

(English Translation of Consolidated Financial Statements and Report Originally Issued in Chinese)

**PEGATRON CORPORATION  
AND ITS SUBSIDIARIES**

**CONSOLIDATED FINANCIAL STATEMENTS**

**December 31, 2017 and 2016  
(With Independent Auditors' Report Thereon)**

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The auditors' report and the accompanying consolidated financial statements are the partial English translation of the Chinese version prepared and used in the Republic of China. If there is any conflict between, or any difference in the interpretation of the English and Chinese language auditors' report and consolidated financial statements, the Chinese version shall prevail.

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## **Representation Letter**

The entities that are required to be included in the combined financial statements of Pegatron Corporation as of and for the year ended December 31, 2017 under the Criteria Governing the Preparation of Affiliation Reports, Consolidated Business Reports, and Consolidated Financial Statements of Affiliated Enterprises are the same as those included in the consolidated financial statements prepared in conformity with International Financial Reporting Standards No. 10 by the Financial Supervisory Commission, "Consolidated and Separate Financial Statements." In addition, the information required to be disclosed in the combined financial statements is included in the consolidated financial statements. Consequently, Pegatron Corporation and its Subsidiaries do not prepare a separate set of combined financial statements.

Company name: Pegatron Corporation  
Chairman: Tzu-Hsien Tung  
Date: March 15, 2018

## Independent Auditors' Report

To the Board of Directors of Pegatron Corporation:

### Opinion

We have audited the consolidated financial statements of Pegatron Corporation and its subsidiaries (“the Group”), which comprise the consolidated statement of financial position as of December 31, 2017 and 2016, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the years ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, based on our audits and the reports of other auditors (please refer to Other Matters paragraph), the accompanying financial statements present fairly, in all material respects, the consolidated financial position of the Group as at December 31, 2017 and 2016, and its financial performance and its cash flows for the years then ended in accordance with the Regulations Governing the Preparation of Financial Reports by Securities Issuers and with the International Financial Reporting Standards (“IFRSs”), International Accounting Standards (“IASs”), interpretations as well as related guidance endorsed by the Financial Supervisory Commission of the Republic of China.

### Basis for Opinion

We conducted our audit in accordance with the “Regulations Governing Auditing and Certification of Financial Statements by Certified Public Accountants” and the auditing standards generally accepted in the Republic of China. Our responsibilities under those standards are further described in the Auditor’s Responsibilities for the Audit of the Consolidated Financial Statements section of our report. We are independent of the Group in accordance with the Certified Public Accountants Code of Professional Ethics in the Republic of China (“the Code”), and we have fulfilled our other ethical responsibilities in accordance with the Code. We believe that the audit evidence we have obtained, inclusive of the reports from other auditors, is sufficient and appropriate to provide a basis of our opinion.

### Key Audit Matters

Based on our professional judgment, key audit matters pertain to the most important matters in the audit of consolidated financial statements for the year ended December 31, 2017 of the Group. Those matters have been addressed in our audit opinion on the said consolidated financial statements and during the formation of our audit opinion. However, we do not express an opinion on these matters individually. The key audit matters that, in our professional judgment, should be communicated are as follows:

#### 1. Revenue recognition

The accounting principles on the recognition of revenue and the related sales returns and allowances are discussed in Note 4(q) of the notes to consolidated financial statements.

## (a) Key audit matters:

The timing for the recognition of revenue and the transfer of risk and reward is relatively complex because the transaction terms for each client differ so that warehouses are established overseas according to clients' needs. These factors expose the Group to material risk of untimely recording of revenue.

Therefore, the test of sales and sales returns and allowances recognition was one of the key audit matters in the audit of consolidated financial reports for the years ended December 31, 2017 and 2016 of the Group.

## (b) Auditing procedures performed:

- Review external documents with records on ledger to confirm whether or not the sales transaction really exists, valid and legitimate.
- Randomly select material sales contracts and review the transaction term in order to evaluate the propriety of the timing for the recognition of revenue.
- Conduct cut-off test for sales and sales returns and allowances on the periods before and after balance sheets date.

## 2. Inventory valuation

Please refer to notes 4(h), 5(b) and 6(d) of the notes to consolidated financial statement for the accounting policies on measuring inventory, assumptions used and uncertainties considered in determining net realizable value, allowances for impairment loss and obsolescence and balances of impairment loss and obsolescence, respectively.

## (a) Key audit matters:

Inventories are measured at the lower of cost and net realizable value in the financial statements. However, the cost of inventory might exceed its net realizable value because high-tech products change fast and the industry in which the Group operates is very competitive.

## (b) Auditing procedures performed:

- Analyze the amount of obsolete inventory and inventory market price decline between 2017 and 2016 and understand reasons of the difference. Discuss and resolve those differences with management.
- Obtain an inventory aging analysis and randomly select items to verify the correctness for age of inventory.
- Obtain last selling price for finished goods and replacement cost for raw material, and recalculate net realizable value with selling expense rate to check whether or not the method of inventory measurement adopted by the Group is reasonable.

**Other Matter**

We did not audit the financial statements of certain consolidated subsidiaries with total assets representing 11.08% and 11.72% and net sales representing 2.97% and 3.47% of the related consolidated total as of and for the years ended December 31, 2017 and 2016, respectively. Also, we did not audit the long-term investments in other companies representing 0.03% and 0.03% of consolidated total assets as of December 31, 2017 and 2016, respectively, and the related investment loss thereon representing (0.07)% and (0.24)% of consolidated net income before tax for the years ended December 31, 2017 and 2016, respectively. The financial statements of these subsidiaries and investees accounted for under the equity method were audited by other auditors, whose reports have been furnished to us, and our opinion, insofar as it relates to the amounts for these companies, were based solely on the reports of other auditors.

We have also audited the non-consolidated financial statements of Pegatron Corporation as of and for the years ended December 31, 2017 and 2016 and have issued unqualified audit reports thereon.

### **Responsibilities of Management and Those Charged with Governance for the Consolidated Financial Statements**

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with Regulations Governing the Preparation of Financial Reports by Securities Issuers and with the International Financial Reporting Standards (“IFRSs”), International Accounting Standards (“IASs”), interpretation as well as related guidance endorsed by the Financial Supervisory Commission of the Republic of China, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, management is responsible for assessing the Group’s ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Group’s financial reporting process.

### **Auditor’s Responsibilities for the Audit of the Consolidated Financial Statements**

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor’s report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the auditing standards generally accepted in the Republic of China will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with auditing standards generally accepted in the Republic of China, we exercise professional judgment and maintain professional skepticism throughout the audit. Also, we:

1. Assess for purposes of identifying the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
2. Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group’s internal control.
3. Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
4. Evaluate for purposes of determining the appropriateness of management’s use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group’s ability to continue as a going concern. If we determine that a material uncertainty exists, we are required to draw attention in our auditor’s report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor’s report. However, future events or conditions may cause the Group to cease to continue as a going concern.

5. Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
6. Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

The engagement partners on the audit resulting in this independent auditors' report are Kuo-Yang Tseng and Chi-Lung Yu.

KPMG

Taipei, Taiwan (Republic of China)  
March 15, 2018

#### **Notes to Readers**

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

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(English Translation of Consolidated Financial Statements and Report Originally Issued in Chinese)  
PEGATRON CORPORATION AND ITS SUBSIDIARIES

Consolidated Balance Sheets

December 31, 2017 and 2016

(Expressed in Thousands of New Taiwan Dollars)

		December 31, 2017		December 31, 2016	
		Amount	%	Amount	%
<b>Assets</b>					
<b>Current assets:</b>					
1100	Cash and cash equivalents (Note 6(a))	\$ 107,444,124	22	108,713,312	24
1110	Current financial assets at fair value through profit or loss (Note 6(b))	2,824,913	1	4,367,847	1
1125	Current available-for-sale financial assets (Note 6(b))	384,782	-	266,523	-
1170	Notes and accounts receivable, net (Note 6(c))	149,414,212	31	93,315,940	21
1200	Other receivables, net (Note 6(c))	1,490,873	-	42,590,627	10
130X	Inventories (Note 6(d))	123,874,993	25	107,319,402	24
1476	Other current financial assets (Notes 6(k) and 8)	1,222,740	-	479,510	-
1479	Other current assets (Note 6(k))	<u>8,741,935</u>	<u>2</u>	<u>7,172,425</u>	<u>2</u>
		<u>395,398,572</u>	<u>81</u>	<u>364,225,586</u>	<u>82</u>
<b>Non-current assets:</b>					
1523	Non-current available-for-sale financial assets (Note 6(b))	1,158,831	-	789,622	-
1543	Non-current financial assets carried at cost (Note 6(b))	350,509	-	371,082	-
1550	Investments accounted for using equity method (Note 6(e))	503,718	-	362,909	-
1600	Property, plant and equipment (Notes 6(h) and 8)	78,075,271	16	66,860,809	15
1760	Investment property, net (Note 6(i))	52,870	-	57,221	-
1780	Intangible assets (Note 6(j))	1,497,234	-	1,439,186	-
1840	Deferred tax assets (Note 6(r))	3,345,992	1	2,347,933	1
1915	Prepayments on purchase of equipment	3,717,374	1	3,003,023	1
1980	Other non-current financial assets (Notes 6(k) and 8)	300,700	-	427,655	-
1985	Long-term prepaid rentals (Note 6(p))	3,783,164	1	4,014,064	1
1990	Other non-current assets (Note 6(k))	<u>51,384</u>	<u>-</u>	<u>46,143</u>	<u>-</u>
		<u>92,837,047</u>	<u>19</u>	<u>79,719,647</u>	<u>18</u>
<b>Total assets</b>		<b><u>\$ 488,235,619</u></b>	<b><u>100</u></b>	<b><u>443,945,233</u></b>	<b><u>100</u></b>

See accompanying notes to financial statements.

(English Translation of Consolidated Financial Statements and Report Originally Issued in Chinese)

**PEGATRON CORPORATION AND ITS SUBSIDIARIES****Consolidated Balance Sheets (CONT'D)****December 31, 2017 and 2016****(Expressed in Thousands of New Taiwan Dollars)**

		<b>December 31, 2017</b>		<b>December 31, 2016</b>	
		<b>Amount</b>	<b>%</b>	<b>Amount</b>	<b>%</b>
<b>Liabilities and Equity</b>					
<b>Current liabilities:</b>					
2100	Short-term loans (Note 6(l))	\$ 46,058,620	10	31,148,468	7
2150	Notes and accounts payable (Note 7)	186,896,307	38	171,265,693	39
2209	Accrued expenses (Note 6(q))	27,121,355	6	25,179,749	6
2219	Other payables	11,432,493	2	5,480,741	1
2230	Current tax liabilities	3,132,941	1	4,538,439	1
2250	Current provisions (Note 6(o))	186,802	-	160,064	-
2313	Deferred revenue	902,193	-	1,040,615	-
2322	Long-term loans payable, current portion (Note 6(m))	1,107,312	-	536,257	-
2399	Other current liabilities	14,489,124	3	14,886,797	3
		<u>291,327,147</u>	<u>60</u>	<u>254,236,823</u>	<u>57</u>
<b>Non-Current liabilities:</b>					
2530	Bonds payable (Note 6(n))	6,992,476	2	-	-
2540	Long-term loans (Note 6(m))	6,954,800	1	4,522,890	1
2570	Deferred tax liabilities (Note 6(r))	1,601,481	-	1,803,244	1
2670	Other non-current liabilities (Note 6(q))	1,635,905	-	1,360,075	-
		<u>17,184,662</u>	<u>3</u>	<u>7,686,209</u>	<u>2</u>
	<b>Total liabilities</b>	<u>308,511,809</u>	<u>63</u>	<u>261,923,032</u>	<u>59</u>
<b>Equity Attributable to Owners of the Parent Company (Note 6(s)):</b>					
3100	Share capital	26,140,906	5	25,751,695	6
<b>Capital surplus:</b>					
3210	Capital surplus, premium on capital stock	74,283,165	15	73,312,256	16
3280	Capital surplus, others (Note 6(t))	5,614,586	1	4,902,003	1
		<u>79,897,751</u>	<u>16</u>	<u>78,214,259</u>	<u>17</u>
<b>Retained earnings:</b>					
3310	Legal reserve	9,194,524	2	7,260,543	2
3320	Special reserve	3,368,986	1	-	-
3350	Unappropriated retained earnings	37,412,958	8	40,844,207	9
		<u>49,976,468</u>	<u>11</u>	<u>48,104,750</u>	<u>11</u>
<b>Other equity interest:</b>					
3410	Exchange differences on translation of foreign financial statements	(9,698,374)	(2)	(3,552,939)	(1)
3425	Unrealized gains on available-for-sale financial assets	883,161	-	183,953	-
3491	Deferred compensation cost arising from issuance restricted stock (Note 6(t))	(1,222,232)	-	(429,882)	-
		<u>(10,037,445)</u>	<u>(2)</u>	<u>(3,798,868)</u>	<u>(1)</u>
3500	Treasury stock	(1,942)	-	(2,246)	-
	<b>Equity attributable to the parent company</b>	145,975,738	30	148,269,590	33
36xx	Non-controlling interests	33,748,072	7	33,752,611	8
	<b>Total equity</b>	<u>179,723,810</u>	<u>37</u>	<u>182,022,201</u>	<u>41</u>
	<b>Total liabilities and equity</b>	<u>\$ 488,235,619</u>	<u>100</u>	<u>443,945,233</u>	<u>100</u>

See accompanying notes to financial statements.

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PEGATRON CORPORATION AND ITS SUBSIDIARIES

**Consolidated Statements of Comprehensive Income**

**For the years ended December 31, 2017 and 2016**

**(Expressed in Thousands of New Taiwan Dollars , Except for Earnings Per Common Share)**

		For the years ended December 31			
		2017		2016	
		Amount	%	Amount	%
4110	<b>Operating revenue (Note 6(w))</b>	\$ 1,197,312,896	100	1,163,923,241	101
4170	Less: Sales returns and allowances	<u>3,504,381</u>	-	<u>6,213,128</u>	<u>1</u>
	<b>Operating revenue, net</b>	1,193,808,515	100	1,157,710,113	100
5000	Cost of sales (Notes 6(d), 6(p), 6(q), 6(x), and 7)	<u>1,147,138,626</u>	<u>96</u>	<u>1,094,642,996</u>	<u>95</u>
	<b>Gross profit from operations</b>	<u>46,669,889</u>	<u>4</u>	<u>63,067,117</u>	<u>5</u>
6000	<b>Operating expenses (Notes 6(p), 6(q) and 6(x)):</b>				
6100	Selling expenses	4,920,146	-	5,946,930	-
6200	General and administrative expenses	9,409,135	1	10,620,127	1
6300	Research and development expenses	<u>13,341,912</u>	<u>1</u>	<u>14,086,091</u>	<u>1</u>
	<b>Total operating expenses</b>	<u>27,671,193</u>	<u>2</u>	<u>30,653,148</u>	<u>2</u>
	<b>Results from operating activities</b>	<u>18,998,696</u>	<u>2</u>	<u>32,413,969</u>	<u>3</u>
	<b>Non-operating income and expenses:</b>				
7010	Other income (Note 6(y))	4,173,619	-	3,172,133	-
7020	Other gains and losses (Notes 6(i) and 6(y))	(1,655,179)	-	(5,247,487)	-
7050	Finance costs (Note 6(y))	(1,018,004)	-	(1,005,006)	-
7060	Share of loss of associates and joint ventures accounted for using equity method (Note 6(e))	(4,484)	-	(3,131)	-
7590	Miscellaneous disbursements	<u>(81,598)</u>	<u>-</u>	<u>(250,808)</u>	<u>-</u>
		<u>1,414,354</u>	<u>-</u>	<u>(3,334,299)</u>	<u>-</u>
	<b>Profit from continuing operations before tax</b>	20,413,050	2	29,079,670	3
7950	Less: Tax expense (Note 6(r))	<u>4,398,278</u>	<u>-</u>	<u>6,942,278</u>	<u>1</u>
	<b>Profit for the year</b>	<u>16,014,772</u>	<u>2</u>	<u>22,137,392</u>	<u>2</u>
8300	<b>Other comprehensive income:</b>				
8310	<b>Components of other comprehensive income that will not be reclassified to profit or loss</b>				
8311	Remeasurement effects on net defined benefit liability	1,414	-	4,265	-
8349	Income tax related to components of other comprehensive income that will not be reclassified to profit or loss	<u>(1,088)</u>	<u>-</u>	<u>(1,286)</u>	<u>-</u>
		<u>2,502</u>	<u>-</u>	<u>2,979</u>	<u>-</u>
8360	<b>Other components of other comprehensive income that may be reclassified to profit or loss</b>				
8361	Exchange differences on translation of foreign financial statements	(6,599,633)	(1)	(8,597,708)	(1)
8362	Unrealized gains on valuation of available-for-sale financial assets (Note 6(z))	541,228	-	124,524	-
8370	Share of other comprehensive income of associates and joint ventures accounted for using equity method, components of other comprehensive income that will be reclassified to profit or loss (Note 6(e))	167,389	-	(48,217)	-
8399	Income tax related to components of other comprehensive income that may be reclassified to profit or loss	<u>(10,392)</u>	<u>-</u>	<u>(96,953)</u>	<u>-</u>
8300	<b>Other comprehensive income for the year, net of tax</b>	<u>(5,878,122)</u>	<u>(1)</u>	<u>(8,421,469)</u>	<u>(1)</u>
8500	<b>Total comprehensive income for the year</b>	<u>\$ 10,136,650</u>	<u>1</u>	<u>13,715,923</u>	<u>1</u>
	<b>Profit attributable to:</b>				
8610	Owners of the parent company	\$ 14,682,988	2	19,339,815	2
8620	Non-controlling interests	<u>1,331,784</u>	<u>-</u>	<u>2,797,577</u>	<u>-</u>
		<u>\$ 16,014,772</u>	<u>2</u>	<u>22,137,392</u>	<u>2</u>
	<b>Comprehensive income attributable to:</b>				
8710	Owners of the parent company	\$ 9,241,061	1	12,008,187	1
8720	Non-controlling interests	<u>895,589</u>	<u>-</u>	<u>1,707,736</u>	<u>-</u>
		<u>\$ 10,136,650</u>	<u>1</u>	<u>13,715,923</u>	<u>1</u>
	<b>Earnings per share, net of tax (Note 6(v))</b>				
9750	<b>Basic earnings per share</b>	<u>\$ 5.66</u>		<u>7.50</u>	
9850	<b>Diluted earnings per share</b>	<u>\$ 5.63</u>		<u>7.42</u>	

See accompanying notes to financial statements.

(English Translation of Consolidated Financial Statements and Report Originally Issued in Chinese)  
PEGATRON CORPORATION AND ITS SUBSIDIARIES

Consolidated Statements of Changes in Equity  
For the years ended December 31, 2017 and 2016  
(Expressed in Thousands of New Taiwan Dollars)

	Equity attributable to owners of the parent company												Total equity	
	Share capital	Retained earnings				Total other equity interest								
		Common stock	Capital surplus	Legal reserve	Special reserve	Unappropriated retained earnings	Total retained earnings	Exchange differences on translation of foreign financial statements	Unrealized gains (losses) on available-for-sale financial assets	Deferred compensation cost	Total other equity interest	Treasury stock		Owners of the parent company
<b>Balance at January 1, 2016</b>	\$ 26,030,205	78,972,374	4,879,380	-	37,775,792	42,655,172	3,752,117	211,234	(1,238,377)	2,724,974	(2,590)	150,380,135	41,958,390	192,338,525
Profit for the year	-	-	-	-	19,339,815	19,339,815	-	-	-	-	-	19,339,815	2,797,577	22,137,392
Other comprehensive income for the year	-	-	-	-	709	709	(7,305,056)	(27,281)	-	(7,332,337)	-	(7,331,628)	(1,089,841)	(8,421,469)
Total comprehensive income for the year	-	-	-	-	19,340,524	19,340,524	(7,305,056)	(27,281)	-	(7,332,337)	-	12,008,187	1,707,736	13,715,923
Appropriation and distribution of retained earnings:														
Legal reserve appropriated	-	-	2,381,163	-	(2,381,163)	-	-	-	-	-	-	-	-	-
Cash dividends of ordinary share	-	-	-	-	(12,953,501)	(12,953,501)	-	-	-	-	-	(12,953,501)	-	(12,953,501)
Purchase of treasury stock	-	-	-	-	-	-	-	-	-	-	(2,068,328)	(2,068,328)	-	(2,068,328)
Retirement of treasury stock	(264,100)	(830,477)	-	-	(973,751)	(973,751)	-	-	-	-	2,068,328	-	-	-
Changes in ownership interests in subsidiaries	-	2,575	-	-	-	-	-	-	-	-	-	2,575	(2,575)	-
Expiration of restricted shares of stock issued to employees	(14,410)	14,066	-	-	-	-	-	-	-	-	344	-	-	-
Compensation cost arising from restricted shares of stock	-	55,721	-	-	36,306	36,306	-	-	808,495	808,495	-	900,522	-	900,522
Changes in non-controlling interests	-	-	-	-	-	-	-	-	-	-	-	-	(9,910,940)	(9,910,940)
Balance at December 31, 2016	25,751,695	78,214,259	7,260,543	-	40,844,207	48,104,750	(3,552,939)	183,953	(429,882)	(3,798,868)	(2,246)	148,269,590	33,752,611	182,022,201
Profit for the year	-	-	-	-	14,682,988	14,682,988	-	-	-	-	-	14,682,988	1,331,784	16,014,772
Other comprehensive income for the year	-	-	-	-	4,300	4,300	(6,145,435)	699,208	-	(5,446,227)	-	(5,441,927)	(436,195)	(5,878,122)
Total comprehensive income for the year	-	-	-	-	14,687,288	14,687,288	(6,145,435)	699,208	-	(5,446,227)	-	9,241,061	895,589	10,136,650
Appropriation and distribution of retained earnings:														
Legal reserve appropriated	-	-	1,933,981	-	(1,933,981)	-	-	-	-	-	-	-	-	-
Special reserve appropriated	-	-	-	3,368,986	(3,368,986)	-	-	-	-	-	-	-	-	-
Cash dividends of ordinary share	-	-	-	-	(12,873,916)	(12,873,916)	-	-	-	-	-	(12,873,916)	-	(12,873,916)
Changes in ownership interests in subsidiaries	-	(165,279)	-	-	-	-	-	-	-	-	-	(165,279)	165,279	-
Share-based payment transactions	400,000	-	-	-	-	-	-	-	-	-	-	400,000	-	400,000
Expiration of restricted shares of stock issued to employees	(10,789)	10,485	-	-	-	-	-	-	-	-	304	-	-	-
Compensation cost arising from restricted shares of stock	-	1,838,286	-	-	58,346	58,346	-	-	(792,350)	(792,350)	-	1,104,282	-	1,104,282
Changes in non-controlling interests	-	-	-	-	-	-	-	-	-	-	-	-	(1,065,407)	(1,065,407)
<b>Balance at December 31, 2017</b>	\$ 26,140,906	79,897,751	9,194,524	3,368,986	37,412,958	49,976,468	(9,698,374)	883,161	(1,222,232)	(10,037,445)	(1,942)	145,975,738	33,748,072	179,723,810

See accompanying notes to financial statements.

(English Translation of Consolidated Financial Statements and Report Originally Issued in Chinese)  
PEGATRON CORPORATION AND ITS SUBSIDIARIES

**Consolidated Statements of Cash Flows**

**For the years ended December 31, 2017 and 2016**

**(Expressed in Thousands of New Taiwan Dollars)**

	For the years ended December 31	
	2017	2016
<b>Cash flows from operating activities:</b>		
<b>Profit before tax</b>	\$ 20,413,050	29,079,670
<b>Adjustments:</b>		
<b>Adjustments to reconcile profit:</b>		
Depreciation expense	12,875,356	12,770,863
Amortization expense	233,799	141,548
Reversal of allowance for uncollectable accounts	(162,127)	(36,760)
Net gain on financial assets or liabilities at fair value through profit or loss	(146,321)	(67,790)
Interest expense	951,706	912,165
Interest income	(1,499,714)	(1,057,275)
Dividends income	(37,902)	(20,659)
Compensation cost arising from employee stock options	1,386,317	907,285
Amortization of issuance costs on bonds payable	476	-
Share of loss of associates and joint ventures accounted for using equity method	4,484	3,131
Effect of exchange rate changes of long-term loans	(85,597)	(36,176)
Loss on disposal of property, plant and equipment	53,364	240,489
Property, plant and equipment charged to expenses	65,166	49,768
(Gain) loss on disposal of investments	(38,091)	574,526
(Reversal of ) impairment loss	(34,474)	59,968
Long-term prepaid rent charged to expenses	184,111	95,295
(Reversal of ) provisions	49,426	(11,650)
Other loss	470,924	217,855
<b>Total adjustments to reconcile profit</b>	<u>14,270,903</u>	<u>14,742,583</u>
<b>Changes in operating assets and liabilities:</b>		
<b>Changes in operating assets:</b>		
Decrease in financial assets at fair value through profit or loss	1,689,255	424,768
(Increase) decrease in notes and accounts receivable	(55,937,542)	24,197,509
Decrease (increase) in other receivables	40,684,759	(14,022,934)
(Increase) decrease in inventories	(16,555,591)	9,509,597
(Increase) decrease in other financial assets	(743,230)	150,037
(Increase) decrease in other current assets	(1,699,082)	8,128,167
(Increase) decrease in other non-current assets	(1,855)	21,285
<b>Total changes in operating assets</b>	<u>(32,563,286)</u>	<u>28,408,429</u>
<b>Changes in operating liabilities:</b>		
Increase in notes and accounts payable	15,636,278	12,076,464
Increase (decrease) in accrued expenses	1,628,745	(1,648,644)
Increase (decrease) in other payables	5,854,604	(1,403,876)
Decrease in provisions	(22,688)	(24,416)
Decrease in deferred revenue	(158,685)	(69,141)
(Decrease) increase in other current liabilities	(397,673)	670,573
Increase in other non-current liabilities	298,595	22,830
<b>Total changes in operating liabilities</b>	<u>22,839,176</u>	<u>9,623,790</u>
<b>Net changes in operating assets and liabilities</b>	<u>(9,724,110)</u>	<u>38,032,219</u>
<b>Net adjustments</b>	<u>4,546,793</u>	<u>52,774,802</u>
Cash provided by operating activities	24,959,843	81,854,472
Interest received	1,436,231	1,069,904
Dividends received	37,902	70,384
Interest paid	(864,790)	(919,565)
Income taxes paid	(6,745,339)	(10,244,344)
<b>Net cash flows from operating activities</b>	<u>18,823,847</u>	<u>71,830,851</u>

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PEGATRON CORPORATION AND ITS SUBSIDIARIES

**Consolidated Statements of Cash Flows (CONT'D)**

**For the years ended December 31, 2017 and 2016**

**(Expressed in Thousands of New Taiwan Dollars)**

	<b>For the years ended December 31</b>	
	<b>2017</b>	<b>2016</b>
<b>Cash flows from investing activities:</b>		
Proceeds from disposal of available-for-sale financial assets	\$ 69,167	-
Proceeds from disposal of financial assets carried at cost	-	653
Net cash outflow from disposal of subsidiaries	-	(3,674,323)
Acquisition of property, plant and equipment	(20,357,276)	(12,453,467)
Proceeds from disposal of property, plant and equipment	680,928	529,241
Decrease in refundable deposits	126,955	-
Acquisition of intangible assets	(366,923)	(224,591)
Increase in other financial assets	-	(110,298)
Increase in prepayments on purchase of equipment	(7,140,517)	(4,317,635)
Increase in long-term prepaid rentals	(176,920)	(180,965)
<b>Net cash flows used in investing activities</b>	<b>(27,164,586)</b>	<b>(20,431,385)</b>
<b>Cash flows from financing activities:</b>		
Increase (decrease) in short-term loans	14,910,152	(13,919,128)
Proceeds from issuing bonds	6,992,000	-
Proceeds from long-term loans	6,375,600	14,200,000
Repayments of long-term loans	(3,287,038)	(24,020,366)
Cash dividends paid	(14,431,721)	(15,172,473)
Purchase of treasury stock	-	(2,068,328)
Issuance of restricted stock	493,590	-
Redemption of restricted stock	(10,485)	(15,057)
Change in non-controlling interests	223,533	125,000
<b>Net cash flows from (used in) financing activities</b>	<b>11,265,631</b>	<b>(40,870,352)</b>
<b>Effect of exchange rate fluctuations on cash held</b>	<b>(4,194,080)</b>	<b>(4,377,148)</b>
<b>Net (decrease) increase in cash and cash equivalents</b>	<b>(1,269,188)</b>	<b>6,151,966</b>
<b>Cash and cash equivalents, beginning of the year</b>	<b>108,713,312</b>	<b>102,561,346</b>
<b>Cash and cash equivalents, end of the year</b>	<b>\$ 107,444,124</b>	<b>108,713,312</b>

See accompanying notes to financial statements.

