

(English Translation of Financial Report Originally Issued in Chinese)

PEGATRON CORPORATION

FINANCIAL STATEMENTS

DECEMBER 31, 2012 AND 2011

(With Independent Accountants' Audit Report Thereon)

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(English Translation of Financial Report Originally Issued in Chinese)

AUDIT REPORT OF INDEPENDENT ACCOUNTANTS

To the Board of Directors of
Pegatron Corporation

We have audited the accompanying balance sheets of Pegatron Corporation (the “Company”) as of December 31, 2012 and 2011, and the related statements of income, changes in stockholders’ equity and cash flows for the years then ended. These financial statements are the responsibility of the Company’s management. Our responsibility is to express the audit report based on our audits. We did not audit the financial statements of certain investees accounted for under the equity method, in which the Company’s long-term equity investments amounted to NT\$ 22,289,553 thousand and NT\$ 18,996,148 thousand, representing 6.93% and 8.65% of total assets as of December 31, 2012 and 2011, respectively, and related investment income was NT\$ 2,139,088 thousand and NT\$ 2,044,432 thousand, representing 32.70% and 3,493.90% of net income before tax for the years ended December 31, 2012 and 2011, respectively. The financial statements of these investees 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, is based solely on the reports of other auditors.

We conducted our audits in accordance with “Regulation Governing Auditing and Certification of Financial Statements by Certified Public Accountants” and auditing standards generally accepted in the Republic of China. Those regulations and standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatements. An audit includes examining, on a test basis, evidences supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits and the reports issued by other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audits and the reports of other auditors, the accompanying financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2012 and 2011, the results of its operations and its cash flows for the years then ended in conformity with the Guidelines Governing the Preparation of Financial Reports by Securities Issuers and accounting principles generally accepted in the Republic of China.

We have also audited the consolidated financial statements of the Company as of and for the years ended December 31, 2012 and 2011 and have issued modified unqualified audit report thereon.

CPA: Ulyos Maa
Securities and Futures Commission,
Ministry of Finance, R.O.C. regulation
(88) Tai-Tsai-Jung (6) No. 18311

March 21, 2013

Note to Readers

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

For the convenience of readers, the accountants' report and the accompanying financial statements have been translated into English from the original Chinese version prepared and used in the Republic of China. If there is any conflict between the English version and the original Chinese version or any difference in the interpretation of the two versions, the Chinese-language accountants' report and financial statements shall prevail. Also, please refer to the original Chinese version for certain disclosures not translated into English as they are not required under generally accepted accounting principles in the Republic of China.

(English Translation of Financial Report Originally Issued in Chinese)
PEGATRON CORPORATION
BALANCE SHEETS
December 31, 2012 and 2011
(All Amounts Expressed in Thousands of New Taiwan Dollars, Except for Share Data)

ASSETS	December 31, 2012		December 31, 2011	
	Amount	%	Amount	%
Current Assets:				
Cash (Note (4)(a))	\$ 12,006,919	4	6,815,955	3
Notes receivable, net of allowance for uncollectible accounts – Non-related parties (Note (4)(b))	32	-	-	-
Accounts receivable, net of allowance for uncollectible accounts – Non-related parties (Note (4)(b))	79,893,702	25	40,736,056	19
Accounts receivable, net of allowance for uncollectible accounts – Related parties (Note (5))	112,235,263	35	70,676,143	32
Other receivables – Non-related parties (Note (4)(b))	10,476,420	3	40,427	-
Other receivables – Related parties (Note (5))	28,374	-	9,842	-
Other financial assets – current (Note (6))	76,204	-	72,003	-
Inventories (Note (4)(c))	12,018,150	4	9,252,961	4
Other current assets (Note (5))	258,359	-	133,332	-
Deferred income tax assets – current (Note (4)(k))	34,113	-	277,270	-
	<u>227,027,536</u>	<u>71</u>	<u>128,013,989</u>	<u>58</u>
Investments:				
Long-term investments under the equity method (Note (4)(d))	89,819,986	28	86,765,900	40
	<u>30,650</u>	<u>-</u>	<u>29,271</u>	<u>-</u>
Other Financial Assets – Noncurrent (Note (6))				
	<u>30,650</u>	<u>-</u>	<u>29,271</u>	<u>-</u>
Property, Plant and Equipment, at cost :				
Land	2,171,560	1	2,167,308	1
Buildings	1,917,987	-	1,886,473	1
Machinery and equipment	34,479	-	45,169	-
Warehousing equipment	600	-	600	-
Instrument equipment	149,384	-	146,286	-
Transportation equipment	24,650	-	23,339	-
Office equipment	2,718	-	3,951	-
Leased assets	6,003	-	6,003	-
Miscellaneous equipment	302,463	-	386,816	-
	<u>4,609,844</u>	<u>1</u>	<u>4,665,945</u>	<u>2</u>
Less: Accumulated depreciation	(778,705)	-	(731,088)	-
Construction in progress	905	-	-	-
	<u>3,832,044</u>	<u>1</u>	<u>3,934,857</u>	<u>2</u>
Intangible Assets				
	<u>93,947</u>	<u>-</u>	<u>121,223</u>	<u>-</u>
Other Assets – others (Note (4)(e))				
	<u>666,826</u>	<u>-</u>	<u>763,501</u>	<u>-</u>
TOTAL ASSETS	\$ 321,470,989	100	219,628,741	100

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

(English Translation of Financial Report Originally Issued in Chinese)

PEGATRON CORPORATION

BALANCE SHEETS (CONT'D)

December 31, 2012 and 2011

(All Amounts Expressed in Thousands of New Taiwan Dollars, Except for Share Data)

