ASSETS				
Refundable deposits	1,838,260	-	2,282,894	-
Others	20,539,419	1	20,259,034	1
Deferred income tax assets, net	5,363,845	1	6,364,587	1
Total other assets	<u>27,741,524</u>	<u>2</u>	<u>28,906,515</u>	<u>2</u>
<b>TOTAL</b>	<u>\$ 1,671,048,805</u>	<u>100</u>	<u>\$ 1,590,660,554</u>	<u>100</u>

## HUA NAN FINANCIAL HOLDINGS CO., LTD. AND SUBSIDIARIES CONSOLIDATED BALANCE SHEETS

DECEMBER 31, 2005 AND 2004

(In Thousands of New Taiwan Dollars, Except Par Value)

(The Exchange Rates as of December 31, 2005 and 2004 were NT\$32.860 and NT\$31.768)

LIABILITIES AND STOCKHOLDERS' EQUITY	2005		2004	
	Amount	%	Amount	%
<b>LIABILITIES</b>				
Short-term borrowings	\$ 6,024,661	-	\$ 6,909,015	1
Bonds sold under agreements to repurchase	61,895,686	4	60,475,667	4
Stock warrants issued, net	-	-	184,149	-
Due to the Central Bank and other banks	91,150,499	6	98,137,349	6
Payables	54,915,887	3	45,733,541	3
Futures traders' equity	1,031,930	-	1,919,467	-
Advance collections	600,170	-	617,860	-
Deposits and remittances	1,282,562,748	77	1,211,095,387	76
Bank debentures payable	63,033,000	4	60,670,000	4
Bonds payable	6,000,000	-	6,000,000	-
Other liabilities	14,256,991	1	18,298,459	1
Total liabilities	<u>1,581,471,572</u>	<u>95</u>	<u>1,510,040,894</u>	<u>95</u>
<b>STOCKHOLDERS' EQUITY</b>				
Total stockholders' equity before minority interest				
Capital stock - \$10 par value				
Authorized: 10,000,000,000 shares				
Issued: 5,970,208,636 shares and 5,579,634,240 shares in 2005 and 2004, respectively	59,702,086	3	55,796,342	3
Capital surplus				
Additional paid-in capital	12,352,244	1	12,352,244	1
Reserve for property revaluation increments	4,184	-	4,184	-
Donation	2,936	-	2,936	-
Treasury stock reissuance	52,360	-	52,360	-
Others	3,400,187	-	2,077	-
Retained earnings				
Legal reserve	2,147,366	-	1,070,177	-
Special reserve	111,017	-	9,494	-
Unappropriated earnings	11,861,021	1	11,435,643	1
Cumulative translation adjustments	( 67,023)	-	( 111,016)	-
Total stockholders' equity before minority interest	<u>89,566,378</u>	<u>5</u>	<u>80,614,441</u>	<u>5</u>
Minority interest	10,855	-	5,219	-
Total stockholders' equity	<u>89,577,233</u>	<u>5</u>	<u>80,619,660</u>	<u>5</u>
<b>COMMITMENTS AND CONTINGENT LIABILITIES</b>				
<b>TOTAL</b>	<u>\$ 1,671,048,805</u>	<u>100</u>	<u>\$ 1,590,660,554</u>	<u>100</u>

## HUA NAN FINANCIAL HOLDINGS CO., LTD. AND SUBSIDIARIES

### CONSOLIDATED STATEMENTS OF INCOME

#### YEARS ENDED DECEMBER 31, 2005 AND 2004

(In Thousands of New Taiwan Dollars, Except Earnings per Share)

(The Exchange Rates as of December 31, 2005 and 2004 were NT\$32.860 and NT\$31.768)