(English Translation of Consolidated Financial Statements and Report Originally Issued in Chinese)  
**PEGATRON CORPORATION AND ITS SUBSIDIARIES**

**Notes to the Consolidated Financial Statements**

**For the years ended December 31, 2017 and 2016**

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

**(1) Company history**

PEGATRON CORPORATION (the “Company”) was established on June 27, 2007. The Company’s registered office address is located at 5F., No.76, Ligong St., Beitou District, Taipei City 112, Taiwan. In order to enhance competitiveness and boost productivity, the Company resolved to absorb the OEM business from ASUSTek Computer Inc. on January 1, 2008 as part of the Company’s business restructuring. On April 1, 2008, ASUSALPHA Computer Inc. was merged with the Company. The main activities of the Company are to produce, design and sell OEM business. In January 2010, pursuant to the resolutions of the respective board of directors, the Company merged with Pegatron International Investment Co., Ltd., effective June 10, 2010. As the surviving entity from this merger, the Company applied for initial public offering (IPO) to TSEC. The Company’s shares were listed on TSEC on June 24, 2010.

In accordance with Article 19 of the Business Mergers and Acquisitions Act, the Company merged with its subsidiary, UNIHAN CORPORATION, pursuant to the resolutions of the board of directors in November, 2013.

The consolidated financial statements of the Company as of and for the years ended December 31, 2017 comprise the Company and its subsidiaries (together referred to as the “Group” and individually as “Group entities”) and the Group’s interest in associates entities.

**(2) Approval date and procedures of the consolidated financial statements:**

The accompanying consolidated financial statements were authorized for issue by the Board of Directors on March 15, 2018.

**(3) Application of new standards, amendments and interpretations:**

- (a) Impact of adopting the International Financial Reporting Standards (“IFRSs”) endorsed by the Financial Supervisory Commission, R.O.C. (“FSC”).

The Group has prepared its consolidated financial statements in conformity with the new standards, interpretations and amendments of IFRSs which have been endorsed by the FSC and are effective for annual periods beginning on or after January 1, 2017 as follows:

<b>New, Revised or Amended Standards and Interpretations</b>	<b>Effective date per IASB</b>
Amendments to IFRS 10, IFRS 12 and IAS 28 "Investment Entities: Applying the Consolidation Exception"	January 1, 2016
Amendments to IFRS 11 "Accounting for Acquisitions of Interests in Joint Operations"	January 1, 2016
IFRS 14 "Regulatory Deferral Accounts"	January 1, 2016
Amendment to IAS 1 " Presentation of Financial Statements-Disclosure Initiative	January 1, 2016

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

<u>New, Revised or Amended Standards and Interpretations</u>	<u>Effective date per IASB</u>
Amendments to IAS 16 and IAS 38 "Clarification of Acceptable Methods of Depreciation and Amortization"	January 1, 2016
Amendments to IAS 16 and IAS 41 "Agriculture: Bearer Plants"	January 1, 2016
Amendments to IAS 19 "Defined Benefit Plans: Employee Contributions"	July 1, 2014
Amendment to IAS 27 "Equity Method in Separate Financial Statements"	January 1, 2016
Amendments to IAS 36 " Impairment of Non-Financial assets- Recoverable Amount Disclosures for Non Financial Assets"	January 1, 2014
Amendments to IAS 39 " Financial Instruments-Novation of Derivatives and Continuation of Hedge Accounting"	January 1, 2014
Annual Improvements to IFRSs 2010-2012 Cycle and 2011-2013 Cycle	July 1, 2014
Annual Improvements to IFRSs 2012-2014 Cycle	January 1, 2016
IFRIC 21 "Levies"	January 1, 2014

The Group assessed that the initial application of the above IFRSs would not have any material impact on the consolidated financial statements.

(b) Impact of IFRS endorsed by FSC but not yet effective

The following new standards, interpretations and amendments have been endorsed by the FSC and are effective for annual periods beginning on or after January 1, 2018 in accordance with Ruling No. 1060025773 issued by the FSC on July 14, 2017.

<u>New, Revised or Amended Standards and Interpretations</u>	<u>Effective date per IASB</u>
Amendment to IFRS 2 "Clarifications of Classification and Measurement of Share-based Payment Transactions"	January 1, 2018
Amendments to IFRS 4 "Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts"	January 1, 2018
IFRS 9 "Financial Instruments"	January 1, 2018
IFRS 15 "Revenue from Contracts with Customers"	January 1, 2018
Amendment to IAS 7 "Statement of Cash Flows -Disclosure Initiative"	January 1, 2017
Amendment to IAS 12 "Income Taxes- Recognition of Deferred Tax Assets for Unrealized Losses"	January 1, 2017
Amendments to IAS 40 "Transfers of Investment Property"	January 1, 2018
Annual Improvements to IFRS Standards 2014–2016 Cycle:	
Amendments to IFRS 12	January 1, 2017
Amendments to IFRS 1 and Amendments to IAS 28	January 1, 2018
IFRIC 22 "Foreign Currency Transactions and Advance Consideration"	January 1, 2018

Except for the following items, the Group believes that the adoption of the above IFRSs would not have any material impact on its consolidated financial statements. The extent and impact of significant changes are as follows:

(Continued)

**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

(i) IFRS 9 "Financial Instruments"

IFRS 9 replaces IAS 39 "Financial Instruments: Recognition and Measurement" which contains classification and measurement of financial instruments, impairment and hedge accounting.

1) Classification- Financial assets

IFRS 9 contains a new classification and measurement approach for financial assets that reflects the business model in which assets are managed and their cash flow characteristics. IFRS 9 contains three principal classification categories for financial assets: measured at amortized cost, fair value through other comprehensive income (FVOCI) and fair value through profit or loss (FVTPL). The standard eliminates the existing IAS 39 categories of held to maturity, loans and receivables and available for sale. Under IFRS 9, derivatives embedded in contracts where the host is a financial assets in the scope of the standard are never bifurcated. Instead, the hybrid financial instrument as a whole is assessed for classification. In addition, IAS 39 has an exception to the measurement requirements for investments in unquoted equity instruments that do not have a quoted market price in an active market (and derivatives on such an instrument) and for which fair value cannot therefore be measured reliable. Such financial instruments are measured at cost. IFRS 9 removes this exception, requiring all equity investments (and derivatives on them) to be measured at fair value.

Based on its assessment, the Group does not believe that the new classification requirements would have had a material impact on its accounting for trade receivables, investments in debt securities and investments in equity securities that are managed on a fair value basis. At December 31, 2017, the Group had part of equity investments classified as available-for-sale with a fair value of \$836,228. At initial application of IFRS 9, the Group has designated these investments as measured at FVTPL. Consequently, all fair value gains and losses would be reported in comprehensive income. The Group estimated the application of IFRS 9's classification requirements on January 1, 2018 resulting in the increase of \$606,270 in retained earnings, as well as the decrease of \$606,270 in other equity interest.

At December 31, 2017, the remaining part of equity investments classified as available-for-sale with a fair value of \$707,335 and financial assets at fair value through profit or loss of \$28,800 that are held for long-term strategic purposes. At initial application of IFRS 9, the Group has designated these investments as measured at FVOCI. Consequently, all fair value gains and losses would be reported in other comprehensive income, no impairment losses would be recognized in profit or loss and no gains or losses would be reclassified to profit or loss on disposal. The Group estimated the application of IFRS 9's classification requirements on January 1, 2018 resulting in a decrease of \$5,850 in retained earnings, as well as the increase of \$5,850 in other equity interest, respectively.

(Continued)

**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

At December 31, 2017, the Group had part of financial assets measured at cost of \$279,494 and cumulative impairment losses of \$274,587. At initial application of IFRS 9, the Group has designated these financial assets as measured at FVOCI. Consequently, all fair value gains and losses would be reported in other comprehensive income, no impairment losses would be recognized in profit or loss and no gains or losses would be reclassified to profit or loss on disposal. The Group estimated the application of IFRS 9's classification requirements on January 1, 2018 resulting in a decrease of \$274,587 in other equity interest, as well as the increase of \$274,587 in retained earnings, respectively.

Remaining part of financial assets measured at cost of \$71,015 and cumulative impairment losses of \$797. At initial application of IFRS 9, the Group has designated these financial assets as measured at FVTPL. The Group estimated that there would be no effect for the application of IFRS 9's classification requirements on January 1, 2018.

At initial application of IFRS 9, the Group's equity-accounted subsidiaries have designated their financial assets as measured at FVTPL or FVOCI. The Group estimated the application of IFRS 9's classification requirements on January 1, 2018 resulting in the increase of \$157,980 in retained earnings, as well as the decrease of \$157,980 in other equity interest.

2) Impairment-Financial assets and contract assets

IFRS 9 replaces the 'incurred loss' model in IAS 39 with a forward-looking 'expected credit loss' (ECL) model. This will require considerable judgment as to how changes in economic factors affect ECLs, which will be determined on a probability-weighted basis.

The new impairment model will apply to financial assets measured at amortized cost or FVOCI, except for investments in equity instruments, and to contract assets.

Under IFRS 9, loss allowances will be measured on either of the following bases:

- 12-month ECLs. These are ECLs that result from possible default events within the 12 months after the reporting date; and
- Lifetime ECLs. These are ECLs that result from all possible default events over the expected life of a financial instrument.

Lifetime ECL measurement applies if the credit risk of a financial asset at the reporting date has increased significantly since initial recognition and 12-month ECL measurement applies if it has not. An entity may determine that a financial asset's credit risk has not increased significantly if the asset has low credit risk at the reporting date. However, lifetime ECL measurement always applies for trade receivables and contract assets without a significant financing component; an entity may choose to apply this policy also for trade receivables and contract assets with a significant financing component.

(Continued)

**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

The Group believes that impairment losses are likely to increase and become more volatile for assets in the scope of the IFRS 9 impairment model. The Group estimated the application of IFRS 9's impairment requirements on January 1, 2018 resulting in the increase of \$1,348 in the allowance for impairment and the decrease of \$1,348 in retained earnings.

3) Disclosures

IFRS 9 will require extensive new disclosures, in particular about credit risk and expected credit losses. The Group's assessment included an analysis to identify data gaps against current processes and the Group plans to implement the system and controls changes that it believes will be necessary to capture the required data.

4) Transition

Changes in accounting policies resulting from the adoption of IFRS 9 will generally be applied retrospectively, except as described below.

- The Group plans to take advantage of the exemption allowing it not to restate comparative information for prior periods with respect to classification and measurement (including impairment) changes. Differences in the carrying amounts of financial assets and financial liabilities resulting from the adoption of IFRS 9 generally will be recognized in retained earnings and other equity interest as at January 1, 2018.
- The following assessments have to be made on the basis of the facts and circumstances that exist at the date of initial application.
  - The determination of the business model within which a financial asset is held.
  - The designation and revocation of previous designations of certain financial assets and financial liabilities as measured at FVTPL.
  - The designation of certain investments in equity instruments not held for trading as at FVOCI.

(ii) IFRS 15 Revenue from Contracts with Customers

IFRS 15 establishes a comprehensive framework for determining whether, how much and when revenue is recognized. It replaces existing revenue recognition guidance, including IAS 18 "Revenue" and IAS 11 "Construction Contracts".

1) Sales of goods

For the sale of products, revenue is currently recognized when the goods are delivered to the *customers' premises*, which is taken to be the point in time at which the customer accepts the goods and the related risks and rewards of ownership transfer. Revenue is recognized at this point provided that the revenue and costs can be measured reliably, the recovery of the consideration is probable and there is no continuing management involvement with the goods.

(Continued)

**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

Under IFRS 15, revenue will be recognized when a customer obtains control of the goods. The Group has performed an initial comparison of the point in time at which the related risks and rewards of ownership transfer and the control transfers. Since these points in time are similar, the Group does not expect that there will be a significant impact on its consolidated financial statements.

For certain contracts that permit a customer to return an item, revenue is currently recognized when a reasonable estimate of the returns can be made, provided that all other criteria for revenue recognition are met. Otherwise, a revenue recognition is deferred until the return period lapses or a reasonable estimate of returns can be made.

Under IFRS 15, revenue will be recognized for these contracts to the extent that it is probable that a significant reversal in the amount of cumulative revenue recognized will not occur. As a consequence, for those contracts for which the Group is unable to make a reasonable estimate of return, revenue is expected to be recognized sooner than when the return period lapses or a reasonable estimate can be made. A refund liability and an asset for recovery will be recognized for these contracts and presented separately in the balance sheet.

2) Transition

The Group plans to adopt the cumulative effect method in applying IFRS 15 with no restatement of the comparative periods presented. Under IFRS 15, the adjustment for the cumulative effect of initially applying this new accounting standard is required to be charged to the opening balance of retained earnings on January 1, 2018 when this said accounting standard becomes effective.

The Group estimates the adoption of IFRS 15, resulting in the increase of \$111,809, \$902,193 and \$298,611 in right to the returned goods (recognized under other current assets), contract liabilities and refund liabilities (recognized under other current liabilities), respectively; and a decrease of \$902,193, \$186,802 in unearned revenue and current provision, respectively, on January 1, 2018.

(iii) Amendments to IAS 7 "Disclosure Initiative"

The amendments require disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flow and non-cash changes.

To satisfy the new disclosure requirements, the Group intends to present a reconciliation between the opening and closing balances for liabilities with changes arising from financing activities.

The actual impacts of adopting the standards may change depending on the economic conditions and events which may occur in the future.

(Continued)

**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

- (c) The impact of IFRS issued by IASB but not yet endorsed by the FSC

As of the date the following IFRSs that have been issued by the IASB, but not yet endorsed by the FSC:

<u>New, Revised or Amended Standards and Interpretations</u>	<u>Effective date per IASB</u>
Amendments to IFRS 10 and IAS 28 "Sale or Contribution of Assets Between an Investor and Its Associate or Joint Venture"	Effective date to be determined by IASB
IFRS 16 "Leases"	January 1, 2019
IFRS 17 "Insurance Contracts"	January 1, 2021
IFRIC 23 "Uncertainty over Income Tax Treatments"	January 1, 2019
Amendments to IFRS 9 "Prepayment features with negative compensation"	January 1, 2019
Amendments to IAS 28 "Long-term interests in associates and joint ventures"	January 1, 2019
Annual Improvements to IFRS Standards 2015–2017 Cycle	January 1, 2019
Amendments to IAS 19 "Plan Amendment, Curtailment or Settlement"	January 1, 2019

Those which may be relevant to the Group are set out below:

<u>Issuance / Release Dates</u>	<u>Standards or Interpretations</u>	<u>Content of amendment</u>
January 13, 2016	IFRS 16 "Leases"	<p>The new standard of accounting for lease is amended as follows:</p> <ul style="list-style-type: none"> <li>• For a contract that is, or contains, a lease, the lessee shall recognize a right of use asset and a lease liability in the balance sheet. In the statement of profit or loss and other comprehensive income, a lessee shall present interest expense on the lease liability separately from the depreciation charge for the right of-use asset during the lease term.</li> <li>• A lessor classifies a lease as either a finance lease or an operating lease, and therefore, the accounting remains similar to IAS 17.</li> </ul>

The Group is evaluating the impact on its financial position and financial performance upon the initial adoption of the abovementioned standards or interpretations. The results thereof will be disclosed when the Group completes its evaluation.

(Continued)

**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

**(4) Summary of significant accounting policies:**

The following significant accounting policies have been applied consistently to all periods presented in the consolidated financial statements unless otherwise specified.

(a) Statement of compliance

The accompanying consolidated annual financial statements have been prepared in accordance with the revised Regulations Governing the Preparation of Financial Reports by Securities Issuers in the Republic of China (hereinafter referred to the Regulations), International Financial Reporting Standards, International Accounting Standards, IFRIC Interpretations and SIC Interpretations endorsed by the FSC (hereinafter referred to as "IFRS endorsed by the FSC").

(b) Basis of preparation

(i) Basis of measurement

The consolidated financial statements have been prepared on the historical cost basis except for the following material items in the balance sheets:

- 1) Financial instruments measured at fair value through profit or loss are measured at fair value (including derivative financial instruments) ;
- 2) Available-for-sale financial assets are measured at fair value;
- 3) The net defined benefit liability is recognized as the present value of the defined benefit obligation less the fair value of plan assets.

(ii) Functional and presentation currency

The functional currency of each Group entities is determined based on the primary economic environment in which the entities operate. The consolidated financial statements are presented in New Taiwan Dollar, which is the Company's functional currency. All financial information presented in New Taiwan Dollar has been rounded to the nearest thousand.

(c) Basis of consolidation

(i) Principle of preparation of the consolidated financial statements

The consolidated financial statements comprise the Company and its subsidiaries. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. Losses applicable to the non-controlling interests in a subsidiary are allocated to the non-controlling interests even if doing so causes the non-controlling interests to have a deficit balance.

Intra-group balances and transactions, and any unrealized income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements. Unrealized income arising from investment accounted for using equity method is eliminated against the Company invested in its subsidiaries. The accounting treatment for unrealized loss is the same as unrealized income only when there is no indication of impairment.

(Continued)

**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

Changes in the Group's ownership interest in a subsidiary that do not result in a loss of control are accounted for as equity transactions.

(ii) Acquisition of non-controlling interests

Acquisition of non-controlling interests is accounted for as an equity transaction with owners. Under the aforesaid transaction, goodwill is not recognized.

(iii) Subsidiaries

Subsidiaries are entities controlled by the Group. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

(iv) Business combination under common control

The business combinations under common control often occur as the group activities are recognized in which the direct ownership of subsidiaries changes but the ultimate parent remains the same. These combinations are treated as the later of either the earliest comparative period in financial statements or the date of common control that requires the restatement of comparative information of prior period. Upon consolidation, assets and liabilities of the acquired entity are recognized at their carrying amount in the consolidated financial statements of owners of the Company. The equity of the consolidated entity is accounted for under the non-controlling interest, and related income and loss are directly recognized in profits attributable to non-controlling interest.

(v) Losing control

When the Group loses control of a subsidiary it derecognizes the assets and liabilities and related equity components of the former subsidiary. Any gain or loss is recognized in profit or loss. Any investment retained in the former subsidiary is measured at its fair value at the date when control is lost.

(vi) List of subsidiaries included in the consolidated financial statements:

Investor	Subsidiary	Nature of business	Shareholding ratio		Notes
			December 31, 2017	December 31, 2016	
THE COMPANY	UNIHAN HOLDING LTD. (UNIHAN HOLDING)	Investing activities	100.00 %	100.00 %	
UNIHAN HOLDING	CASETEK HOLDINGS LIMITED (CASETEK HOLDINGS)	Investing and trading activities	100.00 %	100.00 %	
CASETEK HOLDINGS	SLITEK HOLDINGS LIMITED	Investing and trading activities	100.00 %	100.00 %	
CASETEK HOLDINGS	CASETEK COMPUTER (SUZHOU) CO., LTD.	Manufacturing, developing and selling computers, computer parts, application systems, and providing after-sales service	100.00 %	100.00 %	
CASETEK HOLDINGS	KAEDAR HOLDINGS LIMITED (KAEDAR HOLDINGS)	Investing and trading activities	100.00 %	100.00 %	

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

Investor	Subsidiary	Nature of business	Shareholding ratio		Notes
			December 31, 2017	December 31, 2016	
KAEDAR HOLDINGS	KAEDAR ELECTRONICS (KUNSHAN) CO., LTD.	Tooling molds of stainless steel computer cases	100.00 %	100.00 %	
CASETEK HOLDINGS	KAEDAR TRADING LTD.	Investing and trading activities	100.00 %	100.00 %	
CASETEK HOLDINGS	CORE-TEK (SHANGHAI) LIMITED	Researching and producing spare parts for notebook computers, designing nonmetal tooling, electronic specific equipment and related products, repairing and producing precision equipment and providing after-sales service	100.00 %	100.00 %	
CASETEK HOLDINGS	KAI-CHUAN ELECTRONICS (CHONGQING) CO., LTD.	Manufacturing, developing and inspecting computers and application systems, designing and manufacturing nonmetal and metal tooling, developing plastic and electronic component, selling self-manufactured products.	100.00 %	100.00 %	
THE COMPANY, ASUSPOWER INVESTMENT AND ASUSTEK INVESTMENT	AZURE WAVE TECHNOLOGIES, INC. (AZURE WAVE)	Manufacturing office machinery, electronic parts and computer peripherals and selling precision equipment, and digital cameras	37.04 %	38.08 %	Notes 1 and 3
AZURE WAVE	EZWAVE TECHNOLOGIES, INC.	Manufacturing office machinery, electronic parts and computer peripherals	100.00 %	100.00 %	Note 1
AZURE WAVE	Azwave Holding (Samoa) Inc.(Azwave Samoa)	Investing activities	100.00 %	100.00 %	Note 1
AZURE WAVE	Azurewave Technologies (USA) Inc.	Market development activities	100.00 %	100.00 %	Note 1
AZURE WAVE	AZURE LIGHTING TECHNOLOGIES, INC.	Selling electronic parts	100.00 %	100.00 %	Note 1
Azwave Samoa	AZURE WAVE TECHNOLOGIES (SHANGHAI) INC.	Designing, manufacturing and trading computer products	100.00 %	100.00 %	Note 1
Azwave Samoa	AZURE LIGHTING TECHNOLOGIES, INC. (YANGZHOU)	Manufacturing and selling LED and relevant lighting products	100.00 %	100.00 %	Note 1
Azwave Samoa	AIGALE CORPORATION (SHANGHAI)	Designing and selling communication equipment and electronic products	100.00 %	100.00 %	Note 1
THE COMPANY	AMA PRECISION INC.(AMA PRECISION)	Designing and developing computer parts	100.00 %	100.00 %	
AMA PRECISION	AMA Holdings Limited(AMA)	Investing activities	100.00 %	100.00 %	
AMA	EXTECH LTD.	Trading electronic parts	- %	90.51 %	Note 9
EXTECH LTD.	GRANDTECH PRECISION (TONGZHOU) CO., LTD.	Manufacturing, developing and selling electronic parts	- %	100.00 %	Note 10
AMA, MAINTEK COMPUTER (SUZHOU) CO., LTD.	TOPTTEK PRECISION INDUSTRY(SUZHOU) CO., LTD.	Manufacturing and selling new electronic parts and premium hardware	100.00 %	100.00 %	Note 11
THE COMPANY	PEGATRON HOLLAND HOLDING B.V.(PHH)	Investing activities	100.00 %	100.00 %	

(Continued)

**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

Investor	Subsidiary	Nature of business	Shareholding ratio		Notes
			December 31, 2017	December 31, 2016	
PHH	PEGATRON Czech s.r.o.	Installing, repairing and selling electronic products	100.00 %	100.00 %	
PHH	Pegatron Service Holland B.V.	Sales and repair service center in Europe	- %	100.00 %	Note 12
THE COMPANY	PEGATRON HOLDING LTD. (PEGATRON HOLDING)	Investing activities	100.00 %	100.00 %	
PEGATRON HOLDING	POWTEK HOLDINGS LIMITED (POWTEK)	Investing and trading activities	100.00 %	100.00 %	
POWTEK	POWTEK (SHANGHAI) LTD.	Selling main boards, computer peripherals, note books, servers and software, and providing after-sales service	100.00 %	100.00 %	
PEGATRON HOLDING KINSUS SAMOA	PIOTEK HOLDINGS LTD. (CAYMAN) (PIOTEK CAYMAN)	Investing activities	100.00 %	100.00 %	Note 14
PIOTEK CAYMAN	PIOTEK HOLDING LIMITED (PIOTEK HOLDING)	Investing activities	100.00 %	100.00 %	Note 14
PIOTEK HOLDING	PIOTEK COMPUTER (SUZHOU) CO., LTD.	Developing, manufacturing and selling new electronic components, circuit boards and relevant products, and providing after-sales service	100.00 %	100.00 %	Note 14
PIOTEK HOLDING	PIOTEK(H.K.) TRADING LIMITED	Trading activities	100.00 %	100.00 %	Note 14
PEGATRON HOLDING	GRAND UPRIGHT TECHNOLOGY LIMITED	Investing and trading activities	100.00 %	100.00 %	
PEGATRON HOLDING	ASLINK PRECISION CO., LTD. (ASLINK)	Investing and trading activities	100.00 %	100.00 %	
ASLINK	PEGAGLOBE (KUNSHAN) CO.,LTD.	Manufacturing GPS, computer electronic devices, mobile phone, high-end server, disk drive, and other related components	100.00 %	100.00 %	
PEGATRON HOLDING	DIGITEK GLOBAL HOLDINGS LIMITED (DIGITEK)	Investing and trading activities	100.00 %	100.00 %	
DIGITEK	DIGITEK (CHONGQING) LTD.	Manufacturing, developing, and selling GPS, electronic calculators, and aftersale service	100.00 %	100.00 %	
PEGATRON HOLDING	MAGNIFICENT BRIGHTNESS LIMITED (MAGNIFICENT)	Investing and trading activities	100.00 %	100.00 %	
MAGNIFICENT	MAINTEK COMPUTER (SUZHOU) CO., LTD.	Manufacturing, developing and selling power supply units, computer cases, computer systems, notebooks, main boards, and computer peripherals, and providing after-sales service	100.00 %	100.00 %	
PEGATRON HOLDING	PROTEK GLOBAL HOLDINGS LTD. (PROTEK)	Investing and trading activities	100.00 %	100.00 %	
PROTEK	PROTEK (SHANGHAI) LTD.	Developing, manufacturing and selling GPS, new electronic components, circuit boards and relevant products, and providing after-sales service	100.00 %	100.00 %	
PEGATRON HOLDING	COTEK HOLDINGS LIMITED(COTEK)	Investing and trading activities	100.00 %	100.00 %	

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

Investor	Subsidiary	Nature of business	Shareholding ratio		Notes
			December 31, 2017	December 31, 2016	
COTEK	COTEK ELECTRONICS (SUZHOU) CO., LTD.	Developing, manufacturing and selling new electronic components, circuit boards and relevant products, and providing after-sales service	100.00 %	100.00 %	
PEGATRON HOLDING	TOP QUARK LIMITED(TOP QUARK)	Investing activities	100.00 %	100.00 %	
TOP QUARK	RUNTOP (SHANGHAI) CO., LTD.	Manufacturing and selling computer parts and peripherals of digital automatic data processors, multimedia computer system accessories, power supply units, network switches, and modems	100.00 %	100.00 %	
THE COMPANY	ASUSPOWER INVESTMENT CO., LTD.	Investing activities	100.00 %	100.00 %	
THE COMPANY	ASUS INVESTMENT CO., LTD.	Investing activities	100.00 %	100.00 %	
THE COMPANY	ASUSTEK INVESTMENT CO., LTD.	Investing activities	100.00 %	100.00 %	
ASUSPOWER INVESTMENT, ASUS INVESTMENT AND ASUSTEK INVESTMENT	ASROCK INCORPORATION (ASROCK)	Data storage and processing equipment, manufacturing wired and wireless communication equipment, and whole selling of computer equipment and electronic components	55.87 %	58.65 %	Note 7
ASROCK	ASIAROCK TECHNOLOGY LIMITED (ASIAROCK)	Manufacturing and selling database storage and processing equipment	100.00 %	100.00 %	
ASIAROCK	ASROCK EUROPE B.V.	Selling database service and trading electronic components	100.00 %	100.00 %	
ASIAROCK	Calrock Holdings, LLC.	Office building leasing	100.00 %	100.00 %	
ASROCK	Leader Insight Holdings Limited (Leader)	Investing and holding activities	100.00 %	100.00 %	
Leader	First place International Limited (First place)	Investing and holding activities	100.00 %	100.00 %	
First place	ASRock America, Inc.	Selling database service and trading electronic components	100.00 %	100.00 %	
ASROCK	ASRock Rack Incorporation	Manufacturing and selling computer and related peripherals	65.97 %	69.40 %	Note 4
ASUSPOWER INVESTMENT AND ASUS INVESTMENT	PEGATRON Mexico, S.A. DE C.V.	Sales and repair service center in Mexico	100.00 %	100.00 %	
ASUSPOWER INVESTMENT, ASUS INVESTMENT AND ASUSTEK INVESTMENT	KINSUS INTERCONNECT TECHNOLOGY CORP. (KINSUS)	Manufacturing electronic parts, whole selling and retailing electronic components, and providing business management consultant service	39.00 %	39.04 %	Notes 13 and 14
KINSUS	KINSUS INVESTMENT CO., LTD. (KINSUS INVESTMENT)	Investing activities	100.00 %	100.00 %	Notes 2 and 14