	December 31, 2012		December 31, 2011	
	Amount	%	Amount	%
LIABILITIES AND STOCKHOLDERS' EQUITY				
Current Liabilities:				
Short-term loans (Note (4)(f))	\$ 6,359,760	2	6,176,100	3
Accounts payable – Non-related parties	95,814,244	29	42,449,007	19
Accounts payable – Related parties (Note (5))	85,225,163	27	57,939,610	26
Income tax payable	345,592	-	-	-
Accrued expenses – Non-related parties (Note (4)(l))	3,548,816	1	2,345,724	1
Accrued expenses – Related parties (Note (5))	520,399	-	3,588,099	2
Other payables – Related parties (Note (5))	5,808,000	2	-	-
Long-term loans payables – current portion (Note (4)(h))	2,323,200	1	-	-
Other current liabilities (Note (5))	7,294,969	2	3,034,004	1
	<u>207,240,143</u>	<u>64</u>	<u>115,532,544</u>	<u>52</u>
Long-Term Loans:				
Financial liabilities at fair value through profit or loss (Note (4)(g) and (i))	6,275	-	-	-
Long-term loans (Note (4)(h))	9,292,800	3	12,110,000	6
	<u>9,299,075</u>	<u>3</u>	<u>12,110,000</u>	<u>6</u>
Other Liabilities:				
Bonds payable (Note (4)(i))	8,403,406	3	-	-
Refundable guarantee deposits	11,014	-	10,232	-
Deferred income tax liabilities – Noncurrent (Note (4)(k))	331,972	-	334,145	-
Accrued pension liabilities	4,041	-	-	-
Other long-term liabilities (Note (5))	102,505	-	57,611	-
	<u>8,852,938</u>	<u>3</u>	<u>401,988</u>	<u>-</u>
Total Liabilities	<u>225,392,156</u>	<u>70</u>	<u>128,044,532</u>	<u>58</u>
Stockholders' Equity (Note (4)(i), (4)(k) and 4(l)):				
Common stock	<u>22,903,049</u>	<u>7</u>	<u>22,563,669</u>	<u>10</u>
Capital surplus				
Premium on capital stock	60,393,247	19	60,393,247	28
Other	4,167,021	1	3,072,249	1
	<u>64,560,268</u>	<u>20</u>	<u>63,465,496</u>	<u>29</u>
Retained earnings :				
Legal reserve	1,847,737	1	1,836,601	1
Special reserve	734,859	-	4,327,629	2
Retained earnings	9,829,896	3	144,466	-
	<u>12,412,492</u>	<u>4</u>	<u>6,308,696</u>	<u>3</u>
Other adjustments to stockholders' equity:				
Cumulative translation adjustments	(3,400,838)	(1)	(784,234)	-
Unrecognized (loss) gain on pension cost	(1,717)	-	440	-
Unrealized gain on financial assets	122,071	-	48,936	-
Treasury stock	(18,794)	-	(18,794)	-
Deferred compensation arising from issuance of restricted stock	(497,698)	-	-	-
	<u>(3,796,976)</u>	<u>(1)</u>	<u>(753,652)</u>	<u>-</u>
Total Stockholders' Equity	<u>96,078,833</u>	<u>30</u>	<u>91,584,209</u>	<u>42</u>
Commitments and Contingencies (Note (7))				
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	<u>\$ 321,470,989</u>	<u>100</u>	<u>219,628,741</u>	<u>100</u>

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

(English Translation of Financial Report Originally Issued in Chinese)
PEGATRON CORPORATION
STATEMENTS OF INCOME
FOR THE YEARS ENDED DECEMBER 31, 2012 AND 2011
(All Amounts Expressed in Thousands of New Taiwan Dollars, Except for Share Data)

	For the Years Ended December 31			
	2012		2011	
	Amount	%	Amount	%
Operating revenues (Note (5))	\$ 639,743,674	100	373,745,393	101
Less: Sales returns	545,954	-	1,741,657	1
Sales allowances	498,766	-	291,073	-
Net sales	638,698,954	100	371,712,663	100
Cost of sales (Notes (4)(c) and (5))	631,839,940	99	366,365,728	99
Gross profit	6,859,014	1	5,346,935	1
Less: Unrealized profit on intercompany transactions (Note (5))	(44,894)	-	(47,231)	-
	6,814,120	1	5,299,704	1
Operating expenses (Notes (4)(l) and Note (5))				
Selling expenses	2,216,456	-	1,835,805	1
General and administrative expenses	1,533,256	-	1,328,621	-
Research and development expenses	4,784,643	1	3,958,773	1
	8,534,355	1	7,123,199	2
Loss from operations	(1,720,235)	-	(1,823,495)	(1)
Non-operating income				
Interest income	39,158	-	20,558	-
Investment income under the equity method (Note (4)(d))	7,341,563	1	1,516,472	1
Gain on disposal of fixed assets (Note (4)(e) and (5))	-	-	108,345	-
Gain on disposal of investments (Note (4)(d))	62,028	-	-	-
Foreign exchange gain, net	135,479	-	-	-
Rental revenue (Note (5))	82,816	-	65,994	-
Reversal of allowance for uncollectible accounts	-	-	25,999	-
Gain on reversal of impairment loss (Note (4)(e))	4,127	-	28,450	-
Gain on valuation of financial asset	-	-	843	-
Gain on valuation of financial liability (Note (4)(g) and (4)(i))	14,135	-	-	-
Others (Note (5))	1,573,420	-	910,621	-
	9,252,726	1	2,677,282	1
Non-operating expenses				
Interest expenses (Note (4)(i) and Note (5))	452,203	-	210,687	-
Loss on disposal of assets (Note (4)(e) and Note (5))	1,122	-	-	-
Foreign exchange loss, net	-	-	310,723	-
Others (Note (4)(b) and Note (5))	537,813	-	273,863	-
	991,138	-	795,273	-
Income before income tax	6,541,353	1	58,514	-
Income tax expense (benefit) (Note (4)(k))	437,557	-	(52,851)	-
Net income	<u>\$ 6,103,796</u>	<u>1</u>	<u>111,365</u>	<u>-</u>

	Before Income Tax	After Income Tax	Before Income Tax	After Income Tax
Earnings per share (Note (4)(m))				
Primary earnings per share	\$ 2.90	2.71	0.03	0.05
Diluted earnings per share	\$ 2.72	2.53	0.03	0.05

Pro forma result assuming the Company's shares of stock held by its subsidiary do not count as treasury stock:

	Before Income Tax	After Income Tax	Before Income Tax	After Income Tax
Net income	\$ 6,541,353	6,103,796	58,514	111,365
Earnings per share (Note (4)(m))	\$ 2.90	2.70	0.03	0.05
Diluted earnings per share (Note 4(m))	\$ 2.72	2.53	0.03	0.05

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

(English Translations of Financial Statements Originally Issued in Chinese)
PEGATRON CORPORATION
STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
FOR THE YEARS ENDED DECEMBER 31, 2012 AND 2011
(All Amounts Expressed in Thousands of New Taiwan Dollars, Except for Share Data)

