

ADVANTEST CORP  
Form 20-F/A  
September 29, 2005  
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As filed with the Securities and Exchange Commission on September 29, 2005

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## SECURITIES AND EXCHANGE COMMISSION

Washington D.C. 20549

### FORM 20-F/A

(Amendment No. 1)

(Mark One)

- REGISTRATION STATEMENT PURSUANT TO SECTION 12(B) OR (G) OF THE SECURITIES EXCHANGE ACT OF 1934
- ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended: March 31, 2005

- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number 1-15236

## Kabushiki Kaisha Advantest

(Exact Name of Registrant as Specified in its Charter)

# Advantest Corporation

(Translation of Registrant's Name Into English)

**Japan**

(Jurisdiction of Incorporation or Organization)

**Shin Marunouchi Center Building**

**1-6-2, Marunouchi**

**Chiyoda-ku**

**Tokyo 100-0005**

**Japan**

**(81-3) 3214-7500**

(Address of Principal Executive Offices)

Securities registered or to be registered pursuant to Section 12(b) of the Act:

| <u>Title of Each Class</u> | <u>Name of Each Exchange On Which Registered</u> |
|----------------------------|--|
| <b>Common Stock</b>        | <b>The New York Stock Exchange</b>               |

Securities registered or to be registered pursuant to Section 12(g) of the Act: none

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act: none

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the annual report:

Title of Each Class

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|                     | <b>Amount<br/>outstanding<br/>as of<br/>March 31,<br/>2005</b> |
|---------------------|--|
| <b>Common Stock</b> | <b>92,423,615</b>  |

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Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days: Yes  No

Indicate by check mark which financial statement item the Registrant has elected to follow: Item 17  Item 18

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**EXPLANATORY NOTE**

On July 26, 2005, Advantest filed an annual report for the fiscal year ended March 31, 2005 on Form 20-F with the United States Securities and Exchange Commission. Advantest is filing this Form 20-F/A (Amendment No. 1) to correct certain errors that were included in the version of the report of Ernst & Young ShinNihon that was previously filed with the Form 20-F. These errors were included only in the filed version of the report and did not appear in the original signed report of Ernst & Young ShinNihon. Advantest is filing the correct version of the report of Ernst & Young ShinNihon with this Form 20-F/A (Amendment No. 1). For technical reasons, Advantest is also re-filing the report of KPMG AZSA & Co. and the financial statements listed in Item 18 with this Form 20-F/A (Amendment No. 1). The report of KPMG AZSA & Co. and the financial statements being re-filed with this Form 20-F/A (Amendment No. 1) are identical to the versions previously filed on July 26, 2005.

Advantest has no further changes to the previously filed Form 20-F. All information in this Form 20-F/A (Amendment No. 1) is as of July 26, 2005 and does not reflect any subsequent information or events other than the changes to the report of Ernst & Young ShinNihon mentioned above.

**ITEM 18. FINANCIAL STATEMENTS**

The following financial statements are filed as part of this annual report on Form 20-F/A (Amendment No. 1).

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**ADVANTEST CORPORATION**

**AND SUBSIDIARIES**

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**Report of Independent Registered Public Accounting Firm**

The Board of Directors and Stockholders

Advantest Corporation:

We have audited the consolidated balance sheet of Advantest Corporation and subsidiaries as of March 31, 2004, and the related consolidated statements of operations, stockholders' equity and cash flows for each of the years in the two-year period ended March 31, 2004 (expressed in yen). These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Advantest Corporation and subsidiaries as of March 31, 2004, and the results of their operations and their cash flows for each of the years in the two-year period ended March 31, 2004, in conformity with U.S. generally accepted accounting principles.

/s/ KPMG AZSA & Co.

Tokyo, Japan

April 26, 2004, except for note 20, which is as of July 21, 2005

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**Report of Independent Registered Public Accounting Firm**

The Board of Directors and Stockholders

Advantest Corporation:

We have audited the accompanying consolidated balance sheet of Advantest Corporation and subsidiaries (the Company) as of March 31, 2005, and the related consolidated statements of operations, stockholders' equity, and cash flows for the year then ended, all expressed in Japanese yen. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Advantest Corporation and subsidiaries at March 31, 2005, and the consolidated results of their operations and their cash flows for the year then ended, in conformity with U.S. generally accepted accounting principles.

As discussed in Note 1 to the consolidated financial statements, in 2005 the Company changed its method of accounting for stock-based compensation.

We have also reviewed the translation of the financial statements mentioned above into United States dollars on the basis described in Note 2. In our opinion, such statements have been translated on such basis.

/s/ ERNST & YOUNG SHINNIHON

Tokyo, Japan

May 17, 2005, except for Note 24, as to which the date is July 21, 2005

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**ADVANTEST CORPORATION  
AND SUBSIDIARIES**

**Consolidated Balance Sheets**

**March 31, 2004 and 2005**

|                                    | <u>2004</u>      | <u>2005</u>    | <u>2005</u>         |
|------------------------------------|------------------|----------------|---------------------|
|                                    | Yen              |                | U.S. Dollars        |
|                                    | (Millions)       |                | (Thousands)         |
| <b>Assets</b>                      |                  |                |                     |
| Current assets:                    |                  |                |                     |
| Cash and cash equivalents          | ¥ 101,146        | 120,986        | \$ 1,126,604        |
| Trade receivables, net             | 76,133           | 56,702         | 528,001             |
| Inventories                        | 49,423           | 29,585         | 275,491             |
| Deferred tax assets                | 24,223           | 13,673         | 127,321             |
| Other current assets               | 4,837            | 2,985          | 27,796              |
| <b>Total current assets</b>        | <b>255,762</b>   | <b>223,931</b> | <b>2,085,213</b>    |
| Investment securities              | 7,952            | 7,772          | 72,372              |
| Property, plant and equipment, net | 50,516           | 51,364         | 478,294             |
| Deferred tax assets                | 9,599            | 8,438          | 78,573              |
| Intangible assets, net             | 3,756            | 3,090          | 28,774              |
| Other assets                       | 3,223            | 2,174          | 20,244              |
| <b>Total assets</b>                | <b>¥ 330,808</b> | <b>296,769</b> | <b>\$ 2,763,470</b> |

See accompanying notes to consolidated financial statements.

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**ADVANTEST CORPORATION  
AND SUBSIDIARIES**

**Consolidated Balance Sheets**

**March 31, 2004 and 2005**

|  | <u>2004</u>      | <u>2005</u>    | <u>2005</u>         |
|--|------------------|----------------|---------------------|
|  | Yen              |                | U.S. Dollars        |
|  | (Millions)       |                | (Thousands)         |
| <b>Liabilities and Stockholders Equity</b>                                     |                  |                |                     |
| Current liabilities:   |                  |                |                     |
| Current portion of long-term debt  | ¥ 4,543          | 20,043         | \$ 186,637          |
| Trade accounts payable   | 38,214           | 23,196         | 215,998             |
| Income taxes payable   | 3,845            | 7,278          | 67,772              |
| Accrued expenses   | 9,368            | 13,865         | 129,109             |
| Accrued warranty expenses  | 3,121            | 4,090          | 38,085              |
| Deferred revenue   | 4,543            | 2,220          | 20,672              |
| Other current liabilities  | 2,977            | 3,302          | 30,748              |
|  | <u>66,611</u>    | <u>73,994</u>  | <u>689,021</u>      |
| Total current liabilities  |                  |                |                     |
| Long-term debt, excluding current portion                                      | 20,083           | 40             | 373                 |
| Accrued pension and severance cost   | 18,348           | 12,605         | 117,376             |
| Other liabilities  | 3,411            | 3,381          | 31,483              |
|  | <u>108,453</u>   | <u>90,020</u>  | <u>838,253</u>      |
| Total liabilities  |                  |                |                     |
| Minority interests   | 587              |                |                     |
| Stockholders equity:   |                  |                |                     |
| Common stock,  |                  |                |                     |
| Authorized 220,000,000 shares; issued 99,783,385 shares in 2004 and 2005       | 32,363           | 32,363         | 301,360             |
| Capital surplus  | 32,973           | 35,263         | 328,364             |
| Retained earnings  | 177,404          | 210,121        | 1,956,616           |
| Accumulated other comprehensive income (loss)                                  | (8,061)          | (4,878)        | (45,423)            |
| Treasury stock, 1,507,745 shares in 2004 and 7,359,770 shares in 2005, at cost | (12,911)         | (66,120)       | (615,700)           |
|  | <u>221,768</u>   | <u>206,749</u> | <u>1,925,217</u>    |
| Total stockholders equity  |                  |                |                     |
| Total liabilities and stockholders equity                                      | <u>¥ 330,808</u> | <u>296,769</u> | <u>\$ 2,763,470</u> |

See accompanying notes to consolidated financial statements.



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**ADVANTEST CORPORATION  
AND SUBSIDIARIES**

**Consolidated Statements of Operations**

**Years ended March 31, 2003, 2004 and 2005**

|  | <u>2003</u>       | <u>2004</u>    | <u>2005</u>    | <u>2005</u>       |
|--|-------------------|----------------|----------------|-------------------|
|  | Yen               |                |                | U.S. Dollars      |
|  |                   | (Millions)     |                | (Thousands)       |
| Net sales                                    | ¥ 97,740          | 174,218        | 239,439        | \$ 2,229,621      |
| Cost of sales                                | 56,551            | 85,513         | 115,994        | 1,080,119         |
| <b>Gross profit</b>                          | <b>41,189</b>     | <b>88,705</b>  | <b>123,445</b> | <b>1,149,502</b>  |
| Research and development expenses            | 23,615            | 21,637         | 26,280         | 244,716           |
| Selling, general and administrative expenses | 34,317            | 36,108         | 36,446         | 339,380           |
| <b>Operating income (loss)</b>               | <b>(16,743)</b>   | <b>30,960</b>  | <b>60,719</b>  | <b>565,406</b>    |
| Other income (expense):                      |                   |                |                |                   |
| Interest and dividends income                | 407               | 339            | 597            | 5,559             |
| Interest expense                             | (490)             | (469)          | (441)          | (4,106)           |
| Minority interests                           | (107)             | (214)          | (84)           | (782)             |
| Equity in losses of affiliates               | (109)             | (117)          |                |                   |
| Other  | (1,646)           | (1,621)        | 1,017          | 9,470             |
|  | <b>(1,945)</b>    | <b>(2,082)</b> | <b>1,089</b>   | <b>10,141</b>     |
| <b>Income (loss) before income taxes</b>     | <b>(18,688)</b>   | <b>28,878</b>  | <b>61,808</b>  | <b>575,547</b>    |
| Income taxes                                 | (5,694)           | 11,549         | 23,730         | 220,970           |
| <b>Net income (loss)</b>                     | <b>¥ (12,994)</b> | <b>17,329</b>  | <b>38,078</b>  | <b>\$ 354,577</b> |
|  | <u>2003</u>       | <u>2004</u>    | <u>2005</u>    | <u>2005</u>       |
|  | Yen               |                |                | U.S. Dollars      |
| Net income (loss) per share:                 |                   |                |                |                   |
| Basic  | ¥ (131.99)        | 176.37         | 389.54         | \$ 3.63           |
| Diluted                                      | (131.99)          | 176.02         | 388.51         | 3.62              |

See accompanying notes to consolidated financial statements.

**Table of Contents****ADVANTEST CORPORATION****AND SUBSIDIARIES****Consolidated Statements of Stockholders' Equity**

Years ended March 31, 2003, 2004 and 2005

|   | <u>2003</u>      | <u>2004</u>     | <u>2005</u>     | <u>2005</u>         |
|---|------------------|-----------------|-----------------|---------------------|
|   |                  | <b>Yen</b>      |                 | <b>U.S. Dollars</b> |
|   |                  | (Millions)      |                 | (Thousands)         |
| <b>Common stock:</b>                                  |                  |                 |                 |                     |
| Balance at beginning of year                          | ¥ 32,363         | 32,363          | 32,363          | \$ 301,360          |
| Balance at end of year                                | <u>32,363</u>    | <u>32,363</u>   | <u>32,363</u>   | <u>301,360</u>      |
| <b>Capital surplus:</b>                               |                  |                 |                 |                     |
| Balance at beginning of year                          | 32,973           | 32,973          | 32,973          | 307,040             |
| Stock option compensation expense                     |                  |                 | 2,290           | 21,324              |
| Balance at end of year                                | <u>32,973</u>    | <u>32,973</u>   | <u>35,263</u>   | <u>328,364</u>      |
| <b>Retained earnings:</b>                             |                  |                 |                 |                     |
| Balance at beginning of year                          | 178,998          | 162,547         | 177,404         | 1,651,960           |
| Net income (loss)                                     | (12,994)         | 17,329          | 38,078          | 354,577             |
| Cash dividends  | (3,457)          | (2,456)         | (4,915)         | (45,768)            |
| Loss on disposal of treasury stock                    |                  | (16)            | (446)           | (4,153)             |
| Balance at end of year                                | <u>162,547</u>   | <u>177,404</u>  | <u>210,121</u>  | <u>1,956,616</u>    |
| <b>Accumulated other comprehensive income (loss):</b> |                  |                 |                 |                     |
| Balance at beginning of year                          | (1,184)          | (4,055)         | (8,061)         | (75,063)            |
| Other comprehensive income (loss), net of tax         | (2,871)          | (4,006)         | 3,183           | 29,640              |
| Balance at end of year                                | <u>(4,055)</u>   | <u>(8,061)</u>  | <u>(4,878)</u>  | <u>(45,423)</u>     |
| <b>Treasury stock:</b>                                |                  |                 |                 |                     |
| Balance at beginning of year                          | (2,434)          | (13,165)        | (12,911)        | (120,225)           |
| Treasury stock purchased                              | (10,731)         | (32)            | (54,513)        | (507,617)           |
| Exercise of stock options                             |                  | 180             | 1,302           | 12,124              |
| Decrease in treasury stock upon share exchange        |                  | 105             |                 |                     |
| Treasury stock sold                                   |                  | 1               | 2               | 18                  |
| Balance at end of year                                | <u>(13,165)</u>  | <u>(12,911)</u> | <u>(66,120)</u> | <u>(615,700)</u>    |
| Total stockholders' equity                            | <u>¥ 210,663</u> | <u>221,768</u>  | <u>206,749</u>  | <u>\$ 1,925,217</u> |

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|   |            |         |        |            |
|---|------------|---------|--------|------------|
| Disclosure of comprehensive income (loss):    |            |         |        |            |
| Net income (loss)                             | ¥ (12,994) | 17,329  | 38,078 | \$ 354,577 |
| Other comprehensive income (loss), net of tax |            |         |        |            |
| Foreign currency translation adjustments      | (2,915)    | (3,976) | 1,635  | 15,225     |
| Net unrealized gains on securities            | 44         | 1,366   | 152    | 1,416      |
| Minimum pension liability adjustments         |            | (1,396) | 1,396  | 12,999     |
| Total other comprehensive income (loss)       | (2,871)    | (4,006) | 3,183  | 29,640     |
| Total comprehensive income (loss)             | ¥ (15,865) | 13,323  | 41,261 | \$ 384,217 |

See accompanying notes to consolidated financial statements.