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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Investor	Subsidiary	Nature of business	Shareholding ratio		Notes
			December 31, 2017	December 31, 2016	
KINSUS INVESTMENT, ASUSPOWER INVESTMENT AND ASUSTEK INVESTMENT	PEGAVISION CORPORATION	Manufacturing medical appliances	54.87 %	54.87 %	Notes 2 and 14
KINSUS INVESTMENT, ASUSTEK INVESTMENT AND ASUS INVESTMENT	FUYANG TECHNOLOGY CORPORATION	Manufacturing and wholesaling wires, cables, and electronic components	89.13 %	90.00 %	Notes 2, 5 and 14
PEGAVISION CORPORATION	PEGAVISION HOLDINGS CORPORATION (PEGAVISION)	Investing activities	100.00 %	100.00 %	Note 14
PEGAVISION CORPORATION	PEGAVISION JAPAN INC.	Selling medical appliances	100.00 %	100.00 %	Note 14
FUYANG TECHNOLOGY CORPORATION	FUYANG FLEX HOLDING LTD. (FUYANG HOLDING)	Investing activities	100.00 %	100.00 %	
FUYANG HOLDING	FUYANG ELECTRONICS (SUZHOU) CO., LTD.	Researching, producing, inspecting, repairing and selling flexible multilayer model, computer digital signal process system and card; selling own produced products and providing related technical consulting service	100.00 %	100.00 %	
PEGAVISION	PEGAVISION (SHANGHAI) LIMITED	Selling medical appliances	100.00 %	100.00 %	Note 14
KINSUS	KINSUS CORP. (USA)	Developing and designing new technology and products; analyzing marketing strategy and developing new customers	100.00 %	100.00 %	Note 14
KINSUS	KINSUS HOLDING (SAMOA) LIMITED (KINSUS SAMOA)	Investing activities	100.00 %	100.00 %	Note 14
KINSUS SAMOA	KINSUS HOLDING (CAYMAN) LIMITED(KINSUS CAYMAN)	Investing activities	100.00 %	100.00 %	Note 14
KINSUS CAYMAN	KINSUS INTERCONNECT TECHNOLOGY (SUZHOU) CORP.	Manufacturing and selling circuit boards	100.00 %	100.00 %	Note 14
KINSUS CAYMAN	KINSUS TRADING (SUZHOU) CORP.	Manufacturing and selling circuit boards related products and materials	100.00 %	100.00 %	Note 14
ASUSPOWER INVESTMENT, ASUS INVESTMENT AND ASUSTEK INVESTMENT	STARLINK ELECTRONICS CORPORATION	Manufacturing electronic parts and plastic products, and manufacturing and wholesaling electronic components	100.00 %	100.00 %	
ASUSPOWER INVESTMENT, ASUS INVESTMENT AND ASUSTEK INVESTMENT	ASUSPOWER CORPORATION	Investing and trading activities	100.00 %	100.00 %	

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

Investor	Subsidiary	Nature of business	Shareholding ratio		Notes
			December 31, 2017	December 31, 2016	
ASUSPOWER CORPORATION	CASETEK HOLDINGS LIMITED(CAYMAN) (CASETEK CAYMAN)	Investing activities	60.47 %	60.73 %	Note 8
CASETEK CAYMAN	RIH LI INTERNATIONAL LIMITED (RIH LI)	Investing activities	100.00 %	100.00 %	
RIH LI	RI-TENG COMPUTER ACCESSORY (SHANGHAI) CO., LTD.	Designing, developing, manufacturing and selling electronic components, precision, nonmetal and metal tooling	100.00 %	100.00 %	
RIH LI	RI-PRO PRECISION MODEL (SHANGHAI) CO., LTD.	Designing, developing, manufacturing and selling electronic components, precision, nonmetal and metal tooling	100.00 %	100.00 %	
RIH LI	RI-MING (SHANGHAI) CO., LTD.	Designing, developing, manufacturing and selling electronic components, precision, nonmetal and metal tooling	100.00 %	100.00 %	
RIH LI	SHENG-RUI ELECTRONIC TECHNOLOGY (SHANGHAI) LIMITED	Designing, developing, manufacturing and selling electronic components, precision, nonmetal and metal tooling and surface processing for the aforementioned product.	100.00 %	100.00 %	
RIH LI	RI PEI COMPUTER ACCESSORY (SHANGHAI) CO., LTD.	Designing, developing, manufacturing and selling electronic components, precision, nonmetal and metal tooling	100.00 %	100.00 %	
RIH LI	KAI JIA COMPUTER ACCESSORY CO., LTD.	Designing, developing, manufacturing and selling electronic components, precision, nonmetal and metal tooling and surface processing for the aforementioned product.	100.00 %	100.00 %	
RIH LI	RI KAI COMPUTER ACCESSORY CO., LTD.(RI KAI)	Designing, developing, manufacturing and selling electronic components, precision, nonmetal and metal tooling.	100.00 %	- %	Note 6
CASETEK CAYMAN	APEX SUN LIMITED	Investing activities	100.00 %	100.00 %	
CASETEK CAYMAN	RIH KUAN METAL CORPORATION	Selling iron and aluminum products	100.00 %	100.00 %	
CASETEK CAYMAN	APLUS PRECISION LIMITED(APLUS)	Investing and trading activities	100.00 %	100.00 %	
APLUS	UNITED NEW LIMITED(UNITED)	Investing and trading activities	100.00 %	100.00 %	
UNITED	KAI HE COMPUTER ACCESSORY (SUZHOU) CO., LTD	Designing, developing, manufacturing and selling electronic components, precision, nonmetal and metal tooling and surface processing for the aforementioned product.	100.00 %	100.00 %	
CASETEK CAYMAN	MEGA MERIT LIMITED	Trading activities	100.00 %	100.00 %	
ASUS INVESTMENT	ASFLY TRAVEL SERVICE LIMITED	Travel agency	100.00 %	100.00 %	
ASUSPOWER INVESTMENT	PEGATRON TECHNOLOGY SERVICE INC. (PTSI)	Sales and repair service center in North America	100.00 %	100.00 %	
PTSI	PEGATRON SERVICOS DE INFORMATICA LTDA. (PCBR)	Maintenance service	100.00 %	100.00 %	

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

Investor	Subsidiary	Nature of business	Shareholding ratio		Notes
			December 31, 2017	December 31, 2016	
ASUSPOWER INVESTMENT	PEGA INTERNATIONAL LIMITED	Design service and sales	100.00 %	100.00 %	
ASUSPOWER INVESTMENT	PEGATRON JAPAN INC.	Sales and repair service center in Japan	100.00 %	100.00 %	
ASUSPOWER INVESTMENT	PEGATRON LOGISTIC SERVICE INC.	Sales and logistics center in North America	100.00 %	100.00 %	
ASUSPOWER INVESTMENT, ASUS INVESTMENT AND ASUSTEK INVESTMENT	Lumens Digital Optics Inc. (Lumens Optics)	Developing, manufacturing and selling computer data projectors and related peripherals	56.52 %	56.52 %	
Lumens Optics	Lumens Integration Inc.	Selling computer communication products and peripherals	100.00 %	100.00 %	
Lumens Optics	Lumens Digit Image Inc. (SAMOA)(Lumens)	Investing activities	100.00 %	100.00 %	
Lumens	Lumens (Suzhou) Digital Image Inc.	Developing, manufacturing and selling projectors, projection screens and related products, and providing after-sales service	100.00 %	100.00 %	
ASUSPOWER INVESTMENT	Pegatron Service Singapore Pte. Ltd.(PSG)	Sales and logistics center in Singapore	100.00 %	100.00 %	
PSG	PEGATRON SERVICE KOREA LLC.	Sales and repair service center in Korea	100.00 %	100.00 %	
ASUS INVESTMENT	HUA-YUAN INVESTMENT LIMITED	Investing activities	100.00 %	100.00 %	
THE COMPANY	PEGATRON USA, INC.	Sales and repair service center in North America	100.00 %	100.00 %	

Note 1: AZURE WAVE TECHNOLOGY CORP. was included in the consolidated financial statements even if the Group held 37.04% of their total issued shares because the Group has acquired more than 50% of voting shares of the entity and has the ability to excise control over its board of directors.

Note 2: On May 19, 2017, PEGAVISION INVESTMENT changed its name to KINSUS INVESTMENT CO., LTD.

Note 3: As AZURE WAVE TECHNOLOGY CORP. issued employee restricted shares of stock on June 5, 2017, the Group's shareholding ratio in AZURE WAVE TECHNOLOGY CORP. decreased from 38.08% to 37.04%.

Note 4: On May 19, 2017, ASRock Rack Incorporation launched its capital increase. As the Group did not increase its investment based on its shareholding ratio, the Group's shareholding ratio in ASRock Rack Incorporation decreased from 69.40% to 65.97%.

Note 5: On May 26, 2017, FUYANG TECHNOLOGY CORPORATION launched its capital increase. As the Group did not increase its investment based on its shareholding ratio, the Group's shareholding ratio in FUYANG TECHNOLOGY CORPORATION decreased from 90.00% to 89.13%.

Note 6: RI LI has established and registered a company through capital increase on September 27, 2017.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

Note 7: As ASROCK INCORPORATION issued employee restricted shares of stock on September 22, 2017, the Group's shareholding ratio in ASROCK INCORPORATION decreased from 58.65% to 55.87%.

Note 8: As CASETEK HOLDINGS LIMITED issued employee restricted shares of stock through capital increase on September 5, 2017, the Group's shareholding ratio in CASETEK HOLDINGS LIMITED decreased from 60.73% to 60.47%.

Note 9: It was liquidated in December 2017.

Note 10: It was liquidated in May 2017.

Note 11: In October 2017, the Group has restructured, so that the 100% equity ownership of TOPTEK PRECISION INDUSTRY (SUZHOU) CO., LTD. was held by AMA and MAINTEK COMPUTER (SUZHOU) CO., LTD.

Note 12: It was liquidated in December 2017.

Note 13: As transferred treasury stock to employees on September 22, 2017, the Group's shareholding ratio in KINSUS INTERCONNECT TECHNOLOGY CORP. decrease from 39.04% to 39.00%.

Note 14: Since the Group only held 39% of voting rights of KINSUS INTERCONNECT TECHNOLOGY CORP. (KINSUS), with the remaining 61% shares belonging to different shareholders having no intention of exercising their votes collectively, and also, due to the fact that the Group's participation dominated the previous shareholders' meetings, resulting in the Group having a significant control over KINSUS, therefore, KINSUS has been included in the consolidated financial statements of the Group as of December 31, 2017.

(vii) Subsidiaries excluded from consolidation: None.

(d) Foreign currency

(i) Foreign currency transaction

Transactions in foreign currencies are translated to the respective functional currencies of the Group entities at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between amortized cost in the functional currency at the beginning of the period adjusted for the effective interest and payments during the period.

Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated to the functional currency at the exchange rate at the date that the fair value was determined. Non-monetary items in a foreign currency that are measured based on historical cost are translated using the exchange rate at the date of translation.

Foreign currency differences arising on retranslation are recognized in profit or loss, except for the following accounts which are recognized in other comprehensive income:

- 1) Available-for-sale equity investment;
- 2) A financial liability designated as a hedge of the net investment in a foreign operation to the extent that the hedge is effective; or

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

3) Qualifying cash flow hedges to the extent the hedge is effective.

(ii) Foreign operations

The assets and liabilities of foreign operations, including goodwill and fair value adjustments arising on acquisition, are translated to the Group's functional currency at exchange rates at the reporting date. The income and expenses of foreign operations, excluding foreign operations in hyperinflationary economies, are translated to the Group's functional currency at average rate. Foreign currency differences are recognized in other comprehensive income, and are presented in the exchange differences on translation of foreign financial statements in equity.

However, if the foreign operation is a non-wholly owned subsidiary, then the relevant proportion of the translation difference is allocated to non-controlling interests. When a foreign operation is disposed of such that control, significant influence or joint control is lost, the cumulative amount in the translation reserve related to that foreign operation is reclassified to profit or loss as part of the gain or loss on disposal. When the Group disposes of any part of its interest in a subsidiary that includes a foreign operation while retaining control, the relevant proportion of the cumulative amount is reattributed to non-controlling interest. When the Group disposes of only part of investment in an associate of joint venture that includes a foreign operation while retaining significant or joint control, the relevant proportion of the cumulative amount is reclassified to profit or loss.

When the settlement of a monetary item receivable from or payable to a foreign operation is neither planned nor likely in the foreseeable future, foreign currency gains and losses arising from such items are considered to form part of a net investment in the foreign operation and are recognized in other comprehensive income.

(e) Classification of current and non-current assets and liabilities

An asset is classified as current when:

- (i) It is expected to be realized the asset, or intended to be sold or consumed, during the normal operating cycle;
- (ii) It is held primarily for the purpose of trading;
- (iii) It is expected to be realized within twelve months after the reporting period; or
- (iv) The asset is cash and cash equivalent (as defined in IAS 7) unless the asset is restricted from being exchanged or used to settle a liability for at least twelve months after the reporting period.

All other assets are classified as non-current.

A liability is classified as current when:

- (i) It is expected to be settled within the Group's normal operating cycle;
- (ii) It is held primarily for the purpose of trading;
- (iii) The liability is due to be settled within twelve months after the reporting period; or

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

- (iv) It does not have an unconditional right to defer settlement for at least twelve months after the reporting period. Terms of a liability that could, at the option of the counterparty, result in its settlement by issuing equity instruments do not affect its classification.

All other liabilities are classified as non-current.

(f) Cash and cash equivalents

Cash comprises cash on hand and demand deposits. Cash equivalents are assets that are readily convertible to known amounts of cash, and are subject to an insignificant risk of changes in their fair value.

Time deposits are accounted under cash and cash equivalents if they are accord with the definition aforementioned, and are held for the purpose of meeting short-term cash commitment rather than for investment or other purpose.

(g) Financial instruments

Financial assets and financial liabilities are initially recognized when the Group becomes a party to the contractual provisions of the instruments.

(i) Financial assets

The Group classifies financial assets into the following categories: financial assets at fair value through profit or loss, loans and receivables and available-for-sale financial assets.

1) Financial assets at fair value through profit or loss

A financial asset is classified in this category if it is held-for-trading or is designated as such on initial recognition. Financial assets classified as held-for-trading if it is acquired principally for the purpose of selling in the short term. The Group designates financial assets, other than ones classified as held-for-trading, as at fair value through profit or loss at initial recognition under one of the following situations:

- a) Designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise.
- b) Performance of the financial asset is evaluated on a fair value basis.
- c) Hybrid instrument contains one or more embedded derivatives.

At initial recognition, financial assets classified under this category are measured at fair value. Attributable transaction costs are recognized in profit or loss as incurred. Financial assets at fair value through profit or loss are measured at fair value and changes therein, which takes into account any dividend and interest income, are recognized in profit or loss, and included in statement of comprehensive income. A regular way purchase or sale of financial assets is recognized and derecognized, as applicable, using trade date accounting.

Investments in equity instruments that do not have a quoted market price in an active market, and whose fair value cannot be reliably measured, are measured at amortized cost, and are included in financial assets measured at cost.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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2) Available-for sale financial assets

Available-for-sale financial assets are non-derivative financial assets that are designated available-for-sale or are not classified in any of the other categories of financial assets. At initial recognition, available-for-sale financial assets are recognized at fair value, plus, any directly attributable transaction cost. Subsequent to initial recognition, they are measured at fair value and changes therein, other than impairment losses, interest income calculated using the effective interest method, dividend income, and foreign currency differences on available-for-sale debt instruments, are recognized in other comprehensive income and unrealized gains (losses) on available-for-sale financial assets in equity. When an available-for-sale investment is derecognized, the gain or loss accumulated in equity is reclassified to profit or loss, under other income. A regular way purchase or sale of financial assets is recognized and derecognized, as applicable, using trade date accounting.

Investments in equity instruments that do not have a quoted market price in an active market, and whose fair value cannot be reliably measured, are measured at amortized cost, and are included in financial assets measured at cost.

Dividend income is recognized in profit or loss on the date that the Group's right to receive payment is established, which in the case of quoted securities is normally the ex-dividend date. Such dividend income is included in other income of profit or loss.

Interest income from investment in bond security is recognized in profit or loss, under other income.

3) Loans and receivables

Loans and receivables are financial assets with fixed or determinable payments that are not quoted in an active market. At initial recognition, these assets are recognized at fair value, plus, any directly attributable transaction costs. Subsequent to initial recognition, loans and receivables are measured at amortized cost using the effective interest method, less any impairment losses, other than insignificant interest on short-term receivables. A regular way purchase or sale of financial assets is recognized and derecognized, as applicable, using trade date accounting.

Loans and receivables include accounts receivables and other receivables. Interest income is recognized in profit or loss, under other income.

In accordance with Statement of International Accounting Standards No. 39 "Financial instruments Accounting for Transfers of Financial Assets and Extinguishments of Liabilities," a transfer of financial assets or a portion of a financial asset in which the transferor surrenders control over those financial assets is regarded as a sale to the extent that consideration in the transferred assets is received in exchange. The rights to accounts receivable are derecognized after deducting the estimated charges or losses in commercial dispute when all of the following conditions are met.

- a) The rights to accounts receivable have been isolated from the transferor as they are put presumptively beyond the reach of the transferor and its creditors, even in bankruptcy or other receivership.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES****Notes to the Consolidated Financial Statements**

- b) Each transferee has the right to pledge or exchange the rights to the accounts receivable, and no condition prevents the transferee (or holder) from taking advantage of its right to pledge or exchange and provides more than a trivial benefit to the transferor.
- c) The transferor does not maintain effective control over the rights to the accounts receivable claims through either:
  - i) An agreement that both entitles and obligates the transferor to repurchase or redeem them before their maturity, or
  - ii) The ability to unilaterally cause the holder to return specific rights to the accounts receivable.

Accounts receivable which are assigned but no receipt yet of cash advances are accounted for as other accounts receivable.

**4) Impairment of financial assets**

Except for financial assets at fair value through profit or loss, financial assets are assessed for impairment at each reporting date. A financial asset is impaired if, and only if, there is objective evidence of impairment as a result of one or more events (a loss event) that occurred subsequent to the initial recognition of the asset and that a loss event (or events) has an impact on the future cash flows of the financial assets that can be estimated reliably.

Objective evidence that financial assets are impaired includes default or delinquency by a debtor, restructuring of an amount due to the Group on terms that the Group would not consider otherwise, indications that a debtor or issuer will enter bankruptcy, adverse changes in the payment status of borrowers or issuers, economic conditions that correlate with defaults or the disappearance of an active market for a security. In addition, for an investment in an equity security, a significant or prolonged decline in its fair value below its cost is accounted for as objective evidence of impairment.

All individually significant receivables are assessed for specific impairment. Receivables that are not individually significant are collectively assessed for impairment by grouping together assets with similar risk characteristics. In assessing collective impairment, the Group uses historical trends of the probability of default, the timing of recoveries and the amount of loss incurred, adjusted for management's judgment as to whether current economic and credit conditions are such that the actual losses are likely to be greater or lesser than the one suggested by historical trends.

An impairment loss in respect of a financial asset measured at amortized cost is calculated as the difference between its carrying amount and the present value of its estimated future cash flows discounted at the asset's original effective interest rate.

An impairment loss in respect of a financial asset measured at cost is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the current market rate of return for a similar financial asset. Such impairment loss is not reversible in subsequent periods.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES****Notes to the Consolidated Financial Statements**

The carrying amount of a financial asset is reduced for an impairment loss, except for trade receivables, in which an impairment loss is reflected in an allowance account against the receivables. When it is determined a receivable is uncollectible, it is written off against the allowance account. Any subsequent recovery from written off receivable is charged to the allowance account. Changes in the allowance accounts are recognized in profit or loss.

Impairment losses on available-for-sale financial assets are recognized by reclassifying the losses accumulated in the fair value reserve in equity to profit or loss.

If, in a subsequent period, the amount of impairment loss on a financial asset measured at amortized cost decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the decrease in impairment loss is reversed through profit or loss, to the extent that the carrying value of the asset does not exceed its amortized cost before the impairment loss was recognized at the reversal date.

Impairment losses recognized on available-for-sale equity security are not reversed through profit or loss. Any subsequent recovery in the fair value of an impaired available-for-sale equity security is recognized in other comprehensive income, and accumulated in equity.

If, in a subsequent period, the fair value of an impaired available-for-sale debt security increases and the increase can be related objectively to an event occurring after the impairment loss was recognized, then impairment loss is reversed against profit or loss.

Impairment losses and recoveries are recognized in profit or loss, under “other gains and losses, net.”

5) Derecognition of financial assets

The Group derecognizes financial assets when the contractual rights of the cash inflow from the asset are terminated, or when the group transfers substantially all the risks and rewards of ownership of the financial assets.

On partial derecognition of a financial assets, the difference between the carrying amount and the sum of the consideration received or receivable and any cumulative gain or loss that had been recognized in other comprehensive income and presented in other equity account unrealized gains or losses from available for sale financial assets is reclassified to profit or loss, under “other gains and losses, net”.

The Group separates the part that continues to be recognized and the part that is derecognized, based on the relative fair values of those parts on the date of the transfer. The difference between the carrying amount allocated to the part derecognized and the sum of the consideration received for the part derecognized and any cumulative gain or loss allocated to it that had been recognized in other comprehensive income is charged to profit or loss.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

(ii) Financial liabilities and equity instruments

1) Classification of debt or equity instruments

Debt or equity instruments issued by the Group are classified as financial liabilities or equity instruments in accordance with the substance of the contractual agreement.

An equity instrument is any contract that evidences residual interest in the assets of an entity after deducting all of its liabilities. Equity instruments issued are recognized based on amount of consideration received less the direct issuance cost.

Preference share is classified as equity if it is non-redeemable, or redeemable only at the Group's option. Preference share capital is classified as a financial liability if it is redeemable on a specific date or at the option of the shareholders, or if dividend payments are not discretionary.

Compound financial instruments issued by the Group comprise convertible bonds payable that can be converted to share capital at the option of the holder, when the number of shares to be issued is fixed.

At initial recognition, the liability component of a compound financial instrument is recognized at fair value of a similar liability that does not have an equity conversion option. The equity component is recognized initially based on the difference between the fair value of the compound financial instrument as a whole and the fair value of the liability component. Any directly attributable transaction costs are allocated to the liability and equity components in proportion to their initial carrying amounts.

Subsequent to initial recognition, the liability component of a compound financial instrument is measured at amortized cost using the effective interest method. The equity component of a compound financial instrument is not re-measured subsequent to initial recognition.

Interest related to the financial liability is recognized in profit or loss, under non-operating income and expense. On conversion, financial liability is reclassified to equity, without recognizing any gain or loss.

2) Other financial liabilities

At initial recognition, financial liabilities not classified as held-for-trading, or designated as at fair value through profit or loss, which comprise of loans and borrowings, and trade and other payables, are measured at fair value, plus, any directly attributable transaction cost. Subsequent to initial recognition, they are measured at amortized cost calculated using the effective interest method. Interest expense not capitalized as capital cost is recognized in non-operating income and expenses, under finance cost.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

3) Derecognition of financial liabilities

A financial liability is derecognized when its contractual obligation has been discharged or cancelled or expires. The difference between the carrying amount of a financial liability derecognized and the consideration paid (including any non-cash assets transferred or liabilities assumed) is recognized in profit or loss, and is included in “non-operating income and expenses.”

4) Offsetting of financial assets and liabilities

Financial assets and liabilities are presented on a net basis when the Group has the legally enforceable rights to offset, and intends to settle such financial assets and liabilities on a net basis or to realize the assets and settle the liabilities simultaneously.

5) Financial guarantee contract

A financial guarantee contract is a contract that requires the issuer to make specified payments to reimburse the holder of a loss it incurs because a specified debtor fails to pay on due date in accordance with the original or modified terms of a debt instrument.

At initial recognition, a financial guarantee contracts not classified as financial liabilities at fair value through profit or loss by the Group is recognized at fair value, plus, any directly attributable transaction cost. Subsequent to initial recognition, they are measured at the higher of (a) the amount of contractual obligation determined in accordance with IAS 37; or (b) the amount initially recognized less, when appropriate, cumulative amortization recognized in accordance with IAS 18.

(iii) Derivative financial instruments, including hedge accounting

The Group holds derivative financial instruments to hedge its foreign currency and interest rate fluctuation exposures. At initial recognition, derivatives are recognized at fair value; and attributable transaction costs are recognized in profit or loss as incurred. Subsequent to initial recognition, derivatives are measured at fair value, and changes therein are recognized in profit or loss, under “non-operating income and expenses.”

When a derivative is designated as a hedging instrument, the timing for recognizing gain or loss is determined based on the nature of the hedging relationship. When the result of the valuation at fair value of a derivative instrument is positive, it is classified as a financial asset; otherwise, it is classified as a financial liability.

Derivatives linked to investments in equity instruments that do not have a quoted market price in an active market and must be settled by delivery of unquoted equity instruments, are classified as financial assets, which are measured at amortized cost. These derivatives are classified as financial liabilities measured at cost.

Embedded derivatives are separated from the host contract and are accounted for separately when the economic characteristics and risk of the host contract and the embedded derivatives are not closely related, and that the host contract is not measured at fair value through profit or loss.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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The Group designates its hedging instrument, including derivatives, embedded derivatives, and non-derivative instrument for a hedge of a foreign currency risk, as fair value hedge, cash flow hedge, or hedge of a net investment in a foreign operation. Foreign exchange risk of firm commitments are treated as a fair value hedge.

On initial designation of the derivative as a hedging instrument, the Group formally documents the relationship between the hedging instrument and hedged item, including the risk management objectives and strategy in undertaking the hedge transaction and the hedged risk, and whether the hedging instruments are expected to be highly effective in offsetting the changes in the fair value or cash flows of the respective hedged items attributable to the hedged risk.

1) Fair value hedge

Changes in the fair value of a hedging instruments designated and qualified as fair value hedges are recognized in profit or loss, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk.

If the hedging instrument no longer meets the criteria for hedge accounting, expires or is sold, terminated or exercised, or the designation is revoked, then hedge accounting is discontinued prospectively.

Hedged financial instruments using an effective interest rate is amortized to profit or loss when hedge accounting is discontinued over the period to maturity. The effective rate can discount the adjustment amount to zero at the maturity date.

2) Cash flow hedge

When a derivative is designated as a cash flow hedge, the effective portion of changes in the fair value of the derivative is recognized in other comprehensive income and presented in equity, under effective portion of cash flow hedge gain (loss). Any ineffective portion of changes in the fair value of the derivative is recognized immediately in profit or loss, under “non-operating income and expenses.”

When the hedged item is recognized in profit or loss, the amount accumulated in equity and retained in other comprehensive income is reclassified to profit or loss in the same period or periods during which the hedged item affects profit or loss, and is presented in the same accounting caption with the hedged item recognized in the consolidated statement of comprehensive income.

For a cash flow hedge of a forecasted transaction recognized as a non-financial assets or liabilities, the amount accumulated in other equity – effective portion of cash flow hedge gain (loss) in other comprehensive income is reclassified to the initial cost of the non-financial asset or liability.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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(h) Inventories

Inventories are measured at the lower of cost and net realizable value. The cost of inventories is based on the weighted average method, and includes expenditure incurred in acquiring the inventories, production or conversion costs and other costs incurred in bringing them to their existing location and condition. In the case of manufactured inventories and work in progress, cost includes an appropriate share of production overheads based on normal operating capacity.

Net realizable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses. The replacement cost of raw material is its net realizable value.

(i) Investment in associates

Associates are those entities in which the Group has significant influence, but not control, over the financial and operating policies. Significant influence is presumed to exist when the Group holds between 20% and 50% of the voting power of another entity.

Investments in associates are accounted for using the equity method and are recognized initially at cost. The cost of investment includes transaction costs. The carrying amount of investment in associates includes goodwill arising from the acquisition less any accumulated impairment losses.

The Group's share of the profit or loss and other comprehensive income of investments accounted for using equity method are included, after adjustments to align the said investees' accounting policies with those of the Group, in the consolidated financial statements from the date that significant influence commences until the date that significant influence ceases.

