

TAIWAN SEMICONDUCTOR MANUFACTURING CO LTD

Form 6-K

October 30, 2003

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1934 Act Registration No. 1-14700

SECURITIES AND EXCHANGE COMMISSION  
Washington, DC 20549

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FORM 6-K

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

For the month of October 2003

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Taiwan Semiconductor Manufacturing Company Ltd.  
(Translation of Registrant's Name Into English)

No. 8, Li-Hsin Rd. 6,  
Science-Based Industrial Park,  
Hsin-Chu, Taiwan  
(Address of Principal Executive Offices)

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

Form 20-F ☒ [X]

Form 40-F ☐ [ ]

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

Yes ☐ [ ]

No ☒ [X]

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

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Taiwan Semiconductor Manufacturing  
Company Ltd.

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Date: October 30, 2003

By /s/ Lora Ho

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Lora Ho  
Vice President & Chief Financial  
Officer

Taiwan Semiconductor Manufacturing  
Company Ltd.

Financial Statements for the Nine Months Ended  
September 30, 2003 and 2002  
Together with Independent Accountants' Report

Readers are advised that the original version of these financial statements is in Chinese. This English translation is solely for the readers' convenience. If there is any conflict between these financial statements and the Chinese version or any difference in the interpretation of the two versions, the Chinese-language financial statements shall prevail.

English Translation of a Report Originally Issued in Chinese  
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## INDEPENDENT ACCOUNTANTS' REPORT

The Board of Directors and Shareholders  
Taiwan Semiconductor Manufacturing Company Ltd.

We have reviewed the accompanying balance sheets of Taiwan Semiconductor Manufacturing Company Ltd. as of September 30, 2003 and 2002 and the related statements of income and cash flows for the nine months then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to issue a report on these financial statements based on our reviews.

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

Based on our reviews, we are not aware of any material modifications that should be made to the financial statements referred to above for them to be in conformity with accounting principles generally accepted in the Republic of China.

As disclosed in Note 3 to the financial statements, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 30, "Accounting for Treasury Stock" on January 1, 2002. SFAS No. 30 requires a parent company to record stock held by its subsidiary as treasury stock.

Deloitte & Touche  
(T N Soong & Co and Deloitte & Touche (Taiwan))

# Edgar Filing: TAIWAN SEMICONDUCTOR MANUFACTURING CO LTD - Form 6-K

Established Deloitte & Touche Effective June 1, 2003)  
 Taipei, Taiwan  
 The Republic of China

October 16, 2003

## Notice to Readers

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

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## English Translation of Financial Statements Originally Issued in Chinese

TAIWAN SEMICONDUCTOR MANUFACTURING COMPANY LTD.

### BALANCE SHEETS

(UNAUDITED)

SEPTEMBER 30, 2003 AND 2002

(In Thousand New Taiwan Dollars, Except Par Value)

ASSETS	2003		2002	
	Amount	%	Amount	
CURRENT ASSETS				
Cash and cash equivalents (Notes 2 and 4)	\$ 82,730,782	22	\$ 64,516,4	
Short-term investments (Notes 2 and 5)	11,664,302	3		
Receivables from related parties (Note 18)	15,295,065	4	11,221,3	
Notes receivable	43,709	--	30,8	
Accounts receivable	12,704,943	3	10,539,1	
Allowance for doubtful receivables (Note 2)	( 1,021,399)	--	( 1,149,9	
Allowance for sales returns and others (Note 2)	( 2,055,142)	( 1)	( 2,736,9	
Other financial assets	1,192,351	--	1,069,8	
Inventories--net (Notes 2 and 6)	11,813,455	3	13,321,4	
Deferred income taxes (Notes 2 and 13)	2,117,000	1	2,125,5	
Prepaid expenses and other current assets (Notes 2 and 21)	688,212	--	1,466,8	
Total current assets	135,173,278	35	100,404,6	
LONG-TERM INVESTMENTS (Notes 2, 3, 7 and 21)				
Equity method	33,932,303	9	35,292,1	
Cost method	464,629	--	915,7	
Funds	272,024	--	199,5	
Allowance for losses	--	--	( 58,5	
Total Long-term Investments	34,668,956	9	36,348,9	
PROPERTY, PLANT AND EQUIPMENT (Notes 2, 8 and 18)				
Cost				

	70,767,593	18	67,640,5
Buildings			
Machinery and equipment	324,426,114	85	284,024,9
Office equipment	<u>6,077,495</u>	<u>2</u>	<u>5,779,8</u>
Total cost	401,271,202	105	357,445,4
Accumulated depreciation	( 233,609,935)	( 61)	( 177,804,6
Advance payments and construction in progress	<u>24,632,558</u>	<u>6</u>	<u>37,864,7</u>
Net property, plant and equipment	<u>192,293,825</u>	<u>50</u>	<u>217,505,4</u>
DWILL (Note 2)	<u>2,351,634</u>	<u>1</u>	<u>2,700,0</u>
OTHER ASSETS			
Deferred income taxes (Notes 2 and 13)	8,841,310	3	11,428,6
Deferred charges--net (Notes 2 and 9)	8,415,357	2	8,378,6
Refundable deposits (Notes 18 and 20)	287,403	--	579,1
Assets leased to others (Note 2)	85,072	--	87,9
Idle asset (Note 2)	74,644	--	
Miscellaneous	<u>--</u>	<u>--</u>	<u>9,2</u>
Total other assets	<u>17,703,786</u>	<u>5</u>	<u>20,483,6</u>
TOTAL ASSETS	<u>\$ 382,191,479</u>	<u>100</u>	<u>\$ 377,442,7</u>
	=====	====	=====
	2003		2002
	-----		-----
LIABILITIES AND SHAREHOLDERS' EQUITY	Amount	%	Amount
	-----	---	-----
CURRENT LIABILITIES			
Payables to related parties (Note 18)	\$ 3,790,399	1	\$ 2,830,2
Accounts payable	5,596,631	1	4,645,5
Payables to contractors and equipment suppliers	9,480,795	3	17,451,6
Accrued expenses and other current liabilities (Notes 2, 7, 11 and 21)	8,319,012	2	7,419,6
Current portion of bonds (Note 10)	<u>--</u>	<u>--</u>	<u>9,000,0</u>
Total current liabilities	<u>27,186,837</u>	<u>7</u>	<u>41,347,1</u>
LONG-TERM LIABILITIES			
Bonds payable (Note 10)	35,000,000	9	35,000,0
Other long-term payable (Notes 11 and 20)	<u>3,660,493</u>	<u>1</u>	<u>3,648,9</u>
Total long-term liabilities	<u>38,660,493</u>	<u>10</u>	<u>38,648,9</u>
OTHER LIABILITIES			
Accrued pension cost (Notes 2 and 12)	2,533,864	1	2,178,0
Guarantee deposits (Note 20)	838,864	--	1,507,9
Deferred gain on sales and leaseback (Note 2)	<u>--</u>	<u>--</u>	<u>153,2</u>
Total other liabilities	<u>3,372,728</u>	<u>1</u>	<u>3,839,2</u>
Total liabilities	<u>69,220,058</u>	<u>18</u>	<u>83,835,4</u>
	-----	---	-----
SUBTOTAL OF SHAREHOLDERS' EQUITY (Note 15)			
Capital stock--\$10 par value			
Authorized: 24,600,000 thousand shares			
Issued:			

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Preferred--1,300,000 thousand shares	--	--	13,000,0
Common--20,266,619 thousand shares in 2003 and 18,622,887 thousand shares in 2002	202,666,189	53	186,228,8
Capital surplus:			
Merger and others (Note 2)	56,797,280	15	56,961,7
Treasury stock (Note 3)	50,137	--	43,0
Retained earnings:			
Appropriated as legal reserve	20,802,137	5	18,641,1
Appropriated as special reserve	68,945	--	
Unappropriated earnings	34,226,657	9	19,598,3
Others:			
Unrealized loss on long-term investments (Note 2)	( 2,441)	--	( 68,9
Cumulative translation adjustments (Note 2)	5,921	--	1,117,9
Treasury stock (at cost)--40,784 thousand shares in 2003 and 42,001 thousand shares in 2002 (Notes 2, 3 and 16)	( 1,643,404)	--	( 1,914,7
	-----	----	-----
Total shareholders' equity	312,971,421	82	293,607,3
	-----	----	-----
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	\$ 382,191,479	100	\$ 377,442,7
	=====	===	=====

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

(With Deloitte & Touche report dated October 16, 2003)

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English Translation of Financial Statements Originally Issued in Chinese

TAIWAN SEMICONDUCTOR MANUFACTURING COMPANY LTD.