	Common stock	Capital surplus	Retained earnings			Other adjustments to stockholders' equity					Total
			Legal reserve	Special reserve	Retained earnings (accumulated deficit)	Cumulative translation adjustments	Unrecognized gain(loss) on pension	Unrealized gain(loss) of financial assets	Deferred compensation	Treasury stock	
Balance, January 1, 2011	\$ 22,563,669	63,145,448	1,215,457	-	8,253,605	(5,250,188)	(16)	922,576	-	(9,322)	90,841,229
Company shares held by investee	-	-	-	-	-	-	-	-	-	(9,472)	(9,472)
Compensation cost arising from employee stock option	-	49,513	-	-	-	-	-	-	-	-	49,513
Net income for the year ended December 31, 2011	-	-	-	-	111,365	-	-	-	-	-	111,365
Appropriations and distributions of 2010 earnings (Note 1):											
Legal reserve	-	-	621,144	-	(621,144)	-	-	-	-	-	-
Special reserve	-	-	-	4,327,629	(4,327,629)	-	-	-	-	-	-
Cash dividends	-	-	-	-	(3,271,731)	-	-	-	-	-	(3,271,731)
Adjustment arising from long-term equity investments	-	121,024	-	-	-	1,986,855	456	(873,640)	-	-	1,234,695
Cumulative translation adjustments	-	-	-	-	-	2,479,099	-	-	-	-	2,479,099
Interest expense incurred from trust of shareholders of parent company	-	149,511	-	-	-	-	-	-	-	-	149,511
Balance, December 31, 2011	\$ 22,563,669	63,465,496	1,836,601	4,327,629	144,466	(784,234)	440	48,936	-	(18,794)	91,584,209
Balance, January 1, 2012	\$ 22,563,669	63,465,496	1,836,601	4,327,629	144,466	(784,234)	440	48,936	-	(18,794)	91,584,209
Issuance of restricted employee stock	339,380	478,366	-	-	-	-	-	-	(497,698)	-	320,048
Service cost recognized from granting convertible corporate bonds—stock option	-	329,225	-	-	-	-	-	-	-	-	329,225
Compensation cost arising from employee stock option	-	114,472	-	-	-	-	-	-	-	-	114,472
Net income for the year ended December 31, 2012	-	-	-	-	6,103,796	-	-	-	-	-	6,103,796
Appropriations and distributions of 2011 earnings (Note 2):											
Legal reserve	-	-	11,136	-	(11,136)	-	-	-	-	-	-
Special reserve	-	-	-	(3,592,770)	3,592,770	-	-	-	-	-	-
Adjustment arising from long-term equity investments	-	172,709	-	-	-	(1,482,454)	(2,157)	73,135	-	-	(1,238,767)
Cumulative translation adjustments	-	-	-	-	-	(1,134,150)	-	-	-	-	(1,134,150)
Balance, December 31, 2012	\$ 22,903,049	64,560,268	1,847,737	734,859	9,829,896	(3,400,838)	(1,717)	122,071	(497,698)	(18,794)	96,078,833

Note 1: The directors' and supervisors' remuneration of \$12,000 and employees' bonuses of \$127,000 for the year ended December 31, 2010 had been deducted from net income for the year ended December 31, 2010.

Note 2: The directors' and supervisors' remuneration of \$1,000 and employees' bonuses of \$12,100 for the year ended December 31, 2011 had been deducted from net income for the year ended December 31, 2011.

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

(English Translation of Financial Report Originally Issued in Chinese)

PEGATRON CORPORATION

STATEMENTS OF CASH FLOWS

FOR THE YEARS ENDED DECEMBER 31, 2012 and 2011

(All Amounts Expressed in Thousands of New Taiwan Dollars, Except for Share Data)

	For the Years Ended December 31	
	2012	2011
Cash flows from operating activities:		
Net income	\$ 6,103,796	111,365
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation	174,323	205,342
Amortization	468,706	471,361
Reversal of impairment loss	(4,127)	(28,450)
Provision (Reversal) for allowance for uncollectible account:	12,037	(25,999)
Provision (Reversal) for contingent service cost	71,599	(259,509)
Amortization of discount on bonds payable	61,930	-
Gain on foreign currency exchange on bonds payable	(156,066)	-
Amortization of issuance costs on bonds payable	11,537	-
Provision (Reversal) for inventory market price decline and obsolescence	39,157	(186,652)
Investment income under equity method	(7,341,563)	(1,516,472)
Cash dividend from investments under equity method	2,260,957	2,055,436
Loss (gain) on disposal and retirement of assets, net	27,537	(10,491)
Gain on disposal of long-term investments under the equity method	(62,028)	-
Gain on valuation of financial liabilities	(14,135)	-
Unrealized profits on intercompany transactions	44,894	47,231
Gain on foreign currency exchange on long-term loans	(494,000)	-
Employee compensation cost	179,563	199,024
Change in assets and liabilities:		
Notes and accounts receivable	(80,728,835)	(68,773,813)
Other receivables	(10,454,525)	(9,624)
Inventories	(2,804,347)	(1,896,501)
Other current assets	(488,474)	(60,603)
Deferred income tax assets and liabilities, net	240,984	(45,641)
Accounts payable	80,659,176	66,031,937
Income tax payable	192,699	-
Accrued expenses	(1,936,207)	(4,259,795)
Other current liabilities	4,333,042	199,011
Net cash used in operating activities	(9,602,370)	(7,752,843)
Cash flows from investing activities:		
Increase in long-term investments under the equity method	(589,451)	(294,000)
Proceeds from disposal of long-term investments under the equity method	305,082	-
Decrease in long-term investments under the equity method	-	440,880
Purchase of property, plant and equipment and intangible assets	(39,081)	(127,179)
Proceeds from disposal of assets, idle assets, deferred charges	13,966	711,319
Increase in deferred charges	(7,360)	(288,617)
Purchase of intangible assets	(51,704)	(32,920)
Increase in other financial assets	(5,580)	(750)
Net cash (used in) provided by investing activities	(374,128)	408,733
Cash flows from financing activities:		
Increase in short-term loans	183,660	3,510,900
Issuance of bonds payable	8,835,640	-
Increase in long-term loans	-	5,118,800
Increase in other accounts payable—Related parties	5,808,000	-
Increase (Decrease) in other financial liabilities	782	(5,979)
Distribution of cash dividends	-	(3,271,731)
Issuance of restricted stock to employees	339,380	-
Net cash provided by financing activities	15,167,462	5,351,990
Net increase (decrease) in cash	5,190,964	(1,992,120)
Cash, beginning of the year	6,815,955	8,808,075
Cash, end of the year	\$ 12,006,919	6,815,955
Supplemental disclosures of cash flow information:		
Cash paid during the year for:		
Interest, excluding capitalized interest	\$ 313,342	158,264
Income tax	\$ 3,872	408,046
Non-cash investing and financing:		
Long-term loans — current portion	\$ 2,323,200	-
Reclassification of idle assets to fixed assets	\$ 32,710	136,852
Cash paid from acquisition of subsidiaries:		
Increase in long-term investments under the equity method	\$ 589,451	416,935
Less: Accounts payable, end of the year	-	(122,935)
	\$ 589,451	294,000

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

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RPEGATRON CORPORATION
NOTES TO FINANCIAL STATEMENTS
December 31, 2012 AND 2011
(Amounts Expressed in New Taiwan Dollars in Thousands,
Except for Per Share Information and Unless Otherwise Stated)

1. Organization and Business

Pegatron Corporation (the “Company”) was established on June 27, 2007. 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.

As of December 31, 2012 and 2011, the Company had 5,287 and 5,035 employees, respectively.

2. Summary of Significant Accounting Policies

The Company’s financial statements were prepared in accordance with Guidelines Governing the Preparation of Financial Reports by Securities Issuers and generally accepted accounting principles of the Republic of China. The significant accounting policies and their measurement basis are as follows:

a. Use of Estimates

The preparation of the accompanying financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting periods. Actual results could differ from these estimates.