Unrealized profits resulting from the transactions between the Group and an associate are eliminated to the extent of the Group's interest in the associate. Unrealized losses on transactions with associates are eliminated in the same way, except to the extent that the underlying asset is impaired.

When the Group's share of losses exceeds its interest in associates, the recognition of further losses is discontinued except to the extent that the Group has an obligation or has made payments on behalf of the investee.

(j) Investment property

Investment property is a property held either to earn rental income or for capital appreciation or for both, but not for sale in the ordinary course of business, use in the production or supply of goods or services or for administrative purposes. Investment property is measured at cost on initial recognition and subsequently at fair value with any change therein recognized in profit or loss.

Cost includes expenditure that is directly attributable to the acquisition of the investment property. The cost of self-constructed investment property includes the cost of raw materials and direct labor, and any other costs directly attributable to bringing the investment property to a working condition for their intended use and capitalized borrowing costs.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

Depreciation is provided over the estimated economic lives using the straight-line method. Land has an unlimited useful life and therefore is not depreciated. The estimated useful lives for the current and comparative years of significant items of investment properties are as follows:

Buildings	20 years
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When the use of an investment property changes such that it is reclassified as property, plant and equipment, its fair value at the date of reclassification becomes its cost for subsequent accounting.

(k) Property, plant and equipment

(i) Recognition and measurement

Items of property, plant and equipment are measured at cost less accumulated depreciation and accumulated impairment losses. Cost includes expenditure that is directly attributed to the acquisition of the asset. The cost of a self-constructed asset comprises material, labor, any cost directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management, the initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located, and any borrowing cost that eligible for capitalization. Cost also includes transfers from equity of any gain or loss on qualifying cash flow hedges of foreign currency purchases of property, plant and equipment. The cost of the software is capitalized as part of the property, plant and equipment if the purchase of the software is necessary for the property, plant and equipment to be capable of operating.

Each part of an item of property, plant and equipment with a cost that is significant in relation to the total cost of the item shall be depreciated separately.

The gain or loss arising from the derecognition of an item of property, plant and equipment is determined based on the difference between the net disposal proceeds, if any, and the carrying amount of the item, and is recognized in profit or loss, under other gains and losses.

(ii) Reclassification to investment property

A property is reclassified to investment property at its carrying amount when the use of the property changes from owner-occupied to investment property.

(iii) Subsequent cost

Subsequent expenditure is capitalized only when it is probable that future economic benefits associated with the expenditure will flow to the Group. The carrying amount of those parts that are replaced is derecognized. Ongoing repairs and maintenance is expensed as incurred.

(iv) Depreciation

Depreciation is calculated on the depreciable amount of an asset using the straight-line basis over its useful life. The depreciable amount of an asset is determined based on the cost less its residual value. Items of property, plant and equipment with the same useful life may be grouped in determining the depreciation charge. The remainder of the items may be depreciated separately. The depreciation charge for each period is recognized in profit or loss.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

The depreciable amount of a leased asset is allocated to each accounting period during the period of expected use on a systematic basis consistent with the depreciation policy the lessee adopts for depreciable assets that are owned. If there is reasonably certainty that the lessee will obtain ownership by the end of the lease term, the asset is depreciated over the shorter of the lease term and its useful life.

Land has an unlimited useful life and therefore is not depreciated.

The estimated useful lives for the current and comparative years of significant items of property, plant and equipment are as follows:

Buildings	1-50 years
Machinery	1-10 years
Instrument equipment	3-10 years
Office and other equipment	2-10 years
Miscellaneous equipment	1-25 years

Depreciation methods, useful lives, and residual values are reviewed at each reporting date. If expectation of useful life differs from the previous estimate, the change is accounted for as a change in an accounting estimate.

(l) Leased assets

(i) Lessor

Leased asset under finance lease is recognized on a net basis as lease receivable. Initial direct costs incurred in negotiating and arranging an operating lease is added to the net investment of the leased asset. Finance income is allocated to each period during the lease term in order to produce a constant periodic rate of interest on the remaining balance of the receivable.

Lease income from operating lease is recognized in profit or loss on a straight-line basis over the lease term. Initial direct costs incurred in negotiating and arranging an operating lease is added to the carrying amount of the leased asset and recognized as an expense over the lease term on the same basis as the lease income. Incentives granted to the lessee to enter into the operating lease are spread over the lease term on a straight-line basis so that the lease income received is reduced accordingly.

Contingent rents are recognized as income in the period when the lease adjustments are confirmed.

(ii) Lessee

Leases in which the Group assumes substantially all of the risks and rewards of ownership are classified as finance leases. On initial recognition, the lease asset is measured at an amount equal to the lower of its fair value and the present of the minimum lease payments. Subsequent to initial recognition, the asset is accounted for in accordance with the accounting policy applicable to the asset.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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Minimum lease payments made under finance leases are apportioned between the finance expense and the reduction of the outstanding liability. The finance expense is allocated to each period during the lease term in order to produce a constant periodic rate of interest on the remaining balance of the liability.

Other leases are accounted for operating leases and the lease assets are not recognized in the Group's consolidated balance sheets.

Payments made under operating lease (excluding insurance and maintenance expenses) are recognized in profit or loss on a straight-line basis over the term of the lease. Lease incentives received are recognized as an integral part of the total lease expense, over the term of the lease.

Contingent rent is recognized as expense in the periods in which they are incurred.

At inception of an arrangement, the Group determines whether such an arrangement is or contains a lease, which involves the following two criteria:

- 1) The fulfillment of the arrangement is dependent on the use of a specific asset or assets; and
- 2) The arrangement contains a right to use the asset.

At inception or on reassessment of the arrangement, if an arrangement contains a lease, that lease is classified as a finance lease or an operating lease. The Group separates payments and other consideration required by such an arrangement into those for the lease and those for other elements on the basis of their relative fair values. If the Group concludes for a finance lease that it is impracticable to separate the payment reliably, then an asset and a liability are recognized at an amount equal to the fair value of the underlying asset. Subsequently, the liability is reduced as payments are made and an imputed finance cost on the liability is recognized using the Group's incremental borrowing rate. If the Group concludes for an operating lease that it is impracticable to separate the payment reliably, then treat all payments under the arrangement as lease payments, and disclose the situation accordingly.

Prepaid lease payments represent land use rights under long-term operating lease arrangement and are expensed equally over 38 to 67 years.

(m) Intangible assets

(i) Goodwill

1) Recognition

Goodwill arising from the acquisition of subsidiaries is recognized as intangible assets.

2) Measurement

Goodwill is measured at its cost less impairment losses. Investments in associates are accounted for using the equity method. The carrying amount of the investment in associates includes goodwill, which kind of investment of impairment losses are recognized as a part of the carrying amount of the investment, not allocated to goodwill and any other assets.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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(ii) Other Intangible Assets

Other intangible assets that are acquired by the Group are measured at cost less accumulated amortization and any accumulated impairment losses.

(iii) Subsequent Expenditure

Subsequent expenditure is capitalized only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditures, including expenditure on internally generated goodwill and brands, is recognized in profit or loss as incurred.

(iv) Amortization

Depreciable amount of intangible asset is calculated based on the cost of an asset less its residual values.

Amortization is recognized in profit or loss on a straight-line basis over the estimated useful lives of intangible assets, other than goodwill and intangible assets with indefinite useful life, from the date when they are made available for use. The estimated useful lives of intangible assets for the current and comparative periods are as follows:

Computer software cost	0-10 years
Trademark rights	5 years
Intangible assets in development	3-10 years

The residual value, the amortization period and the amortization method for an intangible asset with a finite useful life are reviewed at least at each reporting date. Any change thereof is accounted for as a change in accounting estimate.

(n) Impairment – Non-financial assets

The Group assesses non-financial assets for impairment (except for inventories, deferred income tax assets and employee benefits) at every reporting date, and estimates its recoverable amount.

If it is not possible to determine the recoverable amount (fair value less cost to sell and value in use) for the individual asset, then the Group will have to determine the recoverable amount for the asset's cash-generating unit (CGU).

The recoverable amount for individual asset or a cash-generating unit is the higher of its fair value less costs to sell and its value in use. If, and only if, the recoverable amount of an asset is less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. Such is deemed as an impairment loss, which is recognized immediately in profit or loss.

The Group assess at the end of each reporting period whether there is any indication that an impairment loss recognized in prior periods for an asset other than goodwill may no longer exist or may have decreased. If any such indication exists, the recoverable amount of that asset is estimated.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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An impairment loss recognized in prior periods for an asset other than goodwill is reversed if, and only if, there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognized. In this case, the carrying amount of the asset is increased to its recoverable amount by reversing an impairment loss.

Notwithstanding whether indicators exist, goodwill and intangible assets with indefinite useful lives or those not yet in use are required to be tested at least annually. Impairment loss is recognized if the recoverable amount is less than the carrying amount.

For the purpose of impairment testing, goodwill acquired in a business combination, from the acquisition date, is allocated to each of the acquirer's cash-generating units, or groups of cash-generating units, irrespective of whether other assets or liabilities of the acquiree are assigned to those units or group of units.

If the carrying amount of the cash-generating units exceeds the recoverable amount of the unit, impairment loss is recognized and is allocated to reduce the carrying amount of each asset in the unit.

Reversal of an impairment loss for goodwill is prohibited.

(o) Provisions

A provision is recognized if, as a result of a past event, the Group has a present legal or constructive obligation that can be estimated reliably, and an outflow of economic benefits is possibly required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects the current market assessments of the time value of money and the risks specific to the liability. The unwinding of the discount is recognized as finance cost.

The Group has adopted IFRIC 21 "Levies" which prescribes the initial application date effective January 1, 2017. According to the Interpretation, the obligating event that gives rise to a liability to pay a levy is the activity that triggers the payment of a levy, as identified by the legislation.

(p) Treasury stock

Repurchased shares are recognized as treasury shares (a contra-equity account) based on its repurchase price (including all directly accountable costs), net of tax. Gains on disposal of treasury shares are accounted for as Capital Reserve – Treasury Shares Transactions. Losses on disposal of treasury shares are offset against existing capital reserve arising from similar types of treasury shares. If the capital reserve is insufficient, such losses are charged to retained earnings. The carrying amount of treasury shares is calculated using the weighted average method for different types of repurchase.

If treasury shares are cancelled, Capital Reserve – Share Premiums and Share Capital are debited proportionately. Gains on cancellation of treasury shares are charged to capital reserves arising from similar types of treasury shares. Losses on cancellation of treasury shares are offset against existing capital reserves arising from similar types of treasury shares. If capital reserve is insufficient such losses are charged to retained earnings.

Company shares that are owned by the Company's subsidiaries are treated as treasury stock.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

(q) Revenue

(i) Goods sold

Revenue from the sale of goods in the course of ordinary activities is measured at fair value of the consideration received or receivable, net of returns, trade discounts and volume rebates. Revenue is recognized when persuasive evidence exists, usually in the form of an executed sales agreement, that the significant risks and rewards of ownership have been transferred to the customer, recovery of the consideration is probable, the associated costs and possible return of goods can be estimated reliably, there is no continuing management involvement with the goods, and the amount of revenue can be measured reliably. If it is probable that discounts will be granted and the amount can be measured reliably, then the discount is recognized as a reduction of revenue as the sales are recognized. Allowances for sales returns and allowances are estimated and recognized in provisions based on historical experiences when goods are sold.

The timing of the transfers of risks and rewards varies depending on the individual terms of the sales agreement.

(ii) Service

Revenue from services rendered is recognized in profit or loss in proportion to the stage of completion of the transaction at the reporting date. The stage of completion is assessed by reference to surveys of work performed. Only when the result of the transactions is difficult to estimate, revenues are recognized within the cost that are very possibly recovered.

(r) Employee benefits

(i) Defined contribution plans

Obligations for contributions to defined contribution pension plans are recognized as an employee benefit expense in profit or loss in the periods during which services are rendered by employees.

(ii) Defined benefit plans

A defined benefit plan is a post-employment benefit plan other than a defined contribution plan. The Group's net obligation in respect of defined benefit pension plans is calculated separately for each plan by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods; that benefit is discounted to determine its present value. The fair value of any plan assets is deducted from the aforesaid discounted present value. The discount rate is the yield at the reporting date on (market yields of high quality government bonds) bonds that have maturity dates approximating the terms of the Group's obligations and that are denominated in the same currency in which the benefits are expected to be paid.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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The calculation of defined benefit obligation is performed annually by a qualified actuary using the projected unit credit method. When the calculation results in a benefit to the Group, the recognized asset is limited to the present value of economic benefits available in the form of any future refunds from the plan or reductions in future contributions to the plan. In order to calculate the present value of economic benefits, consideration is given to any minimum funding requirements that apply to any plan in the Group. An economic benefit is available to the Group if it is realizable during the life of the plan, or on settlement of the plan liabilities.

When the benefits of a plan are improved, the portion of the increased benefit relating to past service by employees is recognized in profit or loss immediately.

Re-measurement of net defined benefit liability (asset) (including actuarial gains, losses and the return on plan asset and changes in the effect of the asset ceiling, excluding any amounts included in net interest) is recognized in other comprehensive income (loss). The effect of re-measurement of the defined benefit plan is charged to retained earnings.

The Group recognizes gains or losses on the curtailment or settlement of a defined benefit plan when the curtailment or settlement occurs. The gain or loss on curtailment comprises any resulting change in the fair value of plan assets and change in the present value of defined benefit obligation.

(iii) Short-term employee benefits

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided.

A liability is recognized for the amount expected to be paid under short-term cash bonus or profit-sharing plans if the Group has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee, and the obligation can be estimated reliably.

(s) Share-based payment

The grant-date fair value of share-based payment awards granted to employee is recognized as employee expenses, with a corresponding increase in equity, over the period that the employees become unconditionally entitled to the awards. The amount recognized as an expense is adjusted to reflect the number of awards which the related service and non-market performance conditions are expected to be met, such that the amount ultimately recognized as an expense is based on the number of award that meet the related service and non-market performance conditions at the vesting date.

For share-based payment awards with non-vesting conditions, the grant-date fair value of the share-based payment is measured to reflect such conditions and there is no true-up for differences between expected and actual outcomes.

The fair value of the amount payable to employees in respect of share appreciation rights, which are settled in cash, is recognized as an expense with a corresponding increase in liabilities, over the period that the employees become unconditionally entitled to payment. The liability is re-measured at each reporting date and settlement date. Any change in the fair value of the liability is recognized as personnel expenses in profit or loss.

The grant date of share-based payment is the record date of capital increase passed by shareholders' meeting.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

(t) Income Taxes

Income tax expenses include both current taxes and deferred taxes. Except for expenses that are related to business combinations, expenses recognized in equity or other comprehensive income directly, and other related expenses, all current and deferred taxes are recognized in profit or loss.

Current taxes include tax payables and tax deduction receivables on taxable gains (losses) for the year calculated using the statutory tax rate on the reporting date or the actual legislative tax rate, as well as tax adjustments related to prior years.

Deferred taxes arise due to temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and their respective tax bases. Deferred taxes are not recognized for the following:

- (i) Assets and liabilities that are initially recognized from non-business combination transactions, with no effect on net income or taxable gains (losses).
- (ii) Temporary differences arising from equity investments on subsidiaries or joint ventures, where there is a high probability that such temporary differences will not reverse.
- (iii) Initial recognition of goodwill.

Deferred taxes are measured based on the statutory tax rate on the reporting date or the actual legislative tax rate during the year of expected asset realization or debt liquidation.

Deferred tax assets and liabilities may be offset against each other if the following criteria are met:

- (i) if the entity has the legal right to settle tax assets and liabilities on a net basis; and
- (ii) the taxing of deferred tax assets and liabilities fulfill one of the below scenarios:
  - 1) levied by the same taxing authority; or
  - 2) levied by different taxing authorities, but where each such authority intend to settle tax assets and liabilities (where such amounts are significant) on a net basis every year of the period of expected asset realization or debt liquidation; or where the timing of asset realization and debt liquidation is matched.

A deferred tax asset is recognized for unused tax losses available for carry-forward, unused tax credits and deductible temporary differences to the extent that it is probable that future taxable profit will be available against which the unused tax losses, unused tax credits and deductible temporary differences can be utilized. Such unused tax losses, unused tax credits and deductible temporary differences are also re-evaluated every year on the financial reporting date, and adjusted based on the probability that future taxable profit will be available against which the unused tax losses, unused tax credits and deductible temporary differences can be utilized.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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(u) Business combination

Goodwill is measured at the consideration transferred less amounts of the identifiable assets acquired and the liabilities assumed (generally at fair value) at the acquisition date. If the amounts of net assets acquired or liabilities assumed exceeds the acquisition price, the Group shall re-assess whether it has correctly identified all of the assets acquired and liabilities assumed, and recognize a gain for the excess.

If the business combination achieved in batches, non-controlling equity interest is measured either at fair value at acquisition-date or at the share of the acquirer's identifiable net assets in each acquisition.

In a business combination achieved in batches, the previously held equity interest in the acquiree at its acquisition-date fair value is re-measured and the resulting gain or loss, if any, is recognized in profit or loss.

If the initial accounting for a business combination is incomplete by the end of the reporting period in which the combination occurs, provisional amounts for the items for which the accounting is incomplete are reported in the Group's financial statements. During the measurement period, the provisional amounts recognized are retrospectively adjusted at the acquisition date, or additional assets or liabilities are recognized to reflect new information obtained about facts and circumstances that existed as of the acquisition date. The measurement period shall not exceed one year from the acquisition date.

All transaction costs relating to business combination are recognized immediately as expenses when incurred, except for the issuance of debt or equity instruments.

Business combinations under common control are accounted in the later date of the earliest period financial reports are expressed and the establishment date of common control. Assets and liabilities of the merged entities are recognized at their carrying amount in the non-consolidated financial statements.

(v) Government grant

A government grant is recognized only when there is reasonable assurance that the entity will comply with any conditions attached to the grant and the grant will be received.

The grant is recognized as income over the period necessary to match them with the related costs, for which they are intended to compensate, on a systematic basis. If the grant is used for reimburse loss and expenses that have happened or for immediate financial aid for the Company and no future related cost, it can be recognized gain at the time the Company acquires.

A grant relating to assets is presented as deferred income. If a grant is related to depreciable assets, the grant is recognized over the useful life of the assets and for a grant related to a non-depreciable asset, the grant is credited to income over the same period over which the cost is charged to income.

(Continued)

**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

(w) Earnings per share

Disclosures are made of basic and diluted earnings per share attributable to ordinary equity holders of the Company. The basic earnings per share is calculated based on the profit attributable to the ordinary shareholders of the Company divided by weighted average number of ordinary shares outstanding. The diluted earnings per share is calculated based on the profit attributable to ordinary shareholders of the Company, divided by weighted average number of ordinary shares outstanding after adjustment for the effects of all potentially dilutive ordinary shares, such as remuneration of employees and employee stock options.

(x) Operating segments

An operating segment is a component of the Group that engages in business activities from which it may incur revenues and incur expenses (including revenues and expenses relating to transactions with other components of the Group). Operating results of the operating segment are regularly reviewed by the Group's chief operating decision maker to make decisions about resources to be allocated to the segment and assess its performance. Each operating segment consists of standalone financial information.

**(5) Significant accounting assumptions and judgments, and major sources of estimation uncertainty:**

The preparation of the financial statements in conformity with the IFRSs endorsed by the FSC requires management to make judgments, estimates, and assumptions that affect the application of the accounting policies and the reported amount of assets, liabilities, income, and expenses. Actual results may differ from these estimates.

The management continues to monitor the accounting estimates and assumptions. The management recognizes any changes in accounting estimates during the period and the impact of those changes in accounting estimates in the next period.

(a) Judgment regarding control of subsidiaries

Due to significant judgments involved and material impact on recognized amounts for consolidated financial report, please refer to Notes 4(c) and 6(f) for details.

(b) Valuation of inventories

Regarding assumptions and estimation uncertainties, valuation of inventories has a significant risk of resulting in a material adjustment within the next financial year. As inventories are stated at the lower of cost or net realizable value, the Group estimates the net realizable value of inventories for obsolescence and unmarketable items at the end of the reporting period and then writes down the cost of inventories to net realizable value. The net realizable value of the inventory is mainly determined based on assumptions as to future demand within a specific time horizon. Due to the rapid industrial transformation, there may be significant changes in the net realizable value of inventories. Please refer to Note 6(d) for further description of the valuation of inventories.

(Continued)

**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

**(6) Explanation of significant accounts:**

(a) Cash and cash equivalents

	<b>December 31, 2017</b>	<b>December 31, 2016</b>
Cash on hand	\$ 16,139	16,143
Cash in banks	23,429,025	34,381,705
Time deposits	83,998,960	74,218,714
Cash equivalents-repurchase bonds	-	96,750
	<b><u>\$ 107,444,124</u></b>	<b><u>108,713,312</u></b>

- (i) The above cash and cash equivalents were not pledged as collateral. Pledged time deposits were accounted for under other financial assets. Please refer to Notes 6(k) and 8 for details.
- (ii) Please refer to Note 6(aa) for the fair value sensitivity analysis and interest rate risk of the financial assets and liabilities of the Group.

(b) Investment in financial assets and liabilities

- (i) The components of financial assets and liabilities were as follows:

	<b>December 31, 2017</b>	<b>December 31, 2016</b>
Financial assets at fair value through profit or loss – current:		
Held-for-trading		
Shares of stock of listed companies	\$ 351,785	270,926
Beneficiary certificates	<u>2,473,128</u>	<u>4,096,921</u>
Total	<b><u>\$ 2,824,913</u></b>	<b><u>4,367,847</u></b>
Available-for-sale financial assets – current:		
Shares of stock of overseas listed companies	<b><u>\$ 384,782</u></b>	<b><u>266,523</u></b>
Available-for-sale financial assets – noncurrent:		
Shares of stock of listed companies	\$ 721,071	610,702
Equity securities – common stock	<u>437,760</u>	<u>178,920</u>
Total	<b><u>\$ 1,158,831</u></b>	<b><u>789,622</u></b>
Financial assets carried at cost – noncurrent:		
Equity securities – common stock	\$ 152,853	165,450
Equity securities – preferred stock	<u>197,656</u>	<u>205,632</u>
Total	<b><u>\$ 350,509</u></b>	<b><u>371,082</u></b>

(Continued)

**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

- 1) For the years ended December 31, 2017 and 2016, the Group recognized a net gain on financial assets reported at fair value through profit or loss of \$146,321, and \$67,790, respectively.
  - 2) For the years ended December 31, 2017 and 2016, the unrealized gain on available-for-sale financial assets amounted to \$541,228, and \$124,524, respectively.
  - 3) Considering that the range of reasonable fair value estimates is large and the probability for each estimate cannot be reasonably determined, the Group management believes the fair value cannot be measured reliably. Therefore, the aforementioned investments held by the Group are measured at amortized cost less impairment at each reporting date. The Group evaluated the carrying value and the recoverable amount of the investments and recognized impairment loss of \$20,573 and \$0 for the years ended December 31, 2017 and 2016, respectively. As of December 31, 2017 and 2016, the Group had accumulated impairment loss of \$275,384, and \$254,811, respectively.
  - 4) Please refer to Note 6(y) for further discussion on gains and losses on disposal of investments.
  - 5) Please refer to Note 6(aa) for the Group's information on financial instruments risk management.
  - 6) As of December 31, 2017 and 2016, the aforesaid financial assets were not pledged as collateral.
- (ii) Fair value sensitivity analysis

If the equity price changes, the impact of equity price change to other comprehensive income will be as follows, assuming the analysis is based on the same basis for both years and assuming that all other variables considered in the analysis remain the same:

	<b>For the years ended December 31</b>			
	<b>2017</b>		<b>2016</b>	
	<b>Comprehensive Income (Loss) (net of tax)</b>	<b>Net Income (Loss) (net of tax)</b>	<b>Comprehensive Income (Loss) (net of tax)</b>	<b>Net Income (Loss) (net of tax)</b>
Increase 3%	\$ 46,308	84,747	31,684	131,035
Decrease 3%	\$ (46,308)	(84,747)	(31,684)	(131,035)

- (iii) Foreign equity investments

Significant foreign equity investments at the end of each period were as follows:

(Unit: Foreign currency/NTD in Thousands)

	<b>December 31, 2017</b>			<b>December 31, 2016</b>		
	<b>Foreign Currency</b>	<b>Exchange Rate</b>	<b>NTD</b>	<b>Foreign Currency</b>	<b>Exchange Rate</b>	<b>NTD</b>
	USD	\$ 10,992	29.760	327,122	10,992	32.250
CNY	84,484	4.5545	384,782	57,329	4.6490	266,523

(Continued)

**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

(iv) Derivative not used for hedging

Derivative financial instruments are used to hedge certain foreign exchange and interest risk the Group is exposed to, arising from its operating, investing and financial activities. As of December 31, 2017 and 2016 the Group did not have related transactions that do not qualify for hedge accounting presented as held-for-trading financial assets and financial liability.

(c) Notes and accounts receivable and other receivables, net

	<u>December 31, 2017</u>	<u>December 31, 2016</u>
Notes receivable	\$ 52,010	96,170
Accounts receivable	151,085,518	95,115,492
Other receivables	1,504,367	42,605,518
Less: Allowance for impairment	<u>(1,736,810)</u>	<u>(1,910,613)</u>
	<u><u>\$ 150,905,085</u></u>	<u><u>135,906,567</u></u>

- (i) Refer to Note 6(aa) for the Group's notes receivable, accounts receivable and other receivables exposure to credit risk and currency risk, and the impairment evaluation of notes receivable, accounts receivable and other receivables.
- (ii) Accounts receivable which are transferred in accordance with derecognition standards of IFRS are deemed as sale of accounts receivable. As of December 31, 2017 and 2016, the Company sold its accounts receivable without recourse as follows:

<u>December 31, 2017</u>						
<u>Purchaser</u>	<u>Assignment Facility</u>	<u>Factoring Line</u>	<u>Advanced Amount</u>	<u>Collateral</u>	<u>Significant Factoring Terms</u>	<u>Derecognition Amount</u>
ANZ (Note)	<u>\$ 2,976,000</u>	<u>USD 1,200,000,000</u>	<u>USD 100,000,000</u>	None	The accounts receivable factoring is without recourse but the seller still bears the risks except for eligible obligor's insolvency.	<u>\$ 2,976,000</u>
<u>December 31, 2016</u>						
<u>Purchaser</u>	<u>Assignment Facility</u>	<u>Factoring Line</u>	<u>Advanced Amount</u>	<u>Collateral</u>	<u>Significant Factoring Terms</u>	<u>Derecognition Amount</u>
ANZ (Note)	<u>\$ 38,700,000</u>	<u>USD 1,200,000,000</u>	<u>USD -</u>	None	The accounts receivable factoring is without recourse but the seller still bears the risks except for eligible obligor's insolvency.	<u>\$ 38,700,000</u>

Note: In October 2016, the Company signed a one year joint accounts receivable factoring agreement with ANZ Bank and six other banks where each bank will factor on pro-rata basis.

For the years ended December 31, 2017 and 2016, the Company recognized a fee and interest on bank advance payment of \$67,933 and \$66,988, respectively, from the factoring of accounts receivable, which was accounted under financial costs in the statement of comprehensive income. Also, the difference of \$0, and \$38,700,000 between the carrying value of factored accounts receivable and the amount advanced was accounted under other receivables as of December 31, 2017 and 2016, respectively.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

- (iii) As of December 31, 2017 and 2016, KINSUS INTERCONNECT TECHNOLOGY CORP. sold its accounts receivable without recourse as follows:

December 31, 2017						
Purchaser	Assignment Facility	Factoring Line (thousands)	Advanced Amount	Collateral	Significant Factoring Terms	Derecognition Amount
Mega International Commercial Bank	\$ <u>218,494</u>	USD <u>30,000</u>	\$ <u>89,303</u>	None	The accounts receivable factoring is without recourse	\$ <u>218,494</u>

December 31, 2016						
Purchaser	Assignment Facility	Factoring Line (thousands)	Advanced Amount	Collateral	Significant Factoring Terms	Derecognition Amount
Mega International Commercial Bank	\$ <u>249,402</u>	USD <u>30,000</u>	\$ <u>49,298</u>	None	The accounts receivable factoring is without recourse	\$ <u>249,402</u>

- (d) Inventories

	December 31, 2017	December 31, 2016
Merchandise	\$ 882,380	629,690
Finished goods	79,536,751	65,797,600
Work in process	16,687,884	17,624,217
Raw materials	33,666,478	28,203,409
Subtotal	130,773,493	112,254,916
Less: Allowance for inventory market decline and obsolescence	(6,898,500)	(4,935,514)
Total	\$ <u>123,874,993</u>	<u>107,319,402</u>

For the years ended December 31, 2017 and 2016, the components of cost of goods sold were as follows:

	For the years ended December 31	
	2017	2016
Cost of goods sold	\$ 1,134,712,441	1,067,674,727
Provision on (Reversal of) inventory market price decline	1,962,986	(1,519,661)
Loss on disposal of inventory	9,263,307	27,187,138
Unallocated manufacturing overhead	1,177,097	1,254,990
Loss on physical inventory	22,795	45,802
	\$ <u>1,147,138,626</u>	<u>1,094,642,996</u>

For the year ended December 31, 2017, the Group recognized a provision on inventory market price decline of \$1,962,986, which was charged to profit or loss under cost of goods sold. The gain was recognized from the reversal of provision arising from destocking for the year ended December 31, 2016 of \$1,519,661. Such gain was deducted from cost of goods sold.