## STATEMENTS OF INCOME (UNAUDITED)

FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2003 AND 2002 (In Thousand New Taiwan Dollars, Except Earnings Per Share)

	2003		2002
	Amount	%	Amount
GROSS SALES (Notes 2 and 18)	\$ 147,294,673		\$ 122,717,95
SALES RETURNS AND ALLOWANCES (Note 2)	( 3,169,937)		( 2,910,76
NET SALES	144,124,736	100	119,807,18
COST OF SALES (Notes 14 and 18)	93,940,362	65	78,522,21
GROSS PROFIT	50,184,374	35	41,284,96
OPERATING EXPENSES (Notes 14 and 18)			

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Research and development	8,657,300	6	7,902,58
General and administrative	4,572,503	3	3,984,15
Marketing	932,482	1	873,31
	-----	----	-----
Total operating expenses	14,162,285	10	12,760,04
	-----	----	-----
INCOME FROM OPERATIONS	36,022,089	25	28,524,9
	-----	----	-----
NON-OPERATING INCOME AND GAIN			
Interest	580,879	1	770,20
Gain on sales of property, plant and equipment (Notes 2 and 18)	347,656	--	255,48
Technical service income (Notes 18 and 20)	158,925	--	142,72
Gain on sales of long-term investments (Note 2)	66,428	--	-
Other (Note 18)	273,013	--	226,81
	-----	----	-----
Total non-operating income and gain	1,426,901	1	1,395,23
	-----	----	-----
NON-OPERATING EXPENSES AND LOSS			
Loss on property, plant and equipment and idle assets (Note 2)	1,430,763	1	-
Interest (Notes 2, 8 and 21)	1,323,510	1	1,633,81
Foreign exchange loss--net (Notes 2 and 21)	426,256	1	101,25
Investment loss recognized by equity method--net (Notes 2 and 7)	343,951	--	3,554,17
Loss on disposal of property, plant and equipment (Note 2)	291,077	--	119,10
Premium expense from option contracts--net (Notes 2 and 21)	153,783	--	291,72

(Continued)

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English Translation of Financial Statements Originally Issued in Chinese

	2003		2002	
	Amount	%	Amount	
	-----	----	-----	
Casualty loss--net (Note 2)	\$ --	--	\$ 117,47	
Other	19,440	--	67,86	
	-----	----	-----	
Total non-operating expenses and loss	3,988,780	3	5,885,40	
	-----	----	-----	
INCOME BEFORE INCOME TAX	33,460,210	23	24,034,74	
INCOME TAX EXPENSE (Notes 2 and 13)	2,203,861	1	4,977,22	

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NET INCOME	\$ 31,256,349	22	\$ 19,057,51
	=====	=====	=====

	2003		
	-----	-----	-----
	Before Income Tax	After Income Tax	B I
EARNINGS PER SHARE (Note 17)			
Basic earnings per share	\$ 1.65	\$ 1.54	\$
	=====	=====	=====
Diluted earnings per share	\$ 1.65	\$ 1.54	\$
	=====	=====	=====

The pro forma net income and earnings per share for the adoption of SFAS No. 30 "Accounting for Treasury Stock" is as follows (Notes 3 and 16):

	2003		
	-----	-----	-----
	Before Income Tax	After Income Tax	B Inc
NET INCOME		\$ 31,332,102	
		=====	
EARNINGS PER SHARE			
Basic earnings per share	\$ 1.65	\$ 1.54	\$
	=====	=====	=====
Diluted earnings per share	\$ 1.65	\$ 1.54	\$
	=====	=====	=====

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

(With Deloitte & Touche report dated October 16, 2003)

(Concluded)

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English Translation of Financial Statements Originally Issued in Chinese

TAIWAN SEMICONDUCTOR MANUFACTURING COMPANY LTD.

STATEMENTS OF CASH FLOWS

(UNAUDITED)

FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2003 AND 2002

(In Thousand New Taiwan Dollars)

=====

	2003	
	-----	-----
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	\$ 31,256,349	\$ 19
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	46,290,739	41
Deferred income taxes	2,074,257	4
Investment loss recognized by equity method--net	343,951	3
Loss on property, plant, and equipment, and idle assets	1,430,763	
Loss (gain) on sales of long-term investments--net	( 66,428)	
Gain on disposal of property, plant and equipment--net	( 56,579)	(
Pension cost accrued	323,322	
Allowance for doubtful receivables	91,535	
Allowance for sales returns and others	( 307,925)	
Changes in operating assets and liabilities:		
Decrease (increase) in:		
Receivables from related parties	( 5,111,577)	( 10
Notes receivable	16,531	
Accounts receivable	( 3,209,496)	9
Inventories--net	( 1,473,119)	( 4
Other financial assets	( 222,682)	(
Prepaid expenses and other current assets	1,326,149	
Increase (decrease) in:		
Payables to related parties	1,323,401	
Accounts payable	747,397	3
Accrued expenses and other current liabilities	2,408,255	2
	-----	-----
Net cash provided by operating activities	77,184,843	70
	-----	-----
CASH FLOWS FROM INVESTING ACTIVITIES		
Increase in short-term investments--net	( 11,664,302)	
Acquisitions of:		
Long-term investments	( 1,050,942)	( 9
Property, plant and equipment	( 24,415,743)	( 36
Proceeds from disposal of:		
Property, plant and equipment	158,858	
Long-term investments	458,308	
Increase in deferred charges	( 1,792,664)	( 2
Decrease in refundable deposits	256,066	
Decrease in other assets--miscellaneous	9,250	
	-----	-----
Net cash used in investing activities	( 38,041,169)	( 47
	-----	-----

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	2003	2002
	-----	-----
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from issuance of (repayment on) bonds payable	(\$ 4,000,000)	\$ 15,000,000
Redemption of preferred stock	( 13,000,000)	( 13,000,000)
Decrease in guarantee deposits	( 556,202)	( 556,202)
Remuneration to directors and supervisors	( 58,485)	( 58,485)
Cash dividends paid for preferred stock	( 455,000)	( 455,000)
	-----	-----
Net cash provided by (used in) financing activities	( 18,069,687)	( 18,069,687)
	-----	-----
NET INCREASE IN CASH AND CASH EQUIVALENTS	21,073,987	31,073,987
CASH AND CASH EQUIVALENTS, BEGINNING OF THE PERIOD	61,656,795	33,073,987
	-----	-----
CASH AND CASH EQUIVALENTS, END OF THE PERIOD	\$ 82,730,782	\$ 64,147,974
	=====	=====
SUPPLEMENTAL INFORMATION		
Interest paid (excluding the amounts capitalized of NT\$4,020 thousand and NT\$112,245 thousand in 2003 and 2002, respectively) (Note 8)	\$ 687,283	\$ 687,283
	=====	=====
Income tax paid	\$ 2,500	\$ 2,500
	=====	=====
Non-cash investing and financing activities:		
Reclassification of parent company stock held by subsidiaries from long-term investments to treasury stock	\$ --	\$ 1,000,000
	=====	=====
Credit balances of long-term investments reclassified as part of other current liabilities	\$ --	\$ --
	=====	=====
Current portion of bonds	\$ --	\$ 9,000,000
	=====	=====
Current portion of other long-term payables	\$ 1,228,568	\$ 1,228,568
	=====	=====

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

(With Deloitte & Touche report dated October 16, 2003)

(Concluded)

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English Translation of Financial Statements Originally Issued in Chinese

TAIWAN SEMICONDUCTOR MANUFACTURING COMPANY LTD.

NOTES TO FINANCIAL STATEMENTS

(UNAUDITED)

(Amounts in Thousand New Taiwan Dollars, Unless Specified Otherwise)

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1. GENERAL

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

TSMC is engaged mainly in the manufacturing, selling, packaging, testing and designing of integrated circuits and other semiconductor devices, and the manufacturing of masks.

2. SIGNIFICANT ACCOUNTING POLICIES

The financial statements are presented in conformity with the Guidelines for Securities Issuers' Financial Reporting and accounting principles generally accepted in the Republic of China. Significant accounting policies are summarized as follows:

Classification of Current and Non-current Assets and Liabilities

Current assets are those expected to be converted to cash, sold or consumed within one year from the balance sheet date. Current liabilities are obligations due on demand within one year from the balance sheet date. Assets and liabilities that are not classified as current are non-current assets and liabilities, respectively.

Cash Equivalents

Government bonds under repurchase agreements acquired with maturities less than three months from the date of purchase are classified as cash equivalents.