(English Translation of Financial Report Originally Issued in Chinese)
PEGATRON CORPORATION
NOTES TO FINANCIAL STATEMENTS (CONT'D)

b. Foreign Currency Translation

The Company records its transactions in New Taiwan dollars. Non-derivative foreign currency transactions are recorded at the exchange rates prevailing at the transaction date. At the balance sheet date, monetary assets and liabilities denominated in foreign currencies are translated into New Taiwan dollars using the exchange rates on that date, and the resulting unrealized exchange gains or losses from such translations are reflected in the accompanying statements of income. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Non-monetary assets and liabilities that are measured at fair value in a foreign currency are translated into the reporting currency using the foreign exchange rates at the balance sheet date. If the non-monetary assets or liabilities are measured at fair value through profit or loss, the resulting unrealized exchange gains or losses from such translation are reflected in the accompanying statements of income. If the non-monetary assets or liabilities are measured at fair value through stockholders' equity, the resulting unrealized exchange gains or losses from such translation are recorded as a separate component of stockholders' equity.

For long-term equity investments in foreign investees which are accounted for by the equity method, their foreign currency-denominated assets and liabilities are translated at spot rate on the balance sheet date; the components of their stockholders' equity are translated at the historical rate except for the beginning balance of retained earnings, which is translated using the spot rate at the beginning of the year. Income statement accounts are translated at the weighted-average rate of the year. Translation differences are accounted for as cumulative translation adjustments to stockholders' equity.

c. Basis for Classifying Assets and Liabilities as Current or Non-current

Unrestricted cash, cash equivalents, assets held for trading, or other assets that the Company will convert to cash or use within in a relatively short period of time - one year or one operating cycle, whichever is longer - are classified as current assets; other assets are classified as non-current assets. Debts due within one year or one operating cycle, whichever is longer, are classified as current liabilities; other liabilities are classified as non-current liabilities.

(English Translation of Financial Report Originally Issued in Chinese)
PEGATRON CORPORATION
NOTES TO FINANCIAL STATEMENTS (CONT'D)

d. Asset Impairment

The Company adopted Statement of Financial Accounting Standards No. 35 (SFAS 35) "Impairment of Assets." In accordance with SFAS 35, the Company assesses at each balance sheet date whether there is any indication that an asset (individual asset or cash-generating unit other than goodwill) may have been impaired. If any such indication exists, the Company estimates the recoverable amount of the asset. The Company recognizes impairment loss for an asset whose carrying value is higher than the recoverable amount.

The Company reverses an impairment loss recognized in prior periods for assets other than goodwill if there is any indication that the impairment loss recognized no longer exists or has decreased. The carrying value after the reversal should not exceed the recoverable amount or the depreciated or amortized balance of the assets assuming no impairment loss was recognized in prior periods.

e. Financial Instruments

i. Financial assets or liabilities reported at fair value through profit or loss

Financial instruments are classified into this category if the purpose of acquisition is principally for selling or repurchasing in the near term. All financial instruments that does not meet the criteria for hedge accounting is classified under this category. Financial instruments are measured at fair value at initial recognition. Transaction cost is charged to current expense. Subsequent to initial recognition, changes in fair value are recognized in profit or loss. A regular way purchase or sale of financial assets is recognized using trade date accounting.

ii. Notes and Account receivables, and other receivables

Notes and accounts receivable are rights resulting from the sale of goods or the rendering of services. Other receivables are receivables arising from non-operating activities.

The Company first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognized are not included in a collective assessment of impairment.

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The asset impairment loss is determined based on difference between the asset's carrying amount and the present value of estimated future cash flows discounted by the financial asset's original effective interest rate. The carrying amount of the asset is reduced for impairment through the use of an allowance account. Impairment loss is recognized in profit or loss. In determining the amount of asset impairment, the collateralized financial asset and related insurance recoverable amount are included in calculating the present value of the estimated future cash flows.

If, in a subsequent period, the amount of the impairment loss decreases, and the decrease can be related objectively to an event occurring after the impairment was recognized, the reversal shall not result in a carrying amount of the financial asset that exceeds what the amortized cost would have been had the impairment not been recognized. The amount of the reversal is recognized in profit or loss.

iii. Compound financial instruments

Compound financial instruments issued by the Company comprise both financial liabilities and convertible notes that can be converted into share capital at the option of the holder, and the number of shares to be issued does not vary with changes in their fair value. The liability component of a compound financial instrument is recognized initially at the fair value of a similar liability that does not have an equity conversion option. The equity component is initially recognized based on the excess of the fair value of the compound financial instrument as a whole over 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, unless it is designated at fair value through profit or loss. The equity component of a compound financial instrument is not re-measured subsequent to initial recognition.

f. Transfer of Financial Assets

In accordance with Statement of Financial Accounting Standards No. 33 (SFAS 33) "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 the following conditions are met.

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- i. 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.
- ii. 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.
- iii. The transferor does not maintain effective control over the rights to the accounts receivable claims through either:
 - (1) an agreement that both entitles and obligates the transferor to repurchase or redeem them before their maturity, or
 - (2) the ability to unilaterally cause the holder to return specific rights to the accounts receivable.

An assignment of the Company's accounts receivable which has not been advanced is accounted under other accounts receivable.

g. Inventories

Inventories are carried at the lower of cost or net realizable value using a perpetual inventory basis. Cost is determined using the weighted-average method. According to SFAS 10, the cost of inventories includes all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition. Net realizable value is determined based on the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses at the end of the period. The replacement cost of raw material is its net realizable value.

h. Long-Term Equity Investments (Including Joint Ventures)

Long-term equity investments in which the Company, directly or indirectly, owns 20% or more of the investee's voting shares, or less than 20% of the investee's voting shares but is able to exercise significant influence over the investee's operating and financial policies, are accounted for under the equity method.

Investment in joint ventures in which the Company has the ability to control is accounted for under the equity method.

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Unrealized profits/losses on intercompany transactions are eliminated and deferred. Gains and losses resulting from transactions involving depreciable assets are recognized ratably over their economic lives, while those from other assets are recognized immediately.

Cost and gains or losses on partial disposition of long-term equity investments are determined by the weighted-average method. Capital surplus from partial disposition of such investments is reduced by the percentage sold, with gains and losses included in current earnings.

The change in the carrying value of long-term equity investment as a result of the change in percentage of equity ownership due to disproportionate subscription to additional shares issued by the investee company is charged against capital surplus. When the balance of capital surplus arising from long-term equity investments is insufficient, the difference is charged against retained earnings.

i. Property, Plant, and Equipment, Rental Assets, Idle Assets, and Depreciation

Property, plant, and equipment are stated at cost less accumulated depreciation and accumulated impairment loss. Interest expense incurred up to the time when the asset is ready for its intended use is capitalized as part of the acquisition cost. Major additions, improvements, and replacements are capitalized.

Depreciation is provided over the estimated economic lives using the straight-line method. Assets still in use at the end of their estimated useful lives are continuously depreciated based on their estimated remaining useful lives and estimated salvage values. Economic lives of major property and equipment are as follows:

Buildings	5 to 50 years
Machinery and equipment	1 to 6 years
Warehousing equipment	8 years
Instrument equipment	3 years
Transportation equipment	5 years
Office equipment	5 years
Leased assets	3 years
Miscellaneous equipment	3 to 15 years

Gain and loss on disposal of properties are recorded as non-operating income or loss.