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**Table of Contents****ADVANTEST CORPORATION****AND SUBSIDIARIES****Consolidated Statements of Cash Flows****Years ended March 31, 2003, 2004 and 2005**

|  | <u>2003</u>    | <u>2004</u>    | <u>2005</u>    | <u>2005</u>     |
|--|----------------|----------------|----------------|-----------------|
|  | Yen            |                |                | U.S. Dollars    |
|  | (Millions)     |                |                | (Thousands)     |
| Cash flows from operating activities:  |                |                |                |                 |
| Net income (loss)  | ¥ (12,994)     | 17,329         | 38,078         | \$ 354,577      |
| Adjustments to reconcile net income (loss) to net cash provided by operating activities: |                |                |                |                 |
| Depreciation and amortization  | 10,942         | 9,328          | 8,285          | 77,149          |
| Deferred income taxes  | (8,012)        | 6,703          | 13,540         | 126,083         |
| Impairment loss on long-lived assets   |                | 3,030          |                |                 |
| Stock option compensation expense  |                |                | 2,290          | 21,324          |
| Changes in assets and liabilities:   |                |                |                |                 |
| Trade receivables  | (10,927)       | (35,285)       | 20,953         | 195,111         |
| Inventories  | 17,415         | (14,570)       | 20,218         | 188,267         |
| Trade accounts payable   | 6,963          | 29,190         | (16,375)       | (152,482)       |
| Income taxes payable   | 1,878          | 1,997          | 3,311          | 30,832          |
| Accrued expenses   | (2,264)        | 2,536          | 4,445          | 41,391          |
| Accrued warranty expenses  | (440)          | 709            | 969            | 9,023           |
| Deferred revenue   | 489            | 3,441          | (2,456)        | (22,870)        |
| Accrued pension and severance cost   | 1,022          | 2,639          | (3,409)        | (31,744)        |
| Other  | 895            | 1,168          | 478            | 4,451           |
|  | <u>4,967</u>   | <u>28,215</u>  | <u>90,327</u>  | <u>841,112</u>  |
| Net cash provided by operating activities  |                |                |                |                 |
| Cash flows from investing activities:  |                |                |                |                 |
| Proceeds from sale of available-for-sale marketable securities                           |                | 323            | 1,428          | 13,297          |
| Proceeds from sale of non-marketable securities  | 7              | 387            | 50             | 466             |
| Purchases of non-marketable securities   | (1,000)        | (1,288)        |                |                 |
| Proceeds from sale of property, plant and equipment                                      | 583            | 435            | 132            | 1,229           |
| Purchases of intangible assets   | (947)          | (358)          | (470)          | (4,377)         |
| Purchases of property, plant and equipment   | (6,827)        | (5,068)        | (8,738)        | (81,367)        |
| Other  | (235)          | 499            | (652)          | (6,071)         |
|  | <u>(8,419)</u> | <u>(5,070)</u> | <u>(8,250)</u> | <u>(76,823)</u> |
| Net cash used in investing activities  |                |                |                |                 |
| Cash flows from financing activities:  |                |                |                |                 |
| Principal payments on long-term debt   | (42)           | (3,811)        | (4,543)        | (42,304)        |
| Proceeds from sale of treasury stock   |                | 90             | 939            | 8,744           |
| Payments to acquire treasury stock   | (10,733)       | (31)           | (54,511)       | (507,598)       |
| Dividends paid   | (3,453)        | (2,462)        | (4,907)        | (45,693)        |
| Other  | (260)          | (162)          | (14)           | (131)           |
|  | <u>(260)</u>   | <u>(162)</u>   | <u>(14)</u>    | <u>(131)</u>    |

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|  |          |         |          |              |
|--|----------|---------|----------|--------------|
| Net cash used in financing activities                            | (14,488) | (6,376) | (63,036) | (586,982)    |
| Net effect of exchange rate changes on cash and cash equivalents | (654)    | (2,961) | 799      | 7,440        |
| Net change in cash and cash equivalents                          | (18,594) | 13,808  | 19,840   | 184,747      |
| Cash and cash equivalents at beginning of year                   | 105,932  | 87,338  | 101,146  | 941,857      |
| Cash and cash equivalents at end of year                         | ¥ 87,338 | 101,146 | 120,986  | \$ 1,126,604 |
| Supplemental data:   |          |         |          |              |
| Cash paid during the year for:                                   |          |         |          |              |
| Income taxes   | ¥ 507    | 1,936   | 6,740    | \$ 62,762    |
| Interest   | 490      | 473     | 447      | 4,162        |

See accompanying notes to consolidated financial statements.

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**ADVANTEST CORPORATION**

**AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements**

**(1) Description of Business and Summary of Significant Accounting Policies and Practices**

*(a) Description of Business*

The company and subsidiaries (collectively Advantest ) manufacture and sell semiconductor and component test system product group and mechatronics-related product group such as test handlers and device interfaces. Advantest also engages in research and development activities and provides maintenance and support services associated with these products.

In conjunction with its business and organizational restructuring, effective April 1, 2004, Advantest reclassified its two previous segments, automated test equipment and measuring instruments business segment, into three business segments: semi-conductor and component test system; mechatronics system; and services, support and others.

Description of the business by segment is as follows:

The semiconductor and component test system business provides customers with test system products for the semiconductor industry and the electronic parts industry. Product lines provided by the semiconductor and component test system segment include test systems for memory semiconductors for memory semiconductor devices and test systems for SoC semiconductors for non memory semiconductor devices.

The mechatronics system business provides product lines such as test handlers, mechatronic-applied products, for handling semiconductor devices and device interfaces that serve as interfaces with the devices that are measured and operations related to nano-technology products.

The services, support and others business consists of comprehensive customer solutions provided in connection with the above businesses, support services, equipment lease business and others.

*(b) Principles of Consolidation*

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The Company and its domestic subsidiaries maintain their records and also prepare their statutory financial statements in accordance with accounting principles generally accepted in Japan, and its foreign subsidiaries in conformity with the standards of the country of their domicile. Certain adjustments and reclassifications have been incorporated in the accompanying consolidated financial statements to present them in conformity with accounting principles generally accepted in the United States of America. These adjustments are not recorded in the statutory books of account.

The consolidated financial statements include the accounts of the Company and its majority owned subsidiaries. Advantest is not involved with any variable interest entities as, defined by FASB Interpretation No. 46 (revised December 2003) Consolidation of Variable Interest Entities . All significant intercompany balances and transactions have been eliminated in consolidation.

### *(c) Cash Equivalents*

Cash equivalents consist of deposits and certificates of deposit with an initial maturity of three months or less from the date of purchase. Advantest considers all highly liquid debt instruments with original maturities of three months or less to be cash equivalents.

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**ADVANTEST CORPORATION**

**AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements (Continued)**

***(d) Allowance for Doubtful Accounts***

Advantest recognizes an allowance for doubtful accounts to ensure that trade receivables are not overstated due to uncollectability, which represents Advantest's best estimate of the amount of probable credit losses in Advantest's existing trade receivables. Advantest periodically reviews its estimated allowances for doubtful accounts taking into account the customer's payment history, assessing the customer's current financial position and considering other information that is publicly available and the customer's credit worthiness. Additional reviews are undertaken upon reports of significant changes in the financial condition of Advantest's significant customers and the semiconductor industry.

***(e) Inventories***

Inventories are stated at the lower of cost or market. Cost is determined using the average cost method.

***(f) Investments in Affiliated Companies***

Investments in affiliated companies owned 20% to 50%, where Advantest exercises significant influence over their operating and financial policies, are accounted for on the equity method. All significant intercompany profits from affiliates have been eliminated.

***(g) Investment Securities***

Investment securities at March 31, 2004 and 2005 consist of marketable and non-marketable equity securities. Advantest classifies its marketable equity securities as available-for-sale.

Available-for-sale securities are recorded at fair value. Unrealized gains and losses, net of the related tax effect, on available-for-sale securities are excluded from earnings and are reported as a component of accumulated other comprehensive income (loss) until realized. A decline in the fair value of any available-for-sale security below cost that is deemed to be other than temporary results in an impairment loss. The impairment is charged to earnings and a new cost basis for the security is established. Dividend income is recognized when earned.

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On a continuous basis, but no less frequently than at the end of every half year, Advantest evaluates the cost basis of an available-for-sale security for possible impairment. Factors considered in assessing whether an indication of other than temporary impairment exists include: the degree of change in ratio of market prices per share to book value per share at the date of evaluation compared to that of the date of acquisition, the financial condition and prospects of each investee company, industry conditions in which the investee company operates, the period of time the fair value of an available-for-sale security has been below the cost basis of the investment and other relevant factors. Impairment to be recognized is measured based on the amount by which the carrying amount of the investment exceeds the fair value of the investment. Fair value is determined based on quoted market prices, projected discounted cash flow or other valuation techniques as appropriate.

The cost of a security sold or the amount reclassified out of accumulated other comprehensive income (loss) into earnings is determined by the average cost method.

Non-marketable investment securities are carried at cost. On a periodic basis, Advantest evaluates the investments for the possible impairment. If the fair value of the investment securities is estimated to have declined and such decline is judged to be other than temporary, Advantest recognizes the impairment of the investment and the carrying value is reduced to its fair value. The impairment is charged to earnings and a new cost basis for the security is established.

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**ADVANTEST CORPORATION**

**AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements (Continued)**

***(h) Derivative Financial Instruments***

Derivative financial instruments are accounted for under Statement of Financial Accounting Standards ( SFAS ) No. 133, Accounting for Derivative Instruments and Hedging Activities , and SFAS No. 138, Accounting for Certain Derivative Instruments and Certain Hedging Activities, an amendment of FASB Statement No. 133 . SFAS No. 133, as amended, standardizes the accounting for derivative instruments, including certain derivative instruments embedded in other contracts. Under SFAS No. 133, as amended, entities are required to carry all derivative instruments in the consolidated balance sheets at fair value. The accounting for changes in the fair value (that is, gains or losses) of a derivative instrument depends on whether it has been designated and qualifies as part of a hedging relationship and, if so, the reason for holding the instrument. If certain conditions are met, entities may elect to designate a derivative instrument as a hedge of exposures to changes in fair values, cash flows, or foreign currencies. If the hedged exposure is a fair value exposure, the gain or loss on the derivative instrument is recognized in earnings in the period of change together with the offsetting loss or gain on the hedged item attributable to the risk being hedged. If the hedged exposure is a cash flow exposure, the effective portion of the gain or loss on the derivative instrument is reported initially as a component of other comprehensive income (loss) and subsequently reclassified into earnings when the forecasted transaction affects earnings. Any amounts excluded from the assessment of hedge effectiveness as well as the ineffective portion of the gain or loss are reported in earnings immediately. If the derivative instrument is not designated as a hedge, the gain or loss is recognized in earnings in the period of change.

Advantest uses foreign exchange forward contracts to manage currency exposure, resulting from changes in foreign currency exchange rates, on trade receivables. However, these contracts do not qualify for hedge accounting since they do not meet the hedging criteria specified by SFAS No. 133.

Foreign exchange forward contracts generally have maturities of several months. These contracts are used to reduce Advantest s risk associated with exchange rate movements, as gains and losses on these contracts are intended to offset exchange losses and gains on underlying exposures. Changes in fair value of foreign exchange forward contracts are recognized in earnings under the caption of other income (expense).

Advantest does not, as a matter of policy, enter into derivative transactions for the purpose of speculation.

***(i) Property, Plant and Equipment***

Property, plant and equipment is stated at cost.

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Depreciation is computed principally using the declining-balance method except for buildings for the Company and its domestic subsidiaries and the straight-line method over estimated useful lives of the assets for foreign subsidiaries. Buildings are principally depreciated using the straight-line method over their estimated useful lives. The depreciation period for significant assets ranges from 15 years to 50 years for buildings, 4 years to 10 years for machinery and equipment, and 2 years to 5 years for furniture and fixtures.

Depreciation expense was ¥8,670 million, ¥7,563 million and ¥7,231 million (\$67,334 thousand) in the years ended March 31, 2003, 2004 and 2005, respectively.

### *(j) Intangible Assets and Other Assets*

Intangible assets principally consist of licenses, goodwill and computer software for internal-use, including computer software under capital leases. Other assets consist of investments (other than investment securities), security deposits and prepaid expenses, of which no one individual item was material to the consolidated financial statements of Advantest.

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**ADVANTEST CORPORATION**

**AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements (Continued)**

Advantest capitalizes certain costs incurred to purchase or develop software for internal-use. Costs incurred to develop software for internal-use are expensed as incurred during the preliminary project stage, which includes costs for making strategic decisions about the project, determining performance and system requirements and vendor demonstration cost. Costs incurred subsequent to the preliminary project stage through implementation are capitalized. Advantest also expenses costs incurred for internal-use software projects in the post implementation stage such as costs for training and maintenance.