Short-term Investments

Short-term investments are carried at the lower of cost or market value. The market values of funds and government bonds are determined by the net asset value of the open-end funds and the daily-volume-weighted-average yield/price conversion of GreTai Securities Market, respectively. The costs of investments sold are determined by the specific identification method.

Allowance for Doubtful Receivables

Allowance for doubtful receivables are provided based on a review of the collectibility of accounts receivables. We determine the amount of allowance for doubtful accounts by examining our historical collection experience and current trends in the credit quality of our customers as well as our internal credit policies.

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Revenue Recognition and Allowance for Sales Returns and Others

The four criteria that we use to recognize revenue are the existence of evidence of a contractual arrangement, whether delivery or performance has

occurred, whether the selling price is fixed or determinable and whether collectibility is reasonably assured. Allowance for sales returns and others is estimated based on historical experience and any known factors that would affect the allowance. Such provisions are deducted from sales in the year the products are sold and the estimated related costs are deducted from cost of sales.

Sales are determined using the fair value taking into account related sales discounts agreed to by the Company and customers. Since the receivables from sales are collectible within one year and such transactions are frequent, the fair value of receivables is equivalent to the nominal amount of cash received.

#### Inventories

Inventories are stated at the lower of cost or market value. Inventories are recorded at standard cost and adjusted to approximate weighted-average cost at the end of each period. Market value represents net realizable value for finished goods and work in process, and replacement value for raw materials, supplies and spare parts. The scrap and slow-moving items are recognized as inventory reserve.

#### Long-term Investments

Investments in shares of stock of companies wherein the Company exercises significant influence on the operating and financial policy decisions are accounted for using the equity method. The Company's proportionate share in the net income or net loss of investee companies is recognized as components of the "investment income/loss recognized by equity method--net" account. When acquiring shares of stock, the difference between the cost of investment and the Company's proportionate share of investee's net book value is amortized using straight-line method over five years, and is also recorded as a components of the "investment income/loss recognized by equity method--net". The Company adopted Statements of Financial Accounting Standards (SFAS) No. 30, "Accounting for Treasury Stock" on January 1, 2002. SFAS No. 30 requires a parent company to reclassify its capital stock held by its subsidiaries from short/long-term investments to treasury stock.

When the Company subscribes to additional investee shares at a percentage different from its existing equity interest, the resulting carrying amount of the investment in equity investee differs from the amount of Company's proportionate share in the investee's net equity. The Company records such difference as an adjustment to "capital surplus" as well as the "long-term investments" accounts. In the event an investee uses its capital surplus (excluding reserve for asset revaluation) to offset its accumulated deficit, the Company will also record a corresponding entry equivalent to its proportionate share of the investee's adjustment. If an investee's functional currency is a foreign currency, "cumulative translation adjustments" would result from the process of translating the investee's financial statements into the functional currency of the Company.

Other stock investments are accounted for using the cost method. Cash dividends are recognized as income in the year received but are accounted for as reduction in the carrying values of the long-term investments if the dividends are received in the same year that the related investments are acquired. Stock dividends are recognized neither as investment income nor increase of long-term investments but recorded only as an increase in the number of shares held. An allowance is recognized for any decline in the market value of investments using quoted market prices with the corresponding amount debited to shareholders' equity. A reversal of the allowance will result from a subsequent recovery of the market value of

such investments. The carrying values of investments with no quoted market price are reduced to reflect an other than temporary decline in their values with the related impairment loss charged to income.

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Investments in foreign mutual funds are stated at the lower of aggregate cost or net asset value. An allowance is recognized when the cost of the funds is lower than their net asset values, with the corresponding amount debited to shareholders' equity. A reversal of the allowance will result from a subsequent recovery of the net asset value.

The costs of investments sold are determined using the weighted-average method.

If an investee company has an unrealized loss on a long-term investment evaluated using the lower-of-cost-or-market method, the Company recognizes a corresponding unrealized loss in proportion to its equity interest and records the amount as a component of its own shareholders' equity.

Gains or losses on transactions with investee companies wherein the Company owns at least 20% of the outstanding common stock but less than a controlling interest are deferred in proportion to the Company's ownership percentage until realized through a transaction with a third party. The entire amount of the gains or losses on sales to majority-owned subsidiaries are deferred until such gains or losses are realized through the subsequent sale of the related products to third parties. Gains or losses from sales by investee companies to the Company are deferred in proportion to the ownership percentage until realized through transactions with third parties.

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

Property, plant and equipment and assets leased to others are stated at cost less accumulated depreciation. When significant impairment loss occurs, the related assets are stated at the lower of fair value or the book value. Idle assets are stated at the lower of book value or net realizable value. Significant additions, renewals, betterments, and interest expense incurred during the construction period are capitalized. Maintenance and repairs are expensed in the period incurred.

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

Upon sale or disposal of property, plant and equipment, the related cost and accumulated depreciation are removed from the corresponding accounts, and with any gain or loss is charged to income in the period of disposal.

#### Goodwill

Goodwill represents the excess of the consideration paid for acquisitions over the fair market value of identifiable net assets acquired. Goodwill is amortized using the straight-line method over the estimated life of 10 years.

#### Deferred Charges

Deferred charges consist of software and system design costs, technology know-how, bond issuance costs and technology license fees. The amounts are

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amortized as follows: Software and system design costs--3 years, technology know-how--5 years, bond issuance costs--the term of the bonds, technology license fee--the shorter of the estimated life of the technology or the term of the technology transfer contract.

### Pension Costs

Net periodic pension costs are recorded on the basis of actuarial calculations. Unrecognized net transition obligation and unrecognized net gain are amortized over 25 years.

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### Deferred Gain on Sale and Leaseback

The gain on the sale of property that is simultaneously leased back is deferred by the Company. This deferred gain on sales and leaseback transactions is amortized as follows: operating leases--adjustment of rental expenses over the term of the leases.

### Casualty Loss

Casualty losses mainly caused from the March 31, 2002 earthquake are recorded when incurred and any insurance recoveries are recorded when probable up to the amount of the loss. Recoveries in excess of the amount of the loss are recorded when realized.

### Income Tax

The Company uses an inter-period tax allocation method for income tax. Deferred income tax assets and liabilities are recognized for the tax effects of temporary differences, unused tax credits and net operating loss carryforwards. Valuation allowances are provided to the extent, if any, that it is more likely than not that deferred income tax assets will not be realized. A deferred tax asset or liability is, according to the classification of its related asset or liability, classified as current or non-current. However, if a deferred asset or liability does not relate to an asset or liability in the financial statements, then it is classified as either current or non-current based on the expected length of time before it is realized.

Any tax credit arising from the purchase of machinery, equipment and technology, research and development expenditures, personnel training, marketing expenses for international branding, investments in important technology-based enterprise are recognized using the current method.

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

As of January 1, 1998, income taxes on unappropriated earnings of 10% are expensed in the year of shareholder approval which is the year subsequent to the year incurred.

### Foreign Currency Transactions

Foreign currency transactions are recorded in New Taiwan dollars at the current rate of exchange in effect when the transaction occurs. Exchange gains or losses derived from foreign currency transactions or monetary assets and liabilities denominated in a foreign currency are recognized in current operations. At the end of each period, foreign-currency assets and

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liabilities are revalued at the prevailing exchange rate with the resulting gains or losses recognized in current operations.

### Derivative Financial Instruments

The Company enters into foreign currency forward contracts to manage currency exposures in cash flow and in foreign currency-denominated assets and liabilities. The differences in the New Taiwan dollar amounts translated using the spot rate and the amounts translated using the contracted forward rates on the contract date are amortized over the terms of the forward contracts using the straight-line method. At the balance sheet dates, the receivables or payables arising from forward contracts are restated using the prevailing spot rate and the resulting differences are charged to income. Also, the receivables and payables related to the forward contract are netted with the resulting amount presented as either an asset or a liability. Any resulting gain or loss upon settlement is charged to income in the period of settlement.

The Company enters into interest rate swap transactions to manage exposures to changes in interest rates on existing liabilities. These transactions are accounted for on an accrual basis, in which the cash settlement receivable or payable is recorded as an adjustment to interest income or expense.

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The notional amount of foreign currency option contracts entered into for hedging purposes are not recognized as an asset or liability on the contract dates. The premiums paid or received for the call or put options are amortized and charged to income on a straight-line basis over the term of the related contract. Any resulting gain or loss upon settlement is charged to income in the period of settlement.

### Reclassification

Certain accounts in the financial statements as of and for the nine months ended September 30, 2002 have been reclassified to conform to the financial statements as of and for the nine months ended September 30, 2003.