	2005		2004	
	Amount	%	Amount	%
<b>OPERATING REVENUES AND GAINS</b>				
Interest	\$ 38,047,007	56	\$ 33,223,841	54
Gross written premium	5,414,320	8	5,000,057	8
Recovered reinsurance claims	1,524,694	2	1,174,384	2
Recovered unearned premium reserve	2,036,909	3	2,027,380	3
Recovered special reserve	44,803	-	104,274	-
Recovered claims reserve	29,447	-	26,750	-
Service fees	6,881,821	10	6,890,211	11
Income from securities, net	5,823,291	9	4,013,927	7
Income from long-term stock investments under the equity method, net	762	-	304,824	1
Foreign exchange gain, net	914,616	1	676,776	1
Others	7,312,982	11	8,271,702	13
Total operating revenues and gains	68,030,652	100	61,714,126	100
<b>OPERATING COSTS AND EXPENSES</b>				
Interest	19,996,031	29	15,501,058	25
Reinsurance premium expenses	2,489,725	4	2,598,544	4
Insurance claims paid	2,882,412	4	2,452,721	4
Unearned premium reserve	2,111,087	3	2,036,909	3
Special reserve	297,742	-	329,384	1
Claims reserve	34,501	-	29,447	-
Service charges	1,738,097	3	1,563,449	3
Provision for reserves, bad debts and losses from decline in market value of securities purchased and investments	9,392,780	14	6,765,106	11
Operational, general and administrative expenses	16,630,685	25	15,887,590	26
Others	1,465,224	2	942,752	1
Total operating cost and expenses	57,038,284	84	48,106,960	78
<b>OPERATING INCOME</b>	10,992,368	16	13,607,166	22
<b>NONOPERATING REVENUES AND INCOMES</b>	568,826	1	734,223	1
<b>NONOPERATING EXPENSES AND LOSSES</b>	374,132	1	322,680	1
<b>INCOME BEFORE INCOME TAX</b>	11,187,062	16	14,018,709	22
<b>INCOME TAX EXPENSE</b>	1,658,962	2	3,246,784	5
<b>CONSOLIDATED INCOME</b>	\$ 9,528,100	14	\$ 10,771,925	17
Income before minority interest	\$ 9,526,859	14	\$ 10,771,891	17
Minority interest income	1,241	-	34	-
	\$ 9,528,100	14	\$ 10,771,925	17
	Pre-Tax	After Tax	Pre-Tax	After Tax
<b>BASIC EARNINGS PER SHARE</b>	\$ 1.87	\$ 1.60	\$ 2.35	\$ 1.80

## HUA NAN FINANCIAL HOLDINGS CO., LTD. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

YEARS ENDED DECEMBER 31, 2005 AND 2004

(In Thousands of New Taiwan Dollars)

(The Exchange Rates as of December 31, 2005 and 2004 were NT\$32.860 and NT\$31.768)

	Capital Stock		Capital Surplus	Legal Reserve
	Shares (Thousands)	Amount		
BALANCE, JANUARY 1, 2004	4,728,504	\$ 47,285,036	\$ 13,359,502	\$ 60,022
Appropriation of 2003 earnings				
Legal reserve	-	-	-	1,010,155
Special reserve	-	-	-	-
Remuneration to directors and supervisors	-	-	-	-
Employees bonus	-	-	-	-
Cash dividends	-	-	-	-
Stock dividends	756,560	7,565,605	-	-
Capital surplus appropriated as stock dividends	94,570	945,701	( 945,701)	-
Translation adjustments on long-term equity investments	-	-	-	-
Treasury stock transaction - subsidiary's sale of Company's stock	-	-	-	-
Net income in 2004	-	-	-	-
BALANCE, DECEMBER 31, 2004	5,579,634	55,796,342	12,413,801	1,070,177
Effect on subsidiaries' initial consolidation	-	-	-	-
Appropriation of 2004 earnings				
Legal reserve	-	-	-	1,077,189
Special reserve	-	-	-	-
Remuneration to directors and supervisors	-	-	-	-
Employees bonus	-	-	-	-
Cash dividends	-	-	-	-
Stock dividends	390,575	3,905,744	-	-
Capital surplus appropriated as stock dividends				-
Translation adjustments on long-term equity investments	-	-	3,398,110	-
Net income in 2005	-	-	-	-
BALANCE, DECEMBER 31, 2005	5,970,209	\$ 59,702,086	\$ 15,811,911	\$ 2,147,366