Costs incurred to develop software to be included with and sold as part of the Company's Semiconductor Test Systems are capitalized subsequent to the attainment of technological feasibility in accordance with the provisions of SFAS No. 86, Accounting for the Costs of Computer Software to Be Sold, Leased, or Otherwise Marketed. To date, costs incurred subsequent to the attainment of technological feasibility have been insignificant and, therefore, have been charged directly to expense. Costs incurred prior to reaching technological feasibility are expensed as incurred.

The cost of software is amortized on a straight-line basis over the estimated useful life, which is generally five years. The cost of computer software under capital leases is amortized straight-line over the lease term.

Business combinations are accounted for using the purchase method in accordance with SFAS No. 141, Business Combinations. SFAS No. 141 establishes certain criteria for the recognition of intangible assets separately from goodwill. Under SFAS No. 142, Goodwill and Other Intangible Assets, goodwill is no longer amortized, but instead is tested for impairment at least annually. Intangible assets with definite useful lives are amortized over their respective estimated useful lives and reviewed for impairment in accordance with SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets. Any recognized intangible assets determined to have an indefinite useful life are not amortized, but instead are tested for impairment until its life is determined to be no longer indefinite.

Advantest performs its annual impairment test at the end of each year. Advantest completed its annual impairment test at the end of the years ended March 31, 2004 and 2005, with no indication of impairment identified.

***(k) Impairment of Long-Lived Assets***

Advantest evaluates the impairment of long-lived assets in accordance with the provisions of SFAS No. 144. SFAS No. 144 requires that long-lived assets and certain identifiable intangibles with definite useful lives be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future undiscounted net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets.

For the year ended March 31, 2004, one of the former independent cash flow-generating units, the measuring instruments assets group reported operating losses for two consecutive years, and future operating results of the assets group was not expected to be profitable, due to the customers continuously inactive industries such as wireless communications. Since the carrying amount of the assets group was higher than the undiscounted net cash flows expected to result from the use and eventual disposition of the assets group, Advantest adjusted its carrying amount to the recoverable amount. The recoverable amount was based on the observable market price and Advantest's cash flow analysis. Total recognized impairment loss was ¥3,030 million and is included in selling, general and administrative expenses for the year ended March 31, 2004. The impairment loss consisted of ¥1,226 million from buildings, ¥175 million from machinery and equipment, ¥683 million from furniture and fixtures, ¥681 million from software, and ¥265 million from other assets.

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**ADVANTEST CORPORATION**

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**Notes to Consolidated Financial Statements (Continued)**

***(l) Accrued Warranty Expenses***

Advantest's products are generally subject to warranty, and Advantest provides an allowance for such estimated costs when product revenue is recognized. To provide for future repairs and support during warranty periods, estimated repair and support expenses over the warranty period are accrued based on the historical ratio of actual repair and support expenses to corresponding sales.

***(m) Accrued Pension and Severance Cost***

The Company and certain of its domestic subsidiaries have retirement and severance defined benefit plans covering substantially all of their employees. The benefits are based on years of service and the employee's compensation and vest after one year of service. Prior service cost that results from amendments to the plan is amortized over the average remaining service period of the employees expected to receive benefits. Unrecognized net gain and loss is also amortized over the average remaining service period of the employees expected to receive benefits. See Note (17) to the consolidated financial statements for further discussion.

***(n) Revenue Recognition***

In accordance with the guidance provided by the Securities and Exchange Commission's Staff Accounting Bulletin No. 104, Revenue Recognition, Advantest recognizes revenue when there is persuasive evidence of an arrangement, title and risk of loss have passed, delivery has occurred or the services have been rendered, the sales price is fixed or determinable and collection of the related receivable is reasonably assured.

**Revenue from Sales of Products**

Revenue from sales of products which require installation work is recognized when the related installation work is completed. The revenue recognized upon completion of installation is limited to the amount that is payable based on customer acceptance. Revenue from sales of products and component which do not require installation work by Advantest is recognized upon shipment if the terms of the sale are free on board ( FOB ) shipping point or upon delivery if the terms are FOB destination which coincide with the passage of title and risk of loss.

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For equipment sales involving software that is more than incidental to the product, revenue is recognized when persuasive evidence of an arrangement exists, delivery has occurred, the sales price is fixed or determinable, and collection of the related receivable is probable in accordance with American Institute of Certified Public Accountant ( AICPA ) Statement of Position ( SOP ) No. 97-2, Software Revenue Recognition, as amended by SOP No. 98-9, Modification of SOP 97-2, Software Revenue Recognition, With Respect to Certain Transactions. Revenue for the separate elements is only recognized when the functionality of the undelivered element is not essential to the delivered element.

### Revenue from Long-term Service contracts

Revenue from fixed-price, long-term service contracts is recognized on the straight-line basis over the contract term.

### Operating lease

Revenue from operating leases is primarily recognized on the straight-line basis over the lease term.

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**Notes to Consolidated Financial Statements (Continued)**

**Multiple deliverables**

Multiple Deliverables are accounted for under the Emerging Issues Task Force Issue No. 00-21 ( EITF 00-21 ), Revenue Arrangements with Multiple Deliverables . EITF 00-21 addresses how to determine whether an arrangement involving multiple deliverables contains more than one unit of accounting.

Advantest enters into certain revenue arrangements with multiple deliverables, which include combination of equipment, installation and warranty services. As those installation or warranty services are not interchangeable to be provided by Advantest or other parties and as fair values of those services are not determinable, these elements are not considered to qualify for separate accounting under EITF 00-21 and accordingly Advantest treats them as a single unit of accounting. Advantest adopted the provisions of EITF 00-21 for the transactions entered into on and after July 1, 2003. The effect on Advantest s consolidated financial statements from the adoption of such provisions was insignificant.

***(o) Shipping and Handling Costs***

Shipping and handling costs totaled ¥774 million, ¥1,011 million and ¥1,329 million (\$12,375 thousand) for the years ended March 31, 2003, 2004 and 2005, respectively, and are included in selling, general and administrative expenses in the consolidated statements of operations.

***(p) Research and Development***

Research and development costs totaled ¥23,615 million, ¥21,637 million and ¥26,280 million (\$244,716 thousand) for the years ended March 31, 2003, 2004 and 2005, respectively, and are expensed as incurred.

***(q) Advertising Costs***

Advertising costs totaled ¥428 million, ¥384 million and ¥798 million (\$7,431 thousand) for the years ended March 31, 2003, 2004 and 2005, respectively, and are expensed as incurred.

*(r) Stock-Based Compensation*

Prior to April 1, 2004, the Company accounted for stock-based compensation plans by applying the intrinsic value-based method of accounting under the recognition and measurement provisions of APB Opinion No. 25, Accounting for Stock Issued to Employees, and related Interpretations, as permitted by SFAS No. 123, Accounting for Stock-Based Compensation. No stock-based employee compensation cost was recognized in the statement of operations for the years ended March 31, 2003 and 2004. Effective April 1, 2004, the Company early adopted the fair value recognition provisions of SFAS No. 123 (revised 2004) ( SFAS No. 123R ), Share Based Payment , using the modified-retrospective method. The fair value of the options is estimated using a Black Scholes option pricing model and amortized to expense over the options vesting periods.

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**ADVANTEST CORPORATION**  
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**Notes to Consolidated Financial Statements (Continued)**

The following table illustrates the effect on net income and earnings per share as if Advantest had applied the fair value recognition provisions of SFAS No. 123 to options granted under the stock option plans for the year ended March 31, 2003 and 2004.

|  | 2003                      | 2004    |
|--|---------------------------|---------|
|  | Yen                       |         |
|  | (Millions, except for per |         |
|  | share data)               |         |
| Net income (loss):   | P/L                       | P/L     |
| As reported  | ¥ (12,994)                | 17,329  |
| Deduct: stock-based employee compensation expense, net of tax effect | (2,592)                   | (1,963) |
| Pro forma  | ¥ (15,586)                | 15,366  |
| Basic net income (loss) per share:                                   |                           |         |
| As reported  | ¥ (131.99)                | 176.37  |
| Pro forma  | (158.32)                  | 156.39  |
| Diluted net income (loss) per share:                                 |                           |         |
| As reported  | ¥ (131.99)                | 176.02  |
| Pro forma  | (158.32)                  | 156.08  |

No stock-based compensation expense was reflected in net income, as reported, for the years ended March 31, 2003 and 2004. Stock based compensation expense of ¥2,290 million was included reported net income for the year ended March 31, 2005.

The per share weighted average fair value of stock options granted during the years ended March 31, 2003, 2004 and 2005 was ¥3,526, ¥2,570 and ¥2,993 (\$28) on the date of grant using the Black Scholes option pricing model with the following weighted-average assumptions:

|                         | 2003    | 2004    | 2005    |
|-------------------------|---------|---------|---------|
| Expected dividend yield | 0.5%    | 0.8%    | 0.5%    |
| Risk free interest rate | 0.6%    | 0.6%    | 0.6%    |
| Volatility              | 67.8%   | 69.5%   | 56.6%   |
| Expected life           | 4 years | 4 years | 4 years |

*(s) Income Taxes*

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Advantest records a valuation allowance to reduce the deferred tax assets to the amount that is more likely than not realizable.

*(t) Net Income (Loss) per Share*

Basic net income (loss) per share is calculated by dividing net income (loss) by the weighted average number of shares outstanding during the year. Diluted net income per share is calculated by dividing net income by the sum of the weighted average number of shares plus additional shares that would have been outstanding if potential dilutive shares had been issued for granted stock options and warrants.

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**Notes to Consolidated Financial Statements (Continued)**

At March, 31, 2003, 2004 and 2005, Advantest had outstanding stock options and warrants exercisable into 1,113,800, 329,500 and 7,000 shares of common stock, respectively, which could potentially dilute net income per share in future periods.

***(u) Translation of Foreign Financial Statements***

Foreign currency financial statements have been translated in accordance with SFAS No. 52, *Foreign Currency Translation*. Under SFAS No. 52, assets and liabilities of non-Japanese subsidiaries, which have a functional currency other than the Japanese yen, are translated at the rate of exchange on the balance sheet date. Revenue and expense accounts are translated at the average rate of exchange in effect during the year. Resulting translation adjustments are included as a component of accumulated other comprehensive income (loss).

***(v) Foreign Currency Transactions***

Assets and liabilities denominated in foreign currencies at the balance sheet date are translated at the applicable current rate prevailing at that date. All revenue and expenses associated with foreign currencies are converted at the rate of exchange prevailing when such transactions occur. The resulting exchange gains or losses are reflected in other income (expense) in the accompanying consolidated statements of operations.

***(w) Use of Estimates***

Management of Advantest has made a number of estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statement and the reported amounts of revenues and expenses during the period to prepare these consolidated financial statements in conformity with accounting principles generally accepted in the United States of America. Significant items subject to such estimates and assumptions include valuation allowances for trade receivables, inventories and deferred tax assets, various accruals such as accrued warranty expenses, and assets and obligations related to employees retirement and severance plans. Actual results could differ from those estimates.

***(x) New Accounting Standards***

In March 2004, the Emerging Issues Task Force reached a consensus on Issue No.03-1 ( EITF 03-1 ), *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments*. EITF 03-1 provides guidance on other-than-temporary impairment models for

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marketable debt and equity securities accounted for under Statement of Financial Accounting Standards ( SFAS ) No.115, Accounting for Certain Investments in Debt and Equity Securities ( SFAS 115 ), and non-marketable equity securities accounted for under the cost method. The EITF developed a basic three-step model to evaluate whether an investment is other-than-temporarily impaired. The Financial Accounting Standards Board ( FASB ) issued FASB Staff Position EITF 03-1-1 in September 2004 which delayed the effective date of the recognition and measurement provisions of EITF 03-1. The adoption of EITF 03-1 is not expected to have a material effect on Advantest s consolidated results of operations and financial position.

In November 2004, the FASB issued SFAS No.151, Inventory Costs-an amendment of ARB No. 43, Chapter 4 ( SFAS 151 ). SFAS151 amends the guidance in ARB No.43, Chapter 4, Inventory Pricing, to clarify the accounting for abnormal amounts of idle facility expense, freight, handling costs, and wasted material (spoilage). Among other provisions, the new rule requires that items such as idle facility expense, excessive spoilage, double freight, and rehandling costs be recognized as current period charges regardless of whether they meet the criterion of so abnormal as stated in ARB No. 43. Additionally, SFAS 151 requires that the allocation

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**Notes to Consolidated Financial Statements (Continued)**

of fixed production overheads to the costs of conversion be based on the normal capacity of the production facilities. SFAS 151 is effective for fiscal years beginning after June 15, 2005 and is required to be adopted by Advantest in the first quarter beginning April 1, 2006. Advantest is currently evaluating the effect that the adoption of SFAS 151 will have on its consolidated results of operations and financial condition.

In December 2004, the FASB issued SFAS No.153, Exchange of Nonmonetary Assets-an amendment of APB Opinion No.29 ( SFAS 153 ) eliminates the exception from fair value measurement for nonmonetary exchanges of similar productive assets in paragraph 21(b) of APB Opinion No.29, Accounting for Nonmonetary Transactions , and replaces it with an exception for exchanges that do not have commercial substance. SFAS 153 specifies that a nonmonetary exchange has commercial substance if the future cash flows of the entity are expected to change significantly as a result of the exchange. SFAS 153 is effective for the fiscal periods beginning after June 15, 2005 and is required to be adopted by Advantest in the first quarter beginning April 1, 2006. Advantest is currently evaluating the effect that the adoption of SFAS 153 will have on its consolidated results of operations and financial condition.

***(y) Reclassifications***

Certain reclassifications have been made to the prior years consolidated financial statements to conform with the presentation used for the year ended March 31, 2005.