As of December 31, 2017 and 2016, the aforesaid inventories were not pledged as collateral.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

(e) Investments accounted for using equity method

- (i) The Group's financial information for investments in individually insignificant associates accounted for using equity method at reporting date was as follows. These financial information are included in the consolidated financial statements.

	<b>December 31, 2017</b>	<b>December 31, 2016</b>
Individually insignificant associates	<b>\$ 503,718</b>	<b>362,909</b>
	<b>For the years ended December 31</b>	<b>2017</b>
	<b>2016</b>	<b>2016</b>
The Group's share of profit (loss) of the associates		
Loss for the year	(4,484)	(3,131)
Other comprehensive income (loss)	167,389	(48,217)
Total comprehensive income (loss)	<b>162,905</b>	<b>(51,348)</b>

- (ii) As of December 31, 2017 and 2016, the aforesaid investments accounted for using equity method were not pledged as collateral.

(f) Loss of control of a subsidiary

On June 29, 2016, the shareholders of Ability Enterprise Co., Ltd. elected new set of directors during the shareholders' meeting, so that the Group lost its control over Ability Enterprise Co., Ltd. as the Group is unable to acquire more than half of the voting rights of the board of directors. This resulted in a disposal loss of \$561,251 which was charged to the statement of comprehensive income. The aforementioned loss was measured at the fair value of its equity ownership of 11.73% amounting to \$551,799 as of June 29, 2016.

The derecognized assets and liabilities of Ability as of June 29, 2016, were as follows:

Cash and cash equivalents	\$	3,674,323
Inventories		1,336,460
Accounts receivable and other receivables		1,544,508
Property, plant, and equipment		3,454,631
Investment property		633,185
Intangible assets		174,304
Other assets		2,025,903
Short-term loans		(399,487)
Accounts payable and other payables		(3,245,865)
Other liabilities		(624,136)
	<b>\$</b>	<b>8,573,826</b>

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

(g) Subsidiaries that have material non-controlling interest

Subsidiaries that have material non-controlling interest were as follows:

<u>Subsidiaries</u>	<u>Country of registration</u>	<u>Equity ownership of non-controlling interest</u>	
		<u>December 31, 2017</u>	<u>December 31, 2016</u>
KINSUS and its subsidiaries	Taiwan	61.00 %	60.96 %
ABILITY and its subsidiaries	Taiwan	-	-
ASROCK and its subsidiaries	Taiwan	44.13 %	41.35 %
CASETEK CAYMAN	Taiwan/ Cayman	39.53 %	39.27 %

The following information of the aforementioned subsidiaries have been prepared in accordance with the Regulations Governing the Preparation of Financial Reports by Securities Issuers. Included in these information are the fair value adjustment made during the acquisition and relevant difference in accounting principles between the Company and its subsidiaries as at acquisition date. Intra-group transactions were not eliminated in this information.

(i) Information regarding KINSUS and its subsidiaries

	<u>December 31, 2017</u>	<u>December 31, 2016</u>
Current assets	\$ 18,774,402	21,615,555
Non-current assets	23,503,075	19,638,160
Current liabilities	(10,537,887)	(8,639,797)
Non-current liabilities	<u>(1,824,592)</u>	<u>(1,599,149)</u>
Net assets	<u>\$ 29,914,998</u>	<u>31,014,769</u>
Non-controlling interest	<u>\$ 17,744,607</u>	<u>18,151,995</u>
	<u>For the years ended December 31</u>	
	<u>2017</u>	<u>2016</u>
Operating revenue	<u>\$ 22,335,486</u>	<u>23,165,066</u>
Net income for the year	\$ 335,322	2,073,028
Other comprehensive loss	<u>(110,417)</u>	<u>(326,985)</u>
Comprehensive income	<u>\$ 224,905</u>	<u>1,746,043</u>
Net income attribute to non-controlling interest	<u>\$ 436,428</u>	<u>1,446,006</u>
Comprehensive income attribute to non-controlling interest	<u>\$ 388,981</u>	<u>1,325,193</u>
Cash flows from operating activities	\$ 6,002,634	5,752,676
Cash flows from investing activities	(6,805,361)	(4,971,181)
Cash flows from financing activities	<u>(6,037)</u>	<u>(2,312,646)</u>
Net decrease in cash and cash equivalents	<u>\$ (808,764)</u>	<u>(1,531,151)</u>

(Continued)

**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

(ii) Information regarding ABILITY and its subsidiaries

	<u>December 31, 2017</u>	<u>December 31, 2016</u>
Current assets	\$ -	-
Non-current assets	-	-
Current liabilities	-	-
Non-current liabilities	-	-
Net assets	<u>\$ -</u>	<u>-</u>
Non-controlling interest	<u>\$ -</u>	<u>-</u>
	<u>For the years ended December 31</u>	
	<u>2017</u>	<u>2016 Jan.-Jun. (Note)</u>
Operating revenue	<u>\$ -</u>	<u>5,758,572</u>
Net income for the period	\$ -	48,287
Other comprehensive income	-	30,123
Comprehensive income	<u>\$ -</u>	<u>78,410</u>
Net income attribute to non-controlling interest	<u>\$ -</u>	<u>48,655</u>
Comprehensive income attribute to non-controlling interest	<u>\$ -</u>	<u>74,224</u>
Cash flows from operating activities	\$ -	213,863
Cash flows from investing activities	-	(205,297)
Cash flows from financing activities	-	(11,498)
Net decrease in cash and cash equivalents	<u>\$ -</u>	<u>(2,932)</u>

Note: As disclosed in Note 6(f), the Group ceased control over Ability Enterprise Co., Ltd. on June 29, 2016, so only the financial information for the six months ended June 30, 2016 was disclosed above.

(iii) Information regarding ASROCK and its subsidiaries

	<u>December 31, 2017</u>	<u>December 31, 2016</u>
Current assets	\$ 8,605,071	7,751,292
Non-current assets	362,132	330,798
Current liabilities	(3,252,207)	(2,438,731)
Non-current liabilities	(23,003)	(15,879)
Net assets	<u>\$ 5,691,993</u>	<u>5,627,480</u>
Non-controlling interest	<u>\$ 2,534,768</u>	<u>2,309,248</u>

(Continued)

**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

	<b>For the years ended December 31</b>	
	<b>2017</b>	<b>2016</b>
Operating revenue	\$ <u>9,211,647</u>	<u>7,120,620</u>
Net income for the year	442,487	123,375
Other comprehensive loss	(315,501)	(64,830)
Comprehensive income	\$ <u>126,986</u>	<u>58,545</u>
Net income attribute to non-controlling interest	\$ <u>171,793</u>	<u>29,750</u>
Comprehensive income attribute to non-controlling interest	\$ <u>41,793</u>	<u>340</u>
Cash flows from operating activities	\$ 404,572	541,030
Cash flows from investing activities	(745,570)	8,117
Cash flows from financing activities	(35,676)	(287,604)
Net (decrease) increase in cash and cash equivalents	\$ <u>(376,674)</u>	<u>261,543</u>
 (iv) Information regarding CASETEK CAYMAN		
	<b>December 31,</b>	<b>December 31,</b>
	<b>2017</b>	<b>2016</b>
Current assets	\$ 24,532,609	28,863,585
Non-current assets	24,376,375	21,739,451
Current liabilities	(13,006,681)	(19,445,716)
Non-current liabilities	(7,348,521)	(2,412,077)
Net assets	\$ <u>28,553,782</u>	<u>28,745,243</u>
Non-controlling interest	\$ <u>11,325,194</u>	<u>11,287,107</u>
	<b>For the years ended December 31</b>	
	<b>2017</b>	<b>2016</b>
Operating revenue	\$ <u>33,253,215</u>	<u>32,763,310</u>
Net income for the year	\$ 1,656,491	2,801,624
Other comprehensive loss	(566,263)	(2,340,299)
Comprehensive income	\$ <u>1,090,228</u>	<u>461,325</u>
Net income attribute to non-controlling interest	\$ <u>652,240</u>	<u>1,100,086</u>
Comprehensive income attribute to non-controlling interest	\$ <u>428,498</u>	<u>176,272</u>
Cash flows from operating activities	\$ 4,926,571	5,188,093
Cash flows from investing activities	(6,458,042)	(6,529,986)
Cash flows from financing activities	(1,932,221)	2,075,656
Net (decrease) increase in cash and cash equivalents	\$ <u>(3,463,692)</u>	<u>733,763</u>

(Continued)

**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

(h) Property, plant and equipment

The movements in the cost, depreciation, and impairment of the property, plant and equipment of the Group for the years ended December 31, 2017 and 2016 were as follows:

	<u>Land</u>	<u>Buildings</u>	<u>Machinery and equipment</u>	<u>Instrument equipment</u>	<u>Other facilities</u>	<u>Construction in progress</u>	<u>Total</u>
<b>Cost or deemed cost:</b>							
Balance on January 1, 2017	\$ 4,320,454	41,981,188	55,592,564	1,471,421	22,666,711	6,140,308	132,172,646
Additions	-	2,296,433	7,757,178	80,065	5,357,531	4,854,351	20,345,558
Disposals and obsolescence	-	(304,006)	(3,297,134)	(120,600)	(2,566,241)	-	(6,287,981)
Reclassifications	47,287	1,693,046	6,032,557	106,673	3,080,897	(4,355,037)	6,605,423
Effect of movement in exchange rate	(5,812)	(1,897,336)	(1,502,154)	(84,377)	(1,144,338)	(111,396)	(4,745,413)
Balance on December 31, 2017	<u>\$ 4,361,929</u>	<u>43,769,325</u>	<u>64,583,011</u>	<u>1,453,182</u>	<u>27,394,560</u>	<u>6,528,226</u>	<u>148,090,233</u>
Balance on January 1, 2016	\$ 5,580,222	41,312,837	58,970,443	1,559,813	25,442,907	6,164,893	139,031,115
Additions	-	1,201,866	2,507,628	115,842	1,696,725	7,095,931	12,617,992
Disposals and obsolescence	-	(683,866)	(3,907,119)	(112,741)	(2,508,785)	-	(7,212,511)
Reclassifications	4,642	4,398,938	4,180,183	11,438	1,986,181	(6,254,585)	4,326,797
Effect of movement in exchange rate	(15,462)	(2,818,941)	(3,587,843)	(102,931)	(1,490,261)	(339,203)	(8,354,641)
Loss of control of a subsidiary	(1,248,948)	(1,429,646)	(2,570,728)	-	(2,460,056)	(526,728)	(8,236,106)
Balance on December 31, 2016	<u>\$ 4,320,454</u>	<u>41,981,188</u>	<u>55,592,564</u>	<u>1,471,421</u>	<u>22,666,711</u>	<u>6,140,308</u>	<u>132,172,646</u>
<b>Depreciation and impairment loss :</b>							
Balance on January 1, 2017	\$ -	13,531,902	35,312,005	1,189,276	15,278,654	-	65,311,837
Depreciation for the year	-	2,156,554	6,685,271	178,271	3,852,111	-	12,872,207
Reversal of impairment loss	-	(4)	(44,650)	(7)	(10,386)	-	(55,047)
Reclassifications	-	100,870	(95,680)	59,255	58,071	-	122,516
Disposals and obsolescence	-	(296,890)	(2,816,532)	(118,285)	(2,321,982)	-	(5,553,689)
Effect of movement in exchange rate	-	(629,233)	(1,146,892)	(78,238)	(828,499)	-	(2,682,862)
Balance on December 31, 2017	<u>\$ -</u>	<u>14,863,199</u>	<u>37,893,522</u>	<u>1,230,272</u>	<u>16,027,969</u>	<u>-</u>	<u>70,014,962</u>
Balance on January 1, 2016	\$ -	13,083,979	36,019,984	1,145,084	17,744,290	-	67,993,337
Depreciation for the year	-	2,218,989	6,852,364	242,630	3,448,286	-	12,762,269
(Reversal of) Impairment loss	-	141	56,564	(50)	3,313	-	59,968
Reclassifications	-	288,821	639	-	(193,829)	-	95,631
Disposals and obsolescence	-	(621,287)	(3,423,598)	(111,091)	(2,286,805)	-	(6,442,781)
Effect of movement in exchange rate	-	(938,862)	(2,260,504)	(87,297)	(1,088,449)	-	(4,375,112)
Loss of control of a subsidiary	-	(499,879)	(1,933,444)	-	(2,348,152)	-	(4,781,475)
Balance on December 31, 2016	<u>\$ -</u>	<u>13,531,902</u>	<u>35,312,005</u>	<u>1,189,276</u>	<u>15,278,654</u>	<u>-</u>	<u>65,311,837</u>
<b>Carrying amounts :</b>							
Balance on December 31, 2017	<u>\$ 4,361,929</u>	<u>28,906,126</u>	<u>26,689,489</u>	<u>222,910</u>	<u>11,366,591</u>	<u>6,528,226</u>	<u>78,075,271</u>
Balance on December 31, 2016	<u>\$ 4,320,454</u>	<u>28,449,286</u>	<u>20,280,559</u>	<u>282,145</u>	<u>7,388,057</u>	<u>6,140,308</u>	<u>66,860,809</u>

(i) Based on the results of its evaluation of the recoverability of property, plant and equipment, the Group recognized (reversal gain) impairment loss as follows:

	<u>For the years ended December 31</u>	
	<u>2017</u>	<u>2016</u>
(Reversal gain) impairment loss	<u>\$ (55,047)</u>	<u>59,968</u>

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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- (ii) KINSUS INTERCONNECT TECHNOLOGY CORP. completed a series of farm land purchases covering a total land area of 36,115.24 square meters in the name of KINSUS' s chairman instead of KINSUS, due to the restriction imposed by the local government.
- (iii) For the years ended December 31, 2017 and 2016, an impairment loss on damaged and to be maintained equipment of \$418 and \$16,571, respectively, was recognized by CASETEK CAYMAN and its subsidiaries. In addition, CASETEK CAYMAN and its subsidiaries sold damaged equipment at selling price exceeding their carrying amount by \$925 and \$2,959 which was recognized as a reversal gain for the years ended December 31, 2017 and 2016, respectively.
- (iv) Please refer to Note 6(y) for details of gain and loss on disposal of property, plant and equipment.
- (v) Please refer to Note 8 for details of the property, plant and equipment pledged as collateral.
- (i) Investment property

	<u>Land</u>	<u>Buildings</u>	<u>Total</u>
<b>Cost or deemed cost:</b>			
Balance on January 1, 2017	\$ -	65,086	65,086
Effect of movement in exchange rate	-	(1,323)	(1,323)
Balance on December 31, 2017	<u>\$ -</u>	<u>63,763</u>	<u>63,763</u>
Balance on January 1, 2016	\$ 281,945	610,253	892,198
Effect of movement in exchange rate	-	(5,684)	(5,684)
Loss of control of a subsidiary	(281,945)	(539,483)	(821,428)
Balance on December 31, 2016	<u>\$ -</u>	<u>65,086</u>	<u>65,086</u>
<b>Depreciation and impairment loss :</b>			
Balance on January 1, 2017	\$ -	7,865	7,865
Depreciation for the year	-	3,149	3,149
Effect of movement in exchange rate	-	(121)	(121)
Balance on December 31, 2017	<u>\$ -</u>	<u>10,893</u>	<u>10,893</u>
Balance on January 1, 2016	\$ 9,617	178,450	188,067
Depreciation for the year	-	8,594	8,594
Effect of movement in exchange rate	-	(553)	(553)
Loss of control of a subsidiary	(9,617)	(178,626)	(188,243)
Balance on December 31, 2016	<u>\$ -</u>	<u>7,865</u>	<u>7,865</u>
<b>Carrying amounts :</b>			
Balance on December 31, 2017	<u>\$ -</u>	<u>52,870</u>	<u>52,870</u>
Balance on December 31, 2016	<u>\$ -</u>	<u>57,221</u>	<u>57,221</u>

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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- (i) Rental income and direct operating expenses arising from investment property that generate rental income were as follows:

	For the years ended December 31	
	2017	2016
Rental income	\$ 1,987	18,047
Direct operating expenses arising from investment property that generate rental income	\$ 3,149	8,594

- (ii) As of December 31, 2017 and 2016, the fair value of investment property of the Group was \$86,145 and \$87,564, respectively. The fair value of investment property was based on the market price evaluation of the buildings located in the area.
- (iii) As of December 31, 2017 and 2016, the aforesaid investment properties were not pledged as collateral.

- (j) Intangible assets

The movements in the costs of intangible assets, amortization, and impairment loss of the Group for the years ended December 31, 2017 and 2016 were as follows:

	Goodwill	Others	Total
<b>Costs:</b>			
Balance on January 1, 2017	\$ 1,799,633	1,090,054	2,889,687
Additions	-	366,923	366,923
Disposals	-	(49,423)	(49,423)
Reclassifications	-	14,663	14,663
Effect of movement in exchange rate	(86,962)	(47,464)	(134,426)
Balance on December 31, 2017	\$ 1,712,671	1,374,753	3,087,424
Balance on January 1, 2016	\$ 1,984,574	986,670	2,971,244
Additions	-	224,591	224,591
Disposals	-	(49,585)	(49,585)
Reclassifications	-	2,697	2,697
Effect of movement in exchange rate	(20,082)	(21,294)	(41,376)
Loss of control of a subsidiary	(164,859)	(53,025)	(217,884)
Balance on December 31, 2016	\$ 1,799,633	1,090,054	2,889,687
<b>Amortization and Impairment Loss:</b>			
Balance on January 1, 2017	\$ 671,792	778,709	1,450,501
Amortization for the year	-	233,799	233,799
Disposals	-	(49,423)	(49,423)
Effect of movement in exchange rate	-	(44,687)	(44,687)
Balance on December 31, 2017	\$ 671,792	918,398	1,590,190

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

	<u>Goodwill</u>	<u>Others</u>	<u>Total</u>
Balance on January 1, 2016	\$ 671,792	744,365	1,416,157
Amortization for the year	-	141,548	141,548
Disposals	-	(49,585)	(49,585)
Reclassifications	-	1,185	1,185
Effect of movement in exchange rate	-	(15,224)	(15,224)
Loss of control of a subsidiary	-	(43,580)	(43,580)
Balance on December 31, 2016	<u>\$ 671,792</u>	<u>778,709</u>	<u>1,450,501</u>
<b>Carrying amounts:</b>			
Balance on December 31, 2017	<u>\$ 1,040,879</u>	<u>456,355</u>	<u>1,497,234</u>
Balance on December 31, 2016	<u>\$ 1,127,841</u>	<u>311,345</u>	<u>1,439,186</u>

- (i) The amortization of intangible assets were respectively recognized in the statement of comprehensive income as follows:

	<u>For the years ended December 31</u>	
	<u>2017</u>	<u>2016</u>
Operating costs	\$ 122,562	38,802
Operating expenses	111,237	102,746
	<u>\$ 233,799</u>	<u>141,548</u>

- (ii) Goodwill impairment

For the purpose of impairment testing, goodwill was allocated to the Group's cash-generating units, such as mechanics, consumer electronic and others, as follows:

	<u>December 31,</u> <u>2017</u>	<u>December 31,</u> <u>2016</u>
Mechanics	\$ 997,954	1,081,452
Consumer electronic	41,403	44,867
Others	1,522	1,522
	<u>\$ 1,040,879</u>	<u>1,127,841</u>

At the end of each reporting period, the Group assess whether there is any indication of impairment loss on goodwill. There were no impairment loss recognized on goodwill for the years ended December 31, 2017 and 2016. The key assumptions used in determining the value in use by each cash-generating unit were as follows:

- 1) The recoverable amount of the mechanics cash-generating unit was based on value in use. Key assumptions used in calculating the recoverable amount were as follows:

The key assumptions used to estimate the value in use were as follows:

	<u>December 31,</u> <u>2017</u>	<u>December 31,</u> <u>2016</u>
Discount rate (before tax)	11.20 %	14.21 %

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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The discount rate was a pre-tax measure based on the rate of 10-year government bonds issued by the Taiwan government in the same currency as the cash flows, adjusted for a risk premium to reflect both the increased risk of investing generally in equities and the systemic risk of the specific CGU.

Cash flows of five years were included in the discounted cash flow model, which was based on the financial forecast for the following year approved by the management.

Budgeted EBITDA over the financial forecast period was based on expectations of future outcome, taking into account the past experience, adjusted for the anticipated revenue growth. Revenue growth is projected by taking into account the average growth levels experienced over the past few years.

- 2) The recoverable amount of the customer electronic cash-generating unit was based on value in use. Key assumptions used in calculating the recoverable amount were as follows:
- a) Cash flow estimation was based on past experience, actual operating results and a five-year operating plan.
  - b) Projected revenue and gross profit ratio were extrapolated from management's forecast based on past operating results and future marketing development trends.
  - c) Pre-tax discount rate used in calculating the value in use was determined from weighted average cost of capital (WACC) of the Company.
- (iii) For the years ended December 31, 2017 and 2016, the Group has not noted any indication of potential impairment loss based on the impairment testing performed.

(k) Other financial assets and other assets

Other financial assets and other assets were as follows:

	<b>December 31, 2017</b>	<b>December 31, 2016</b>
Other financial assets-current	\$ 1,222,740	479,510
Other financial assets-noncurrent	300,700	427,655
Other current assets	8,741,935	7,172,425
Other noncurrent assets	51,384	46,143
	<b><u>\$ 10,316,759</u></b>	<b><u>8,125,733</u></b>

- (i) Other financial assets are assets that do not qualify as cash and cash equivalents which consisted of time deposits, restricted time deposits and guarantee deposits. Please refer to Note 8 for details.
- (ii) Other current assets consisted of prepayments, current tax asset and others.
- (iii) Other noncurrent assets consisted of other long-term prepaid expenses and others.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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## (l) Short-term loans

	<b>December 31, 2017</b>	<b>December 31, 2016</b>
Unsecured bank loans	<u>\$ 46,058,620</u>	<u>31,148,468</u>
Interest rate	<u>0.5%~6.85%</u>	<u>0.51%~6.85%</u>

There were no pledged as collateral for short-term loans.

## (m) Long-term loans

	<b>December 31, 2017</b>	<b>December 31, 2016</b>
Unsecured bank loans	\$ 7,961,112	4,896,147
Secured bank loans	<u>101,000</u>	<u>171,000</u>
	8,062,112	5,067,147
Less: current portion	(1,107,312)	(536,257)
Less: fees	<u>-</u>	<u>(8,000)</u>
Total	<u>\$ 6,954,800</u>	<u>4,522,890</u>
Interest rate	<u>1.02%~2.80%</u>	<u>1.02%~2.59%</u>

## (i) Securities for bank loans

- 1) Please refer to Note 8 for details of the related assets pledged as collateral.
- 2) CASETEK CAYMAN's subsidiaries obtained a long-term loan from Mega International Commercial Bank for the year year ended December 31, 2016. CASETEK CAYMAN is the endorsement guarantee provider for such loan.

## (ii) Loan covenants

- 1) On August 1, 2013, the Company signed a syndicated loan agreement with a total credit line of \$12,000,000. According to the agreement with the banks, the Company must comply with the following financial covenants:
  - a) Current ratio (current assets/current liabilities): should not be less than 100%.
  - b) Debt ratio ((total liabilities + contingent liabilities)/tangible net assets): should not be higher than 80%.
  - c) Tangible net assets (stockholders' equity (including minority shareholders) - intangible assets): should not be less than \$90,000,000.
  - d) Interest coverage ratio (Profit before tax + depreciation + amortization + interest expenses)/interest expenses): should not be less than 400%.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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Compliance with the aforesaid financial covenants is determined on the reviewed quarterly consolidated financial statements (March 31, June 30 and September 30) and audited annual (December 31) stand alone and consolidated financial statements of the Company.

If the aforesaid covenants are breached, the syndicate banks will, depending on the circumstances, based on the majority decision of the syndicate banks to either suspend the subsequent credit usage or demand an immediate repayment.

The Company was in compliance with the above financial covenants as of December 31, 2017 and 2016.

- 2) On January 30, 2015, CASETEK CAYMAN signed a USD 300,000 thousand worth of credit facility in the form of credit loan with multiple banks. According to the credit loan facility agreements, during the loan repayment periods, CASETEK CAYMAN must comply with certain financial covenants, such as current ratio, debt ratio, interest coverage ratio and tangible net assets, based on its audited annual consolidated financial statements (December 31).
- a) Current ratio (Current assets/Current liabilities): Not less than 100%.
  - b) Total liabilities 【 Total liabilities (including contingent liability, but excluding those of non-controlling interests)/Total assets less intangible assets 】 : Less than 100%.
  - c) Interest coverage ratio 【 (Profit before tax + depreciation + amortization + interest expenses)/ interest expenses 】 : Not lower than five.
  - d) Tangible net assets (Total assets - total liabilities - intangible assets): Not lower than \$15,000,000.

The compliance with the aforesaid covenants will be examined annually based on the audited CASETEK CAYMAN annual consolidated financial statements.

CASETEK CAYMAN was in compliance with the above financial covenants as of December 31, 2017 and 2016.

(n) Bonds payable

- (i) The Group's unsecured ordinary corporate bonds were as follows:

	<b>December 31, 2017</b>	<b>December 31, 2016</b>
Ordinary corporate bonds issued	\$ 7,000,000	-
Unamortized discount on bonds payable	(7,524)	-
Bonds payable, end of the year	<u><u>\$ 6,992,476</u></u>	<u><u>-</u></u>

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

	<b>For the years ended December 31</b>	
	<b>2017</b>	<b>2016</b>
Interest expense	<b>\$ 34,164</b>	<b>-</b>

On May 9, 2017, the Company's Board of Directors approved to issue unsecured ordinary corporate bonds amounting to no more than \$15,000,000, which were approved and declared effective by the Taipei Exchange (TPEX) on July 4, 2017 and December 29, 2017, respectively.

The offering information and main rights and obligations were as follows:

<b>Item</b>	<b>1<sup>st</sup> unsecured ordinary bonds issued in 2017</b>
1. Issuing amount	The Bonds are issued at \$7,000,000, which comprise Tranche A, Tranche B and Tranche C. The issuing amounts of Tranche A, Tranche B and Tranche C are \$3,000,000, \$2,000,000 and \$2,000,000, respectively.
2. Par value	Each unit is valued at \$1,000.
3. Offering price	The Bonds are issued by par value at the issuance date.
4. Issuance period	Each of Tranche A, Tranche B and Tranche C has 3-year term, 5-year term and 7-year term, respectively. The issuance period of Tranche A commences from July 13, 2017 and matures on July 13, 2020. The issuance period of Tranche B commences from July 13, 2017 and matures on July 13, 2022. The issuance period of Tranche C commences from July 13, 2017 and matures on July 13, 2024.
5. Coupon rate	Tranche A, B and C bear annual coupon rates of 0.91%, 1.06% and 1.20%, respectively.
6. Repayment	Tranche A, Tranche B and Tranche C are repayable on maturity.
7. Interest payment	Interests are payable annually at coupon rate from the issuance date. The payment of each bond is rounded to the nearest dollar. If the repayment date and interest payment date are bank closing days, principal and interest shall be paid without extra interest on the next business day. If bondholders receive principal and interest past due the repayment date and interest payment date, there will no calculation of extra interest.
8. Guarantee	The Bonds are unsecured ordinary corporate bonds.