### 3. NEW ACCOUNTING PRONOUNCEMENTS

In accordance with the SFAS No. 30, "Accounting for Treasury Stock" and other relevant regulations from Securities and Futures Commission (SFC), the Company is required to reclassify its common stock held by its subsidiaries from long-term investments to treasury stock. The reclassification is based on the carrying value recorded by the Company's subsidiaries as of January 1, 2002. The adoption of SFAS No. 30 resulted in the decrease of long-term investments and the increase of treasury stock by NT\$1,914,700 thousand as of September 30, 2002, and the decrease in net income for the nine months ended September 30, 2002 by NT\$43,036 thousand.

### 4. CASH AND CASH EQUIVALENTS

	September 30	
	2003	2002
Cash and bank deposits	\$ 79,403,491	\$ 60,877,986
Government bonds acquired under repurchase agreements	3,327,291	3,638,468
	\$ 82,730,782	\$ 64,516,454

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	September 30, 2003
5. SHORT-TERM INVESTMENTS	
Government bonds	\$ 7,437,502
Money market funds	2,026,800
Government bonds acquired under repurchase agreements	1,200,000
Bond funds	1,000,000
	\$ 11,664,302
Market value	\$ 11,664,302

	September 30	
	2003	2002
6. INVENTORIES--NET		
Finished goods	\$ 2,535,207	\$ 4,237,870
Work in process	9,891,487	9,394,591
Raw materials	373,404	365,558
Supplies and spare parts	712,492	809,486
	13,512,590	14,807,505
Less--inventory reserve	( 1,699,135)	( 1,486,047)
	\$ 11,813,455	\$ 13,321,458

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	September 30		
	2003		2002
	Carrying Value	% of Owner-ship	Carrying Value
7. LONG-TERM INVESTMENTS			
Shares of stock			
Equity method:			
TSMC International Investment Ltd. (TSMC International)	\$ 21,646,213	100	\$ 24,352,833
TSMC Partners Ltd. (TSMC Partners)	4,089,066	100	3,621,330
Vanguard International Semiconductor Corporation (VIS)	3,968,395	28	2,803,855
Systems on Silicon Manufacturing Company Pte Ltd. (SSMC)	2,616,143	32	3,308,020
Emerging Alliance Fund LLP (Emerging Alliance)	755,364	99	787,482
Global UniChip Corp. (GUC)	377,758	47	--
TSMC North America (TSMC--North America)	286,061	100	170,252
TSMC Japan K. K. (TSMC--Japan)	97,567	100	90,537
Chi Cherng Investment Ltd. (Chi Cherng)	43,028	36	62,379
Hsin Ruey Investment Ltd. (Hsin Ruey)	41,787	36	62,779

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Taiwan Semiconductor Manufacturing Company			
Europe B.V. (TSMC--Europe)	10,921	100	9,536
Chi Hsin Investment Ltd. (Chi Hsin)	--	--	23,164
	-----		-----
	33,932,303		35,292,167
	-----		-----
Cost method:			
Publicly traded stock			
Taiwan Mask Corp.	32,129	2	32,129
Amkor Technology	--	--	280,748
Monolithic System Tech.	--	--	104,289
Non-publicly traded stock			
United Gas Co., Ltd.	193,584	11	193,584
Shin-Etsu Handotai Taiwan Company Ltd.	105,000	7	105,000
Hon Tung Venture Capital	83,916	10	150,000
W.K. Technology Fund IV	50,000	2	50,000
	-----		-----
	464,629		915,750
	-----		-----
Funds			
-----			
Horizon Ventures	229,669	--	160,599
Crimson Asia Capital	42,355	--	39,000
	-----		-----
	272,024		199,599
	-----		-----
	34,668,956		36,407,516
Less--allowance for losses	--		( 58,588)
	-----		-----
	\$ 34,668,956		\$ 36,348,928
	=====		=====
Credit balances of long-term investments			
-----			
Presented as part of other current liabilities:			
Kung Cherng Investment Ltd. (Kung Cherng)	\$ --	--	\$ 44,043
Cherng Huei Investment Ltd. (Cherng Huei)	--	--	15,008
Po Cherng Investment Ltd. (Po Cherng)	--	--	4,517
	-----		-----
	\$ --		\$ 63,568
	=====		=====

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On January 8, 2003, the Company's investee company, VIS, issued 600,000 thousand shares of common stock at a price of NT\$7 per share. In this round of equity offering, the Company purchased a total of 230,882 thousand shares. As a result, its ownership in VIS increased from 25% to 28%.

The Company's investees, Hsin Ruey, Chi Hsin and Kung Cherng were merged on October 30, 2002, with Hsin Ruey as the surviving company. In addition, The Company's investees, Chi Cherng, Cherng Huei and Po Cherng were merged on October 30, 2002 with Chi Cherng as the surviving company. The mergers were accounted for as a pooling of interest. The Company's ownership is approximately 36% in Hsin Ruey and approximately 36% in Chi Cherng subsequent to the merger.

The Company established Ya Xin Technology (Ya Xin) in November 2002 and subsequently signed a merger agreement with GUC in December 2002. The merger was effective on January 4, 2003 and GUC is the surviving company.

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The carrying value of investments accounted for using the equity method and the related investment gains or losses were determined based on the reviewed financial statements of the investees in the same periods. The investment gains or (losses) of investee companies consisted of the following:

	Nine Months Ended September 30	
	2003	2002
SSMC	(\$ 442,182)	(\$ 995,619)
Emerging Alliance	(162,985)	( 124,625)
TSMC Partners	194,235	832,608
TSMC-North America	113,249	124,116
TSMC International	21,128	( 2,807,426)
Others	( 67,396)	( 583,227)
	(\$ 343,951)	(\$ 3,554,173)
	=====	=====

The market values of publicly traded stocks accounted for the cost method were \$157,995 thousand and \$359,217 thousand as of September 30, 2003 and 2002, respectively.

## 8. PROPERTY, PLANT AND EQUIPMENT

Accumulated depreciation consisted of the following:

	September 30	
	2003	2002
Buildings	\$ 27,881,029	\$ 20,544,762
Machinery and equipment	202,126,641	154,332,010
Office equipment	3,602,265	2,927,868
	\$ 233,609,935	\$ 177,804,640
	=====	=====

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Information on the status of the expansion or construction plans of the Company's manufacturing facilities as of September 30, 2003 is as follows:

Construction/ Expansion Plan	Estimated Complete Cost	Accumulated Expenditures	Actual Date of Starting Operations	Expected Date of Starting Operations
Fab 12--Phase 1	\$ 80,318,400	\$ 72,466,500	March 2002	
Fab 14--Phase 1	30,411,000	10,586,900	--	2/nd/ half of 2004 at the earliest

Interest expenses (before deducting capitalized amounts of NT\$4,020 thousand and NT\$112,245 thousand for the nine months ended September 30, 2003 and 2002, respectively) were NT\$1,327,530 thousand and NT\$1,746,062

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thousand for the nine months ended September 30, 2003 and 2002, respectively. The interest rate used for calculating the capitalized amount was 5.283% for the nine months ended September 30, 2003 and 2002, respectively.

## 9. DEFERRED CHARGES--NET

	September 30	
	2003	2002
Technology license fees	\$ 5,396,897	\$ 5,404,989
Software and system design costs	2,844,212	2,845,705
Others	174,248	127,967
	<u>\$ 8,415,357</u>	<u>\$ 8,378,661</u>

## 10. BONDS

	September 30	
	2003	2002
Domestic unsecured bonds:		
Issued in March 1998 and payable in March 2003 in one lump sum payment, 7.71% annual interest payable semi-annually	\$ --	\$ 4,
Issued in October 1999 and payable in October 2002 and 2004 in two equal payments, 5.67% and 5.95% annual interest payable annually, respectively	5,000,000	10,
Issued in December 2000 and payable in December 2005 and 2007 in two installments, 5.25% and 5.36% annual interest payable annually, respectively	15,000,000	15,
Issued in January 2002 and payable in January 2007, 2009 and 2012 in three installments, 2.60%, 2.75% and 3.00% annual interest payable annually, respectively	15,000,000	15,
	<u>\$ 35,000,000</u>	<u>\$ 44,</u>

As of September 30, 2003, future principal payments for the Company's bonds are as follows:

Year of Repayment	Amount
2004	\$ 5,000,000
2005	10,500,000
2007	7,000,000
2008 and thereafter	12,500,000
	<u>\$ 35,000,000</u>

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## 11. OTHER LONG-TERM PAYABLES

The Company entered into several license arrangements for certain semiconductor-related patents. Future payments under the agreements as of September 30, 2003 are as follows:

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Year	Amount
-----	-----
October to December, 2003	\$ 631,594
2004	1,257,373
2005	990,184
2006	456,030
2007	472,920
2008 and thereafter	1,080,960
	-----
	\$ 4,889,061
	=====

## 12. PENSION PLAN

The Company has a pension plan for all regular employees that provides benefits based on length of service and average monthly salary for the six-month period prior to retirement.