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Rental assets and idle fixed assets, which are not used for operating purposes, are classified as other assets.

j. Intangible Assets

According to the Statement of Financial Accounting Standard No. 37 (SFAS 37) “Intangible Assets,” intangible assets are initially stated at cost, except for the government grant which is stated at fair value. Intangible assets with finite life are measured at cost plus the revaluation increment arising from the revaluation in accordance with the laws, less any accumulated amortization and any impairment losses.

The amortizable amount of intangible assets with definite lives is determined after deducting its residual value. Amortization is recognized as an expense on a straight-line basis over the estimated useful lives of intangible assets from the date that they are made available for use. The economic useful lives of intangible assets are as follows:

Computer software cost	3 to 5 years
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The residual value, amortization period, and amortization method for an intangible asset with a finite useful life are reviewed at least at each financial year end. Any change thereof is accounted for as a change in accounting estimates.

k. Deferred Charges

The costs of renovation project and office decorations are deferred and amortized equally over 3 to 5 years, and the costs of molds and fixtures are deferred and amortized equally over 1 to 2 years.

l. Pension Plan

In accordance with the “Labor Pension Act,” that prescribes a defined contribution plan, the Company contributes monthly to the Labor Pension Fund at the rate of 6% of the employees' monthly wages. These contributions are accrued and recognized as pension expense in the period when the service is rendered.

m. Warranty Reserve

For products under warranty, warranty costs are accrued based on the past record of the cost of returns for repair, failure rate and warranty period. Warranty costs are accounted for as current expenses when the sales are recognized.

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n. Revenue and Cost Recognition

Revenue is recognized when title to the product and the risks and rewards of ownership are transferred to the customer; otherwise revenue recognition is deferred until these criteria are met. The related cost and expenses are recognized as the revenue is recognized. The expenses are recognized on accrual basis. Also, allowances for sales returns and discounts are estimated based on historical experience. Such allowances are recognized in the same period in which sales are made.

o. Classification of Capital and Operating Expenditures

Expenditures that benefit the Company in future years are capitalized, while immaterial expenditures or those with no future benefits are treated as current expense or loss when incurred.

p. Share-based payment transactions

The Company adopted SFAS No. 39, "Share-based Payment," for share-based payment arrangements with a grant date on or after January 1, 2008, and Interpretations (92) 070, 071 and 072 issued by ROC Accounting Research and Development Foundations (ARDF) for employee stock options that were granted before January 1, 2008.

- i. An equity-settled share-based payment transaction is measured based on the fair value of the award at grant date, and is recognized as expenses over the vesting period with a corresponding increase in equity. The vesting period is estimated based on the vesting conditions under the share-based payment arrangement. Vesting conditions include service conditions and performance conditions (including market conditions). In estimating the fair value of an equity-settled share-based award, only the effect of market conditions is taken into consideration.
- ii. A cash-settled share-based payment transaction is measured at the balance sheet date and the settlement date based on the fair value of the stock option as of those dates and is recorded as a liability incurred for the goods and services received. Changes in fair values are recognized in profit or loss for the period.
- iii. The fair value of employee stock options and similar instruments at grant date is estimated using the Black-Scholes option-pricing model, taking into account the exercise price, the current market price of the underlying shares, management's best estimate of the expected term, the expected volatility, the expected dividends, and the risk-free interest rate.

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iv. Company shares of stock award to employees subject to certain restrictions is an equity-settled share-based payment transaction, which is measured based on the fair value of the award at grant date, and is recognized as expenses over the vesting period with a corresponding increase in equity. Employees receiving restricted stock awards are not limited to the right to receive dividends, and need not return receipt of dividends as they resign within the vesting period. However, upon the Company's declaration of dividend, dividends expected to be received by employees resigning within the vesting period are estimated based on grant-date fair value and are recognized as a compensation cost.

q. Employee Bonuses and Remuneration to Directors and Supervisors

Appropriations for employee bonuses and remuneration to directors and supervisors are accounted for in accordance with Interpretation (96) 052 issued by the ROC Accounting Research and Development Foundation. According to this Interpretation, the Company estimates the amount of employee bonuses and remuneration to directors and supervisors and recognizes it as expenses in the period when services are rendered. The differences between the amounts approved in the shareholders' meeting and those recognized in the financial statements, if any, are accounted for as changes in accounting estimates and recognized in profit or loss.

r. Commitments and Contingencies

If loss from a commitment or contingency is deemed highly likely and the amount can be reasonably estimated, then such loss is immediately recognized. Otherwise only the nature of such loss is disclosed in the notes to the financial statements.

s. Income Tax

In accordance with Statement of Financial Accounting Standards No. 22 (SFAS 22) "Income Taxes," income taxes are accounted for using the asset and liability method. The income tax effects resulting from taxable temporary differences are recognized as deferred income tax liabilities. The income tax effects resulting from deductible temporary differences, loss carry forwards and investment tax credits are recognized as deferred income tax assets. The realization of the deferred income tax assets is evaluated, and if it is considered more likely than not that the deferred tax assets will not be realized, a valuation allowance is recognized accordingly. The deferred income tax liabilities and deferred income tax assets are recalculated based on newly modified effective tax rate, and the difference between newly calculated amount and the originally calculated one is reported as current expense or benefit when the new tax rate is announced. Adjustments to prior years' income taxes are reported as current income taxes.

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Deferred income tax assets or liabilities are classified as current and non-current in accordance with the nature of the related assets and liabilities or the length of time to their reversal.

Income taxes credits from purchase of equipment, technical research and development, and personnel training are recognized by the flow-through method.

The 10% surtax on undistributed earnings of the Company is reported as current expense on the date when the stockholders declared not to distribute the earnings during their annual meeting.

t. Earnings per Share (“EPS”)

Earnings per share of common stock is determined based on net income available to common stockholders divided by the weighted-average number of outstanding shares of common stock. The effect on earnings per share from an increase in capital stock through the distribution of stock dividends from unappropriated earnings, capital surplus, or employee stock bonuses approved in the annual stockholders’ meetings held before and in 2008 is computed retroactively.

Diluted EPS is calculated by dividing net income by the weighted-average number of common shares used in the basic EPS calculation plus the number of common shares that would be issued assuming all potentially dilutive common shares are converted and outstanding. The convertible corporate bonds, employee stock option and employee stock bonus which are not yet resolved for distribution in the shareholders’ meeting are treated as potentially dilutive common shares. If a dilutive effect does not exist, only basic EPS is disclosed; otherwise, diluted EPS is disclosed in addition to the basic EPS.

u. Spin-Off Transactions

Spin-off transactions are accounted for under Interpretation (91) 128 issued by the ROC Accounting Research and Development Foundation. Under this Interpretation, if a transferor company and a transferee company are affiliated and the spin-off transaction arise from group reorganization, the assets and liabilities are recognized by the transferee based on the book value of the assets and liabilities of the transferor company without recognizing any transfer gain/loss. However, if the book value of the assets exceeds their fair value, the excess is recognized as impairment loss before the transfer of these assets.