<b>Item</b>	<b>2<sup>nd</sup> unsecured ordinary bonds issued in 2017</b>
1. Issuing amount	The Bonds are issued at \$8,000,000, which comprise Tranche A, Tranche B and Tranche C. The issuing amounts of Tranche A, Tranche B and Tranche C are \$1,000,000, \$4,500,000 and \$2,500,000, respectively.
2. Par value	Each unit is valued at \$1,000.
3. Offering price	The Bonds are issued by par value at the issuance date.
4. Issuance period	Each of Tranche A, Tranche B and Tranche C has 3-year term, 5-year term and 7-year term, respectively. The issuance period of Tranche A commences from January 10, 2018 and matures on January 10, 2021. The issuance period of Tranche B commences from January 10, 2018 and matures on January 10, 2023. The issuance period of Tranche C commences from January 10, 2018 and matures on January 10, 2025.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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<u>Item</u>	<u>2<sup>nd</sup> unsecured ordinary bonds issued in 2017</u>
5. Coupon rate	Tranche A, B and C bear annual coupon rates of 0.78%, 0.92% and 1.08%, respectively.
6. Repayment	Tranche A, Tranche B and Tranche C are repayable on maturity.
7. Interest payment	Interests are payable annually at coupon rate from the issuance date. The payment of each bond is rounded to the nearest dollar. If the repayment date and interest payment date are bank closing days, principal and interest shall be paid without extra interest on the next business day. If bondholders receive principal and interest past due the repayment date and interest payment date, there will be no calculation of extra interest.
8. Guarantee	The Bonds are unsecured ordinary corporate bonds.

(o) Provisions

	<u>Warranties</u>	<u>Allowance for sales returns and discounts</u>	<u>Total</u>
Balance on January 1, 2017	\$ 83	159,981	160,064
Provisions made during the year	-	54,744	54,744
Provisions used during the year	(78)	(22,610)	(22,688)
Provisions reversed during the year	-	(4,417)	(4,417)
Effect of movement in exchange rate	(5)	(896)	(901)
Balance on December 31, 2017	<u>\$ -</u>	<u>186,802</u>	<u>186,802</u>
Balance on January 1, 2016	\$ 233,443	191,958	425,401
Provisions made during the year	-	10,380	10,380
Provisions used during the year	(3,409)	(21,007)	(24,416)
Provisions reversed during the year	-	(19,683)	(19,683)
Effect of movement in exchange rate	(680)	(1,667)	(2,347)
Loss of control of a subsidiary	(229,271)	-	(229,271)
Balance on December 31, 2016	<u>\$ 83</u>	<u>159,981</u>	<u>160,064</u>

Allowance for sales return and discounts

Allowances for sales returns and discounts are estimated based on historical experience, managers' judgment, and other known reasons. Such allowances are recognized as a deduction of sales revenue in the same period in which sales are made.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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## (p) Operating leases

## (i) Lessee

At the end of reporting year, the lease commitments were as follows:

	<u>December 31, 2017</u>	<u>December 31, 2016</u>
Less than one year	\$ 2,331,263	1,603,335
Between one and five years	3,281,836	1,564,062
More than five years	<u>120,346</u>	<u>206,720</u>
	<u><u>\$ 5,733,445</u></u>	<u><u>3,374,117</u></u>

The Group leases a number of office, warehouse, factory facilities and staff dormitories under operating leases. The leases typically run for a period of 1 to 10 years, with an option to renew the lease after that date.

For the years ended December 31, 2017 and 2016, expenses recognized in profit or loss in respect of operating leases were as follows:

	<u>For the years ended December 31</u>	
	<u>2017</u>	<u>2016</u>
Cost of sales	\$ 1,899,926	1,588,808
Operating expenses	<u>431,008</u>	<u>496,377</u>
	<u><u>\$ 2,330,934</u></u>	<u><u>2,085,185</u></u>

## (ii) Long-term prepaid rentals

	<u>December 31, 2017</u>	<u>December 31, 2016</u>
Long-term prepaid rentals	<u><u>\$ 3,783,164</u></u>	<u><u>4,014,064</u></u>

- 1) Long-term prepaid rentals represent land use rights under operating lease arrangement and is expensed equally over 38 to 67 years.
- 2) As of December 31, 2017 and 2016, the aforesaid land use rights were not pledged as collateral.

## (q) Employee benefits

## (i) Defined benefit plans

The Group's defined benefit obligations and fair value of plan assets were as follows:

	<u>December 31, 2017</u>	<u>December 31, 2016</u>
Present value of defined benefit obligations	\$ 234,479	230,574
Fair value of plan assets	<u>(147,608)</u>	<u>(143,849)</u>
Net defined benefit liabilities	<u><u>\$ 86,871</u></u>	<u><u>86,725</u></u>

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The Group makes defined benefit plan contributions to the pension fund account with Bank of Taiwan that provide pension benefits for employees upon retirement. Plans (covered by the Labor Standards Law) entitle a retired employee to receive retirement benefits based on years of service and average monthly salary for six months prior to retirement.

1) Composition of plan assets

The Group set aside pension funds in accordance with the Regulations for Revenues, Expenditures, Safeguard and Utilization of the Labor Retirement Fund and such funds are managed by the Bureau of Labor Funds, Ministry of Labor. Under these regulations, the minimum earnings from these pension funds shall not be less than the earnings from two-year time deposits with the interest rates offered by local banks.

The Group's contributions to the pension funds were deposited with Bank of Taiwan. For information on the utilization of the labor pension fund assets including the asset allocation and yield of the fund, please refer to the website of the Bureau of Labor Funds, Ministry of Labor.

2) Movements in present value of the defined benefit obligations

The movements in the present value of the defined benefit obligations for the years ended December 31, 2017 and 2016 were as follows:

	<b>For the years ended December 31</b>	
	<b>2017</b>	<b>2016</b>
Defined benefit obligation, January 1	\$ 230,574	331,194
Current service costs and interest	10,347	38,041
Re-measurements of the net defined benefit liability		
— Actuarial gains (losses) arose from changes in demographic assumptions	2,050	(2,432)
— Actuarial gains arose from changes in financial assumption	8,948	9,163
— Experience adjustments	(13,500)	(11,405)
Benefits paid by the plan	(3,940)	-
Loss of control of a subsidiary	-	(133,987)
Defined benefit obligation, December 31	<b>\$ 234,479</b>	<b>331,194</b>

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3) Movements in the fair value of plan assets

The movements in the fair value of the defined benefit plan assets for the years ended December 31, 2017 and 2016 were as follows:

	<b>For the years ended December 31</b>	
	<b>2017</b>	<b>2016</b>
Fair value of plan assets, January 1	\$ 143,849	195,829
Interests revenue	2,421	10,799
Re-measurements of the net defined benefit liability		
— Experience adjustments	(1,088)	(409)
Contributions made	6,241	6,286
Benefits paid by the plan	(3,940)	-
Expected return on plan assets	125	(914)
Loss of control of a subsidiary	-	(67,742)
Fair value of plan assets, December 31	<b>\$ 147,608</b>	<b>143,849</b>

4) Expenses recognized in profit or loss

The Group's pension expenses recognized in profit or loss for the years ended December 31, 2017 and 2016 were as follows:

	<b>For the years ended December 31</b>	
	<b>2017</b>	<b>2016</b>
Current service cost	\$ 6,318	33,651
Net interest on net defined benefit liability	1,608	(6,409)
	<b>\$ 7,926</b>	<b>27,242</b>
Operating costs	\$ 577	841
Operating expenses	7,349	26,401
	<b>\$ 7,926</b>	<b>27,242</b>

5) Re-measurement of net defined benefit liability recognized in other comprehensive income

The Group's net defined benefit liability recognized in other comprehensive income for the years ended December 31, 2017 and 2016 were as follows:

	<b>For the years ended December 31</b>	
	<b>2017</b>	<b>2016</b>
Cumulative amount, January 1	\$ 79,280	83,545
Recognized during the year	(1,414)	(4,265)
Cumulative amount, December 31	<b>\$ 77,866</b>	<b>79,280</b>

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6) Actuarial assumptions

The following were the key actuarial assumptions at the reporting date:

	<b>December 31, 2017</b>	<b>December 31, 2016</b>
Discount rate	1.15%~1.63%	1.35%~1.80%
Future salary increase rate	2.00%~3.00%	2.00%~3.00%

Based on the actuarial report, the Group is expected to make a contribution payment of \$6,191 to the defined benefit plans for the one year period after the reporting date.

The weighted-average duration of the defined benefit plans is between 8 and 24 years.

7) Sensitivity Analysis

In determining the present value of the defined benefit obligation, the Group's management makes judgments and estimates in determining certain actuarial assumptions on the balance sheet date, which includes discount rate and future salary increase rate. Changes in actuarial assumptions may have significant impact on the amount of defined benefit obligation.

As of December 31, 2017 and 2016, the changes in the principal actuarial assumptions will impact on the present value of defined benefit obligation as follows:

	<b>Impact on the present value of defined benefit obligation</b>	
	<b>Increase by 0.50%</b>	<b>Decrease by 0.50%</b>
December 31, 2017		
Discount rate	(21,733)	24,362
Future salary increase rate	23,767	(21,443)
December 31, 2016		
Discount rate	(21,587)	24,285
Future salary increase rate	20,536	(18,137)

The sensitivity analysis assumed all other variables remain constant during the measurement. This may not be representative of the actual change in defined benefit obligation as some of the variables may be correlated in the actual situation. The model used in the sensitivity analysis is the same as the defined benefit obligation liability.

The analysis is performed on the same basis for prior year.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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(ii) Defined contribution plans

The Group contributes an amount at the rate of 6% of the employee's monthly wages to the Labor Pension personal account with the Bureau of the Labor Insurance and Council of Labor Affairs in R.O.C. in accordance with the provisions of the Labor Pension Act. The Group's contributions to the Bureau of the Labor Insurance and Social Security Bureau for the employees' pension benefits require no further payment of additional legal or constructive obligations.

The cost of the pension contributions to the Labor Insurance Bureau for the years ended December 31, 2017 and 2016 amounted to \$5,273,507 and \$5,785,909, respectively.

(iii) Short-term employee benefits

As of December 31, 2017 and 2016, the Group's short-term employee benefits liabilities were \$330,441 and \$333,344, respectively.

(r) Income Tax

(i) The income tax expense for the years ended December 31, 2017 and 2016 was calculated as follows:

	<u>For the years ended December 31</u>	
	<u>2017</u>	<u>2016</u>
Current income tax expense		
Current period incurred	\$ 5,630,157	6,172,734
Prior years income tax adjustment	(163,761)	120,865
10% surtax on undistributed earnings	203,174	991,507
Deferred tax expense		
The origination and reversal of temporary differences	<u>(1,271,292)</u>	<u>(342,828)</u>
Income tax expense	<u>\$ 4,398,278</u>	<u>6,942,278</u>

(ii) The amount of income tax recognized in other comprehensive income (loss) for the years ended December 31, 2017 and 2016 was as follows:

	<u>For the years ended December 31</u>	
	<u>2017</u>	<u>2016</u>
Items that will not be reclassified subsequently to profit or loss:		
Re-measurements of the net defined benefit plans	<u>\$ (1,088)</u>	<u>1,286</u>
Items that may be reclassified subsequently to profit or loss		
Exchange differences on translation of foreign financial statements	<u>\$ (10,392)</u>	<u>(96,953)</u>

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- (iii) Income tax on pre-tax financial income was reconciled with income tax expense for the years ended December 31, 2017 and 2016 as follows:

	<b>For the years ended December 31</b>	
	<b>2017</b>	<b>2016</b>
Profit before income tax	\$ <u>20,413,050</u>	<u>29,079,670</u>
Income tax on pre-tax financial income calculated at the domestic rates applicable to profits in the country concerned	6,129,532	7,925,416
Permanent differences	(1,063,023)	(1,997,374)
Changes in unrecognized temporary differences	(1,409,781)	(1,224,929)
Oversea dividends received	480,802	1,072,864
Prior years income tax adjustment	(163,761)	120,865
10% surtax on undistributed earnings	203,174	991,507
Others	<u>221,335</u>	<u>53,929</u>
Income tax expense	<u>\$ <b>4,398,278</b></u>	<u><b>6,942,278</b></u>

- (iv) Deferred tax assets and liabilities

- 1) Unrecognized deferred tax liabilities

As of December 31, 2017 and 2016, the temporary differences associated with investments in subsidiaries were not recognized as deferred income tax liabilities as the Group has the ability to control the reversal of these temporary differences which are not expected to reverse in the foreseeable future. The related amounts were as follows:

	<b>December 31, 2017</b>	<b>December 31, 2016</b>
The aggregate temporary differences associated with investments in subsidiaries	\$ <u><b>43,076,877</b></u>	<u><b>34,747,332</b></u>
Unrecognized deferred tax liabilities	<u><b>7,323,069</b></u>	<u><b>5,907,046</b></u>

- 2) Unrecognized deferred tax assets

	<b>December 31, 2017</b>	<b>December 31, 2016</b>
Deductible temporary differences	\$ 656,964	692,807
Tax losses	<u>852,174</u>	<u>810,089</u>
	<u><b>\$ 1,509,138</b></u>	<u><b>1,502,896</b></u>

The ROC Income Tax Act allows the carry forward of net losses, as assessed by the tax authorities, to offset against taxable income. Deferred tax assets have not been recognized in respect of these items because it is not probable that future taxable profit will be available against which the Group can utilise the benefits therefrom.

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As of December 31, 2017, the Group had not recognized the prior years' loss carry-forwards as deferred tax assets, and the expiry years thereof were as follows:

<u>Company Name</u>	<u>Year of occurrence</u>	<u>Unused balance</u>	<u>Expiry year</u>
KINSUS and its subsidiaries	2012~2017	\$ 2,037,861	2018~2022
ASROCK and its subsidiaries	2013~2017	339,364	2023~2027
CASETEK CAYMAN and its subsidiaries	2015~2017	1,862,211	2020~2022
AZUREWAVE and its subsidiaries	2013~2016	394,481	2023~2026
AMA PRECISION	2009~2017	<u>147,345</u>	2019~2027
		<u>\$ 4,781,262</u>	

3) Recognized deferred tax assets and liabilities

The movements in deferred tax assets and liabilities for the years ended December 31, 2017 and 2016 were as follows:

	<u>Gain on foreign investments</u>	<u>Others</u>	<u>Total</u>
<b>Deferred tax liabilities:</b>			
Balance on January 1, 2017	\$ 1,766,001	37,243	1,803,244
Recognized in profit	(165,393)	(13,380)	(178,773)
Recognized in other comprehensive income	(9,387)	-	(9,387)
Exchange differences on translation	<u>(14,404)</u>	<u>801</u>	<u>(13,603)</u>
Balance on December 31, 2017	<u>\$ 1,576,817</u>	<u>24,664</u>	<u>1,601,481</u>
Balance on January 1, 2016	\$ 2,519,429	59,552	2,578,981
Recognized in (profit) loss	(603,270)	23,505	(579,765)
Recognized in other comprehensive income	(57,119)	(39,834)	(96,953)
Exchange differences on translation	(93,039)	(1,871)	(94,910)
Loss of control of a subsidiary	<u>-</u>	<u>(4,109)</u>	<u>(4,109)</u>
Balance on December 31, 2016	<u>\$ 1,766,001</u>	<u>37,243</u>	<u>1,803,244</u>

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	<b>Provision for Contingent Service Cost</b>	<b>Gain on valuation of inventory</b>	<b>Unrealized expenses</b>	<b>Others</b>	<b>Total</b>
<b>Deferred tax assets:</b>					
Balance on January 1, 2017	\$ 84,387	752,469	1,337,980	173,097	2,347,933
Recognized in profit	24,178	542,971	403,502	121,868	1,092,519
Recognized in other comprehensive income	-	-	1,005	1,088	2,093
Exchange differences on translation	<u>-</u>	<u>(41,881)</u>	<u>(54,728)</u>	<u>56</u>	<u>(96,553)</u>
Balance on December 31, 2017	<u><b>\$ 108,565</b></u>	<u><b>1,253,559</b></u>	<u><b>1,687,759</b></u>	<u><b>296,109</b></u>	<u><b>3,345,992</b></u>
Balance on January 1, 2016	\$ 151,534	1,106,849	1,452,824	141,299	2,852,506
Recognized in (profit) loss	(33,089)	(287,105)	42,112	41,145	(236,937)
Recognized in other comprehensive income	-	-	-	(1,286)	(1,286)
Exchange differences on translation	(1,267)	(67,275)	(113,724)	5,642	(176,624)
Loss of control of a subsidiary	<u>(32,791)</u>	<u>-</u>	<u>(43,232)</u>	<u>(13,703)</u>	<u>(89,726)</u>
Balance on December 31, 2016	<u><b>\$ 84,387</b></u>	<u><b>752,469</b></u>	<u><b>1,337,980</b></u>	<u><b>173,097</b></u>	<u><b>2,347,933</b></u>

(v) Status of approval of income tax

- 1) The Company's income tax returns through 2014 have been assessed and approved by the Tax Authority.
- 2) The Group have income tax returns approved by the Tax Authority were as follows:

<u>Years of Approval</u>	<u>Company Name</u>
2015	AZURE WAVE, AZURE LIGHTING, EZWAVE TECHNOLOGIES, AMA, ASUS INVESTMENT, ASUSTEK INVESTMENT, ASUSPOWER INVESTMENT, KINSUS INTERCONNECT TECHNOLOGY CORP. (whose 2014 income tax return has not been approved yet), PEGAVISION, KINSUS INVESTMENT, STARLINK, ASFLY TRAVEL SERVICE LTD., HUA-YUAN INVESTMENT LTD., ASROCK INCORPORATION (whose 2014 income tax return has not been approved yet), ASROCK RACK, INC., PEGA INTERNATIONAL LIMITED, LUMENS OPTICS and RIH KUAN METAL.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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(vi) Stockholders' imputation tax credit account and tax rate:

	<b>December 31,</b> <b>2017</b>	<b>December 31,</b> <b>2016</b>
	<u>(Note)</u>	<u>4,779,126</u>
Stockholders' imputation tax credit account		
	<b>2017</b>	<b>2016 (Actual)</b>
	<u>(Note)</u>	<u>14.70 %</u>
Tax deduction ratio for earnings distributable to R.O.C. residents		

All of the Company's earnings generated for the period up to December 31, 1997 have been appropriated.

The aforesaid imputation tax related information was prepared in accordance with Decree No.10204562810 issued by Taxation Administration, Ministry of Finance, R.O.C. on October 17, 2013.

Note: According to the amendments to the "Income Tax Act" enacted by the office of the President of the Republic of China (Taiwan) on February 7, 2018, effective from January 1, 2018, companies will no longer be required to establish, record, calculate, and distribute their ICA due to the abolishment of the imputation tax system.

(s) Share capital and other interests

As of December 31, 2017 and 2016, the authorized capital of the Company consisted of 3,000,000 thousand shares, with par value of \$10 per share. The outstanding shares consisted of 2,614,090 and 2,575,169 thousand common shares, respectively, and the capital that rose from the shares had all been retrieved.

(i) Nominal ordinary shares

The movements in ordinary shares of stock outstanding for the years ended December 31, 2017 and 2016 were as follows:

Ordinary Shares (In thousands of shares)	<b>For the years ended December 31</b>	
	<b>2017</b>	<b>2016</b>
Beginning balance on January 1	2,575,169	2,603,020
Issuance of restricted shares of stock	40,000	-
Retirement of restricted shares of stock	(1,079)	(1,441)
Retirement of treasury stock	-	(26,410)
Ending balance on December 31	<u>2,614,090</u>	<u>2,575,169</u>

The Company issued restricted shares of stock totaling 40,000 thousand shares to employees for the year ended December 31, 2017.

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For the years ended December 31, 2017 and 2016, the Company had retired 1,079 and 1,441 thousand shares, respectively, of restricted stock to employees. Likewise, the Company retired treasury stock totaling 26,410 thousand shares in order to protect the Company's integrity and shareholders' equity for the year ended December 31, 2016. Therefore, the authorized capital of the Company consisted of both 3,000,000 thousand shares, with par value of \$10 per share, and its outstanding capital consisted of 2,614,090 and 2,575,169 thousand common shares of stock, as of December 31, 2017, and 2016, respectively.

As of December 31, 2017 and 2016, the restricted Company shares of stock issued to employees have expired, of which 194 and 225 thousand shares, respectively, have not been retired.

(ii) Global depositary receipts

ASUSTeK GDR holders who surrendered their ASUSTeK GDRs on or after the Effective Date of Spin-off and Merger in Taiwan will receive new ASUSTeK GDRs and the Company's entitlement. The Company's entitlement represents the rights to receive 60,819,026 of the Company's common shares in Taiwan.

The Company may issue new GDRs with no more than 60,819,020 of the Company's common shares and deliver them to ASUSTeK GDR holders pursuant to the "Guidelines for Offering and Issuing by Issuer of Overseas Securities". As of December 31, 2017 and 2016, the Company has listed, in total, 10,945 and 6,250 thousand units of GDRs, respectively, on the Euro MTF market of the Luxembourg Stock Exchange. As each unit of these GDRs represents 5 common shares of the Company, the Company has listed Company shares totaling 54,724 and 31,251 thousand shares of stock, respectively. Major terms and conditions for GDRs were as follows:

1) Voting Rights

Holders of GDRs may exercise voting rights with respect to the common shares in the manner set out in "Terms and Conditions of the Global Depositary Shares – Voting Rights," as such provisions may be amended from time to time to comply with applicable ROC law.

2) Dividend Distributions, Pre-emptive Rights, and Other Rights

Holders of GDRs have same rights on dividend distribution and share distribution as the Company's existing common shareholders.

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(iii) Capital surplus

The components of the capital surplus were as follows:

	<b>December 31, 2017</b>	<b>December 31, 2016</b>
From issuance of share capital	\$ 63,209,502	62,238,593
From conversion of convertible bonds	11,073,663	11,073,663
From treasury stock transactions	23,614	23,614
Difference between consideration and carrying amount of subsidiaries acquired or disposed	2,383,056	2,383,056
Changes in ownership interest in subsidiaries	576,033	741,312
Employee stock options	1,304	1,304
Restricted stock to employees	2,220,662	1,342,800
Other	<u>409,917</u>	<u>409,917</u>
	<b><u>\$ 79,897,751</u></b>	<b><u>78,214,259</u></b>

In accordance with Amended Companies Act 2012, realized capital reserves can only be capitalized or distributed as cash dividends after offsetting against losses. The aforementioned capital reserves include share premiums and donation gains. In accordance with Securities Offering and Issuance Guidelines, the amount of capital reserves that can be capitalized shall not exceed 10 percent of the actual share capital amount.

(iv) Retained earnings

The Company's Articles of Incorporation require that after-tax earnings shall first be offset against any deficit, and 10% of the balance shall be set aside as legal reserve. The appropriation for legal reserve is discontinued when the balance of the legal reserve equals the total authorized capital. Aside from the aforesaid legal reserve, the Company may, under its Articles of Incorporation or as required by the government, appropriate for special reserve. The remaining balance of the earnings, if any, may be appropriated according to a resolution of a stockholders' meeting.

In order to bring about stability in the payment of dividends, the Company distributes dividends depending on the level of earnings of each year. The Company is facing a rapidly changing industrial environment. In consideration of the Company's long-term operating plan and funding needs, the Company adopts a stable dividends policy. Therefore, dividend distributions should not be less than 10% of distributable earnings. The Company distributes dividends of at least 10% of the aggregate dividends, if the distributions include cash dividends.

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1) Legal reserve

In accordance with the Amended Companies Act 2012, 10 percent of net income should be set aside as legal reserve, until it is equal to share capital. If the Company incurred profit for the year, the meeting of shareholders shall decide on the distribution of the statutory earnings reserve either by issuing new shares or by paying cash, of up to 25 percent of the actual share capital.

2) Special reserve

In accordance with Permit No. 1010012865 as issued by the Financial Supervisory Commission on April 6, 2012, a special reserve equal to the contra account of other shareholders' equity is appropriated from current and prior period earnings. When the debit balance of any of the contra accounts in the shareholders' equity is reversed, the related special reserve can be reversed. The subsequent reversals of the contra accounts in shareholders' equity shall qualify for additional distributions.

3) Earnings Distribution

On June 20, 2017 and June 21, 2016, the Company's shareholders' meeting resolved to appropriate the 2016 and 2015 earnings. These earnings were appropriated or distributed as follows:

	<b>2016</b>	<b>2015</b>
Common stock dividends per share (dollars)		
— Cash	\$ <b>5.00</b>	<b>5.00</b>

(v) Treasury stock

In 2016, in accordance with the Article 28-2 of the Securities and Exchange Act, the Company repurchased 26,410 shares as treasury shares in order to protect the Company's integrity and shareholders' equity. As of December 31, 2016, treasury stock totaling 26,410 shares were retired.

In accordance with the Securities and Exchange Act requirements as stated above, the number of shares repurchased should not exceed 10 percent of total issued shares. Also the value of the repurchased shares should not exceed the sum of the Company's retained earnings, share premium, and realized reserves.

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(vi) Other equity accounts (net of tax)

	<b>Exchange differences on translation of foreign financial statements</b>	<b>Available -for-sale investments</b>	<b>Deferred compensation arising from issuance of restricted stock</b>	<b>Total</b>
Balance on January 1, 2017	\$ (3,552,939)	183,953	(429,882)	(3,798,868)
Exchange differences on foreign operation	(6,154,844)	-	-	(6,154,844)
Exchange differences on associates accounted for using equity method	9,409	-	-	9,409
Unrealized gain on available-for-sale financial assets	-	541,228	-	541,228
Unrealized gain on available-for-sale financial assets of associates accounted for using equity method	-	157,980	-	157,980
Deferred compensation cost	-	-	(792,350)	(792,350)
Balance on December 31, 2017	<u>\$ (9,698,374)</u>	<u>883,161</u>	<u>(1,222,232)</u>	<u>(10,037,445)</u>
Balance on January 1, 2016	\$ 3,752,117	211,234	(1,238,377)	2,724,974
Exchange differences on foreign operation	(7,263,087)	-	-	(7,263,087)
Exchange differences on associates accounted for using equity method	(48,217)	-	-	(48,217)
Unrealized loss on available-for-sale financial assets	-	(14,425)	-	(14,425)
Deferred compensation cost	-	-	808,495	808,495
Disposal of subsidiaries	6,248	(12,856)	-	(6,608)
Balance on December 31, 2016	<u>\$ (3,552,939)</u>	<u>183,953</u>	<u>(429,882)</u>	<u>(3,798,868)</u>

(vii) Non-controlling interests (net of tax)

	<b>For the years ended December 31</b>	
	<b>2017</b>	<b>2016</b>
Balance on January 1	\$ 33,752,611	41,958,390
Profit attributable to non-controlling interests	1,331,784	2,797,577
Other comprehensive income attributable to non-controlling interests		
Exchange differences on foreign operation	(434,397)	(1,243,916)
Unrealized gain on available-for-sale financial assets	-	151,805
Actuarial (loss) gain on defined benefit plans	(1,798)	2,270
Disposal of subsidiaries	-	(7,454,156)
Changes in ownership interest in subsidiaries	165,279	(2,575)
Changes in non-controlling interests	(1,065,407)	(2,456,784)
Balance on December 31	<u>\$ 33,748,072</u>	<u>33,752,611</u>

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(t) Share-based payment

Information on share-based payment transactions as of December 31, 2017 and 2016 were as follows:

	<b>Equity-settled share-based payment</b>		
	<b>Restricted stock to employee</b>		
	<b>Issued in 2016</b>	<b>Issued in 2014</b>	<b>Issued in 2013</b>
Thousand units granted	40,000	40,000	6,062
Contractual life	3 years	3 years	3 years
Vesting period	Note A	Note A	Note B
Actual turnover rate of employees	1.70%	7.11%	5.80%
Estimated future turnover rate for each or the three years of employees	7.66%、15.44% 、25.92%	10.48%、20.18% 、34.36%	10.94%、25.07% 、33.76%

Note A : Employees are entitled to receive 20%, 40%, and 40% of the restricted stock in the first, second and third year, respectively, of their service.

Note B : Employees are entitled to receive 40%, 30%, and 30% of the restricted stock in the first, second and third year, respectively, of their service.

On August 12, 2013, pursuant to the resolutions of its board of directors, the Company issued 6,062 thousand shares of restricted shares of stock to employees with par value of NT\$10 per share. These were unissued shares whose total number is limited to up to 40,000 thousand shares of stock approved by the Financial Supervisory Commission for purposes of issuing restricted Company shares of stock to employees on October 19, 2012. The effective date of this capital increase was September 12, 2013. The legal procedure for the change in the registration of capital stock has been completed. Unless the vesting conditions have lapsed, the restricted shares of stock may not be sold, pledged, transferred, hypothecated or otherwise disposed. Holders of restricted shares of stock are entitled to rights as the Company's existing common shareholders except for the fact that restricted shares of stock are held by the trust and have vesting conditions. Also, the Company bears the right to buy back the restricted shares of stock at the issuance price and to cancel all restricted shares of stock issued to any employee who fails to comply with the vesting condition without returning the distributed dividend.