**(2) U.S. Dollar Amounts**

U.S. dollar amounts presented in the consolidated financial statements and related notes are included solely for the convenience of the reader. These translations should not be construed as representations as to what the yen amounts actually represent, or have been or could be converted into, U.S. dollars. For this purpose, the rate of ¥107.39 per U.S.\$1, the approximate current exchange rate at March 31, 2005, was used for the translation of the accompanying financial results of Advantest as of and for the year ended March 31, 2005.

**(3) Trade Receivables**

Trade receivables at March 31, 2004 and 2005 are as follows:

| 2004 | 2005 | 2005 |
|------|------|------|
|------|------|------|

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|                                      | Yen        |        | U.S. Dollars |
|--------------------------------------|------------|--------|--------------|
|                                      | (Millions) |        | (Thousands)  |
| Notes                                | ¥ 8,642    | 14,133 | \$ 131,604   |
| Accounts                             | 69,955     | 44,743 | 416,641      |
|                                      | 78,597     | 58,876 | 548,245      |
| Less allowance for doubtful accounts | 2,464      | 2,174  | 20,244       |
|                                      | ¥ 76,133   | 56,702 | \$ 528,001   |

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AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements (Continued)**

**(4) Allowance for Doubtful Accounts**

Changes in the allowance for doubtful accounts for the years ended March 31, 2003, 2004 and 2005 were as follows:

|                                 | <u>2003</u>    | <u>2004</u>  | <u>2005</u>  | <u>2005</u>      |
|---------------------------------|----------------|--------------|--------------|------------------|
|                                 | Yen            |              |              | U.S. Dollars     |
|                                 | (Millions)     |              |              | (Thousands)      |
| Balance at beginning of year    | ¥ 533          | 1,240        | 2,464        | \$ 22,944        |
| Amount written off              | (103)          | (17)         | (51)         | (475)            |
| Reversal of doubtful accounts   |                | (212)        | (397)        | (3,697)          |
| Provision for doubtful accounts | 810            | 1,453        | 158          | 1,472            |
|                                 | <u>¥ 1,240</u> | <u>2,464</u> | <u>2,174</u> | <u>\$ 20,244</u> |

**(5) Inventories**

Inventories at March 31, 2004 and 2005 are composed of the following:

|                            | <u>2004</u>     | <u>2005</u>   | <u>2005</u>       |
|----------------------------|-----------------|---------------|-------------------|
|                            | Yen             |               |                   |
|                            | (Millions)      |               |                   |
|                            | U.S. Dollars    |               |                   |
|                            | (Thousands)     |               |                   |
| Finished goods             | ¥ 14,819        | 7,347         | \$ 68,414         |
| Work in process            | 25,433          | 16,879        | 157,175           |
| Raw materials and supplies | 9,171           | 5,359         | 49,902            |
|                            | <u>¥ 49,423</u> | <u>29,585</u> | <u>\$ 275,491</u> |

**(6) Property, Plant and Equipment**

Property, plant and equipment at March 31, 2004 and 2005 is composed of the following:

|                               | <u>2004</u>     | <u>2005</u>    | <u>2005</u>       |
|-------------------------------|-----------------|----------------|-------------------|
|                               | Yen             |                | U.S. Dollars      |
|                               | (Millions)      |                | (Thousands)       |
| Land                          | ¥ 19,174        | 19,192         | \$ 178,713        |
| Buildings                     | 49,368          | 49,641         | 462,249           |
| Machinery and equipment       | 24,660          | 27,162         | 252,929           |
| Furniture and fixtures        | 21,200          | 22,934         | 213,558           |
| Construction in progress      | 647             | 349            | 3,250             |
|                               | <u>115,049</u>  | <u>119,278</u> | <u>1,110,699</u>  |
| Less accumulated depreciation | <u>64,533</u>   | <u>67,914</u>  | <u>632,405</u>    |
|                               | <u>¥ 50,516</u> | <u>51,364</u>  | <u>\$ 478,294</u> |

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**Notes to Consolidated Financial Statements (Continued)**

**(7) Goodwill and Other Intangible Assets**

The components of acquired intangible assets excluding goodwill at March 31, 2004 and 2005 were as follows:

|  | 2004                     |                             | 2005                     |                             |
|--|--------------------------|-----------------------------|--------------------------|-----------------------------|
|  | Gross carrying<br>amount | Accumulated<br>amortization | Gross carrying<br>amount | Accumulated<br>amortization |
|  | Yen                      |                             |                          |                             |
|  | (Millions)               |                             |                          |                             |
| Intangible assets subject to amortization: |                          |                             |                          |                             |
| Software                                   | ¥ 5,852                  | 3,930                       | ¥ 4,976                  | 3,668                       |
| Other                                      | 1,464                    | 1,282                       | 1,473                    | 1,343                       |
| <b>Total</b>                               | <b>¥ 7,316</b>           | <b>5,212</b>                | <b>¥ 6,449</b>           | <b>5,011</b>                |

|  | 2005                     |                             |
|--|--------------------------|-----------------------------|
|  | Gross carrying<br>amount | Accumulated<br>amortization |
|  | U.S. dollars             |                             |
|  | (Thousands)              |                             |
| Intangible assets subject to amortization: |                          |                             |
| Software                                   | \$ 46,336                | 34,156                      |
| Other                                      | 13,716                   | 12,506                      |
| <b>Total</b>                               | <b>\$ 60,052</b>         | <b>46,662</b>               |

Intangible assets not subject to amortization at March 31, 2004 and 2005 were insignificant.

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Aggregate amortization expense for the years ended March 31, 2003, 2004 and 2005 was ¥2,292 million, ¥1,765 million and ¥1,054 million (\$9,815 thousand), respectively. Estimated amortization expense for the next five years ending March 31 is: ¥756 million (\$7,040 thousand) in 2006, ¥344 million (\$3,203 thousand) in 2007, ¥150 million (\$1,397 thousand) in 2008, ¥74 million (\$689 thousand) in 2009, and ¥35 million (\$326 thousand) in 2010, respectively.

Changes in the carrying amount of goodwill for the years ended March 31, 2004 and 2005 were as follows:

|                              | 2004       | 2005    | 2005         |
|------------------------------|------------|---------|--------------|
|                              | Yen        |         | U.S. dollars |
|                              | (Millions) |         | (Thousands)  |
| Balance at beginning of year | ¥ 645      | ¥ 1,426 | \$ 13,279    |
| Acquisition during the year  | 781        |         |              |
|                              | ¥ 1,426    | ¥ 1,426 | \$ 13,279    |
|                              | ¥ 1,426    | ¥ 1,426 | \$ 13,279    |

The goodwill relates to the semiconductor and component test system segment.

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**ADVANTEST CORPORATION  
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**Notes to Consolidated Financial Statements (Continued)**

**(8) Investment Securities**

Marketable securities consist of equity securities. The acquisition cost, gross unrealized gains, gross unrealized losses and fair value at March 31, 2004 and 2005 were as follows:

|                     | 2004                |            |            | Fair value |
|---------------------|---------------------|------------|------------|------------|
|                     | Acquisition<br>cost | Gross      | Gross      |            |
|                     |                     | unrealized | unrealized |            |
|                     |                     | gains      | losses     |            |
| Yen (Millions)      |                     |            |            |            |
| Noncurrent:         |                     |            |            |            |
| Available-for-sale: |                     |            |            |            |
| Equity securities   | ¥ 2,238             | 2,093      | 1          | 4,311      |

|                     | 2005                |            |            | Fair value |
|---------------------|---------------------|------------|------------|------------|
|                     | Acquisition<br>cost | Gross      | Gross      |            |
|                     |                     | unrealized | unrealized |            |
|                     |                     | gains      | losses     |            |
| Yen (Millions)      |                     |            |            |            |
| Noncurrent:         |                     |            |            |            |
| Available-for-sale: |                     |            |            |            |
| Equity securities   | ¥ 3,803             | 2,516      |            | 6,328      |

|                | 2005                |            |            | Fair value |
|----------------|---------------------|------------|------------|------------|
|                | Acquisition<br>cost | Gross      | Gross      |            |
|                |                     | unrealized | unrealized |            |
|                |                     | gains      | losses     |            |
| Yen (Millions) |                     |            |            |            |

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|                     | U.S. dollars (Thousands) |        |        |
|---------------------|--------------------------|--------|--------|
| Noncurrent:         |                          |        |        |
| Available-for-sale: |                          |        |        |
| Equity securities   | \$ 35,031                | 23,429 | 58,925 |

Gross realized gains and losses on available-for-sales equity securities for the years ended March 31, 2003, 2004 and 2005 were as follows:

|                     | 2003                       |                             | 2004                       |                             |
|---------------------|----------------------------|-----------------------------|----------------------------|-----------------------------|
|                     | Gross<br>realized<br>gains | Gross<br>realized<br>losses | Gross<br>realized<br>gains | Gross<br>realized<br>losses |
|                     | Yen (Millions)             |                             | Yen (Millions)             |                             |
| Noncurrent:         |                            |                             |                            |                             |
| Available-for-sale: |                            |                             |                            |                             |
| Equity securities   | ¥                          | 1,010                       | ¥ 178                      | 2                           |

|                     | 2005                       |                             | 2005                        |                             |
|---------------------|----------------------------|-----------------------------|-----------------------------|-----------------------------|
|                     | Gross<br>realized<br>gains | Gross<br>realized<br>losses | Gross<br>realized<br>gains  | Gross<br>realized<br>losses |
|                     | Yen (Millions)             |                             | U.S. dollars<br>(Thousands) |                             |
| Noncurrent:         |                            |                             |                             |                             |
| Available-for-sale: |                            |                             |                             |                             |
| Equity securities   | ¥ 934                      |                             | \$ 8,697                    |                             |

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Gross realized gains and losses based on the averaged cost method are included in other income (expense) in the consolidated statements of operations, and other in net cash provided by operating activities in the consolidated statements of cash flows.

Proceeds from the sale of available-for-sales equity securities for the years ended March 31, 2003, 2004 and 2005 were nil, ¥323 million and ¥1,428 million (\$13,297 thousand), respectively.

As of March 31 2005, there was no available-for-sale equity security in an unrealized loss position.

Advantest maintains non-marketable investment securities, which are recorded at cost. The carrying amounts of non-marketable investment securities were ¥3,641 million and ¥1,444 million (\$13,447 thousand) at March 31, 2004 and 2005, respectively. Investments with an aggregate cost of ¥1,444 million (\$13,447 thousand) did not have indicators of impairment and Advantest did not identify any events or changes in circumstances that might have had significant adverse effect on the fair value of those investments.

**(9) Derivative Financial Instruments**

Derivative financial instruments are utilized by Advantest primarily to reduce foreign currency exchange risk. Advantest does not hold or issue derivative financial instruments for trading purposes. Advantest generally does not require or place collateral for these derivative financial instruments.

Derivative financial instruments contain an element of risk in the event the counterparties are unable to meet the terms of the agreements. However, Advantest minimizes risk exposure by limiting the counterparties to major international banks and financial institutions meeting established credit guidelines. Management of Advantest does not expect any counterparty to default on its obligations and, therefore, does not expect to incur any losses due to counterparty default on its obligations.

Advantest had foreign exchange forward contracts to exchange currencies among Japanese yen, U.S. dollars and Euro at March 31, 2004 and 2005. The notional amounts of these contracts were ¥8,736 million at March 31, 2004 and ¥7,603 million (\$70,798 thousand) at March 31, 2005. The fair values of these contracts at March 31, 2004 and 2005 are shown in Note (10) to the consolidated financial statements. These contracts do not qualify for hedge accounting since they do not meet the hedging criteria specified by SFAS No. 133. Changes in the fair value are recognized in earnings under the caption of other income (expense).



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**Notes to Consolidated Financial Statements (Continued)**

**(10) Fair Value of Financial Instruments**

The following table presents the carrying amounts and estimated fair values of Advantest's financial instruments at March 31, 2004 and 2005, except for cash and cash equivalents, trade receivables, other current assets, trade accounts payable and accrued expenses for which fair value approximate their carrying amounts. Fair value estimates are made at a specific point in time based on relevant market information and information about the financial instrument. These estimates are subjective in nature and involve uncertainties and matters of significant judgement and, therefore, cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

|  | 2004               |               | 2005               |               |
|--|--------------------|---------------|--------------------|---------------|
|  | Carrying<br>amount | Fair<br>value | Carrying<br>amount | Fair<br>value |
|  | Yen (Millions)     |               |                    |               |
| Financial assets:                        |                    |               |                    |               |
| Investment securities for which it is:   |                    |               |                    |               |
| Practicable to estimate fair value       | ¥ 4,311            | 4,311         | 6,328              | 6,328         |
| Not practicable to estimate fair value   | 3,641              |               | 1,444              |               |
| Foreign exchange forward contracts       | 91                 | 91            | 1                  | 1             |
| Financial liabilities:                   |                    |               |                    |               |
| Foreign exchange forward contracts       | 105                | 105           | 49                 | 49            |
| Long-term debt including current portion | 24,626             | 25,223        | 20,083             | 20,354        |

|  | 2005                        |               |
|--|-----------------------------|---------------|
|  | Carrying<br>amount          | Fair<br>value |
|  | U.S. Dollars<br>(Thousands) |               |
| Financial assets:                        |                             |               |
| Investment securities for which it is:   |                             |               |
| Practicable to estimate fair value       | \$ 58,925                   | 58,925        |
| Not practicable to estimate fair value   | 13,447                      |               |
| Foreign exchange forward contracts       | 9                           | 9             |
| Financial liabilities:                   |                             |               |
| Foreign exchange forward contracts       | 456                         | 456           |
| Long-term debt including current portion | 187,010                     | 189,533       |

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The carrying amounts shown in the table are included in the consolidated balance sheets under the indicated captions. And the carrying amounts of foreign exchange forward contracts are included in other current assets and other current liabilities.

The following methods and assumptions were used to estimate the fair value of each class of financial instruments:

*Cash and cash equivalents, trade receivables, other current assets, trade accounts payable, and accrued expenses (nonderivatives):* The carrying amounts approximate fair value because of the short maturity of these instruments.