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v. Treasury Stock

As the Company purchased its outstanding shares, the Company adopted Financial Accounting Standard No. 30 "Accounting for Treasury Stock" in the accounting of treasury shares of stock, which are stated at cost. When treasury stock is sold, the excess of the proceeds from sale over the book value of treasury stock is recorded as capital surplus-treasury stock transaction. If the disposal price is lower than the book value, the difference is offset against capital surplus resulting from other treasury stock transactions, and any deficiency is debited to retained earnings. The carrying amount of treasury stock is calculated by using the weighted-average method according to the same class of treasury stock.

When treasury stock is cancelled, "capital surplus-premium on capital stock" is debited proportionately according to the equity shareholding ratio. If the book value of the treasury stock exceeds the sum of par value and premium on capital stock, the difference is offset against capital surplus arising from similar treasury stock transactions, and any deficiency is charged against retained earnings. If the book value is less than the total par value and premium on stock, the difference is added to capital surplus arising from treasury stock transaction of the same category.

In accordance with Financial Accounting Standard No. 30 "Accounting for Treasury Stock," the Company's shares of stock held by its subsidiaries are deemed as treasury stock when recognizing investment income (loss) and when preparing the financial statements.

w. Operating Segments

Segment information is disclosed in the consolidated financial statements, and need not be presented in the individual or stand-alone financial statements.

x. Business Combinations

According to SFAS No.25 "Business Combination," the equity of the acquiring corporation in a business acquisition in cash is valued either at the fair value of the assets contributed or at the fair value of the property acquired, whichever is more objectively evident. All identified assets acquired and liability assumed in a business combination, whether or not shown in the financial statements of the acquired corporation, are measured based on their fair value at the acquisition date.

The period for the allocation of acquisition price may not exceed one year after the date of acquisition. If the Company cannot get further information to identify and determine the fair value of assets acquired and liability assumed, the period for the allocation of the acquisition price is consummated.

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3. Reasons for and Effect of Accounting Changes:

Effective from January 1, 2011, the Company adopted the third revision of SFAS No. 34 “Financial Instrument Recognition and Measurement” on the recognition, subsequent measurement and impairment testing of originated loans and receivables and on trouble debt restructuring and modification of debt agreement commencing from January 1, 2011. The adoption of this amended accounting principle disclosed no significant influences on profit or loss for the year ended December 31, 2011.

Effective from January 1, 2011, the Company adopted SFAS No. 41 “Operating Segments.” In accordance with SFAS No. 41, information is disclosed to enable users of the Company’s financial statements to evaluate the nature and financial effects of the business activities in which the Company engages and the economic environment in which it operates. Accordingly, the Company determines and presents operating segments based on the information that internally is provided to the chief operating decision maker. This new accounting Standard superseded SFAS No. 20 “Segment Reporting.” The adoption of this accounting standard did not have any cumulative effect for the year ended December 31, 2011.

4. Summary of Major Accounts:

a. Cash

	<u>December 31, 2012</u>	<u>December 31, 2011</u>
Cash on hand	\$ 160	50
Demand deposits	467,730	773,503
Foreign currency deposits	6,550,197	3,424,527
Foreign currency time deposits	4,088,832	1,967,875
Time deposits	900,000	650,000
Total	<u>\$ 12,006,919</u>	<u>6,815,955</u>

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b. Notes and Accounts Receivable — Non-related parties

	December 31, 2012	December 31, 2011
Notes receivable	\$ 140	-
Less: Allowance for uncollectible accounts	(108)	-
Net	<u>32</u>	<u>-</u>
Accounts receivable	79,982,474	40,788,850
Less: Allowance for uncollectible accounts	(29,533)	(17,604)
Less: Allowance for sales returns and discounts	(59,239)	(35,190)
Net	<u>79,893,702</u>	<u>40,736,056</u>
Total	<u>\$ 79,893,734</u>	<u>40,736,056</u>

An assignment of the Company's accounts receivable is generally be treated as sales if the derecognition criteria for the factoring of accounts receivable under SFAS 33 are met. As of December 31, 2012, the assigned accounts receivable which met the derecognition criteria were as follows:

December 31, 2012							
Purchaser	Assignment Facility	Factoring Line	Advanced Amount	Range of Interest Rate	Collateral	Significant Transferring Terms	Derecognition Amount
SMBC	<u>\$ 7,104,133</u>	<u>USD 300,000,000</u>	<u>USD 243,405,143</u>	0.8937%~ 0.9112%	None	The accounts receivable factoring is without recourse but the sellers still bears the risks except for eligible obligor's insolvency.	<u>\$ 7,104,133</u>
ANZ(Note)	<u>\$ 26,185,725</u>	<u>USD 900,000,000</u>	<u>USD 540,000,000</u>	0.90%	None	"	<u>\$ 26,185,725</u>

For the year ended December 31, 2012, the Company recognized a loss of \$ 51,194 from the assignment of accounts receivable, which is accounted for under financial expenses. Also, the difference of \$10,464,025 between the amount of accounts receivable assigned and the advanced is accounted under other receivable.

Note: In October 2012, the Company signed a one year joint accounts receivable factoring agreement with ANZ Bank, Mizuho Bank, Bank of Nova Scotia, Bank of Communications, United Overseas Bank, and Bank of Toyko-Mitsubishi UFJ where each bank will factor on pro-rata basis.

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c. Inventories

	<u>December 31, 2012</u>	<u>December 31, 2011</u>
Merchandise (including inventory-in-transit)	\$ 11,806,401	7,486,732
Less: Allowance for inventory market decline and obsolescence	(172,766)	(135,912)
Sub-total	<u>11,633,635</u>	<u>7,350,820</u>
Finished goods	11,812	254,019
Less: Allowance for inventory market decline and obsolescence	(4,602)	(4,719)
Sub-total	<u>7,210</u>	<u>249,300</u>
Work in process	54,402	70,921
Less: Allowance for inventory market decline and obsolescence	(16,307)	(21,665)
Sub-total	<u>38,095</u>	<u>49,256</u>
Raw materials	430,295	1,704,361
Less: Allowance for inventory market decline and obsolescence	(91,085)	(100,776)
Sub-total	<u>339,210</u>	<u>1,603,585</u>
Total	<u>\$ 12,018,150</u>	<u>9,252,961</u>

For the years ended December 31, 2012 and 2011, the components of cost of goods sold were as follows:

	<u>For the Years Ended December 31</u>	
	<u>2012</u>	<u>2011</u>
Cost of goods sold	\$ 631,800,783	366,552,380
Provision (Reversal) for inventory market price decline	21,688	(191,859)
Loss on inventory obsolescence	17,469	5,207
	<u>\$ 631,839,940</u>	<u>366,365,728</u>

For the year ended December 31, 2011, the conditions that previously caused inventories to be written down below cost had disappeared due to the disposal of related inventories, so that the related allowance for loss on decline in the value of inventories was reversed, which resulted in a reversal gain on inventory valuation allowance.