The Company contributes at an amount equal to 2% of salaries paid every month to a pension fund (the Fund). The Fund is administered by a pension fund monitoring committee (the Committee) and deposited in the Committee's name in the Central Trust of China.

The changes in the plan assets and unfunded accrued pension cost for the nine months ended September 30, 2003 and 2002 are summarized as follows:

	Nine Months Ended September 30	
	2003	2002
	-----	-----
Plan assets		
Balance, beginning of the period	\$ 993,404	\$ 804,437
Contribution	136,240	128,981
Interest	20,682	29,606
Payment	( 3,473)	( 5,360)
	-----	-----
Balance, end of the period	\$ 1,146,853	\$ 957,664
	=====	=====
Unfunded accrued pension cost		
Balance, beginning of the period	\$ 2,210,542	\$ 1,854,853
Accruals	323,322	326,461
Payment	--	( 3,250)
	-----	-----
Balance, end of the period	\$ 2,533,864	\$ 2,178,064
	=====	=====

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## 13. INCOME TAX

- A reconciliation of income tax expense on income before income tax at the statutory rate and current income tax expense before income tax credits is shown below:

Nine Months Ended September 30	
2003	2002
-----	-----

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Income tax expense based on income before income tax at statutory rate (25%)	\$ 8,365,053	\$ 6,008,686
Tax-exempt income	( 3,598,750)	( 1,818,250)
Temporary and permanent differences	( 334,828)	231,984
	-----	-----
Current income tax expense before income tax credits	\$ 4,431,475	\$ 4,422,420
	=====	=====

## b. Income tax expense consists of:

Current income tax expense before income tax credits	\$ 4,431,475	\$ 4,422,420
Additional 10% tax on the unappropriated earnings	1,271,759	162,938
Income tax credits	( 5,703,234)	( 4,585,358)
Other income tax	2,500	9,321
	-----	-----
Income tax expense	2,500	9,321
Net change in deferred income tax liabilities (assets)		
Investment tax credits	( 1,351,106)	( 2,643,301)
Temporary differences	340,310	315,247
Valuation allowance	3,212,157	7,295,958
	-----	-----
	\$ 2,203,861	\$ 4,977,225
	=====	=====

## c. Deferred income tax assets (liabilities) consist of the following:

	September 30	
	2003	2002
	-----	-----
Current:		
Investment tax credits	\$ 2,117,000	\$ 2,125,541
	=====	=====
Noncurrent:		
Investment tax credits	\$ 25,801,759	\$ 24,575,221
Temporary differences	( 3,906,151)	( 2,809,002)
Valuation allowances	( 13,054,298)	( 10,337,594)
	-----	-----
	\$ 8,841,310	\$ 11,428,625
	=====	=====

## d. Integrated income tax information:

The balances of the imputation credit account as of September 30, 2003 and 2002 were NT\$14,748 thousand and NT\$8,809 thousand, respectively.

The expected and actual creditable ratio for 2002 and 2001 were 0.08% and 0.04%, respectively.

The imputation credits allocated to the shareholders are based on its balance as of the date of dividend distribution. The expected creditable ratio for 2002 may be adjusted when the distribution of the imputation credits are made.

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e. All retained earnings generated prior to December 31, 1997 were appropriated as of September 30, 2003 and 2002.

f. As of September 30, 2003, investment tax credits consisted of the following:

Regulation	Items	Total Creditable Amounts	Remaining Creditable Amounts	Expire Year
-----	-----	-----	-----	-----
Statute for Upgrading Industries	Purchase of machinery and equipment	\$ 4,754,787	\$ 1,798,490	2003
		8,203,530	5,955,336	2004
		3,806,346	3,806,346	2005
		4,884,533	4,884,533	2006
		975,381	975,381	2007
		-----	-----	
		\$ 22,624,577	\$ 17,420,086	
		=====	=====	
Statute for Upgrading Industries	Research and development expenditures	\$ 671,545	\$ 190,359	2003
		1,974,321	1,974,321	2004
		3,111,472	3,111,472	2005
		3,322,453	3,322,453	2006
		1,454,138	1,454,138	2007
		-----	-----	
		\$ 10,533,929	\$ 10,052,743	
		=====	=====	
Statute for Upgrading Industries	Personnel training	\$ 16,104	\$ 4,285	2003
		43,265	43,265	2004
		28,886	28,886	2005
		27,311	27,311	2006
		-----	-----	
		\$ 115,566	\$ 103,747	
		=====	=====	
Statute for Upgrading Industries	Marketing expenses for international branding	\$ 318	\$ --	2003
		=====	=====	
Statute for Upgrading Industries	Investments in important technology-based enterprise	\$ 5,420	\$ --	2003
		203,319	203,319	2004
		138,864	138,864	2005
		-----	-----	
		\$ 347,603	\$ 342,183	
		=====	=====	

g. The sales generated from the following expansion and construction of the Company's manufacturing plants are exempt from income tax:

	Tax-Exemption Period
-----	-----
Construction of Fab 6	2001 to 2004
Construction of Fab 8--module B	2002 to 2005
Expansion of Fab 2--modules A and B, Fab 3, Fab 4, Fab 5 and Fab 6	2003 to 2006

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

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through 1999. However, the Company is contesting the assessment by the tax authority for 1992, 1993, 1997 and 1998.

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14. LABOR COST, DEPRECIATION AND AMORTIZATION EXPENSE	Nine Months Ended September 30, 2003		
	Classified as Cost of Sales	Classified as Operating Expense	Total
Labor cost			
Salary	\$ 5,437,931	\$ 2,273,059	\$ 7,710,990
Labor and health insurance	349,560	174,175	523,735
Pension	306,331	152,956	459,287
Other	160,399	84,203	244,602
Depreciation	41,815,245	1,735,170	43,550,415
Amortization	1,074,049	1,807,137	2,881,186
	=====	=====	=====
	\$ 49,143,515	\$ 6,226,700	\$ 55,370,215
	=====	=====	=====
	Nine Months Ended September 30, 2002		
	Classified as Cost of Sales	Classified as Operating Expense	Total
Labor cost			
Salary	\$ 4,902,475	\$ 2,274,317	\$ 7,176,792
Labor and health insurance	307,148	155,196	462,344
Pension	303,724	153,427	457,151
Other	134,976	105,576	240,552
Depreciation	37,617,233	1,836,251	39,453,484
Amortization	574,379	1,472,699	2,047,078
	=====	=====	=====
	\$ 43,839,935	\$ 5,997,466	\$ 49,837,401
	=====	=====	=====

## 15. SHAREHOLDERS' EQUITY

### Capital, Capital Surplus and Retained Earnings

The Company has issued a total of 485,898 thousand ADSs which were traded on the NYSE as of September 30, 2003. The total number of common shares represented by all issued ADSs is 2,429,491 thousand shares (one ADS represents five common shares).

On October 8, 2003, the Board of Director approved the Company's sponsorship of the offering by certain existing shareholders of up to 500,000 thousand common shares in the form of ADSs. As of October 16, 2003, the offering was not effective as of SFC's approval.

Capital surplus can only be used to offset a deficit under the ROC Company Law. However, the components of capital surplus generated from donated capital and the excess of the issue price over the par value of capital stock (including the stock issued for new capital, mergers, and the purchase of treasury stock) can be transferred to capital stock as stock dividends.

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The Company's Articles of Incorporation provide that the following shall be appropriated from annual earnings if in excess of any cumulative deficit:

- a. 10% legal reserve; until the accumulated legal reserve has equaled the total paid-in capital of the Company;
- b. Special reserve in accordance with relevant laws or regulations;

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- c. Remuneration to directors and supervisors and bonus to employees equals to 0.3% and at least 1% of the remainder, respectively. Individuals eligible for the employee bonus may include employees of affiliated companies as approved by the board of directors or a representative of the board of directors;
- d. Dividends to holders of preferred shares at a 3.5% annual rate, based on the period which the preferred shares have been outstanding. Following the redemption of all of its issued and outstanding preferred shares in May 2003, the Company amended its Articles of Incorporation on June 3, 2003, to remove the provision for issuance of any future dividends to preferred shareholders as of that date;
- e. The appropriation of any remaining balance shall be approved by the shareholders.