**HUA NAN FINANCIAL HOLDINGS CO., LTD. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY**  
**YEARS ENDED DECEMBER 31, 2005 AND 2004**

(In Thousands of New Taiwan Dollars)

(The Exchange Rates as of December 31, 2005 and 2004 were NT\$32.860 and NT\$31.768)

Retained Earnings			Cumulative Translation Adjustments	Treasury Stock	Minority Interest	Total Stockholders' Equity
Others	Unappropriated Earnings (Loss)	Total				
\$ -	\$ 10,292,792	\$ 10,352,814	\$ ( 9,494)	\$ ( 22)	5,185	\$ 70,993,021
-	( 1,010,155)	-	-	-	-	-
9,494	(9,494)	-	-	-	-	-
-	(90,819)	( 90,819)	-	-	-	( 90,819)
-	(7,266)	( 7,266)	-	-	-	( 7,266)
-	(945,701)	( 945,701)	-	-	-	( 945,701)
-	( 7,565,605)	( 7,565,605)	-	-	-	-
-	-	-	-	-	-	-
-	-	-	( 101,522)	-	-	( 101,522)
-	-	-	-	22	-	22
-	<u>10,771,891</u>	<u>10,771,891</u>	-	-	<u>34</u>	<u>10,771,925</u>
9,494	11,435,643	12,515,314	( 111,016)	-	5,219	80,619,660
-	-	-	-	-	5,805	5,805
-	( 1,077,189)	-	-	-	-	-
101,523	( 101,523)	-	-	-	-	-
-	( 95,932)	( 95,932)	-	-	( 45)	( 95,977)
-	( 15,349)	( 15,349)	-	-	( 280)	( 15,629)
-	( 3,905,744)	( 3,905,744)	-	-	( 1,085)	( 3,906,829)
-	( 3,905,744)	( 3,905,744)	-	-	-	-
-	-	-	-	-	-	-
-	-	-	43,993	-	-	3,442,103
-	<u>9,526,859</u>	<u>9,526,859</u>	-	-	<u>1,241</u>	<u>9,528,100</u>
<u>\$ 111,017</u>	<u>\$ 11,861,021</u>	<u>\$ 14,119,404</u>	<u>\$ ( 67,023)</u>	<u>\$ -</u>	<u>\$ 10,855</u>	<u>\$ 89,577,233</u>



HUA NAN FINANCIAL HOLDINGS CO., LTD. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

YEARS ENDED DECEMBER 31, 2005 AND 2004

(In Thousands of New Taiwan Dollars)

(The Exchange Rates as of December 31, 2005 and 2004 were NT\$32.860 and NT\$31.768)

	2005	2004
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Consolidated income	\$ 9,528,100	\$ 10,771,925
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation and amortization	1,221,902	1,161,064
Amortization of premium on long-term bond investments	943,078	334,313
Gain from long-term stock investments under the equity method	( 762)	( 304,824)
Realized loss from sale of long-term investments, net	( 113,609)	8,130
Realized loss from capital decrease of investee	310,745	-
(Gain)on disposal of properties, net	( 176,698)	( 326,493)
Cash dividends and remuneration to directors and supervisors from long-term stock investments under the equity method	-	169,253
Provision for reserves, bad debts and losses from decline in market value of securities purchased and investments	9,790,377	7,660,864
Net changes in operating assets and liabilities		
Accrued pension cost	114,169	169,782
Deferred income tax	1,016,158	2,946,544
Receivables and prepayments	( 3,793,833)	( 5,804,840)
Securities purchased	26,115,567	( 67,328,622)
Payables and advance collections	9,217,580	7,115,823
Liabilities for stock warrants issued	( 184,149)	( 11,544)
Bonds sold under agreements to repurchase	1,080,524	37,950,166
Others	( 260,418)	49,856
Net cash provided by used in operating activities	<u>54,808,731</u>	<u>( 5,438,603)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
(Increase) Decrease in due from the Central Bank and other banks	( 17,889,648)	14,045,111
Increase in bills purchased, discounts and loans	(64,784,024)	( 34,082,518)
Increase in long-term stock investments	( 19,796,530)	( 43,382,401)
Proceeds from sale of long-term equity investments	812,220	1,057,663
Acquisition of properties and intangible assets	( 985,604)	( 1,411,009)
Increase in other assets	( 1,132,298)	( 689,486)
Proceeds from sale of properties	4,072	467,670
Decrease (Increase) in restricted asset	<u>1,179,236</u>	<u>( 3,364,581)</u>
Net cash used in investing activities	<u>( 102,592,576)</u>	<u>( 67,359,551)</u>