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d. Long-Term Equity Investments

<u>Name of Investee Company</u>	December 31, 2012			December 31, 2011		
	Equity Holding	Book Value	Original Investment	Equity Holding	Book Value	Original Investment
PEGATRON HOLDING LTD.	100.00%	\$ 30,151,495	24,825,750	100.00%	29,398,324	24,238,150
UNIHAN CORPORATION	100.00%	12,944,240	10,194,416	100.00%	12,031,272	12,098,279
ASUSPOWER INVESTMENT CO., LTD.	100.00%	14,128,052	13,033,429	100.00%	14,031,301	13,033,429
ASUS INVESTMENT CO., LTD.	100.00%	15,732,207	16,184,982	100.00%	15,379,992	16,184,982
ASUSTEK INVESTMENT CO., LTD.	100.00%	14,782,757	14,593,543	100.00%	14,281,002	14,593,543
ADVANSUS CORP.	- %	-	-	50.00%	243,069	166,364
ASUS HOLLAND HOLDING B.V.	100.00%	2,064,406	1,278,287	100.00%	1,383,843	1,276,436
PEGATRON USA, INC.	100.00%	16,829	16,085	100.00%	17,097	16,085
		\$ 89,819,986			86,765,900	

- i. The investment income recognized under the equity method amounted to \$7,341,563 and \$1,516,472 for the years ended December 31, 2012 and 2011, respectively.
- ii. For the year ended December 31, 2012, the Company had participated in the capital increase of PEGATRON HOLDING LTD. and invested USD20,000 thousand (approximately \$587,600).
- iii. For the purpose of organization restructuring, the Company acquired 7.55% equity ownership of ASUS HOLLAND HOLDING (B.V.) (AHH) from ASUS INVESTMENT CO., LTD. for \$122,935 which is equal to the carrying value of ASUS INVESTMENT CO., LTD.'s long-term investment in AHH. Following such acquisition, the Company participated in the capital increase of AHH and invested EUR\$ 50 thousand (approximately \$1,851) for the year ended December 31, 2012.
- iv. In order to enhance resource efficiency, the Company sold all its equity ownership in ADVANSUS CORP. ("ADVANSUS") to the other joint venture party for \$306,000 on January 5, 2012. The transfer of equity ownership was completed in June 2012, and a disposal gain of \$ 62,028 was recognized thereon.
- v. On November 19, 2012, Unihan Corporation's shareholders resolved to offset Unihan Corporation's accumulated deficits of \$1,322,043 via capital reduction. This resulted in a decrease in the Company's equity investment in Unihan Corporation by \$1,903,863, divided into 132,204 thousand shares, according to the capital reduction ratio.

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- vi. ADVANSUS CORP. is a joint venture entity of the Company, which held the assets and liabilities of ADVANSUS CORP. as follows:

	December 31, 2011	
Current Assets	\$	411,541
Non-current Assets		11,417
Current Liabilities		179,889

	For the Year Ended December 31, 2011	
Revenues	\$	1,447,598
Expenses		1,416,366

- vii. For the years ended December 31, 2012 and 2011, the Company received cash dividend of \$2,260,957 and \$2,055,436, respectively, from its investee companies accounted under equity method.
- viii. For the years ended December 31, 2012 and 2011, the Company's shares held by its subsidiaries are treated as treasury stock in accordance with ROC SFAS 30 as described in Note 4(1).
- ix. Investees, in which the Company has controlling interest over their operation, are included in the Company's consolidated financial statements, except for ADVANSUS CORP.

e. Idle Assets

- (i) In accordance with Statement of Financial Accounting Standards No. 35 (SFAS 35) "Accounting for Asset Impairment," the Company performed asset impairment test by comparing the recoverable amount with the carrying value of idle assets. Based on the results of such assessment, the Company recognized provisions for impairment loss of \$3,911 and \$8,038 as of December 31, 2012 and 2011, respectively.
- (ii) For the years ended December 31, 2012 and 2011, the Company recognized a gain from impairment recovery of \$4,127 and \$28,450, respectively, and a gain (loss) on disposal of idle assets of \$(1,581) and \$107,964, respectively.

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f. Short-Term Loans

<u>Nature of the loan</u>	<u>December 31, 2012</u>	<u>December 31, 2011</u>
Credit loan	\$ 6,359,760	6,176,100
Range of interest rate	0.72%~1.40%	0.70%~1.56%

The Company issued promissory notes as guarantee for part of credit loan facility. The majority of this credit facility was used jointly by the Company and Unihan Corporation.

g. Financial Liabilities Reported at Fair Value Through Profit or Loss

	<u>December 31, 2012</u>
Financial liabilities — put and call options embedded in overseas convertible bonds	\$ 6,275

(ii) For the year ended December 31, 2012, the Company recognized a gain of \$14,135 on valuation of financial liabilities reported at fair value through profit or loss — noncurrent.

(iii) The Company separately accounts for the equity and liability components of overseas convertible corporate bonds in accordance with SFAS 36. Please refer to Note 4(i) for details of bonds payable.

h. Long-Term Loans

<u>Creditor</u>	<u>Types of Debt</u>	<u>Credit Line</u>	<u>Repayment Schedule</u>	<u>December 31</u>	
				<u>2012</u>	<u>2011</u>
Citibank Taiwan and 14 other banks	Credit loan	USD 400,000,000	2010.10.25~2015.10.25. This loan is payable in 5 semi-annual installments, commencing October 25, 2013.	\$ 11,616,000	12,110,000
Less: current portion of long-term loans				(2,323,200)	-
				\$ 9,292,800	12,110,000

For the years ended December 31, 2012 and 2011, long-term loans bore interest at average rates of 0.9086% ~ 2.3256% and 1.0647% ~2.3256%, respectively. According to the syndicated loan agreement, during the loan repayment periods, the Company must comply with certain financial covenants based on its audited consolidated financial statements as of the balance sheet date (June 30 and December 31) as follows:

(i) Current ratio (current assets/current liabilities): should not be less than 100%.

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- (ii) Debt ratio ((total liabilities + contingent liabilities)/tangible net assets): should not be higher than 50%.
- (iii) Interest coverage ratio (EBITDA/interest expense): should not be less than 400%.
- (iv) Tangible net assets (stockholders' equity (including minority shareholders) - intangible assets): should not be less than \$90,000,000.

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

As of December 31, 2012, the Company was in compliance with the loan covenants mentioned above.

The Company's promissory notes were pledged as a guarantee for the credit loan facility as of December 31, 2012 and 2011.

i. Bonds Payable

	<u>December 31, 2012</u>	<u>Collateral</u>
Overseas convertible bonds payable	\$ 8,874,000	None
Less: Discount on bonds payable	(309,074)	
Less: Foreign currency valuation, end of the period	(161,520)	
Net	<u>8,403,406</u>	
Less: Current portion of bonds payable	-	
Total	<u><u>\$ 8,403,406</u></u>	

As of December 31, 2012, the offering information on the unsecured convertible bonds were as follows:

<u>Item</u>	<u>First overseas unsecured convertible bonds issued in 2012</u>
1. Offering amount	USD300 million with each unit valued at USD200 thousand.
2. Issue date	February 6, 2012
3. Listing place	Singapore Exchange Securities Trading Limited (the "SGX-ST")
4. Interest	The Bonds will not bear any interest.
5. Issue period	5 years, commencing from February 6, 2012 and matured on February 6, 2017.
6. Settlement	Unless the Bonds have been previously redeemed, repurchased and cancelled or converted, the Bonds will be redeemed by the Company on Maturity Date at an amount equal to the principal amount of the Bonds with a yield-to-maturity of 1.5% per annum, calculated on semi-annual basis.