*Investment securities:* The fair values of equity investments are based on quoted market prices at the reporting date for those investments. It was not practicable to estimate the fair value of nonpublic companies; those investments are carried at cost.

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*Long-term debt:* The fair value of long-term debt is estimated by discounting future cash flows of each instrument at rates currently offered to Advantest for similar debt instruments of comparable maturities by financial institutions.

*Foreign exchange forward contracts:* The fair value of foreign exchange forward contracts are estimated by obtaining quotes from financial institution.

**(11) Leases Lessor**

Advantest provides leases that enable its customers to use semiconductor test systems. All leases are classified as operating leases. Lease terms range from 1 year to 5 years, and certain of the lease agreements are cancelable. The gross amount of machinery and equipment and the related accumulated depreciation under operating leases as of March 31, 2004 and 2005 were as follows:

|                               | <u>2004</u>    | <u>2005</u>  | <u>2005</u>      |
|-------------------------------|----------------|--------------|------------------|
|                               | Yen            |              | U.S. Dollars     |
|                               | (Millions)     |              | (Thousands)      |
| Machinery and equipment       | ¥ 5,450        | 8,221        | \$ 76,553        |
| Less accumulated depreciation | 2,398          | 3,450        | 32,126           |
|                               | <u>¥ 3,052</u> | <u>4,771</u> | <u>\$ 44,427</u> |

Depreciation of machinery and equipment held under operating leases are included with depreciation expense. These assets are included in property, plant and equipment.

Future minimum lease income under noncancelable operating leases as of March 31, 2005 is as follows:

| <u>Year ending March 31</u> | Yen        | U.S. Dollars |
|-----------------------------|------------|--------------|
|                             | (Millions) | (Thousands)  |

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|                                   |                |                  |
|-----------------------------------|----------------|------------------|
| 2006                              | ¥ 1,549        | \$ 14,424        |
| 2007                              | 648            | 6,034            |
| 2008                              | 382            | 3,557            |
| 2009                              | 86             | 801              |
| <b>Total minimum lease income</b> | <b>¥ 2,665</b> | <b>\$ 24,816</b> |

**(12) Leases Lessee**

Tangible and intangible assets under capital leases at March 31, 2004 and 2005 were insignificant.

Advantest also has several noncancelable operating leases, primarily for office space and office equipment that expire within the next five years. Rent expense, including rental payments for cancelable leases, for the years ended March 31, 2003, 2004 and 2005 was ¥1,638 million, ¥1,352 million and ¥1,423 million (\$13,251 thousand), respectively.

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Future minimum lease payments under noncancelable operating leases (with initial or remaining lease terms in excess of one year) as of March 31, 2005 are as follows:

| <u>Year ending March 31</u>         | <u>Yen</u><br><u>(Millions)</u> | <u>U.S. Dollars</u><br><u>(Thousands)</u> |
|-------------------------------------|---------------------------------|---|
| 2006                                | ¥ 329                           | \$ 3,064                                  |
| 2007                                | 294                             | 2,738                                     |
| 2008                                | 77                              | 717                                       |
| 2009                                | 8                               | 74  |
| <b>Total minimum lease payments</b> | <b>¥ 708</b>                    | <b>\$ 6,593</b>                           |

**(13) Short-Term and Long-Term Debt**

Long-term debt at March 31, 2004 and 2005 consists of the following:

|  | <u>2004</u>       | <u>2005</u>   | <u>2005</u>         |
|--|-------------------|---------------|---------------------|
|  | <u>Yen</u>        |               | <u>U.S. Dollars</u> |
|  | <u>(Millions)</u> |               | <u>(Thousands)</u>  |
| Partially secured borrowings by mortgage of property, plant and equipment, due 2004 to 2008 with annual interest rates ranging from 1.05% to 4.125% in 2004 and 2005 | ¥ 126             | 83            | \$ 773              |
| Unsecured 0.88% bonds, due February 5, 2005  | 4,500             |               |                     |
| Unsecured 1.88% bonds, due December 14, 2005   | 20,000            | 20,000        | 186,237             |
| <b>Total long-term debt</b>  | <b>24,626</b>     | <b>20,083</b> | <b>187,010</b>      |
| Less current portion   | 4,543             | 20,043        | 186,637             |
| <b>Long-term debt, excluding current portion</b>   | <b>¥ 20,083</b>   | <b>40</b>     | <b>\$ 373</b>       |

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Unsecured 0.88% bonds were issued with detachable warrants in connection with one of Advantest's stock-based compensation plans. As described in Note (16) to the consolidated financial statements, upon issuance of each bond, the Company purchased all detachable warrants from the underwriter and distributed such warrants to the directors and selected employees of the Company and its subsidiaries. No gain or loss was recognized on the sale and purchase of the warrants. For financial reporting purposes, these transactions were accounted for as the issuance of debt to third parties and separately as the issuance of warrants to directors and employees.

At March 31, 2005, property, plant and equipment with a carrying amount of ¥393 million (\$3,660 thousand) was pledged as collateral for certain debt obligations in the amount of ¥24 million (\$223 thousand).

The aggregate maturities of long-term debt for each of the five years subsequent to March 31, 2005 are as follows:

| <u>Year ending March 31</u> | <u>Yen</u><br><u>(Millions)</u> | <u>U.S. Dollars</u><br><u>(Thousands)</u> |
|-----------------------------|---------------------------------|---|
| 2006                        | ¥ 20,043                        | \$ 186,637                                |
| 2007                        | 30                              | 280                                       |
| 2008                        | 10                              | 93  |
| <b>Total long-term debt</b> | <b>¥ 20,083</b>                 | <b>\$ 187,010</b>                         |

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**Notes to Consolidated Financial Statements (Continued)**

**(14) Income Taxes**

The components of income (loss) before income taxes and provision (benefit) for income taxes as shown in the consolidated statements of operations are as follows:

|                                       | <u>2003</u>       | <u>2004</u>   | <u>2005</u>   | <u>2005</u>       |
|---------------------------------------|-------------------|---------------|---------------|-------------------|
|                                       | Yen               |               |               | U.S. Dollars      |
|                                       | (Millions)        |               |               | (Thousands)       |
| Income (loss) before income taxes:    |                   |               |               |                   |
| The Company and domestic subsidiaries | ¥ (18,581)        | 20,096        | 47,020        | \$ 437,843        |
| Foreign subsidiaries                  | (107)             | 8,782         | 14,788        | 137,704           |
|                                       | <u>¥ (18,688)</u> | <u>28,878</u> | <u>61,808</u> | <u>\$ 575,547</u> |
|                                       |                   |               |               |                   |
|                                       | <u>2003</u>       | <u>2004</u>   | <u>2005</u>   | <u>2005</u>       |
|                                       | Yen               |               |               | U.S. Dollars      |
|                                       | (Millions)        |               |               | (Thousands)       |
| Provision (benefit) for income taxes: |                   |               |               |                   |
| Current:                              |                   |               |               |                   |
| The Company and domestic subsidiaries | ¥ 624             | 1,356         | 5,719         | \$ 53,255         |
| Foreign subsidiaries                  | 1,694             | 3,490         | 4,471         | 41,633            |
| Deferred:                             |                   |               |               |                   |
| The Company and domestic subsidiaries | (6,939)           | 6,749         | 13,424        | 125,002           |
| Foreign subsidiaries                  | (1,073)           | (46)          | 116           | 1,080             |
|                                       | <u>¥ (5,694)</u>  | <u>11,549</u> | <u>23,730</u> | <u>\$ 220,970</u> |

The Company and its domestic subsidiaries are subject to a corporate tax of 30%, an inhabitant tax of between 18.1% and 20.7% and a deductible business tax of between 7.2% and 10.1%, which in the aggregate resulted in a statutory income tax rate of approximately 40% for the year ended March 31, 2005. Amendments to the Japanese tax regulations were enacted on March 24, 2003. As a result of these amendments, the statutory income tax rate was reduced from approximately 42% to 40% effective from the year beginning April 1, 2004. Consequently, the statutory tax rate was to be lowered to approximately 40% applicable for deferred tax assets and liabilities expected to be settled or realized subsequent to April 1, 2004. The adjustment of deferred tax assets and liabilities for this change in the tax rate was ¥143 million and reflected in the consolidated statements of operations for the year ended March 31, 2004.

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A reconciliation of the Japanese statutory income tax rate and the effective income tax rate as a percentage of income (loss) before income taxes is as follows:

|   | <u>2003</u>    | <u>2004</u>  | <u>2005</u>  |
|---|----------------|--------------|--------------|
| Statutory tax rate  | (42.0)%        | 42.0%        | 40.0%        |
| Increase (reduction) in income taxes resulting from:                                      |                |              |              |
| Earnings of foreign subsidiaries taxed at different rate from the statutory rate in Japan | (0.6)          | (2.7)        | (2.3)        |
| Tax credits earned  | (0.4)          | (0.5)        | (1.4)        |
| Expenses not deductible for tax purposes  | 0.3            | 1.2          | 1.7          |
| Change in valuation allowance   | 7.3            | (0.3)        | (0.3)        |
| Tax rate change   | 6.0            | (0.5)        |              |
| Other, net  | (1.1)          | 0.8          | 0.7          |
|   | <u>(30.5)%</u> | <u>40.0%</u> | <u>38.4%</u> |

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The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities at March 31, 2004 and 2005 are presented below.

|  | <u>2004</u>     | <u>2005</u>   | <u>2005</u>       |
|--|-----------------|---------------|-------------------|
|  | Yen             |               | U.S. Dollars      |
|  | (Millions)      |               | (Thousands)       |
| <b>Deferred tax assets:</b>                                    |                 |               |                   |
| Inventories  | ¥ 7,698         | 4,950         | \$ 46,094         |
| Tax effect on intercompany profit                              |                 | 2,534         | 23,596            |
| Accrued warranty expenses                                      | 566             | 1,060         | 9,871             |
| Accrued pension and severance cost                             | 6,500           | 5,049         | 47,016            |
| Minimum pension liability adjustments                          | 943             |               |                   |
| Accrued expenses   | 2,460           | 4,543         | 42,304            |
| Research and development expenses capitalized for tax purposes | 1,688           | 1,957         | 18,223            |
| Operating loss carryforwards                                   | 13,079          | 444           | 4,134             |
| Property, plant and equipment and intangible assets            | 1,097           | 689           | 6,416             |
| Tax credits  |                 | 2,048         | 19,071            |
| Other  | 2,177           | 2,241         | 20,867            |
|  | <u>36,208</u>   | <u>25,515</u> | <u>237,592</u>    |
| Total gross deferred tax assets                                |                 |               |                   |
| Less valuation allowance                                       | 2,149           | 3,025         | 28,168            |
|  | <u>34,059</u>   | <u>22,490</u> | <u>209,424</u>    |
| <b>Deferred tax liabilities:</b>                               |                 |               |                   |
| Net unrealized gains on marketable securities                  | 669             | 874           | 8,139             |
| Other  | 67              | 44            | 410               |
|  | <u>736</u>      | <u>918</u>    | <u>8,549</u>      |
| Total gross deferred tax liabilities                           |                 |               |                   |
| Net deferred tax assets  | <u>¥ 33,323</u> | <u>21,572</u> | <u>\$ 200,875</u> |

The net changes in the valuation allowance for the years ended March 31, 2003, 2004 and 2005 were an increase of ¥1,371 million, ¥509 million and ¥876 million (\$8,157 thousand), respectively.

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Net operating loss carryforwards utilized during the years ended March 31, 2003, 2004 and 2005 were ¥633 million, ¥24,510 million and ¥31,132 million (\$289,897 thousand), respectively.

At March 31, 2005, Advantest had net operating loss carried forwards for income tax purposes of approximately ¥1,102 million (\$10,262 thousand) which are available to reduce future income taxes, if any. These operating losses will expire starting from the year ending March 31, 2006 through the year ending March 31, 2010.

Management of Advantest intends to reinvest certain undistributed earnings of the Company's foreign subsidiaries for an indefinite period of time. As a result, no provision for income taxes has been made on undistributed earnings of these subsidiaries not expected to be remitted in the foreseeable future, aggregating ¥52,022 million (\$484,421 thousand) at March 31, 2005. The related deferred tax liability would have been ¥7,501 million (\$69,848 thousand) at March 31, 2005.

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized.

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The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income, and tax planning strategies in making this assessment. At March 31, 2005, Advantest has recorded on its consolidated balance sheet, net deferred tax assets of ¥21,572 million (\$200,875 thousand). Based upon projections for future taxable income over the periods in which the deferred tax assets are deductible including management's expectations of future semiconductor market and semiconductor and component test systems market prospects and other factors, management believes it is more likely than not that Advantest will realize the benefits of these deductible differences, net of the existing valuation allowance, at March 31, 2005. The amount of the deferred tax assets considered realizable, however, could be reduced in the near term if estimates of future taxable income are reduced and the effect on Advantest's consolidated financial position and results of operations could be significant.