(Continued)

## HUA NAN FINANCIAL HOLDINGS CO., LTD. AND SUBSIDIARIES

### CONSOLIDATED STATEMENTS OF CASH FLOWS

YEARS ENDED DECEMBER 31, 2005 AND 2004

(In Thousands of New Taiwan Dollars)

(The Exchange Rates as of December 31, 2005 and 2004 were NT\$32.860 and NT\$31.768)

	2005	2004
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Decrease in short-term borrowings	\$ ( 884,354)	\$ ( 1,002,773)
Decrease increase in due to the Central Bank and other banks	( 6,986,850)	( 21,708,655)
Increase in deposits and remittances	72,065,835	83,061,389
Increase in bank debentures payable	2,363,000	10,000,000
Decrease in funds borrowed from the Central Bank and other banks		-
Payment of cash dividends	( 3,907,440)	( 945,700)
Remuneration and bonuses paid to directors, supervisors and employees	( 690,966)	( 604,640)
(Decrease)Increase in other liabilities	( 1,479,007)	357,072
Net cash provided by financing activities	60,480,218	69,156,693
EFFECT ON SUBSIDIARIES' INITIAL CONSOLIDATION	1,426,894	-
INCREASE(DECREASE) IN CASH AND CASH EQUIVALENTS	14,123,267	( 3,641,461)
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	30,236,716	33,878,177
CASH AND CASH EQUIVALENTS, END OF YEAR	\$ 44,359,983	\$ 30,236,716
<b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION</b>		
Interest paid	\$ 19,616,510	\$ 15,259,441
Income tax paid	\$ 1,234,648	\$ 1,022,534

## APPOINTED OFFICES AND OFFICERS HANDLING INTERNATIONAL BUSINESS

TELEX 11307, 23216, AND 26266 ARE VALIDATED ALL BRANCHES (EXCEPT \*)

Dec. 31, 2005

TELEX ANSWER BACK: HUANANBK

### INTERNATIONAL BANKING DEPARTMENT

Senior Vice President & General Manager: Carl, S.M. Hung  
Senior Vice President & Deputy General Manager: George F.K. Lu  
Vice President & Deputy General Manager: Pau-chu Lo  
Vice President & Deputy General Manager: Tomson, N.T. Lin  
Vice President & Deputy General Manager: Shin-Shung Chow  
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SWIFT Address: HNBKWTWP  
Telex: 11307, 23216, 26266  
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Senior Vice President & General Manager: Tin-Yaw Koa  
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### SUNGSAN BRANCH

Vice President & General Manager: Sheila Tsai  
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### CHUNG LUN BRANCH

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### HO PING BRANCH

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### SHIHLIN BRANCH

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### TUNG-TAIPEI BRANCH

Vice President & General Manager: Tien-Ying Kuo  
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### DA AN BRANCH

Vice President & General Manager: Shue-Mei Cheng  
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### MING SHEN BRANCH

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## TUNHUA BRANCH

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## CHUNGHSING BRANCH

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## TUNHO BRANCH

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