On June 18, 2014, the shareholders approved a resolution passed during their meeting to award 40,000 thousand new restricted shares of stock to those full-time employees who meet certain requirement of the Company. The restricted stock has been registered with and approved by the Securities and Futures Bureau of the Financial Supervisory Commission, R.O.C. On May 7, 2015, the board of directors issued 39,678 thousand restricted shares with fair value of NT\$91.9 each at grant date.

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Employees with restricted stock awards are entitled to purchase the Company's shares at the price of NT\$10 with the condition that these employees continue to work for the Company for the following three years. 20%, 40% and 40% of the restricted shares of stock is vested in year 1, 2 and 3, respectively. The restricted stock is kept by a trust, which is appointed by the Company, before it is vested. These shares of stock shall not be sold, pledged, transferred, gifted or by any other means of disposal to third parties during the custody period. These shares of stock are entitled to the right as the holders of common shares once issued, except for those shares kept by a trust or shares that do not meet the vesting condition. If the shares remain unvested after the vesting period, the Company will repurchase all the unvested shares at the issue price, and cancel the shares thereafter.

On June 21, 2016, the shareholders approved a resolution passed during their meeting to award 40,000 thousand new restricted shares of stock to those full-time employees who meet certain requirement of the Company. The restricted stock has been declared effective by the Securities and Futures Bureau of the Financial Supervisory Commission, R.O.C. On May 9, 2017, the board of directors approved to issue 38,191 thousand shares of restricted shares of stock with fair value of NT\$89.7 each at grant date. The record date for the capital increase through issuance of restricted shares of stock was July 11, 2017. The actual issuance number for the capital increase was 37,808 thousand shares. On July 27, 2017, the registration procedures were completed. On September 15, 2017, board of directors of the Company approved to issue secondary new restricted shares of stock totaling 2,192 thousand shares. The record date for the capital increase through issuance of restricted shares of stock was October 19, 2017.

Employees with restricted stock awards are entitled to purchase the Company's shares at the price of NT\$ 10 per share provided that these employees continue to work for the Company for the following three years. 20%, 40% and 40% of the restricted shares of stock is vested in year 1, 2 and 3, respectively. The restricted stock is kept by a trust, which is appointed by the Company, before it is vested. These shares of stock shall not be sold, pledged, transferred, gifted or by any other means of disposal to third parties during the custody period. These shares of stock are entitled to the right as the holders of common shares once issued, except for those shares kept by a trust or shares that do not meet the vesting condition. If the shares remain unvested after the vesting period, the Company will repurchase all the unvested shares at the issue price, and cancel the shares thereafter.

(i) Determining the fair value of equity instruments granted

The Company adopted the Black-Scholes model to calculate the fair value of the stock option at grant date, and the assumptions adopted in this valuation model were as follows:

	<b>Equity-settled share-based payment</b>			
	<b>Restricted stock to employee</b>			
	<b>Issued in 2016</b>	<b>Issued in 2016</b>	<b>Issued in 2014</b>	<b>Issued in 2013</b>
Fair value at grant date	09/15/2017	05/09/2017	05/07/2015	08/12/2013
Stock price at grant date	\$ 88.50	89.70	91.90	45.20
Exercise price	10.00	10.00	10.00	10.00
Expected life of the option	3 years	3 years	3 years	3 years
Current market price	88.50	89.70	91.90	45.20
Expected volatility	25.16%~31.95%	30.19%~32.92%	33.37%	32.68%
Expected dividend yield	-%	-%	-%	-%
Risk-free interest rate	(Note A)	(Note A)	(Note B)	(Note C)

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Note A : The risk-free interest rate is 0.23% for the 1st year, 0.25% for the 2nd year, and 0.28% for the 3rd year.

Note B : The risk-free interest rate is 0.4902% for the 1st year, 0.6632% for the 2nd year, and 0.7992% for the 3rd year.

Note C : The risk-free interest rate is 0.5997% for the 1st year, 0.7167% for the 2nd year, and 0.8764% for the 3rd year.

(ii) Restricted stock to employee

For the year ended December 31, 2017, the Company issued restricted shares of stock to employees of 40,000 thousand shares, which resulted in a capital surplus — restricted employee stock of \$1,702,900. Also, for the years ended December 31, 2017 and 2016, 1,049 and 1,407 thousand shares of the restricted shares of stock issued to employees have expired, which were charged to capital surplus of \$10,485 and \$14,066, respectively. As of December 31, 2017 and 2016, the Company has deferred compensation cost arising from issuance of restricted stock of \$1,222,232 and \$429,882, respectively.

For the years ended December 31, 2017 and 2016, the Company recognized salary cost of \$58,346 and \$36,306 from the distribution of cash dividends to estimated non-vesting restricted shares of stock distributed to employees from prior period earnings. Such salary cost was accounted under retained earnings as it remained to be unrealized.

(iii) Expenses resulting from share-based payments

The Company incurred expenses from share-based payment transactions for the years ended December 31, 2017 and 2016 were as follows:

	<b>For the years ended December 31</b>	
	<b>2017</b>	<b>2016</b>
Expenses resulting from issuance of restricted stock to employees	<b>\$ 1,221,618</b>	<b>900,522</b>

(u) Subsidiary's share-based payments

(i) For the year ended December 31, 2016, Ability (TW) had a share-based payment arrangement as follows:

<b>Type of arrangement</b>	<b>Grant date</b>	<b>Thousand shares granted</b>	<b>Contractual life</b>	<b>Vesting condition</b>
Restricted stock to employees (Note)	May 21, 2014	22,000	3 years	3 years of service

The aforementioned share-based arrangement was equity-settled.

Note: The restricted shares of stock issued by Ability Enterprise may not be transferred unless the vesting conditions have elapsed. The holder of the restricted shares are entitled to the right as existing common shareholders; Employee resigns in the vesting period is obligate to return the restricted shares of stock but without returning the distributed dividend.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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1) Determining the fair value of equity instruments granted

The Trinomial Tree Option Valuation Model was adopted to estimate the fair value of the second batch of Ability (TW) employee stock option on the day of granted and at the end of each period. The measurement inputs were as follows:

	<b>Equity-settled Restricted stock to employee</b>
	<b>Issued in 2014</b>
Grant date	May 21, 2014
Stock price at grant date	\$ 20.90
Exercise price	10.00
Expected duration	3 years
Current market price	20.90
Expected volatility	Note A
Expected dividend yield	Note B
Risk-free interest rate	Note C

Note A : The expected volatility is 22.22% for the 1st year, 21.15% for the 2nd year, and 25.67% for the 3rd year.

Note B : The dividend yield is 8.22% for the 1st year, - % for the 2nd year, and - % for the 3rd year.

Note C : The risk-free interest rate is 1.4628% for the 1st year, 1.6421% for the 2nd year, and 1.9488% for the 3rd year.

2) Expenses resulting from share-based payments

Ability (TW) incurred expenses from share-based payment transactions as follows:

	<b>For the years ended December 31</b>	
	<b>2017</b>	<b>2016 (Note)</b>
Equity-settled	\$ -	<b>10,170</b>

Note: As disclose in Note 6(f), the Group ceased control over Ability Enterprise Co., Ltd. on June 29, 2016, so only the financial information for the six months ended June 30, 2016 was disclosed above.

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(ii) Restricted stock to employee of AZURE WAVE

On June 16, 2016, pursuant to the resolution of its shareholders during their meeting, AZURE WAVE will issue 5,000 thousand new restricted shares of stock to those full-time employees who meet certain requirements of AZURE WAVE. The restricted shares of stock has been registered with and approved by the Securities and Futures Bureau of the Financial Supervisory Commission, R.O.C. On March 13, 2017, board of directors approved to issue all restricted shares of stock with fair value of NT\$14.55 each at grant date. The record date for the capital increase through issuance of restricted shares of stock was May 25, 2017. On June 5, 2017, AZURE WAVE's board of directors approved to decrease issued shares to 3,655 thousand shares. Furthermore, the record date for the capital increase through issuance of restricted shares of stock was changed to June 5, 2017.

Employees with restricted stock awards are entitled to purchase shares at the price of NT\$10 per share provided that these employees continue to work for AZURE WAVE for the following three years. 20%, 40% and 40% of the restricted shares of stock is vested in year 1, 2 and 3, respectively. The restricted stock is kept by a trust, which is appointed by AZURE WAVE, before it is vested. These shares of stock shall not be sold, pledged, transferred, gifted, or by any other means of disposed to third parties during the custody period. These shares of stock are entitled to the same right as the holders of common stock once issued, except for those shares kept by a trust or shares that do not meet the vesting condition. If the shares remain unvested after the vesting period, AZURE WAVE will repurchase all the unvested shares at the issue price, and cancel the shares thereafter.

For the years ended December 31, 2017, AZURE WAVE recognized share-based compensation cost of \$5,715. As of December 31, 2017, AZURE WAVE has deferred compensation cost arising from issuance of restricted stock of \$7,589.

(iii) Restricted stock to employee of ASROCK

On June 7, 2017, the shareholders of ASROCK approved a resolution passed during their meeting to award 6,000 thousand new restricted shares of stock to those full-time employees who meet certain requirement of ASROCK. The restricted shares of stock totaling 5,750 thousand shares have been registered with and approved by the Securities and Futures Bureau of the Financial Supervisory Commission, R.O.C. On September 22, 2017, 5,704 thousand shares were actually issued for such award with fair value of NT\$68.8 each at grant date.

Employees with restricted stock awards are entitled to purchase shares at the price of NT\$10 per share provided that these employees continue to work for ASROCK for the following three years. 40%, 30% and 30% of the restricted shares of stock is vested in year 1, 2 and 3, respectively. The restricted stock is kept by a trust, which is appointed by ASROCK, before it is vested. These shares of stock shall not be sold, pledged, transferred, gifted or by any other means of disposal to third parties during the custody period. These shares of stock are entitled to the same right as holders of common shares once issued, except for those shares kept by a trust or shares that do not meet the vesting condition.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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The aforesaid information of restricted stock to employees was follows:

	<b>Restricted stock to employee</b>			
	<b>Year 1</b>	<b>Year 2</b>	<b>Year 3</b>	<b>Total</b>
Vesting period				
Original vested shares (In thousands)	2,282	1,711	1,711	5,704
Estimated employee turnover rate	14.04 %	28.02 %	42.73 %	
Vested shares after considering employee turnover rate (In thousands)	1,961	1,232	980	4,173
Embedded value	NT\$58.80	58.80	58.80	
Service costs	\$ 115,323	72,425	57,624	245,372

On September 22, 2017, ASROCK issued restricted shares of stock to employees totaling 5,704 thousand shares, which was charged to capital surplus of \$245,372. As of December 31, 2017, ASROCK has deferred compensation cost arising from issuance of restricted stock of \$174,268.

1) Cancellation or amendment to share-based payment transactions

ASROCK did not made any cancellation or amendment to share-based payment transactions for the year ended December 31, 2017.

2) The expense resulting from the share-based payment transactions was as follows:

	<b>For the year ended December 31</b>
	<b>2017</b>
Expense resulting from equity-settled share-based payment	<b>\$ 71,104</b>

(iv) Restricted stock to employee of CASETEK CAYMAN

On June 22, 2017, pursuant to the resolution of its shareholders during their meeting, CASETEK CAYMAN will issue 1,500 thousand new restricted shares of stock to those full-time employees who meet certain requirement of CASETEK CAYMAN and its subsidiaries. The restricted shares of stock has been registered with and approved by the Securities and Futures Bureau of the Financial Supervisory Commission, R.O.C. On August 31, 2017, board of directors of CASETEK CAYMAN approved to issue all restricted shares of stock. The record date for the capital increase through issuance of restricted shares of stock was September 5, 2017.

Employees with restricted stock awards are entitled to obtain shares without consideration provided that these employees continue to work for CASETEK CAYMAN for at least six months. 50% of the restricted stock is vested in six months, and the remaining shares of stock is vested in year 1. The restricted stock is kept by a trust, which is appointed by CASETEK CAYMAN, before it is vested. These shares of stock shall not be sold, pledged, transferred, gifted, or by any other means of disposed to third parties during the custody period. The voting rights of these shareholders are executed by the custodian. If the shares remain unvested after the vesting period, CASETEK CAYMAN bears the right to retire the restricted shares of stock without any payment and to cancel all restricted shares of stock issued to any employee who fails to comply with the vesting condition without returning the distributed dividend.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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Information on aforesaid restricted shares of stock to employee was as follows:

	<b>For the year ended December 31</b>
	<b>2017</b>
(In thousands of shares)	
Outstanding as of January 1	\$ -
Granted during the year	1,500
Outstanding as of December 31	<b>\$ 1,500</b>

Capital surplus of \$135,000 was recognized from the measurement of aforesaid restricted employee stock, at fair value of NT\$100 per share based on the closing price of CASETEK CAYMAN shares at grant date. As of December 31, 2017, CASETEK CAYMAN has deferred compensation cost arising from issuance of restricted shares of stock of \$76,858.

In addition to the aforementioned restricted shares of stock to employee, for the years ended December 31, 2017, CASETEK CAYMAN and its subsidiaries had share-based payment transactions as follows:

	<b>Equity-settled Cash-settled share-based payment plan (reserved for employees to subscribe)</b>
Grant date (The date when employees confirmed)	December 18, 2017
Number of shares granted	3,569 thousand shares
Contractual life	0.137 year
Recipients	Employees of CASETEK CAYMAN and its subsidiaries
Vesting conditions	Immediately vested

- 1) Determining the fair value of equity instruments granted

CASETEK CAYMAN and its subsidiaries estimated the fair value of their share-based payment transactions at grant date. The measurement inputs were as follows:

	<b>For the year ended December 31 2017</b>
	<b>Cash-settled share-based payment plan (reserved for employees to subscribe)</b>
Fair value at grant date	NT\$ 1.12
Stock price at grant date	NT\$ 101
Exercise price	NT\$ 92
Expected volatility (%)	39.08%
Expected life of the option (year)	0.137 year
Expected dividend	-
Risk-free interest rate (%)	0.60%

(Continued)

**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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The expected volatility is based on the stock price volatility, which is calculated by the natural logarithmic rate of return, the annualized standard deviation of daily returns and the annual historical adjusted closing price. It is adjusted when there is additional market information about the volatility. The expected life of the option is in compliance with the issuance regulation of CASETEK CAYMAN and its subsidiaries. The expected dividend yield and risk-free interest rates were determined based on 1-3 month time deposits with fixed interest rate from Bank of Taiwan. Service and non-market performance conditions attached to the transactions were not taken into account in determining the fair value.

2) Expenses and equity resulting from share-based payments

Incurred expenses and equity from share-based payment transactions of CASETEK CAYMAN and its subsidiaries were as follows:

	<b>For the year ended December 31 2017</b>
Expenses resulting from issuance of restricted stock to employees	\$ 73,142
Expenses resulting from cash-settled share-based payment to employees	3,997
Total	<b>\$ 77,139</b>

(v) Treasury stock transferred to employee of KINSUS

On September 22, 2017, KINSUS transferred its treasury stock totaling 550 thousand shares to employees at the price of NT\$59.79 per share in accordance with the regulations governing secondary transfer of treasury stock to employees.

The stock option was measured at fair value at grant date.

Information on aforesaid share-based payment was as follows:

<b>Grant date</b>	<b>Total shares issued (In thousands of shares)</b>	<b>Exercise price per share</b>
September 22, 2017	550	NT\$59.79

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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Fair value of aforementioned share-based payment was measured by Black-Scholes valuation model. The assumptions adopted in this model were as follows:

	<b>Treasury stock transferred to employees</b>
Exercise price	NT\$59.79
Market price on measurement date (per share)	NT\$75.2
Expected price volatility rate (%)	25.26%
Risk-free interest rate (%)	0.6%
Expected dividend yield (%)	-%
Expected duration	0.032877 year
Fair value	NT\$15.4

Related information on the transfer of treasury stock was as follows:

	<b>For the year ended December 31</b>	
	<b>2017</b>	
	<b>Outstanding number of options (In thousand units)</b>	<b>Weighted average exercise price per share</b>
Outstanding as of January 1	-	\$ -
Granted during the year	550	59.79
Exercise during the year	(550)	(59.79)
Outstanding as of December 31	-	\$ -
Weighted-average fair value of the options granted	<b>\$ 15.4</b>	

The expense resulting from the share-based payment transactions was as follows:

	<b>For the year ended December 31</b>
	<b>2017</b>
Expense resulting from equity-settled share-based payment	<b>\$ 8,371</b>

(vi) Employee stock option of FUYANG TECHNOLOGY CORPORATION

As of December 31, 2017, FUYANG TECHNOLOGY CORPORATION had the following share-based payment transaction:

	<b>Equity-settled Employee stock option</b>
Grant date	July 10, 2017
Number of shares granted (In thousands of shares)	10,000
Contractual life	4 years
Vesting conditions	At least 2 years of service after acquisition

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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1) Determining the fair value of equity instruments granted

FUYANG TECHNOLOGY CORPORATION adopted the Black-Scholes model to calculate the fair value of the stock option at grant date, and the assumptions adopted in this valuation model were as follows:

	<b>For the year ended December 31</b>	
	<b>2017</b>	
	<b>Employee stock option issued in 2017</b>	
<u>Valuation model</u>		
Fair value at grant date	NT\$	1.54
Stock price at grant date	NT\$	8.05
Exercise price	NT\$	10.00
<u>Assumptions</u>		
Dividend yield	-	
Expected price volatility		32.81 %
Expected life of the option (years)		4 years
Risk-free interest rate (%)		0.73 %

The expected volatility rate is estimated based on peers' average annualized standard deviation of daily returns. The expected life of the option is in compliance with the issuance regulation of FUYANG TECHNOLOGY CORPORATION. The risk-free interest rate was determined based on government bonds. Service and non-market performance conditions attached to the transactions were not taken into account in determining the fair value.

2) Information on employee stock options was as follows:

	<b>For the year ended December 31</b>	
	<b>2017</b>	
	<b>Weighted- average exercise price</b>	<b>Units of stock option (In thousand units)</b>
Outstanding as of January 1, 2017	\$ -	-
Granted during the year	8.05	10,000
Exercised during the year	-	-
Outstanding as of December 31, 2017		<b>10,000</b>
Exercisable as of December 31, 2017		-

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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3) Expenses resulting from share-based payments

As of December 31, 2017, the expense resulting from the share-based payment transactions were as follows:

	<b>For the year ended December 31</b>
	<b>2017</b>
Expenses resulting from employee stock option	<b>\$ 2,370</b>

(vii) Stock appreciation rights of FUYANG ELECTRONICS (SUZHOU) CO., LTD.

On April 28, 2017, board of directors of FUYANG ELECTRONICS (SUZHOU) CO., LTD. approved to issue 5,000 thousand units of stock appreciation rights to employees with fair value of NT\$10 each. As of December 31, 2017, FUYANG ELECTRONICS (SUZHOU) CO., LTD. had two share-based payment arrangements as follows:

	<b>Stock appreciation rights (employee)</b>	
	6 years	7 yrsrs
Vesting period		
Original vested units (In thousand units)	2,500	2,500
Expected employee turnover rate	93.16%	95.63%
Vested units after considering employee turnover rate (In thousand units)	171	109
Fair value (dollars)	\$ 2.86	2.86
Service costs	\$ 489	312

(v) Earnings per share

The basic earnings per share and diluted earnings per shares were calculated as follows:

	<b>For the years ended December 31</b>	
	<b>2017</b>	<b>2016</b>
Basic earnings per share		
Profit attributable to ordinary shareholders	<b>\$ 14,682,988</b>	<b>19,339,815</b>
Weighted-average number of ordinary shares	2,592,882	2,579,930
	<b>\$ 5.66</b>	<b>7.50</b>
Diluted earnings per share		
Profit attributable to ordinary shareholders (diluted)	<b>\$ 14,682,988</b>	<b>19,339,815</b>
Weighted-average number of ordinary shares	2,592,882	2,579,930
Effect of potentially dilutive ordinary shares		
Employee stock bonus	16,663	27,941
Weighted-average number of ordinary shares (diluted)	2,609,545	2,607,871
	<b>\$ 5.63</b>	<b>7.42</b>

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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## (w) Revenue

	<b>For the years ended December 31</b>	
	<b>2017</b>	<b>2016</b>
Sale of goods	\$ 1,152,703,488	1,074,052,905
Others	41,105,027	83,657,208
	<b><u>\$ 1,193,808,515</u></b>	<b><u>1,157,710,113</u></b>

## (x) Remuneration of employees and directors

Based on the amended Company's Articles of Incorporation, remuneration of employees and directors are appropriated at the rate of at least 7% and no more than 0.7% of profit before tax, respectively. Prior years' accumulated deficit is first offset before any appropriation of profit. Employees of subsidiaries may also be entitled to the employee remuneration of the Company, which can be settled in the form of cash or stock.

For the years ended December 31, 2017 and 2016, remuneration of employees of \$1,188,000 and \$1,734,000, respectively, and remuneration of directors of \$115,000 and \$166,000, respectively, were estimated on the basis of the Company's net profit before tax, excluding the remuneration of employees and directors of each period, multiplied by the percentage of remuneration of employees and directors as specified in the Company's Articles of Incorporation. Such amounts were recognized as operating cost or operating expense for the years ended December 31, 2017 and 2016. Management is expecting that the differences, if any, between the actual distributed amounts and estimated amounts will be treated as changes in accounting estimates and charged to profit or loss. The number of shares to be distributed were calculated based on the closing price of the Company's ordinary shares, one day prior to Board of Directors meeting. There was no difference between the amounts approved in Board of Directors meeting and recognized for the years ended December 31, 2017 and 2016. For further information, please refer to Market Observation Post System.

## (y) Non-operating income and expenses

## (i) Other income

	<b>For the years ended December 31</b>	
	<b>2017</b>	<b>2016</b>
Interest income	\$ 1,499,714	1,057,275
Subsidy income	1,106,003	845,078
Rental income	235,994	253,063
Technical service income	393,739	251,385
Other income	938,169	765,332
	<b><u>\$ 4,173,619</u></b>	<b><u>3,172,133</u></b>

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

## (ii) Other gains and losses

	<b>For the years ended December 31</b>	
	<b>2017</b>	<b>2016</b>
Gain on reversal of uncollectable account	\$ 198,966	70,336
Loss on disposal of property, plant and equipment	(46,833)	(150,078)
Gain (loss) from disposal of investments	38,091	(574,526)
Foreign exchange loss	(1,555,274)	(4,383,186)
Reversal of (Impairment loss)	34,474	(59,968)
Net gain on evaluation of financial assets measured at fair value through profit or loss	146,321	67,790
Other losses	(470,924)	(217,855)
	<b><u>\$ (1,655,179)</u></b>	<b><u>(5,247,487)</u></b>

## (iii) Finance costs

	<b>For the years ended December 31</b>	
	<b>2017</b>	<b>2016</b>
Interest expenses	\$ 951,706	912,165
Finance expense – bank fees	66,298	92,841
	<b><u>\$ 1,018,004</u></b>	<b><u>1,005,006</u></b>

## (z) Reclassification of other comprehensive income

	<b>For the years ended December 31</b>	
	<b>2017</b>	<b>2016</b>
Available-for-sale financial assets		
Net change in fair value	\$ 541,228	(14,425)
Share of other comprehensive income of associates accounted for using equity method	157,980	-
Reclassification to profit or loss for losing control of subsidiaries	-	(12,856)
Net fair value change recognized in other comprehensive income	<b><u>\$ 699,208</u></b>	<b><u>(27,281)</u></b>
Cumulative adjustment		
Cumulative adjustment from current year	\$ (6,154,844)	(7,263,087)
Share of other comprehensive income (loss) of associates accounted for using equity method	9,409	(48,217)
Reclassification to profit or loss for losing control of subsidiaries	-	6,248
Net fair value change recognized in other comprehensive income	<b><u>\$ (6,145,435)</u></b>	<b><u>(7,305,056)</u></b>

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

(aa) Financial instruments

(i) Credit risk

1) Exposure to credit risk

The carrying amount of financial assets represents the Group's maximum credit exposure.

2) Credit risk concentrations

As of December 31, 2017 and 2016, the accounts receivable from the Group's top three customers amounted to \$92,809,599 and \$44,383,971, representing 61% and 47% of accounts receivable, respectively, which exposes the Group to credit risk.

3) Impairment losses

Aging analysis of the receivables on the balance sheet date were as follows:

	<b>December 31, 2017</b>	<b>December 31, 2016</b>
Not past due	\$ 147,767,079	133,275,190
Past due 0 - 30 days	2,429,404	2,478,288
Past due 31 - 120 days	151,490	286,556
Past due 121 - 365 days	283,491	86,671
Past due more than 1 year	<u>2,010,431</u>	<u>1,690,475</u>
	<b><u>\$ 152,641,895</u></b>	<b><u>137,817,180</u></b>

The movement in the allowance for impairment with respect to the receivables for the years ended December 31, 2017 and 2016 was as follows:

	<b>Individually assessed impairment</b>	<b>Collectively assessed impairment</b>	<b>Total</b>
Balance on January 1, 2017	\$ 71,343	1,839,270	1,910,613
Recognition of loss from impairment	53,993	9,461	63,454
Reversal of impairment loss	(15)	(225,566)	(225,581)
Written off unrecoverable amount	-	(1,223)	(1,223)
Foreign exchange gain	<u>(5,866)</u>	<u>(4,587)</u>	<u>(10,453)</u>
Balance on December 31, 2017	<b><u>\$ 119,455</u></b>	<b><u>1,617,355</u></b>	<b><u>1,736,810</u></b>

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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	<b>Individually assessed impairment</b>	<b>Collectively assessed impairment</b>	<b>Total</b>
Balance on January 1, 2016	\$ 73,559	2,054,366	2,127,925
Recognition of loss from impairment	12	-	12
Reversal of impairment loss	-	(36,772)	(36,772)
Foreign exchange gain	(2,228)	(2,302)	(4,530)
Loss of control of a subsidiary	-	(176,022)	(176,022)
Balance on December 31, 2016	<u>\$ 71,343</u>	<u>1,839,270</u>	<u>1,910,613</u>

(ii) Liquidity risk

The following are the contractual maturities of financial liabilities, excluding estimated interest payment and the impact of netting agreements.

	<u>Carrying amount</u>	<u>Contractual cash flows</u>	<u>Within 1 year</u>	<u>1-2 years</u>	<u>More than 2 years</u>
<b>December 31, 2017</b>					
Non-derivative financial liabilities					
Secured bank loans	\$ 101,000	101,000	54,625	28,375	18,000
Unsecured bank loans	54,019,732	54,019,732	47,111,307	640,700	6,267,725
Unsecured ordinary corporate bond	7,000,000	7,000,000	-	-	7,000,000
Non-interest bearing liabilities	<u>225,450,155</u>	<u>225,450,155</u>	<u>225,450,155</u>	<u>-</u>	<u>-</u>
	<u>\$ 286,570,887</u>	<u>286,570,887</u>	<u>272,616,087</u>	<u>669,075</u>	<u>13,285,725</u>
<b>December 31, 2016</b>					
Non-derivative financial liabilities					
Secured bank loans	\$ 171,000	171,000	56,000	46,625	68,375
Unsecured bank loans	36,044,615	36,044,615	31,628,725	3,180,575	1,235,315
Non-interest bearing liabilities	<u>201,926,183</u>	<u>201,926,183</u>	<u>201,926,183</u>	<u>-</u>	<u>-</u>
	<u>\$ 238,141,798</u>	<u>238,141,798</u>	<u>233,610,908</u>	<u>3,227,200</u>	<u>1,303,690</u>

The liquidity of the aforesaid bank loans does not include interest expense on cash outflow.