**(15) Other Comprehensive Income (Loss)**

The accumulated balances for each classification of other comprehensive income (loss) for the years ended March 31, 2003, 2004 and 2005 are as follows:

|   | Foreign<br>currency<br>translation<br>adjustments | Net<br>unrealized<br>gains on<br>securities | Minimum<br>pension<br>liability<br>adjustments | Accumulated<br>other<br>comprehensive<br>income (loss) |
|---|---|---|--|--|
|   | Yen (Millions)                                    |   |  |  |
| Balance at April 1, 2002                          | ¥ (1,196)   | 12  |  | (1,184)  |
| Change during the year                            | (2,915)   | (159)                                       |  | (3,074)  |
| Reclassification adjustments for realized portion |   | 203   |  | 203  |
|   | (2,915)   | 44  |  | (2,871)  |
| Balance at March 31, 2003                         | (4,111)   | 56  |  | (4,055)  |
| Change during the year                            | (3,976)   | 1,330                                       | (1,396)  | (4,042)  |
| Reclassification adjustments for realized portion |   | 36  |  | 36   |
|   | (3,976)   | 1,366                                       | (1,396)  | (4,006)  |
| Balance at March 31, 2004                         | (8,087)   | 1,422                                       | (1,396)  | (8,061)  |

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|   |                  |              |              |                |
|---|------------------|--------------|--------------|----------------|
| Change during the year                            | 1,635            | 583          | 1,396        | 3,614          |
| Reclassification adjustments for realized portion |                  | (431)        |              | (431)          |
|   | <u>1,635</u>     | <u>152</u>   | <u>1,396</u> | <u>3,183</u>   |
| Balance at March 31, 2005                         | <u>¥ (6,452)</u> | <u>1,574</u> |              | <u>(4,878)</u> |

|   | <b>Foreign<br/>currency<br/>translation<br/>adjustments</b> | <b>Net<br/>unrealized<br/>gains on<br/>securities</b> | <b>Minimum<br/>pension<br/>liability<br/>adjustments</b> | <b>Accumulated<br/>other<br/>comprehensive<br/>income (loss)</b> |
|---|---|---|--|--|
|   | <b>U.S. Dollars (Thousands)</b>                             |   |  |  |
| Balance at March 31, 2004                         | \$ (75,305)   | 13,241  | (12,999)   | (75,063)   |
| Change during the year                            | 15,225  | 5,428   | 12,999   | 33,652   |
| Reclassification adjustments for realized portion |   | (4,012)   |  | (4,012)  |
|   | <u>15,225</u>   | <u>1,416</u>  | <u>12,999</u>  | <u>29,640</u>  |
| Balance at March 31, 2005                         | <u>\$ (60,080)</u>  | <u>14,657</u>   |  | <u>(45,423)</u>  |

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The related tax effects allocated to each component of other comprehensive income (loss) for the years ended March 31, 2003, 2004 and 2005 are as follows:

|  | <b>Before-tax<br/>amount</b> | <b>Tax<br/>(expense)<br/>or benefit</b> | <b>Net-of-tax<br/>amount</b> |
|--|------------------------------|---|------------------------------|
|  | Yen (Millions)               |   |                              |
| <b>Year ended March 31, 2003:</b>                                    |                              |   |                              |
| Foreign currency translation adjustments                             | ¥ (2,915)                    |   | (2,915)                      |
| Net unrealized gains on securities:                                  |                              |   |                              |
| Net unrealized gains arising during the year                         | (266)                        | 107                                     | (159)                        |
| Less reclassification adjustments for net gains realized in earnings | 340                          | (137)                                   | 203                          |
|  | <u>74</u>                    | <u>(30)</u>                             | <u>44</u>                    |
| Net unrealized gains   |                              |   |                              |
| Other comprehensive income (loss)                                    | ¥ (2,841)                    | (30)                                    | (2,871)                      |
|  | <u>¥ (2,841)</u>             | <u>(30)</u>                             | <u>(2,871)</u>               |
| <b>Year ended March 31, 2004:</b>                                    |                              |   |                              |
| Foreign currency translation adjustments                             | ¥ (3,976)                    |   | (3,976)                      |
| Net unrealized gains on securities:                                  |                              |   |                              |
| Net unrealized gains arising during the year                         | 1,938                        | (608)                                   | 1,330                        |
| Less reclassification adjustments for net gains realized in earnings | 36                           |   | 36                           |
|  | <u>1,974</u>                 | <u>(608)</u>                            | <u>1,366</u>                 |
| Net unrealized gains   |                              |   |                              |
| Minimum pension liability adjustments                                | (2,339)                      | 943                                     | (1,396)                      |
|  | <u>(2,339)</u>               | <u>943</u>                              | <u>(1,396)</u>               |
| Other comprehensive income (loss)                                    | ¥ (4,341)                    | 335                                     | (4,006)                      |
|  | <u>¥ (4,341)</u>             | <u>335</u>                              | <u>(4,006)</u>               |
| <b>Year ended March 31, 2005:</b>                                    |                              |   |                              |
| Foreign currency translation adjustments                             | ¥ 1,635                      |   | 1,635                        |
| Net unrealized gains on securities:                                  |                              |   |                              |
| Net unrealized gains arising during the year                         | 857                          | (274)                                   | 583                          |
| Less reclassification adjustments for net gains realized in earnings | (431)                        |   | (431)                        |
|  | <u>426</u>                   | <u>(274)</u>                            | <u>152</u>                   |
| Net unrealized gains   |                              |   |                              |
| Minimum pension liability adjustments                                | 2,339                        | (943)                                   | 1,396                        |
|  | <u>2,339</u>                 | <u>(943)</u>                            | <u>1,396</u>                 |
| Other comprehensive income (loss)                                    | ¥ 4,400                      | (1,217)                                 | 3,183                        |
|  | <u>¥ 4,400</u>               | <u>(1,217)</u>                          | <u>3,183</u>                 |

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|  | <b>Before-tax<br/>amount</b> | <b>Tax<br/>(expense)<br/>or benefit</b> | <b>Net-of-tax<br/>amount</b> |
|--|------------------------------|---|------------------------------|
| <b>U.S. Dollars (Thousands)</b>                                      |                              |   |                              |
| <b>Year ended March 31, 2005:</b>                                    |                              |   |                              |
| Foreign currency translation adjustments                             | \$ 15,225                    |   | 15,225                       |
| Net unrealized gains on securities:                                  |                              |   |                              |
| Net unrealized gains arising during the year                         | 7,979                        | (2,551)                                 | 5,428                        |
| Less reclassification adjustments for net gains realized in earnings | (4,012)                      |   | (4,012)                      |
| Net unrealized gains   | 3,967                        | (2,551)                                 | 1,416                        |
| Minimum pension liability adjustments                                | 21,780                       | (8,781)                                 | 12,999                       |
| Other comprehensive income (loss)                                    | \$ 40,972                    | (11,332)                                | 29,640                       |

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**Notes to Consolidated Financial Statements (Continued)**

**(16) Stock-Based Compensation**

Advantest has two types of stock-based compensation plans as incentive plans for directors and selected employees. One plan uses stock options and the other plan detachable warrants.

In January 2000 and February 2001, the Company issued unsecured bonds with detachable warrants. Simultaneously with the issuance of the unsecured bonds, the Company purchased all of the detachable warrants from the underwriter and distributed such warrants to directors and selected employees of the Company and its subsidiaries. By exercising a warrant, directors and selected employees could purchase the shares of the Company, the number of which was 99,000 shares and 319,500 shares at the exercise price of ¥21,840 and ¥14,018 for warrants issued in January 2000 and February 2001, respectively. Warrants were granted with an exercise price equal to 1.05 times the closing prices of the Company's shares traded on the Tokyo Stock Exchange on the date of each grant. Under each plan, 990 warrants and 3,195 warrants in January 2000 and February 2001, respectively, were issued. The warrants vested fully immediately, and were exercisable up to 4 years from the date of grant. For financial reporting purposes, these transactions were accounted for as the issuance of debt to third parties and separately as the issuance of warrants to directors and employees. The issuance of the warrants to directors and employees was accounted for under APB Opinion No. 25. All unexercised warrants issued during the year ended March 31, 2000 and 2001 expired in accordance with their original terms during the years ended March 31, 2004 and 2005.

In July 2002, stock options were issued to directors, corporate auditors and certain employees of the Company and its subsidiaries under a stock option plan approved by the Board of Directors. The number of granted shares totaled 735,000. Options were granted with an exercise price of ¥8,148 per share that is equal to the higher of (1) 1.05 times the average price of the Company's common shares of the preceding month on the date of grant and (2) the closing price of the Company's common shares traded on the Tokyo Stock Exchange on the date of grant. The options have an exercise period of 4 years and is exercisable from April 1, 2003.

In April 2003, stock options were issued to a director and certain employees of foreign subsidiaries under a stock option plan approved by the Board of Directors. The number of granted shares totaled 14,000. Options were granted with an exercise price of ¥8,148 per share that is equal to the higher of (1) 1.05 times the average price of the Company's common shares of the preceding month on the date of grant, (2) the closing price of the Company's common shares traded on the Tokyo Stock Exchange on the date of grant, and (3) the exercise price at which the July 2002 options were granted. The options have an exercise period of no later than March 31, 2007 and is exercisable from May 1, 2003.

In June 2003, stock options were issued to directors, executive officers, corporate auditors and certain employees of the Company and its subsidiaries under a stock option plan approved by the Board of Directors. The number of granted shares totaled 734,000. Options were granted with an exercise price of ¥5,160 per share that is equal to the higher of (1) 1.05 times the average price of the Company's common shares of the preceding month on the date of grant and (2) the closing price of the Company's common shares traded on the Tokyo Stock Exchange on the date of grant. The options have an exercise period of 4 years and is exercisable from April 1, 2004.

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In August 2003, January 2004 and March 2004, stock options were issued to a director and certain employees of foreign subsidiaries under a stock option plan approved by the Board of Directors. The number of granted shares totaled 6,000, 7,000 and 3,000, respectively. Options were granted with exercise prices of ¥8,090, ¥9,220 and ¥8,550 per share, respectively, those are equal to the higher of (1) 1.05 times the average price of the Company's common shares of the preceding month on the date of grant, (2) the closing price of the Company's

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common shares traded on the Tokyo Stock Exchange on the date of grant, and (3) the exercise price at which the June 2003 options were granted. All of the options have an exercise period of 4 years and is exercisable from April 1, 2004.

In July 2004, stock options were issued to directors, executive officers, corporate auditors and certain employees of the Company and its subsidiaries under a stock option plan approved by the Board of Directors. The number of granted shares totaled 761,000. Options were granted with an exercise price of ¥7,464 per share that is equal to the higher of (1) 1.05 times the average price of the Company's common shares of the preceding month on the date of grant and (2) the closing price of the Company's common shares traded on the Tokyo Stock Exchange on the date of grant. The options have an exercise period of 4 years and is exercisable from April 1, 2005.

In November 2004, stock options were issued to certain employees of foreign subsidiaries under a stock option plan approved by the Board of Directors. The number of granted shares totaled 4,000. Options were granted with an exercise price of ¥7,464 per share that is equal to the exercise price of the July 2004 options. The options have an exercise period of 4 years and is exercisable from April 1, 2005.

Stock option and warrant activity during the years ended March 31, 2003, 2004 and 2005 is as follows:

|                                  | 2003             |                                 | 2004             |                                 | 2005             |                                 |
|----------------------------------|------------------|---------------------------------|------------------|---------------------------------|------------------|---------------------------------|
|                                  | Number of shares | Weighted average exercise price | Number of shares | Weighted average exercise price | Number of shares | Weighted average exercise price |
| Outstanding at beginning of year | 739,200          | ¥ 12,187                        | 1,113,800        | ¥ 10,942                        | 1,772,500        | ¥ 7,973                         |
| Granted                          | 735,000          | 8,148                           | 764,000          | 5,288                           | 765,000          | 7,464                           |
| Exercised                        |                  |                                 | (21,000)         | (8,148)                         | (152,000)        | 5,632                           |
| Expired                          | (360,400)        | (7,799)                         | (84,300)         | (21,060)                        | (321,500)        | 13,981                          |
| Outstanding at end of year       | 1,113,800        | 10,942                          | 1,772,500        | 7,973                           | 2,064,000        | 7,021                           |
| Exercisable at end of year       | 403,800          | 15,854                          | 1,022,500        | 9,982                           | 1,299,000        | 6,760                           |

Weighted average remaining contractual life of exercisable options at March 31, 2005 were 2.5 years.

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At March 31, 2005, all of the outstanding stock options were as follows:

| <u>Exercise price</u> | <u>Number</u><br><u>outstanding</u> | <u>Weighted average</u><br><u>remaining contractual life</u> |
|-----------------------|-------------------------------------|--|
| <b>Yen</b>            |                                     |  |
| ¥ 5,160               | 606,000                             | 3.0 years  |
| 7,464 - 9,220         | 1,458,000                           | 3.1 years  |
|                       | <u>2,064,000</u>                    |  |

**(17) Accrued Pension and Severance Cost**

The Company and certain of its subsidiaries have unfunded retirement and severance plans. On terminating employment, substantially all employees of the Company and certain subsidiaries are entitled to lump-sum payments based on the employees' compensation and years of service.

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The Company and its domestic subsidiaries also have a contributory defined benefit retirement and severance plan covering substantially all employees. Benefits payable under the plan is based on employee earnings and years of service. The contributory plan mainly represents the Employees Pension Fund ( EPF ) plan, composed of the substitutional portions based on the pay-related part of the old age pension benefits prescribed by the Welfare Pension Insurance Law in Japan and the corporate portions based on contributory defined benefit pension arrangements established at the discretion of the Company and its subsidiaries.

In January 2003, the EITF reached a final consensus on EITF 03-2, Accounting for the Transfer to the Japanese Government of the Substitutional Portion of Employee Pension Fund Liabilities . EITF 03-2 addresses accounting for a transfer to the Japanese government of the substitutional portion of an EPF plan. EITF 03-2 requires employers to account for the entire separation process of the substitutional portion from the EPF upon completion of the transfer to the government of the substitutional portion of the benefit obligation and related plan assets as the culmination of a series of steps in a single settlement transaction. Under this approach, the difference between the fair value of the obligation and the assets required to be transferred to the government should be accounted for and separately disclosed as a subsidy. On October 1, 2004, the Company and certain of its consolidated domestic subsidiaries received approval from the Minister of Health and Labor to return the substitutional portion of its Employees Pension Fund plans for the prior employees services under the transfer of its Employees Pension Fund plans to the defined benefit corporate pension plan, and made the payment of the amount pertinent to the return (minimum liability reserve) to the national treasury on February 24, 2005. Advantest accounted for the elimination of future benefits and relief of past obligations with the transfer of assets as the culmination of a series of steps in a single settlement transaction and recognized a net gain of ¥3,317 million (\$30,887 thousand) through these transactions for the year ended March 31, 2005, which is included in selling, general and administrative expenses and consists of ¥6,116 million (\$56,951 thousand) of a subsidy from the government, calculated as the difference between the obligation settled and the plan assets transferred to the government, and ¥2,799 million (\$26,064 thousand) of a settlement loss on recognition of related unrecognized actuarial loss.