Dividends are distributed in shares of common stock or a combination of cash and common stock. Since the Company is in a capital-intensive industry and is currently in the growth stage of its operation, distributions of profits is made preferably in the form of stock dividend. The total of cash dividends paid in any given year may not exceed 50% of total dividends distributed in that year.

Any appropriations of net income are recorded in the financial statement in the year of shareholder approval.

The appropriation for legal reserve is made until the reserve equals the aggregate par value of the Company's outstanding capital stock. The reserve can only be used to offset a deficit or be distributed to capital stock as a stock dividend up to half of the reserve balance when the reserve balance has reached 50% of the aggregate par value of the outstanding capital stock of the Company.

A special reserve equivalent to the debit balance of any account shown in the shareholder's equity section of the balance sheet (except for the recorded cost of treasury stock held by subsidiaries), other than the deficit, shall be made from unappropriated retained earnings pursuant to existing regulations promulgated by the SFC. The special reserve is allowed to be appropriated when the debit balance of such accounts is reversed.

The appropriations of the earnings of 2002 and 2001 were approved in the shareholders' meeting on June 3, 2003 and May 7, 2002, respectively. The appropriations and dividend per share are as follows:

Appropriation of Earnings		Dividend Per
-----		-----
For Fiscal	For Fiscal	For Fiscal

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	Year 2002	Year 2001	Year 2002
	-----	-----	-----
Legal reserve	\$ 2,161,029	\$ 1,448,317	\$ --
Special reserve	68,945	( 349,941)	--
Bonus paid to employees--in stock	1,539,013	1,070,783	--
Preferred stock dividend--in cash	455,000	455,000	0.35
Common stock dividend--in stock	14,898,309	16,832,553	0.80
Remuneration to directors and supervisors-- in cash	58,485	133,848	--
	-----	-----	
	\$ 19,180,781	\$ 19,590,560	
	=====	=====	

The above appropriation of the earnings in fiscal year 2002 and 2001 is consistent with the resolution of the meetings of board of directors on March 4, 2003 and March 26, 2002, respectively. If the above employee bonus and remuneration to directors and supervisors were paid in cash and charged against income for 2002 and 2001, the basic earnings per share for the years ended December 31, 2002 and 2001 would decrease from NT\$1.14 to NT\$1.05 and NT\$0.83 to NT\$0.76, respectively. The shares distributed as a bonus to employees represented 0.83% and 0.64% of the Company's total outstanding common shares as of December 31, 2002 and 2001, respectively.

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The above information associated with the appropriations of bonus to employees and remuneration to directors and supervisors is available at Market Observation System website.

Under the Integrated Income Tax System that became effective on January 1, 1998, ROC resident shareholders are allowed a tax credit for their proportionate share of the income tax paid by the Company on earnings generated as of January 1, 1998. An imputation credit account is maintained by the Company for such income tax and the tax credit allocated to each shareholder.

#### Employee Stock Option Plans

On June 25, 2002, the SFC approved the Company's Employee Stock Option Plan (the Plan). The Plan provides qualified employees with 100,000 thousand units of option rights with each unit representing one common share of stock. The option rights are valid for ten years and exercisable at certain percentages subsequent to the second anniversary of issuance. Under the terms of the Plan, stock options are granted at an exercise price equal to the closing price of the Company's common shares listed on the TSE on the date of grant. Under the Plan, there were 50,378 thousand option rights that had never been granted, or had been granted but cancelled. These un-granted or cancelled option rights expired on September 30, 2003.

Information as of September 30, 2003 with respect to stock option rights activities under the Plan is as follows:

Outstanding Option Rights	
-----	
Number of Option Rights (in Thousand)	Range of Exercise Price (NT\$)
-----	-----

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Balance, January 1, 2003	19,369	46.86-48.70
Options granted	32,031	38.23-53.76
Options cancelled	( 1,778)	38.23-53.76
	-----	
Balance, September 30, 2003	49,622	=====

The aforementioned number of outstanding option rights and exercise prices have been adjusted, taken stock dividends into consideration, in accordance with the Plan.

On September 2, 2003, the Board of Directors approved the 2003 employee stock option plan (the 2003 Plan). The maximum number of shares authorized to be granted is 120,000 thousand option rights. As of October 16, 2003, the 2003 Plan is in the process of SFC's approval.

## Preferred Stock

The Company issued 1,300,000 thousand shares of unlisted Series A--preferred stock to certain investors on November 29, 2000. All of the preferred stock was redeemed at par value and retired on May 29, 2003. Under the Company's Articles of Incorporation, as amended on June 3, 2003, the Company is no longer authorized to issue preferred stock.

The following are the rights of the preferred shareholders and the related terms and conditions prior to redemption:

## Preferred shareholders

- are entitled to receive cumulative cash dividends at an annual rate of 3.5%.
- are not entitled to receive any common stock dividends (whether declared out of unappropriated earnings or capital surplus).

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- have priority over the holders of common shares to the assets of the Company available for distribution to shareholders upon liquidation or dissolution; however, the pre-emptive rights to the assets shall not exceed the issue value of the shares.
- have voting rights similar to that of the holders of common shares.
- have no right to convert their shares into common shares. The preferred shares are to be redeemed within thirty months from their issuance. The preferred shareholders have the aforementioned rights and the Company's related obligations remain the same until the preferred shares are redeemed by the Company.

## 16. TREASURY STOCK (COMMON STOCK)

Purpose	(Shares in Thousand)			
	Beginning Shares	Dividend	Sell	Ending Shares
-----	-----	-----	-----	-----

Nine months ended September 30, 2003

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Reclassification of parent company stock held by subsidiaries from long-term investment	42,001	3,357	4,574	40,784
	=====	=====	=====	=====
Nine months ended September 30, 2002				
Reclassification of parent company stock held by subsidiaries from long-term investment	39,270	3,818	1,087	42,001
	=====	=====	=====	=====

Proceeds from the sale of treasury stock for the nine months ended September 30, 2003 and 2002 were NT\$318,850 thousand and NT\$96,501 thousand, respectively. As of September 30, 2003 and 2002, the book value of the treasury stock was NT\$1,643,404 thousand and NT\$1,914,700 thousand, respectively; the market value was NT\$2,776,198 thousand and NT\$1,956,454 thousand, respectively. Capital stock held by a subsidiary as an investment is recorded as treasury stock, with the holder having the same rights as other common shareholders.

## 17. EARNINGS PER SHARE

Earnings per share (EPS) is computed as follows:

	Amounts (Numerator)		Shares (Denominator) (Thousand)	
	Before Income Tax	After Income Tax		
Nine months ended September 30, 2003				
Net income	\$ 33,460,210	\$ 31,256,349		
Less--preferred stock dividends	( 184,493)	( 184,493)		
Basic earnings per share				
Income available to common shareholders	\$ 33,275,717	\$ 31,071,856	20,222,602	\$
Effect of diluted securities--stock options	--	--	4,246	
Diluted earnings per share				
Income available to common shareholders	\$ 33,275,717	\$ 31,071,856	20,226,848	\$
Nine months ended September 30, 2002				
Net income	\$ 24,034,742	\$ 19,057,517		
Less--preferred stock dividends	( 340,315)	( 340,315)		
Basic and diluted earnings per share				
Income available to common shareholders	\$ 23,694,427	\$ 18,717,202	20,220,989	\$

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The potential common shares issuable under the employee stock option plan (see Note 15) are included in the denominator of the diluted EPS computation by using the treasury stock method under the SFAS No. 24, "Earnings Per Share", but such shares resulted in a non-dilutive per share amount for the nine months ended September 30, 2002. The average number of shares outstanding for the EPS calculation has been adjusted retroactively for issuance of stock dividends and stock bonuses. The retroactive adjustment caused the basic EPS before income tax and after income tax for the nine months ended September 30, 2002 to decrease from NT\$1.28 to NT\$1.17 and NT\$1.01 to NT\$0.93, respectively.