The Group is not expecting that the cash flows included in the maturity analysis could occur significantly earlier or at significantly different amounts.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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(iii) Currency risk

1) Currency risk exposure

The Group's exposures to significant currency risk were those from its foreign currency denominated financial assets and liabilities as follows:

(Unit: Foreign currency / NTD in Thousands)

	December 31, 2017			December 31, 2016		
	Foreign Currency	Exchange Rate	NTD	Foreign Currency	Exchange Rate	NTD
<u>Financial assets</u>						
<u>Monetary items</u>						
USD:NTD	\$ 11,672,655	29.760	347,378,213	10,433,545	32.25	336,481,826
USD:CNY	339,735	6.5342	10,110,518	8,227,417	6.937	265,335,128
USD:CZK	56,342	21.2916	1,676,738	39,837	25.6342	1,284,759
CNY:NTD	111,783	4.5545	509,116	1,175,798	4.649	5,466,285
<u>Financial liabilities</u>						
<u>Monetary items</u>						
USD:NTD	11,389,063	29.760	338,938,515	10,062,359	32.25	324,511,078
USD:CNY	262,842	6.5342	7,822,182	9,582,667	6.937	309,042,094
USD:CZK	28,305	21.2916	842,357	21,448	25.6342	691,706
CNY:NTD	149,726	4.5545	681,927	729,450	4.649	3,391,213

2) Sensitivity analysis

The Group's exposure to foreign currency risk arises from the translation of the foreign currency exchange gains and losses on cash and cash equivalents, accounts receivable, other receivables, loans, accounts payable and other payables that are denominated in foreign currency. A 1% of appreciation or depreciation of each major foreign currency against the Group's functional currency as of December 31, 2017 and 2016 would have increased (decreased) the before-tax net income for the years ended December 31, 2017 and 2016 by \$13,442 and \$(291,494), respectively. This analysis is based on foreign currency exchange rate variances that the Group considered to be reasonably possible at the reporting date. The analysis assumes that all other variables remain constant. The analysis is performed on the same basis for both periods.

3) Gains or losses on monetary item

As the Group deals in diverse foreign currencies, gains or losses on foreign exchange were summarized as a single amount. For the years ended December 31, 2017 and 2016, the foreign exchange losses, including both realized and unrealized, amounted to \$1,555,274 and \$4,383,186, respectively.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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(iv) Interest rate analysis

The interest risk exposure from financial assets and liabilities has been disclosed in the note of liquidity risk management.

The following sensitivity analysis is based on the risk exposure to interest rates on the derivative and non-derivative financial instruments at the reporting date.

For variable rate instruments, the sensitivity analysis assumes the variable rate liabilities are outstanding for the whole year at the reporting date. The Group's internal management reported the increases/decreases in the interest rates and the exposure to changes in interest rates of 1% is considered by management to be a reasonable change of interest rate.

If the interest rate increases / decreases by 1%, the Group's net income will decrease /increase by \$103,242 and \$97,067 for the years ended December 31, 2017 and 2016, respectively, assuming all other variable factors remain constant. This is mainly due to the Group's variable rate borrowing.

(v) Fair value of financial instruments

The fair value of financial assets and liabilities were as follows (including information on fair value hierarchy, but excluding measurements that have similarities to fair value but are not fair value and those fair value cannot be reliably measured or inputs are unobservable in active markets) :

1) Categories of financial instruments

Financial Assets:

	<b>December 31, 2017</b>	<b>December 31, 2016</b>
Financial assets at fair value through profit or loss		
Held-for-trading non-derivative financial assets	\$ <u>2,824,913</u>	<u>4,367,847</u>
Available-for-sale financial assets	<u>1,543,613</u>	<u>1,056,145</u>
Financial assets carried at cost	<u>350,509</u>	<u>371,082</u>
Deposits and receivables		
Cash and cash equivalents	107,444,124	108,713,312
Notes, accounts and other receivables	150,905,085	135,906,567
Other financial assets	<u>1,523,440</u>	<u>907,165</u>
Sub-total	<u>259,872,649</u>	<u>245,527,044</u>
Total	<u>\$ <b>264,591,684</b></u>	<u><b>251,322,118</b></u>

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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Financial liabilities:

	<u>December 31, 2017</u>	<u>December 31, 2016</u>
Financial liabilities carried at amortized cost		
Short-term loans	\$ 46,058,620	31,148,468
Notes, accounts, other payables and accrued expenses	225,450,155	201,926,183
Bonds payable	6,992,476	-
Long-term loans (including current portion)	8,062,112	5,059,147
Guarantee deposit (recognized in other noncurrent liabilities)	<u>818,529</u>	<u>527,461</u>
Total	<u>\$ 287,381,892</u>	<u>238,661,259</u>

2) Fair value hierarchy

The table below analyses financial instruments carried at fair value, by the levels in the fair value hierarchy. The different levels have been defined as follows:

- a) Level 1: quoted prices (unadjusted) in active markets for identified assets or liabilities.
- b) Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).
- c) Level 3: inputs for the assets or liability that are not based on observable market data (unobservable inputs).

	<u>December 31, 2017</u>				
	<u>Book Value</u>	<u>Fair Value</u>			<u>Total</u>
	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>		
Financial Assets					
Financial assets designated as at fair value through profit or loss					
Held-for-trading non-derivative financial assets	\$ 2,824,913	2,824,913	-	-	2,824,913
Available-for-sale financial assets					
Stock of listed companies	721,071	721,071	-	-	721,071
Equity investment – common stock	437,760	-	437,760	-	437,760
Stock of overseas listed companies	<u>384,782</u>	<u>384,782</u>	<u>-</u>	<u>-</u>	<u>384,782</u>
Total	<u>\$ 4,368,526</u>	<u>3,930,766</u>	<u>437,760</u>	<u>-</u>	<u>4,368,526</u>

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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	December 31, 2016				
	Book Value	Fair Value			Total
		Level 1	Level 2	Level 3	
Financial Assets					
Financial assets designated as at fair value through profit or loss					
Held-for-trading non-derivative financial assets	\$ 4,367,847	4,367,847	-	-	4,367,847
Available-for-sale financial assets					
Stock of listed companies	610,702	610,702	-	-	610,702
Equity investment – common stock	178,920	-	178,920	-	178,920
Stock of overseas listed companies	<u>266,523</u>	<u>266,523</u>	<u>-</u>	<u>-</u>	<u>266,523</u>
Total	<u>\$ 5,423,992</u>	<u>5,245,072</u>	<u>178,920</u>	<u>-</u>	<u>5,423,992</u>

There have been no transfers from each level for the years ended December 31, 2017 and 2016.

3) Valuation techniques for financial instruments not measured at fair value:

The assumptions and methods used in valuing financial instruments that are not measured at fair value are as follows:

a) Financial assets measured at amortized cost

Fair value measurement for financial assets and liabilities is based on the latest quoted price and agreed-upon price if these prices are available in active market. When market value is unavailable, fair value of financial assets and liabilities are evaluated based on the discounted cash flow of the financial assets and liabilities.

4) Valuation techniques for financial instruments measured at fair value:

a) Non-derivative financial instruments

Financial instruments trade in active markets is based on quoted market prices.

If quoted price of a financial instrument can be obtained in time and often from exchanges, brokers, underwriters, industrial union, pricing institute, or authorities and such price can reflect those actual trading and frequently happen in the market, then the financial instrument is considered to have quoted price in active market. If a financial instrument does not accord with the definition aforementioned, then it is considered to be without quoted price in active market. In general, market with low trading volume or high bid-ask spreads is an indication of non-active market.

Measurements of fair value of financial instruments without active market are based on valuation technique or quoted price from competitor. Fair value measured by valuation technique can be extrapolated from similar financial instruments, discounted cash flow method or other valuation technique which include model calculating with observable market data at the balance sheet date.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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b) Derivative financial instruments

It is based on the valuation model accepted by the most market users, ex: Discount rate and option pricing model. Forward exchange agreement is usually based on the current forward rate.

Fair value of structured financial instruments is based on appropriated valuation model, ex: Black-Scholes model, or other valuation model, ex: Monte Carlo simulation.

(vi) Offsetting of financial assets and financial liabilities

The Group has financial assets and liabilities which are subject to the guidance concerning financial instrument transactions under paragraph 42 of IAS 32 as endorsed by the Financial Supervisory Commission. These financial assets and liabilities are presented on a net basis in balance sheet.

The following table presents the recognized financial instruments that are subject to offsetting agreement or contract and have legally enforceable right to set off:

December 31, 2017						
Financial assets subject to offsetting agreement or contract and have legally enforceable right to set off.						
	Gross Assets (a)	Gross Liabilities Offset (b)	Net amounts presented (c)=(a)-(b)	Amounts not offset (d)		
				Financial Instruments (Note)	Cash collected as pledge	Net amounts (e)=(c)-(d)
Accounts Receivable and Payable	\$ 31,766,866	22,767,959	8,998,907	-	-	8,998,907
December 31, 2017						
Financial liabilities subject to offsetting agreement or contract and have legally enforceable right to set off.						
	Gross Liabilities (a)	Gross Assets Offset (b)	Net amounts presented (c)=(a)-(b)	Amounts not offset (d)		
				Financial Instruments (Note)	Cash collected as pledge	Net amounts (e)=(c)-(d)
Accounts Receivable and Payable	\$ 22,767,959	22,767,959	-	-	-	-
December 31, 2016						
Financial assets subject to offsetting agreement or contract and have legally enforceable right to set off.						
	Gross Assets (a)	Gross Liabilities Offset (b)	Net amounts presented (c)=(a)-(b)	Amounts not offset (d)		
				Financial Instruments (Note)	Cash collected as pledge	Net amounts (e)=(c)-(d)
Accounts Receivable and Payable	\$ 31,365,382	25,397,763	5,967,619	-	-	5,967,619
December 31, 2016						
Financial liabilities subject to offsetting agreement or contract and have legally enforceable right to set off.						
	Gross Liabilities (a)	Gross Assets Offset (b)	Net amounts presented (c)=(a)-(b)	Amounts not offset (d)		
				Financial Instruments (Note)	Cash collected as pledge	Net amounts (e)=(c)-(d)
Accounts Receivable and Payable	\$ 25,397,763	25,397,763	-	-	-	-

Note: The master netting arrangement and non-cash collateral were included.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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(ab) Financial risk management

(i) Overview

The nature and the extent of the Group's risks arising from financial instruments, which include credit risk, liquidity risk and market risk, are discussed below. Also, the Group's objectives, policies and procedures of measuring and managing risks are discussed below.

For more quantitative information about the financial instruments, please refer to the other related notes of consolidated interim financial reports.

(ii) Risk management framework

The Board of Directors has overall responsibility for the establishment and oversight of the risk management framework. The Board has deputized managements of core business departments for developing and monitoring the Group's risk management policies. Management reports regularly to the Board of Directors on its activities.

The Group's risk management policies are established to identify and analyze the risks faced by the Group, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Group's activities. The Group, through their training and management standards and procedures, aims to develop a disciplined and constructive control environment in which all employees understand their roles and obligations.

The Group's Internal Audit Department oversees how management monitors compliance with the Group's risk management policies and procedures and reviews the adequacy of the risk management framework in relation to the risks faced by the Group. Internal Audit undertakes both regular and ad hoc reviews of risk management controls and procedures and exception management, the results of which are reported to the Board of Directors.

(iii) Credit risk

The primary potential credit risk is from financial instruments like cash, equity securities, and accounts receivable. Also, the Group deposits cash in different financial institutions. The Group manages credit risk exposure related to each financial institution and believes that there is no significant concentration of credit risk on cash and equity securities.

The Group transacted only with the approved third parties with good financial conditions and reputation. For those customers with poor financial situation, the Group would transfer the risk through acquiring guarantees or transacting by L/C. Therefore, the Group believes that there is no significant credit risk.

1) Accounts receivables and other receivables

The Group's exposure to credit risk is influenced mainly by the individual characteristics of each customer. However, management also considers the demographics of the Group's customer base, including the default risk of the industry and country in which customers operate, as these factors may have an influence on credit risk, particularly in the current deteriorating economic circumstances.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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Under its customer credibility evaluation policies, the Group evaluates the customer's credibility and collectability of notes and account receivables regularly before doing business. Thus, management is not expecting any significant uncollectible accounts.

The major customers of the Group are concentrated in the high-tech computer industry. As the customers of the Group have good credits and profit records, the Group evaluates the financial conditions of these customers continually to reduce credit risk from accounts receivable. Moreover, the Group also periodically evaluates the customers' financial positions and the possibility of collecting trade receivables. Thus, management is not expecting any significant issue on credit risk.

The Group establishes an impairment allowance that represents its estimate of incurred losses in respect of trade receivables. The two components of this impairment allowance are specific loss component that relates to individually significant exposure and collective loss component which the loss was incurred but not identified. The collective component is based on historical payment experience of similar financial assets.

2) Investment

The credit risk exposure in the bank deposits, fixed income investments and other financial instruments are measured and monitored by the Group's finance department. As the Group deals with the banks and other external parties with good credit standing and financial institutions, corporate organization and government agencies which are graded above investment level, management believes that the Group do not have compliance issues and no significant credit risk.

3) Guarantee

The Group's policies were prepared in accordance with Guidelines for Lending of Capital, Endorsements and Guarantees by Public Companies. Please refer to Notes 9 and 13 for details of endorsements and guarantees provided by the Group as of December 31, 2017 and 2016.

(iv) Liquidity risk

Liquidity risk is a risk that the Group is unable to meet the obligations associated with its financial liabilities that are settled by delivering cash or another financial asset. The Group's approach to managing liquidity is to ensure, as much as possible, that it always has sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation.

The capital and working funds of the Group are sufficient to meet its entire contractual obligations and non-hedging forward exchange contracts; therefore, management is not expecting any significant issue on liquidity risk.

The funds and marketable securities investments held by the Group have publicly quoted prices and could be sold at approximate market price.

Equity investments recorded as financial assets carried at cost do not have reliable market prices and are expected to have liquidity risk.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

(v) Market risk

Market risk is a risk that arises from changes in market prices, such as foreign exchange rates, interest rates and equity prices that affect the Group's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimizing the return.

1) Currency risk

The Group is exposed to currency risk on sales, purchases and borrowings that are denominated in a currency other than the respective functional currencies of the Group's entities, primarily the New Taiwan Dollars (NTD), US Dollars (USD) and Chinese Yuan (CNY). The currencies used in these transactions are denominated in NTD, EUR, USD, and CNY.

The Group's foreign currency denominated purchases and sales are denominated mainly in US dollars. This exposes the Group to the current and future foreign exchange fluctuation risk that arises from cash flows of foreign currency assets and liabilities. However, the risks may be regarded as insignificant, because foreign currency losses from sales are subsequently offset by the foreign currency gain from purchases. In addition, the Group conducts foreign exchange activities on spot market in order to manage its foreign exchange risks.

The interest is denominated in the same currency as borrowings. Generally, borrowings are denominated in currencies that match the cash flows generated by the underlying operations of the Group. This provides an economic hedge without derivatives being entered into, and therefore, hedge accounting is not applied in these circumstances.

In respect of other monetary assets and liabilities denominated in foreign currencies, the Group ensures that its net exposure is kept to an acceptable level by buying or selling foreign currencies at spot rates when necessary to address short-term imbalances.

2) Interest rate risk

The Group's interest rate risk arises from short-term and long-term loans bearing floating interest rates. Future cash flow will be affected by a change in market interest rate.

3) Price floating risk on equity instruments

The equity securities held by the Group are classified as financial assets measured at fair value through profit or loss and available-for-sale financial assets. As these assets are measured at fair value, the Group is exposed to the market price fluctuation risk in the equity securities market.

The Group's investment portfolios of equity instruments are reviewed regularly by management, and significant investment decision is approved by the Board of Directors.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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(ac) Capital management

The Board's policy is to maintain a strong capital base in order to maintain investor, creditor and market confidence and to sustain future development of the business. Capital consists of ordinary shares, non-redeemable preference shares, retained earnings and non-controlling interests of the Group. The Board of Directors monitors the return on capital as well as the level of dividends to ordinary shareholders.

The Group uses the debt-to-equity ratio, interest bearing liability-to-equity ratio and other financial ratio to maintain an optimal capital structure and raise returns on equity.

The Group's debt to equity ratios at the balance sheet date were as follows:

	<u>December 31,</u> <u>2017</u>	<u>December 31,</u> <u>2016</u>
Total liabilities	\$ 308,511,809	261,923,032
Less: cash and cash equivalents	<u>107,444,124</u>	<u>108,713,312</u>
Net debt	<u>\$ 201,067,685</u>	<u>153,209,720</u>
Total capital (Note)	<u>\$ 380,791,495</u>	<u>335,231,921</u>
Debt to equity ratio	<u>52.80%</u>	<u>45.70%</u>

Note : Total capital includes share capital, capital surplus, retained earnings, other equity and non-controlling interest and net debt.

Management believes that there were no changes in the Group's approach to capital management for the year ended December 31, 2017.

**(7) Related-party transactions:**

(a) The ultimate parent company

The Company is the ultimate parent company of the Group.

(b) Names and relationship with related parties

The following are entities that have had transactions with related parties and the Group during the periods covered in the consolidated financial statements.

<u>Name of related party</u>	<u>Relationship with the Group</u>
HONGJIE (SUZHOU) PACKING LIMITED	Other related party
Altasec Technology Corporation	Other related party
GREEN PACKING LIMITED	Other related party

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements**

(c) Significant transactions with related parties

(i) Sale of Goods to Related Parties

The amounts of significant sales transactions and outstanding balances between the Group and related parties were as follows:

	<u>Sales</u>		<u>Receivables from related parties</u>	
	<u>For the years ended December 31</u>		<u>December 31,</u>	<u>December 31,</u>
	<u>2017</u>	<u>2016</u>	<u>2017</u>	<u>2016</u>
Other related parties	\$ <u>-</u>	<u>662</u>	<u>-</u>	<u>-</u>

There were no significant differences between the terms and pricing of sales transactions with related enterprises and those carried out with other normal vendors. The average collection period for notes and accounts receivable pertaining to such sale transactions ranged from one to three months. Receivables from related parties were not secured with collaterals, and did not require provisions for bad debt expenses.

(ii) Purchase of Goods from Related Parties

The amounts of significant purchase transactions and outstanding balances between the Group and related parties were as follows:

	<u>Purchases</u>		<u>Payables to Related Parties</u>	
	<u>For the years ended December 31</u>		<u>December 31,</u>	<u>December 31,</u>
	<u>2017</u>	<u>2016</u>	<u>2017</u>	<u>2016</u>
Other related parties	\$ <u>88</u>	<u>41,357</u>	<u>14</u>	<u>4,472</u>

There were no significant differences between the terms and pricing of purchase transactions with related enterprises and those carried out with other normal vendors. The average payment period for notes and accounts payable pertaining to such purchase transactions ranged from one to four months, which is similar to that of other normal vendors.

(d) Key management personnel compensation:

	<u>For the years ended December 31</u>	
	<u>2017</u>	<u>2016</u>
Short-term employee benefits	\$ 488,481	443,410
Post-employment benefits	3,371	3,527
Share-based payments	<u>286,538</u>	<u>158,955</u>
	<u>\$ 778,390</u>	<u>605,892</u>

Please refer to Notes 6(t) and 6(u) for further explanations related to share-based payment transactions.

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**(8) Pledged assets:**

As of December 31, 2017 and 2016, pledged assets were as follows:

<u>Asset</u>	<u>Purpose of pledge</u>	<u>December 31, 2017</u>	<u>December 31, 2016</u>
Other financial asset-restricted deposit	Post-release duty deposits, customs duty, rental deposits, travel agency guarantee, etc.	\$ 73,297	46,691
Property, plant and equipment	Bank loans	143,554	249,649
Other financial asset-guarantee deposits	Customs duty guarantee, rental deposits, and deposits for performance guarantee	35,348	37,382
		<u>\$ 252,199</u>	<u>333,722</u>

**(9) Significant commitments and contingencies:**

(a) Significant commitments and contingencies were as follows:

(i) Unused standby letters of credit

	<u>December 31, 2017</u>	<u>December 31, 2016</u>
EUR	\$ 2,589	2,655
JPY	2,968,349	1,454,932
USD	5,853	8,469
CNY	-	955

(ii) Promissory notes and certificates of deposit obtained for business purpose were as follows:

	<u>December 31, 2017</u>	<u>December 31, 2016</u>
NTD	<u>\$ 78,998</u>	<u>87,869</u>

(iii) As of December 31, 2017 and 2016, the significant contracts for purchase of properties by the Group amounted to \$24,033,496 and \$11,554,587, of which \$10,860,011 and \$2,830,075, respectively, were unpaid.

(iv) As of December 31, 2017 and 2016, the Group provided endorsement guarantee for bank loans obtained by the related parties, including Group entities, amounting to \$3,779,520 and \$8,850,948, respectively.

(v) As of December 31, 2017 and 2016, the Group issued a tariff guarantee of \$1,689,442 and \$662,165, respectively, to the bank for the purpose of importing goods.

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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(b) Significant contingent liability:

In May 2017, QUALCOMM INCORPORATED filed a lawsuit against the Group for royalty payment under the license agreement in the U.S. District Court for the Southern District of California. In July 2017, the Group counterclaimed. The outcome of this lawsuit depends on court proceedings and is not expected to have a material effect on the Group's operation.

**(10) Losses due to major disasters: None.**

**(11) Subsequent events:**

According to the amendments to the "Income Tax Act" enacted by the office of the President of the Republic of China (Taiwan) on February 7, 2018, an increase in the corporate income tax rate from 17% to 20% is applicable upon filing the FY 2018 corporate income tax return. This increase does not affect the amounts of the current and deferred income taxes recognized on December 31, 2017. However, it will increase the Group's current and deferred tax charge accordingly in the future. On the other hand, if the new tax rate is applied in calculating the taxable temporary differences and unused tax losses recognized on December 31, 2017, the deferred tax assets and deferred tax liabilities would increase by \$117,256 and \$57,531, respectively.

**(12) Other:**

The nature of employee benefits, depreciation and amortization expenses categorized by function, were as follows:

By function	For the year ended December 31, 2017			For the year ended December 31, 2016		
	Operating Cost	Operating expense	Total	Operating Cost	Operating expense	Total
Employee benefit						
Salary	\$ 50,119,863	14,779,941	64,899,804	44,130,325	16,128,396	60,258,721
Health and labor insurance	5,103,857	934,649	6,038,506	4,824,910	933,909	5,758,819
Pension	4,433,255	848,178	5,281,433	4,920,426	892,725	5,813,151
Others	1,773,415	858,011	2,631,426	1,713,449	789,294	2,502,743
Depreciation	11,157,465	1,714,742	12,872,207	11,438,450	1,323,819	12,762,269
Amortization	122,562	111,237	233,799	38,802	102,746	141,548

Above depreciations did not include depreciation in investment property which was accounted under non-operating expense as follows:

	<u>For the years ended December 31</u>	
	<u>2017</u>	<u>2016</u>
Depreciation in investment property	<u>\$ 3,149</u>	<u>8,594</u>

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**PEGATRON CORPORATION AND ITS SUBSIDIARIES**  
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**(13) Segment information:****(a) General Information**

The Group's operating segments required to be disclosed are categorized as DMS (Design, Manufacturing and Service) and Strategic Investment Group. DMS's main operating activities are designing and manufacturing computer, communication and consumer electronics' end products, and providing after-sales service. Strategic Investment Group is DMS's upstream and downstream supply chain, strategic investments and other related investments arms. The chief operating decision maker's main responsibility is to integrate strategy that creates operating synergy throughout the supply chain and to allocate the profit from the operating result. The Group assesses performance of the segments based on the segments' profit, and report the amounts of revenues based on the financial information used to prepare the consolidated interim financial report.

**(b) Reportable segment profit or loss, segment assets, segment liabilities, and their measurement and reconciliations**

The Group uses the internal management report that the chief operating decision maker reviews as the basis to determine resource allocation and make a performance evaluation. The internal management report includes profit before taxation, excluding any extraordinary activity and foreign exchange gain or losses, because taxation, extraordinary activity and foreign exchange gains or losses are managed on a group basis, and hence they are not able to be allocated to each reportable segment. In addition, not all reportable segments include depreciation and amortization of significant non-cash items. The reportable amount is similar to that in the report used by the chief operating decision maker.

The operating segment accounting policies are similar to the ones described in Note 4 "Significant accounting policies" except for the recognition and measurement of pension cost, which is on a cash basis. The Group treated intersegment sales and transfers as third-party transactions. They are measured at market price.

The Group's operating segment information and reconciliation were as follows:

	<b>For the year ended December 31</b>			
	<b>2017</b>			
	<b>DMS</b>	<b>Strategic Investment Group</b>	<b>Adjustment and eliminations</b>	<b>Total</b>
Revenue :				
Revenue from external customers	\$ 1,114,498,123	79,310,392	-	1,193,808,515
Intersegment revenues	598,538	5,337,413	(5,935,951)	-
Total revenue	<u>\$ 1,115,096,661</u>	<u>84,647,805</u>	<u>(5,935,951)</u>	<u>1,193,808,515</u>
Share of profit of associates and joint ventures accounted for using equity method	<u>\$ 964,610</u>	<u>10,175,786</u>	<u>(11,144,880)</u>	<u>(4,484)</u>
Other significant non-monetary items:				
Goodwill	\$ -	1,040,879	-	1,040,879
<b>Reportable segment profit or loss</b>	<u>\$ 17,617,935</u>	<u>13,932,664</u>	<u>(11,137,549)</u>	<u>20,413,050</u>
Assets:				
Investments accounted for using equity method	\$ 41,824,169	98,099,017	(139,419,468)	503,718
<b>Reportable segment assets</b>	<u>\$ 411,234,014</u>	<u>216,441,900</u>	<u>(139,440,295)</u>	<u>488,235,619</u>
<b>Reportable segment liabilities</b>	<u>\$ 265,258,276</u>	<u>43,274,359</u>	<u>(20,826)</u>	<u>308,511,809</u>

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	<b>For the year ended December 31</b>			
	<b>2016</b>			
	<b>DMS</b>	<b>Strategic Investment Group</b>	<b>Adjustment and eliminations</b>	<b>Total</b>
Revenue :				
Revenue from external customers	\$ 1,078,907,440	78,802,673	-	1,157,710,113
Intersegment revenues	<u>1,831,481</u>	<u>2,775,907</u>	<u>(4,607,388)</u>	<u>-</u>
Total revenue	<u>\$ 1,080,738,921</u>	<u>81,578,580</u>	<u>(4,607,388)</u>	<u>1,157,710,113</u>
Share of profit of associates and joint ventures accounted for using equity method	<u>\$ 3,056,365</u>	<u>9,734,983</u>	<u>(12,794,479)</u>	<u>(3,131)</u>
Other significant non-monetary items:				
Goodwill	<u>\$ -</u>	<u>1,127,841</u>	<u>-</u>	<u>1,127,841</u>
<b>Reportable segment profit or loss</b>	<u>\$ 24,288,805</u>	<u>17,581,738</u>	<u>(12,790,873)</u>	<u>29,079,670</u>
Assets:				
Investments accounted for using equity method	<u>\$ 43,218,838</u>	<u>92,221,847</u>	<u>(135,077,776)</u>	<u>362,909</u>
<b>Reportable segment assets</b>	<u>\$ 373,147,174</u>	<u>206,242,122</u>	<u>(135,444,063)</u>	<u>443,945,233</u>
<b>Reportable segment liabilities</b>	<u>\$ 224,877,585</u>	<u>37,411,735</u>	<u>(366,288)</u>	<u>261,923,032</u>

## (c) Geographic information

In presenting information on the basis of geography, segment revenue is based on the geographical location of customers, and segment assets are based on the geographical location of the assets.

## (i) External Sales

<b>Region</b>	<b>For the years ended December 31</b>	
	<b>2017</b>	<b>2016</b>
Europe	\$ 453,169,704	332,669,838
USA	407,742,938	396,964,194
Taiwan	149,381,904	170,921,579
China	71,290,164	103,033,702
Japan	67,788,946	87,650,950
Others	<u>44,434,859</u>	<u>66,469,850</u>
	<u>\$ 1,193,808,515</u>	<u>1,157,710,113</u>

(Continued)

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## (ii) Non-current assets

<u>Region</u>	<u>December 31, 2017</u>	<u>December 31, 2016</u>
Taiwan	\$ 24,801,356	20,868,460
China	60,560,120	52,969,239
Others	<u>778,442</u>	<u>882,559</u>
Total	<u>\$ 86,139,918</u>	<u>74,720,258</u>

Non-current assets include property, plant and equipment, investment property, intangible assets and other non-current assets, excluding financial instruments, deferred tax assets, pension fund assets, and rights arising from an insurance contract (non-current).

## (d) Major Customer

Major customers from DMS in 2017 and 2016 were as follows:

<u>Customer</u>	<u>2017</u>	<u>2016</u>
A	\$ 733,049,391	691,091,107
B	111,201,206	125,455,471
C	<u>60,744,975</u>	<u>77,163,832</u>
	<u>\$ 904,995,572</u>	<u>893,710,410</u>