Effective April 1, 2005, the Company and its domestic subsidiaries amended their severance indemnity plan by introducing a point-based benefits system, under which benefits are calculated based on accumulated points allocated to employees each year according to their job classification and their performance.

Effective April 1, 2005, the Company and its domestic subsidiaries amended their defined benefit pension plans, and a cash balance pension plan was established. Under a cash balance pension plan, the benefits are calculated based on accumulated points allocated to employees each year according to their job classification and their performance with a certain interest rate calculated based on the upper and lower limit of a market interest rate. These amendments resulted in a decrease in the Company s projected benefit obligation.

In December 2003, the FASB issued SFAS No. 132 (revised 2003) ( SFAS No. 132R ), Employers Disclosures about Pensions and Other Postretirement Benefits . SFAS No. 132R revises and prescribes employers disclosures about pension plans and other postretirement benefit plans; it does not change the measurement or recognition of those plans. SFAS No. 132R retains the disclosure requirements contained in the original SFAS No. 132. It also requires additional disclosures about the assets, obligations, cash flows, and net periodic benefit cost of defined benefit pension plans and other postretirement benefit plans.



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Information about the retirement and severance plans of Advantest are as follows:

|  | <u>2003</u>    | <u>2004</u>  | <u>2005</u>  | <u>2005</u>      |
|--|----------------|--------------|--------------|------------------|
|  | Yen            |              |              | U.S. Dollars     |
|  | (Millions)     |              |              | (Thousands)      |
| Components of net periodic benefit cost: |                |              |              |                  |
| Service cost                             | ¥ 2,529        | 1,691        | 1,710        | \$ 15,923        |
| Interest cost                            | 960            | 860          | 853          | 7,943            |
| Expected return on plan assets           | (622)          | (495)        | (583)        | (5,429)          |
| Amortization of unrecognized:            |                |              |              |                  |
| Net transition obligation                | 214            | 214          |              |                  |
| Net actuarial (gain) or loss             | 318            | 317          | 547          | 5,094            |
| Prior service cost                       | (117)          | (116)        | (144)        | (1,341)          |
| Settlement loss                          |                |              | 2,799        | 26,064           |
|  | <u>¥ 3,282</u> | <u>2,471</u> | <u>5,182</u> | <u>\$ 48,254</u> |

The following table sets forth the plans' benefit obligation, fair value of plan assets, funded status at March 31, 2004 and 2005.

|  | <u>2004</u>   | <u>2005</u>   | <u>2005</u>    |
|--|---------------|---------------|----------------|
|  | Yen           |               | U.S. Dollars   |
|  | (Millions)    |               | (Thousands)    |
| Change in benefit obligation:          |               |               |                |
| Balance at beginning of year           | ¥ 34,507      | 42,976        | \$ 400,186     |
| Service cost                           | 1,691         | 1,710         | 15,923         |
| Interest cost                          | 860           | 853           | 7,943          |
| Employee contributions                 | 85            |               |                |
| Plan amendment                         |               | (1,912)       | (17,804)       |
| Actuarial (gain) or loss               | 6,644         | (2,169)       | (20,198)       |
| Benefits paid                          | (904)         | (379)         | (3,529)        |
| Transfer of the substitutional portion |               | (12,392)      | (115,392)      |
| Acquisition                            | 93            |               |                |
|  | <u>42,976</u> | <u>28,687</u> | <u>267,129</u> |

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|  |                   |                   |                   |
|--|-------------------|-------------------|-------------------|
| Change in plan assets:   |                   |                   |                   |
| Balance at beginning of year   | 16,492            | 19,441            | 181,032           |
| Employer contributions   | 631               | 2,348             | 21,864            |
| Employee contributions   | 85                |                   |                   |
| Actual return on plan assets   | 2,994             | 667               | 6,210             |
| Benefits paid  | (761)             | (258)             | (2,402)           |
| Transfer of the substitutional portion                                       |                   | (6,276)           | (58,441)          |
|  | <u>          </u> | <u>          </u> | <u>          </u> |
| Balance at end of year   | 19,441            | 15,922            | 148,263           |
|  | <u>          </u> | <u>          </u> | <u>          </u> |
| Funded status  | 23,535            | 12,765            | 118,866           |
| Unrecognized prior service cost  | 1,714             | 3,482             | 32,424            |
| Unrecognized net actuarial gain or (loss)                                    | (9,240)           | (3,642)           | (33,914)          |
|  | <u>          </u> | <u>          </u> | <u>          </u> |
| Net amount recognized  | ¥ 16,009          | 12,605            | \$ 117,376        |
|  | <u>          </u> | <u>          </u> | <u>          </u> |
| Amounts recognized in the balance sheet:                                     |                   |                   |                   |
| Accrued pension and severance cost   | ¥ 18,348          | 12,605            | \$ 117,376        |
| Accumulated other comprehensive income (loss), gross of tax                  | (2,339)           |                   |                   |
|  | <u>          </u> | <u>          </u> | <u>          </u> |
| Net amount recognized  | ¥ 16,009          | 12,605            | \$ 117,376        |
|  | <u>          </u> | <u>          </u> | <u>          </u> |
| Pension plans with accumulated benefit obligations in excess of plan assets: |                   |                   |                   |
| Projected benefit obligation   | ¥ 42,976          | 28,687            | \$ 267,129        |
| Accumulated benefit obligation   | 37,789            | 26,614            | 247,826           |
| Fair value of plan assets  | 19,441            | 15,922            | 148,263           |

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Other information about the retirement and severance plans of Advantest is as follows:

Measurement date:

The measurement date for the pension plans is March 31.

Assumptions:

|  | <u>2004</u> | <u>2005</u> |      |
|--|-------------|-------------|------|
| Weighted-average assumptions used to determine benefit obligations as of March 31:                     |             |             |      |
| Discount rate  | 2.0%        | 2.0%        |      |
| Rate of compensation increase  | 3.3%        | 3.1%        |      |
|  | <u>2003</u> | <u>2004</u> |      |
|  | <u>2005</u> | <u>2005</u> |      |
| Weighted-average assumptions used to determine net periodic benefit cost for the years ended March 31: |             |             |      |
| Discount rate  | 2.5%        | 2.5%        | 2.0% |
| Expected return on plan assets   | 3.0%        | 3.0%        | 3.0% |
| Rate of compensation increase  | 3.3%        | 3.3%        | 3.3% |

Advantest determines the expected return based on the asset portfolio, historical returns and estimated future returns.

Plan assets:

Advantest's domestic benefit plans' weighted-average asset allocation at March 31, 2004 and 2005 by asset category are as follows:

2004      2005

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|   |        |        |
|---|--------|--------|
| Equity securities                       | 42.7%  | 63.8%  |
| Debt securities                         | 18.3   | 27.2   |
| Cash                                    | 32.2   | 2.2    |
| Life insurance company general accounts | 6.8    | 6.8    |
|   | 100.0% | 100.0% |

Advantest converted certain of its securities into cash in acknowledgement of the pending separation of the remaining substitutional portion (that is, the benefit obligation related to past services) by the year ended March 31, 2004.

Advantest's investment policies are designed to ensure adequate plan assets are available to provide future payments of pension benefits to eligible participants by attaining necessary long-term total returns on plan assets. Taking into consideration the expected returns, associated risks and correlations of returns between asset categories in plan assets, Advantest determines an optimal combination of equity and debt securities as Policy Asset Allocation ( PAA ). Plan assets are invested in individual equity and debt securities according to PAA with mid-term to long-term viewpoint, which is revised periodically to the extent considered necessary to achieve the expected long-term rate of return on plan assets.

Cash flows:

Advantest expects to contribute ¥2,125 million (\$19,788 thousand) to its domestic defined benefit plans during the year ending March 31, 2006.

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Estimated future benefit payments:

The following benefit payments, which reflect expected future service, as appropriate, are expected:

| <u>Year ending March 31</u> | <u>Yen</u><br><u>(Millions)</u> | <u>U.S. Dollars</u><br><u>(Thousands)</u> |
|-----------------------------|---------------------------------|---|
| 2006                        | ¥ 323                           | \$ 3,008                                  |
| 2007                        | 381                             | 3,548                                     |
| 2008                        | 477                             | 4,442                                     |
| 2009                        | 607                             | 5,652                                     |
| 2010                        | 690                             | 6,425                                     |
| 2011 - 2015                 | 4,308                           | 40,115                                    |

**(18) Stockholders Equity**

Changes in the number of shares issued and treasury stock during the years ended March 31, 2003, 2004 and 2005 are as follows:

|                                       | <u>Total shares of</u><br><u>common stock</u> | <u>Shares of</u><br><u>treasury stock</u> |
|---------------------------------------|---|---|
| Number of shares as of April 1, 2002  | 99,783,385                                    | 325,654                                   |
| Purchase of shares                    |   | 1,211,372                                 |
| Number of shares as of March 31, 2003 | 99,783,385                                    | 1,537,026                                 |
| Purchase of shares                    |   | 4,141                                     |
| Exercise of stock options             |   | (21,000)                                  |
| Decrease upon share exchange          |   | (12,283)                                  |
| Sale of shares                        |   | (139)                                     |
| Number of shares as of March 31, 2004 | 99,783,385                                    | 1,507,745                                 |
| Purchase of shares                    |   | 6,004,290                                 |
| Exercise of stock options             |   | (152,000)                                 |

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|                                       |            |           |
|---------------------------------------|------------|-----------|
| Sale of shares                        |            | (265)     |
|                                       |            |           |
| Number of shares as of March 31, 2005 | 99,783,385 | 7,359,770 |

The Commercial Code of Japan provides that an amount equal to at least 10% of appropriations paid in cash be appropriated as a legal reserve until an aggregated amount of additional paid-in capital and the legal reserve equals 25% of common stock. Certain foreign subsidiaries are also required to appropriate their earnings to legal reserves under the laws of the respective countries.

Cash dividends for the years ended March 31, 2003, 2004 and 2005 represent dividends paid out during those years. The accompanying consolidated financial statements do not include any provision for the dividend for the second half-year of ¥25 (\$0.23) per share, aggregating ¥2,311 million (\$21,520 thousand), subsequently proposed by the Board of Directors in respect of the year ended March 31, 2005.

The amount available for dividends is determined under the Commercial Code of Japan is amounted to ¥89,360 million (\$832,107 thousand) at March 31, 2005.

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**(19) Accrued Warranty Expenses**

Advantest issues contractual product warranties under which it generally guarantees the performance of products delivered and services rendered for a certain period or term. Changes in accrued warranty expenses for the years ended March 31, 2004 and 2005 were summarized as follows:

|                              | <u>2004</u>    | <u>2005</u>  | <u>2005</u>      |
|------------------------------|----------------|--------------|------------------|
|                              | Yen            |              | U.S. Dollars     |
|                              | (Millions)     |              | (Thousands)      |
| Balance at beginning of year | ¥ 2,396        | 3,121        | \$ 29,062        |
| Addition                     | 4,571          | 6,087        | 56,681           |
| Acquisition                  | 16             |              |                  |
| Utilization                  | (3,695)        | (5,174)      | (48,180)         |
| Translation adjustments      | (167)          | 56           | 522              |
|                              | <u>¥ 3,121</u> | <u>4,090</u> | <u>\$ 38,085</u> |

**(20) Operating Segment and Geographic Information**

The Company and subsidiaries (collectively Advantest ) manufacture and sell semiconductor and component test system product group and mechatronics-related product group such as test handlers and device interfaces. Advantest also engages in research and development activities and provides maintenance and support services associated with these products. In accordance with SFAS No. 131, Disclosure about Segments of an Enterprise and Related Information , Advantest has three operating and reportable segments, which are the design, manufacturing, and sale of semiconductor and component test system, mechatronics system and services, support and others. These operating segments are determined based on the nature of the products and the markets.

The semiconductor and component test system business provides customers with test system products for the semiconductor industry and the electronic parts industry. Product lines provided by the semiconductor and component test system segment include test systems for memory semiconductors for memory semiconductor devices and test systems for SoC semiconductors for non memory semiconductor devices. The mechatronics system business provides product lines such as test handlers, mechatronic-applied products, for handling semiconductor devices and device interfaces that serve as interfaces with the devices that are measured and operations related to nano-technology products. The services, support and others business consists of comprehensive customer solutions provided in connection with the above businesses, support services, equipment lease business and others. Fundamental research and development activities and headquarters functions are represented by Corporate.

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As of April 1, 2004, Advantest reclassified and regrouped its two reportable segments of automated test equipment and measuring instruments into the following three new segments; semiconductor and component test system , mechatronics system and services, support and others . Accordingly, the segment information for the years ended March 31, 2003 and 2004 have been restated based on the three new business segments.