## 18. RELATED PARTY TRANSACTIONS

The Company engages in business transactions with the following related parties:

- a. Industrial Technology Research Institute (ITRI); one of whose directors is the Chairman of the Company
- b. Koninklijke Philips Electronics N.V. (Philips); a major shareholder of the Company
- c. Subsidiaries
  - TSMC--North America
  - TSMC--Europe
  - TSMC--Japan
- d. Investees
  - VIS
  - SSMC
  - GUC
- e. Indirect subsidiaries
  - WaferTech, LLC (WaferTech)
  - TSMC Technology

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The transactions with the aforementioned parties in addition to those disclosed in other notes, are summarized as follows:

	Nine Months Ended September 30			
	2003		2002	
	Amount	%	Amount	%
During the period				
Sales				
TSMC--North America	\$ 84,777,377	58	\$ 69,807,307	57
Philips and its affiliates	2,370,142	2	2,005,606	2
GUC	465,626	--	334,171	--
ITRI	29,856	--	55,854	--
SSMC	1,151	--	7,018	--
VIS	19	--	92,119	--
WaferTech	--	--	1,152	--
	\$ 87,644,171	60	\$ 72,303,227	59

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	=====	=====	=====	=====
Purchases				
WaferTech	\$ 7,815,373	35	\$ 7,782,809	42
SSMC	3,805,999	17	1,832,217	10
VIS	3,454,704	16	2,500,777	13
	-----	-----	-----	-----
	\$ 15,076,076	68	\$ 12,115,803	65
	=====	=====	=====	=====
Operating expense--rental				
ITRI	\$ --	--	\$ 40,401	4
	=====	=====	=====	=====
Manufacturing expenses--technical assistance fee Philips	\$ 2,250,285	3	\$ 2,174,810	3
	=====	=====	=====	=====
Marketing expenses--commission				
TSMC--Japan	\$ 158,717	17	\$ 158,855	18
TSMC--Europe	111,780	12	89,396	10
	-----	-----	-----	-----
	\$ 270,497	29	\$ 248,251	28
	=====	=====	=====	=====
Sale of property, plant, and equipment VIS	\$ 8,098	5	\$ --	--
	=====	=====	=====	=====
Non-operating income and gain				
SSMC (technical service income mainly)	\$ 119,041	8	\$ 85,159	6
WaferTech	1,528	--	1,226	--
VIS	271	--	--	--
	-----	-----	-----	-----
	\$ 120,840	8	\$ 86,385	6
	=====	=====	=====	=====

(Continued)

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	September 30			
	2003		2002	
	-----	-----	-----	-----
At end of the period	Amount	%	Amount	%
-----	-----	-----	-----	-----
Receivables				
TSMC--North America	\$ 14,337,121	94	\$ 10,780,498	97
Philips and its affiliates	752,568	5	278,788	2
VIS	95,111	1	41,848	--
GUC	86,093	--	85,722	1
TSMC Technology	12,103	--	10,517	--
SSMC	11,176	--	7,176	--
ITRI	893	--	16,636	--
WaferTech	--	--	196	--
	-----	-----	-----	-----
	\$ 15,295,065	100	\$ 11,221,381	100
	=====	=====	=====	=====
Payables				
Philips and its affiliates	\$ 1,481,653	39	\$ 1,370,101	49
WaferTech	964,659	26	569,778	20
VIS	796,865	21	648,203	23
SSMC	501,281	14	168,729	6
TSMC--Japan	16,860	--	24,636	1
TSMC--Europe	16,076	--	27,519	1

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TSMC Technology	7,027	--	10,821	--
TSMC--North America	5,978	--	10,477	--
	-----	-----	-----	-----
	\$ 3,790,399	100	\$ 2,830,264	100
	=====	=====	=====	=====
Refundable deposits--VIS	\$ 260,992	91	\$ 550,660	95
	=====	=====	=====	=====

Except for WaferTech and TSMC--North America, sales to related parties are based on normal selling prices and collection terms. The payables to WaferTech represent the purchase of finished goods. The purchase prices of finished goods were determined in accordance with the related contractual agreements. The selling prices to TSMC--North America are approximately 99% of the comparable selling prices to third parties and the payment terms are thirty days from the date of invoice, which is not significantly different from payment terms with third parties.

## 19. SIGNIFICANT LONG-TERM OPERATING LEASES

The Company leases land from the Science-Based Industrial Park (SBIP) Administration where its Fab 2 through Fab 14 manufacturing facilities reside. These agreements expire on various dates from March 2008 to December 2020 and have annual rent payments aggregating NT\$230,449 thousand. The agreements can be renewed upon their expiration.

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Future remaining lease payments are as follows:

Year	Amount
-----	-----
October to December, 2003	\$ 57,612
2004	230,449
2005	230,449
2006	230,449
2007	230,449
2008	206,406
2009 and thereafter	1,586,359
	-----
	\$ 2,772,173
	=====

## 20. SIGNIFICANT COMMITMENTS AND CONTINGENCIES

The significant commitments and contingencies as of September 30, 2003 are as follows:

- a. Under a Technical Cooperation Agreement with Philips, as amended on May 12, 1997, the Company shall pay technical assistance fees at a percentage of net sales (as defined in the agreement) with respect to certain products. The agreement shall remain in force through July 8, 2007 and may be automatically renewed for successive periods of three years thereafter. Under the amended agreement, starting from the fifth anniversary date of the amended agreement, the fees are subject to reduction by the amounts the Company pays to any third party for settling any licensing/infringement disputes, provided that the fees to be paid after reduction will not be below a certain percentage of the net sales.
- b. Subject to certain equity ownership and notification requirements,

Philips and its affiliates can avail themselves each year of up to 30% of the Company's production capacity.

- c. Under a technical cooperation agreement with ITRI, the Company shall reserve and allocate up to 35% of certain of its production capacity for use by the Ministry of Economic Affairs (MOEA) or any other party designated by the MOEA.
- d. Under several foundry agreements, the Company shall reserve a portion of its production capacity for certain major customers who have made guarantee deposits to the Company. As of September 30, 2003, the Company has a total of US\$24,929 thousand of guarantee deposits.
- e. Under a Shareholders Agreement entered into with Philips and EDB Investments Pte Ltd. on March 30, 1999, the parties formed a joint venture company, SSMC, for the purpose of constructing an integrated circuit foundry in Singapore, and allowed the Company to invest in 32% of SSMC's capital. The Company and Philips committed to buy a specific percentage of the production capacity of SSMC. If any party defaults on the commitment and the capacity utilization of SSMC falls below a specific percentage of its total capacity, the defaulting party is required to compensate SSMC for all related unavoidable costs.
- f. The Company provides technical services to SSMC under a Technical Cooperation Agreement (the Agreement) entered into on May 12, 1999. The Company receives compensation for such services computed at a specific percentage of net selling prices of certain products sold by SSMC. The Agreement shall remain in force for ten years and may be automatically renewed for successive periods of five years unless pre-terminated by either party under certain conditions.
- g. The Company provided guarantees on loans amounting to US\$200,000 thousand, US\$40,000 thousand and US\$440,000 thousand for TSMC Development, Inc. (TSMC Development), TSMC--North America and WaferTech, respectively.

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- h. Under a Technology Transfer Agreement (TTA) with National Semiconductor Corporation (National) entered into on June 27, 2000, the Company shall receive payments for license of certain technology to National. The agreement will remain in force for ten years and will be automatically renewed for successive periods of two years thereafter unless either party gives notice for early termination under certain conditions. In January 2003, the Company and National entered into a Termination Agreement whereby the TTA was terminated for convenience. Under the termination agreement, the Company will be relieved of any further obligation to transfer any additional technology. In addition, the Company granted National an option to request additional technology transfers under the same terms and conditions as the terminated TTA through January 2008.
- i. The Company entered into a Manufacturing Agreement with VIS. VIS agrees to reserve certain production capacity for the Company to manufacture certain logic devices or other technologies required by the Company's customers at selling prices agreed upon by the parties. The Company paid NT\$1,200,000 thousand to VIS as a guarantee deposit. VIS shall return portions of the guarantee deposit without any interest to the Company upon reaching certain levels of purchase commitment by the Company. The contract will remain in force for five

years. As of September 30, 2003, the refundable deposit was NT\$260,992 thousand.

- j. Starting from 2001, the Company entered into several license arrangements for certain semiconductor patents. The terms of the contracts range from five to ten years with payments to be paid in the form of royalties over the term of the related contracts. The Company has recorded the related amounts as a liability and deferred charges which is amortized and charged to cost of sales on a straight-line basis over the estimated life of the technology or the term of the contract, whichever is shorter.
- k. In November 2002, the Company entered into an Amended and Restated Joint Technology Cooperation Agreement with Philips, Motorola, Inc. and STMicroelectronics to jointly develop 90-nanometer to 65-nanometer advanced CMOS Logic and e-DRAW technologies. The Company also agreed to align 0.12 micron CMOS Logic technology to enhance its foundry business opportunities. The Company will contribute process technologies and share a portion of the costs associated with this joint development project.
- l. Amounts available under unused letter of credits as of September 30, 2003 were NT\$6,480 thousand, EUR36 thousand and Singapore dollar \$85 thousand.
- m. As of September 30, 2003, unused credit lines for short-term loans were NT\$8,730,000 thousand and US\$327,000 thousand.
- n. As of September 30, 2003, unused credit lines for long-term loans were NT\$27,500 thousand.