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Operating segment information during the years ended March 31, 2003, 2004 and 2005 are as follows:

|   | Semiconductor<br>and Component | Mechatronics       | Services,<br>Support<br>and Others | Elimination<br>and<br>Corporate | Total    |
|---|--------------------------------|--------------------|------------------------------------|---------------------------------|----------|
|   | Test System<br>Business        | System<br>Business |                                    |                                 |          |
|   | _____                          | _____              | _____                              | _____                           | _____    |
|   | Yen (Millions)                 |                    |                                    |                                 |          |
| <b>As of and for the year ended March 31, 2003:</b> |                                |                    |                                    |                                 |          |
| Net sales to unaffiliated customers                 | 59,191                         | 19,341             | 19,208                             |                                 | 97,740   |
| Inter-segment                                       | 5,177                          | 124                | 19                                 | (5,320)                         |          |
|   | _____                          | _____              | _____                              | _____                           | _____    |
| Sales   | 64,368                         | 19,465             | 19,227                             | (5,320)                         | 97,740   |
| Depreciation and amortization                       | 4,474                          | 1,503              | 4,057                              | 908                             | 10,942   |
| Operating income (loss)                             | (5,790)                        | (837)              | (3,199)                            | (6,917)                         | (16,743) |
| Expenditures for additions to long-lived assets     | 1,747                          | 544                | 4,732                              | 541                             | 7,564    |
| Equity in losses of affiliates                      | (109)                          |                    |                                    |                                 | (109)    |
| Total assets  | 76,223                         | 20,924             | 26,090                             | 157,987                         | 281,224  |
| Equity investments                                  | 591                            |                    |                                    |                                 | 591      |
| <b>As of and for the year ended March 31, 2004:</b> |                                |                    |                                    |                                 |          |
| Net sales to unaffiliated customers                 | 119,765                        | 33,988             | 20,465                             |                                 | 174,218  |
| Inter-segment                                       | 3,724                          | 237                |                                    | (3,961)                         |          |
|   | _____                          | _____              | _____                              | _____                           | _____    |
| Sales   | 123,489                        | 34,225             | 20,465                             | (3,961)                         | 174,218  |
| Depreciation and amortization                       | 3,676                          | 1,144              | 3,627                              | 881                             | 9,328    |
| Operating income (loss)                             | 28,690                         | 11,233             | (2,587)                            | (6,376)                         | 30,960   |
| Expenditures for additions to long-lived assets     | 1,457                          | 913                | 3,161                              | 90                              | 5,621    |
| Equity in losses of affiliates                      | (117)                          |                    |                                    |                                 | (117)    |
| Total assets  | 118,838                        | 29,191             | 17,472                             | 165,307                         | 330,808  |
| <b>As of and for the year ended March 31, 2005:</b> |                                |                    |                                    |                                 |          |
| Net sales to unaffiliated customers                 | 173,938                        | 45,821             | 19,680                             |                                 | 239,439  |
| Inter-segment                                       | 6,747                          | 574                |                                    | (7,321)                         |          |
|   | _____                          | _____              | _____                              | _____                           | _____    |
| Sales   | 180,685                        | 46,395             | 19,680                             | (7,321)                         | 239,439  |
| Depreciation and amortization                       | 3,225                          | 1,220              | 3,361                              | 479                             | 8,285    |
| Operating income (loss)                             | 50,624                         | 13,662             | 3,402                              | (7,996)                         | 59,692   |
| Expenditures for additions to long-lived assets     | 2,431                          | 654                | 5,709                              | 554                             | 9,348    |
| Total assets  | 86,104                         | 22,587             | 16,197                             | 171,881                         | 296,769  |

Mechatronics    Services,    Total



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**ADVANTEST CORPORATION**

**AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements (Continued)**

Adjustments to operating income (loss) in Corporate principally represent corporate general and administrative expenses and research and development expenses related to fundamental research activities that are not allocated to operating segments.

The operating income in the business segment information for the year ended March 31, 2005 do not match the consolidated statements of operations as the business segment information does not include a net gain on settlement of substitutional portions of EPF of ¥3,317 million (\$30,887 thousand) and the stock option cost of ¥2,290 million (\$21,324 thousand). Profit and loss from these are not included in management's analysis of results.

As discussed in Note 1 (k) to the consolidated financial statements, an impairment charge of ¥3,030 million for long-lived assets was included in the operating income (loss) of semiconductor and component test system and services, support and others for the year ended March 31, 2004.

Additions to long-lived assets included in Corporate consist of purchases of software and fixed assets for general corporate use.

Total assets included in Corporate consist of cash and cash equivalents, assets for general corporate use and assets used for fundamental research activities, which are not allocated to reportable segments.

One customer and its related entities mainly in the semiconductor and component test system segment and the mechatronics system segment accounted for approximately 12%, 12% and 10% of total consolidated net sales for the years ended March 31, 2003, 2004 and 2005. Another customer accounted for approximately 15% for the years ended March 31, 2005.

Information as to Advantest's net sales and long-lived assets in various geographical areas is as follows:

Net sales to unaffiliated customers for the years ended March 31, 2003, 2004 and 2005 are as follows:

| <u>2003</u> | <u>2004</u>    | <u>2005</u> | <u>2005</u>  |
|-------------|----------------|-------------|--------------|
|             | Yen (Millions) |             | U.S. Dollars |

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|              | (Thousands)       |                   |                   |                     |
|--------------|-------------------|-------------------|-------------------|---------------------|
| Japan        | ¥ 38,873          | 57,990            | 60,025            | \$ 558,944          |
| Americas     | 8,666             | 16,264            | 23,024            | 214,396             |
| Europe       | 8,940             | 10,401            | 12,270            | 114,256             |
| Asia         | 41,261            | 89,563            | 144,120           | 1,342,025           |
|              | <u>          </u> | <u>          </u> | <u>          </u> | <u>          </u>   |
| <b>Total</b> | <b>¥ 97,740</b>   | <b>174,218</b>    | <b>239,439</b>    | <b>\$ 2,229,621</b> |
|              | <u>          </u> | <u>          </u> | <u>          </u> | <u>          </u>   |

Net sales to unaffiliated customers are based on the customer's location. Net sales indicated as Asia are generated in Korea, Taiwan, Singapore and others in the amount of ¥13,321 million, ¥13,605 million and ¥14,335 million for the year ended March 31, 2003, and ¥28,613 million, ¥31,819 million and ¥29,131 million for the year ended March 31, 2004, and ¥39,767 million (\$370,304 thousand), ¥51,774 million (\$482,112 thousand) and ¥52,579 million (\$489,609 thousand) for the year ended March 31, 2005, respectively. Substantially all net sales indicated as Americas are generated in the United States of America.

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**ADVANTEST CORPORATION  
AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements (Continued)**

Long-lived assets as of March 31, 2003, 2004 and 2005 are as follows:

|              | <u>2003</u>     | <u>2004</u>   | <u>2005</u>   | <u>2005</u>       |
|--------------|-----------------|---------------|---------------|-------------------|
|              |                 | Yen           |               | U.S. Dollars      |
|              |                 | (Millions)    |               | (Thousands)       |
| Japan        | ¥ 52,961        | 48,226        | 50,096        | \$ 466,487        |
| Americas     | 2,019           | 1,552         | 1,153         | 10,737            |
| Europe       | 1,137           | 707           | 427           | 3,976             |
| Asia         | 4,605           | 3,787         | 2,778         | 25,868            |
| <b>Total</b> | <b>¥ 60,722</b> | <b>54,272</b> | <b>54,454</b> | <b>\$ 507,068</b> |

Long-lived assets are those assets located in each geographic area.

There is no individually material country with respect to long-lived assets outside Japan. Substantially all long-lived assets indicated as Americas are located in the United States of America.

**(21) Related Party Transactions**

Advantest sells products and purchases raw materials from Fujitsu Limited, its 10.9% owner as March 31, 2005 and its group companies (collectively Fujitsu). The terms of sales are the same as those with third parties. Advantest purchases raw materials after receiving competitive bids from several suppliers. Advantest also purchases various pieces of software for internal use, information system related services, research and development materials and services from Fujitsu. Advantest had the following transactions with Fujitsu as of and for the years ended March 31:

|  | <u>2003</u> | <u>2004</u> | <u>2005</u> | <u>2005</u>  |
|--|-------------|-------------|-------------|--------------|
|  |             | Yen         |             | U.S. Dollars |
|  |             | (Millions)  |             | (Thousands)  |

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|   |         |        |       |           |
|---|---------|--------|-------|-----------|
| Sales of products   | ¥ 2,327 | 2,766  | 2,933 | \$ 27,312 |
| Purchases of raw materials  | 2,893   | 10,028 | 9,500 | 88,463    |
| Receivables   | 1,381   | 1,882  | 1,552 | 14,452    |
| Payables  | 2,198   | 6,746  | 4,648 | 43,281    |
| Purchases of software, hardware and others  | 417     | 262    | 235   | 2,188     |
| Research and development expenses, computer rentals, maintenance and other expenses | 1,779   | 2,048  | 1,786 | 16,631    |

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**ADVANTEST CORPORATION  
AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements (Continued)**

**(22) Per Share Data**

The following table sets forth the computation of basic and diluted net income (loss) per share and cash dividends per share as of March 31:

|   | <u>2003</u> | <u>2004</u>               | <u>2005</u> | <u>2005</u>           |
|---|-------------|---------------------------|-------------|-----------------------|
|   |             | <b>Yen</b>                |             |                       |
|   |             | <b>(Millions) except</b>  |             | <b>U.S. Dollars</b>   |
|   |             | <b>for per share data</b> |             | <b>(Thousands)</b>    |
|   |             |                           |             | <b>except for per</b> |
|   |             |                           |             | <b>share data</b>     |
| <b>Numerator:</b>   |             |                           |             |                       |
| Net income (loss)   | ¥ (12,994)  | 17,329                    | 38,078      | \$ 354,577            |
| <b>Denominator:</b>   |             |                           |             |                       |
| Basic weighted average shares of common stock outstanding   | 98,445,111  | 98,250,830                | 97,750,345  |                       |
| Dilutive effect of exercise of stock options and warrants   |             | 195,306                   | 260,394     |                       |
| Diluted weighted average shares of common stock outstanding | 98,445,111  | 98,446,136                | 98,010,739  |                       |
| Basic net income (loss) per share                           | ¥ (131.99)  | 176.37                    | 389.54      | \$ 3.63               |
| Diluted net income (loss) per share                         | (131.99)    | 176.02                    | 388.51      | 3.62                  |
| Cash dividends per share                                    | ¥ 30.00     | 40.00                     | 50.00       | \$ 0.47               |

Cash dividends per share are computed based on dividends declared with respect to earnings for the periods.

**(23) Commitments and Contingent Liabilities**

In November 2002, the FASB issued FIN 45, Guarantors Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others, an interpretation of SFAS No. 5, 57, and 107 and rescission of FASB Interpretation No. 34. FIN 45 requires that a liability be recorded in the guarantor's balance sheet upon issuance of a guarantee. The initial recognition and measurement provisions of FIN 45 were applicable to guarantees issued or modified after December 31, 2002.

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Advantest provides guarantees to third parties mainly for customers lease obligations. Advantest would be required to satisfy customers lease obligations in the event of default. The maximum amount of undiscounted payments is ¥569 million and ¥387 million (\$3,604 thousand) at March 31, 2004 and 2005, respectively. The guarantees are collateralized by the leased equipment. At March 31, 2005, Advantest has not accrued any obligation with respect to such guarantees as it estimates the fair value of its obligations to be insignificant.

Advantest is involved in various claims and legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on Advantest's consolidated financial position, results of operations, or cash flows.

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**ADVANTEST CORPORATION**

**AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements (Continued)**

**(24) Subsequent Events**

In July 2005, stock options were issued under a stock option plan approved by the meeting of Board of Directors and the 63rd annual general meeting of shareholders that were held in June 28, 2005. The details of issued stock options are as follows:

|  |   |
|--|---|
| 1. Date of Issuance  | July 4, 2005  |
| 2. Number of stock acquisition right issued  | 7,590   |
| 3. Class and total number of shares underlying the stock acquisition rights          | 759,000 shares of common stock of Advantest Corporation (each stock acquisition right shall be exercisable for 100 shares)              |
| 4. Total subscription price to be paid upon exercise of each stock acquisition right | 860,000 Yen per unit (8,600 Yen per share)  |
| 5. Exercise period of the stock acquisition rights                                   | Between April 1, 2006 and March 31, 2010  |
| 6. The number of employees receiving stock acquisition rights                        | Directors, corporate auditors, executive officers and employees of the Company and its domestic and overseas subsidiaries, totaling 208 |

The company has not yet determined the fair value of the stock option granted on July 4, 2005.

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**ITEM 19. EXHIBITS**

**Index to Exhibits**

- 1.1 Amended and Restated Articles of Incorporation of the Registrant (English translation)\*\*\*\*
- 1.2 Regulations of the Board of Directors of the Registrant (English translation)\*\*
- 1.3 Regulations of the Board of Corporate Auditors of the Registrant (English translation)\*\*
- 2.1 Share Handling Regulations of the Registrant (English translation)\*\*\*
- 2.2 Form of Deposit Agreement among the Registrant, JPMorgan Chase Bank (as successor to Morgan Guaranty Trust Company of New York), as depository, and the owners and beneficial owners from time to time of American Depositary Receipts, including the form of American Depositary Receipt\*
- 2.3 Form of ADR (included in Exhibit 2.2)
- 8.1 List of Principal Subsidiaries \*\*\*\*
- 11.1 Code of Ethics of the Registrant applicable to its directors and executive officers, including its principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions\*\*\*
- 12.1 Certifications of the Registrant's Chairman of the Board and Chief Executive Officer and Director and Managing Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act
- 13.1 Certifications of the Registrant's Chairman of the Board and Chief Executive Officer and Director and Managing Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act
- 15.1 Consent of Independent Registered Public Accounting Firm

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\* Incorporated by reference to Advantest's registration statement on Form 20-F filed with the SEC on September 4, 2001 (file no. 1-15236).

\*\* Incorporated by reference to Advantest's annual report on Form 20-F filed with the SEC on June 30, 2003 (file no. 1-15236).

\*\*\* Incorporated by reference to Advantest's annual report on Form 20-F filed with the SEC on June 29, 2004 (file no. 1-15236).

\*\*\*\* Incorporated by reference to Advantest's annual report on Form 20-F filed with the SEC on July 26, 2005 (File No. 1-15236).

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**SIGNATURES**

The registrant hereby certifies that it meets all of the requirements for filing on Form 20-F/A Amendment No. 1 and that it has duly caused and authorized the undersigned to sign this annual report on its behalf.

ADVANTEST CORPORATION

By: /s/ HITOSHI OWADA  
Name: **Hitoshi Owada**  
Title: **Director and Managing Executive Officer**

Date: September 29, 2005