21. ADDITIONAL DISCLOSURES

Following are the additional disclosures required by the SFC for TSMC and investees:

- a. Financing provided: Please see Table 1 attached;
  - b. Endorsement/guarantee provided: Please see Table 2 attached;
  - c. Marketable securities held: Please see Table 3 attached;
  - d. Marketable securities acquired and disposed of at costs or prices of at least NT\$100 million or 20% of the paid-in capital: Please see Table 4 attached;
  - e. Acquisition of individual real estate at costs of at least NT\$100 million or 20% of the paid-in capital: Please see Table 5 attached;
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- f. Disposal of individual real estate at prices of at least NT\$100 million or 20% of the paid-in capital: None;
  - g. Total purchase from or sale to related parties amounting to at least NT\$100 million or 20% of the capital: Please see Table 6 attached;
  - h. Receivables from related parties amounting to at least NT\$100 million or 20% of the capital: Please see Table 7 attached;

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- i. Names, locations, and related information of investees on which the Company exercises significant influence: Please see Table 8 attached;
- j. Financial instrument transactions:

## 1) Derivative financial instruments

The Company entered into derivative financial instrument transactions for the nine months ended September 30, 2003 to manage exposures related to foreign-currency denominated receivables or payables, and interest rate fluctuations. Certain information on these contracts is as follows:

- a) Outstanding forward exchange contracts as of September 30, 2003:

Financial Instruments	Maturity Period	Contract Amount (Nominal Amount) (in Thousand)
Sell	October 2003 to March 2004	US\$ 1,430,000 (US\$/NT\$)
Buy	October 2003 to November 2003	EUR 38,000 (EUR/US\$)

As of September 30, 2003, receivables from forward exchange contracts (included in the "other financial assets" account) aggregate approximately NT\$458,902 thousand, and payables from forward exchange contracts (included in the "other current liabilities" account) aggregate approximately NT\$79,306 thousand. Net exchange gain for the nine months ended September 30, 2003 was NT\$902,549 thousand.

The assets and liabilities related to the above forward exchange contracts are as follows:

Assets and liabilities	As of September 30, 2003 (in Thousand)
Time Deposit	US\$ 845,544
Notes and accounts receivable	US\$ 731,587
Accounts payable	EUR 87,261

- b) Interest rate swaps

The Company has entered into interest rate swap contracts to manage exposures to rising interest rates on its floating rate long-term loans. Interest expense on these transactions for the nine months ended September 30, 2003 was NT\$141,097 thousand.

Outstanding contracts as of September 30, 2003 were as follows:

Contract Date	Period	Contract Amount (in Thousand)
July 1, 1999	July 1, 1999 to June 28, 2004	US\$ 5,714
September 19, 2003	September 19, 2003 to December 15, 2005	NT\$ 500,000

## c) Option contracts

The Company entered into foreign currency option contracts to manage exchange rate fluctuations arising from its anticipated US dollar cash receipts on export sales or its Yen currency obligations for purchases of machinery and equipment.

As of September 30, 2003, there were no outstanding option contracts.

For the nine months ended September 30, 2003, the Company realized premium income of NT\$50,273 thousand and premium expense of NT\$204,056 thousand.

## d) Transaction risk

i) Credit risk. Credit risk represents the positive net settlement amount of those contracts with positive fair values at the balance sheet date. The positive net settlement amount represents the loss incurred by the Company if the counter-parties breached the contracts. The banks, which are the counter-parties to the foregoing derivative financial instruments, are reputable financial institutions. Management believes its exposures related to the potential default by those counter-parties are low.

ii) Market price risk. All derivative financial instruments are intended as hedges for fluctuations in currency exchange rates on the Company's foreign currency denominated receivables or payables and interest rate fluctuations on its floating rate long-term loans. Gains or losses from forward exchange contracts are likely to be offset by gains or losses from the hedged receivables and payables. Interest rate risks are also controlled as the expected cost of capital is fixed. Thus, market price risks are believed to be minimal.

iii) Liquidity and cash flow risk and uncertainty of amount and term of future cash demand.

As of September 30, 2003, the Company's future cash demand for outstanding forward exchange contracts, interest rate swaps and option contracts are as follows:

Term	Forward Exchange Contracts	
	Inflow	Outflow
	(In Thousand)	(In Thousand)
Within one year	NT\$ 48,639,807	US\$ 1,472,647
	EUR 38,000	

The Company has sufficient operating capital to meet the above cash demand. The interest rate of the interest rate swaps has taken the Company's cost of capital into account. In addition, the exchange rates of forward foreign exchange contracts and option contracts are fixed. Therefore, there is no material fund raising risk and cash flow risk.

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2) Fair value of financial instruments:

Non-derivative financial instruments	September 30, 2003		September 30, 2002	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Assets				
Cash and cash equivalents	\$ 82,730,782	\$ 82,730,782	\$ 64,516,454	\$ 64,516,454
Short-term investments	11,664,302	11,664,302	--	--
Receivables from related parties	15,295,065	15,295,065	11,221,381	11,221,381
Notes and accounts receivable	12,748,652	12,748,652	10,570,082	10,570,082

(Continued)

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	September 30, 2003		September 30, 2002	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Other financial assets	\$ 1,192,351	\$ 1,192,351	\$ 1,069,866	\$ 1,069,866
Long-term investments (including credit balances of long-term investments)	34,668,956	39,200,246	36,285,366	36,285,366
Refundable deposits	287,403	287,403	579,146	579,146
Liabilities				
Payables to related parties	3,790,399	3,790,399	2,830,266	2,830,266
Accounts payable	5,596,631	5,596,631	4,645,596	4,645,596
Payables to contractors and equipment suppliers	9,480,795	9,480,795	17,451,666	17,451,666
Bonds payable (includes current portion)	35,000,000	35,641,304	44,000,000	44,000,000
Other long-term payable (including current portion)	4,889,061	4,889,061	4,184,706	4,184,706
Guarantee deposits	838,864	838,864	1,507,976	1,507,976
Derivative financial instruments				
Forward exchange contracts (buy)	45,189	52,376	( 7,312)	( 7,312)
Forward exchange contracts (sell)	334,407	540,975	( 251,606)	( 251,606)
Interest rate swaps	--	( 5,812)	25,426	25,426
Option	--	--	--	--

Fair values of financial instruments were determined as follows:

- The carrying amounts reported in the balance sheets for cash and cash equivalents, notes and accounts receivable, other financial assets, accounts payable, payables to contractors and equipment suppliers are approximate to their fair values.
- Fair value of short-term and long-term investments is based on quoted market prices. If quoted market prices are

unavailable, fair value is based on net asset value or book value of investment.

- c) Fair value of refundable deposits and guarantee deposits is based on carrying values.
- d) The fair value of bonds payable is the quoted market value. Fair value of other long-term payable is approximate to its carrying value.
- e) Fair value of derivative financial instruments is the estimated net receivable or (payable) if the contracts are terminated on the relevant balance sheet date.

The fair values of some financial and non-financial instruments were not included in the fair values disclosed above. Accordingly, the sum of the fair values of the financial instruments listed above does not represent the fair value of the Company as a whole.

3) Investment in Mainland China:

The Company filed an investment project with the Investment Commission of MOEA to establish a foundry in Mainland China. On February 27, 2003, the authority approved phase one of the foregoing project and permitted direct investment in establishing TSMC-Shanghai. The Company entered into an investment related agreement with Shanghai Songjiang District People's Government on June 8, 2003. On August 4, 2003, TSMC-Shanghai has been established and is 100% held by the Company. TSMC-Shanghai is engaged mainly in the manufacturing and selling of integrated circuits. The Company invested US\$56,000 thousand on October 8, 2003.

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TABLE 1

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TAIWAN SEMICONDUCTOR MANUFACTURING COMPANY LTD.

FINANCING PROVIDED

FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2003

(Amounts in Thousand New Taiwan Dollars, Unless Otherwise Specified)

=====

No.	Financing Name	Counter-party	Financial Statement Account	Maximum	Ending	Interest
				Balance for the Period (US\$ in Thousand)	Balance (US\$ in Thousand)	
1	TSMC International	TSMC Technology	Other receivables	\$ 542,278 (US\$ 16,049)	\$ 542,278 (US\$ 16,049)	4.2

				Collateral		Financing Limit for Each Borrowing Company	Financing Company's Amount Limits (US\$ in Thousand)
Transaction Amounts	Reasons For Short-term Financing	Allowance for Bad Debt	Item	Value			
\$ --	Operating capital	\$ --	\$ --	\$ --		N/A	\$ 33,384,427 (US\$ 987,968) (Note 2)