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Item	First overseas unsecured convertible bonds issued in 2012
7. Redemption at the option of the Company	<p>(1) The Company may redeem the Bonds, in whole but not in part, at the early redemption amount at any time on or after February 6, 2015 if the closing price of the common shares on TWSE (translated into U.S. Dollars at the fixing rate at 11:00 a.m. Taipei time as quoted by Taipei Forex Inc.) on each trading day during a period of 20 consecutive trading dates exceeds at least 125% of the quotient of the early redemption amount divided by the number of shares to be issued upon conversion of USD200,000 principal amount of Bonds on the applicable trading day based on the conversion price then in effect (translated into U.S. Dollars at the fixed exchange rate of NT\$29.761 = USD1.00).</p> <p>(2) If more than 90% in principal amount of the Bonds originally outstanding has been redeemed, repurchased and cancelled or converted, the Company has the right to redeem all but not portion of the principal amount of such Holder's Bonds at the early redemption amount equal to the principal amount of the Bonds with a yield-to-maturity of 1.5% per annum, calculated on semi-annual basis.</p> <p>(3) The Bonds may be redeemed, in whole but not in part, if the affect of change in the tax laws of ROC will increase the Company's tax liability, interest expense or related cost from the Bonds. Holders may elect not to have their bonds redeemed with no entitlement to any additional amount of reimbursement of additional tax.</p>
8. Redemption at the option of the Holder	<p>(1) Each Holder has the right to require the Company to redeem all or any portion of the principal amount of such Holder's Bonds on February 6, 2015 at a redemption price equal to the principal amount of the Bonds with a yield-to-maturity of 1.5% per annum, calculated on semi-annual basis.</p> <p>(2) In the event that the Company's common shares ceased to be listed or admitted to trading on the TWSE, each Holder has the right to require the Company to redeem all or any portion of the principal amount of such Holder's Bonds at the early redemption amount equal to the principal amount of the Bonds with a yield-to-maturity of 1.5% per annum, calculated on semi-annual basis.</p> <p>(3) In the event of change of control occurs with respect to the Company, each Holder has the right to require the Company to redeem all or any portion of the principal amount of such Holder's Bonds at the early redemption amount.</p>

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Item	First overseas unsecured convertible bonds issued in 2012
9. Conversion	<p>(1) Conversion period</p> <p>Unless the Bonds have been previously redeemed, repurchased and cancelled or converted, each Holder of the Bonds will have the right at anytime during the conversion period commencing March 18, 2012 (the 41st day following the Closing Date) and ending at the close of business on January 27, 2017 (the 10th day prior to the Maturity Date), to convert their bonds.</p> <p>(2) Conversion price</p> <p>The conversion price was NT\$42.11 per share which was 112% of the closing price reported by the TWSE in respect of the Common Shares of the Company on January 30, 2012. However, upon the issuance of restricted Company shares of stock to employees, the conversion price has been adjusted to NT\$41.66 per share effective December 20, 2012.</p> <p>(3) Conversion to common shares</p> <p>Upon conversion, the number of common shares converted is calculated by the issuance price (translated at a fixed exchange rate applicable on conversion of Bonds of NT\$29.761 = USD1.00) divided by the conversion price on the conversion date.</p>

The Company separately accounts overseas convertible corporate bonds into the equity components and liability components. The equity components are accounted for under capital surplus and the liability components are accounted for under financial liabilities reported at fair value through profit or loss or bonds payable in accordance with SFAS 36. As of December 31, 2012, information on the aforesaid convertible bonds were as follows:

First overseas unsecured convertible bonds issued in 2012	December 31, 2012
Total issue price	\$ 8,874,000
Discount on bonds payable	(282,252)
Discount on bonds payable — transaction cost	(26,822)
Accumulated converted amount	-
Accumulated redeemed amount	-
Bonds payable, end of the period	8,564,926
Less: Valuation of bonds payable	(161,520)
Less: Current portion of bonds payable	-
Bonds payable, net, end of the period	\$ 8,403,406
Equity components — capital surplus on stock options	\$ 329,225
Liability components — financial liabilities (put and call options) reported at fair value through profit or loss	\$ 6,275
Liability components — gain on valuation	\$ (14,135)
Interest expense	\$ 182,163

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j. Pension Plan

For the years ended December 31, 2012 and 2011, the pension costs for the defined contribution pension plan of the Company amounted to \$187,117 and \$179,349, respectively.

k. Income Tax

(i) The Company is subject to statutory income tax rate of 17% for both the years ended December 31, 2012 and 2011. The Company also complies with the Basic Income Tax Act when calculating its income tax.

(ii) For the years ended December 31, 2012 and 2011, the components of income tax expense (benefit) were as follows:

	For the Years Ended December 31	
	2012	2011
Current income tax benefit	\$ -	(50,893)
Deferred income tax expense	240,984	5,251
10% surtax on undistributed earnings	184,650	-
Prior years income tax adjustment	11,923	(7,209)
Income tax expense (benefit)	\$ 437,557	(52,851)

The components of deferred income tax expense were as follows:

	For the Years Ended December 31	
	2012	2011
Unrealized exchange gain (loss)	\$ 89,513	(188,884)
Reversal (Provision) of allowance for loss on inventory market decline and obsolescence	(3,687)	32,616
Allowance for sales return and discount	(10,071)	-
Unrealized profits on sales	(7,632)	(8,029)
Amortization of employee benefits	17	17
Gain on (provision) reversal of warranty reserve	(12,171)	44,117
Investment tax credits	259,035	249,252
Unrealized expenses and foreign exchange gain on bonds payable	6,091	-
Gain on reversal of impairment loss on assets	701	4,836
Unrealized foreign investment income	-	34,285
Reserve for foreign investment losses	(8,965)	-
Reversal of valuation on allowance for deferred tax assets	(71,847)	(162,959)
Deferred income tax expense	\$ 240,984	5,251

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(iii) The income tax calculated on pretax financial income at a statutory income tax rate was reconciled with the income tax expense (benefit) as reported in the accompanying financial statements for the years ended December 31, 2012 and 2011 as follows:

	For the Years Ended December 31	
	2012	2011
Income tax calculated on pre-tax financial income at statutory tax rate	\$ 1,112,030	9,947
Permanent differences	(1,475,234)	(241,093)
10% surtax on undistributed earnings	369,300	-
Investment tax credits	2,538	85,203
Non deductible loss carry-forward	417,000	100,301
Prior years income tax adjustment	11,923	(7,209)
Income tax expense (benefit)	\$ 437,557	(52,851)

(iv) As of December 31, 2012 and 2011, the temporary differences, loss carry-forwards and income tax credits and the related income tax effect thereof resulting in deferred income tax assets (liabilities) were as follows:

Temporary differences of deferred income tax assets (liabilities) — current	December 31, 2012		December 31, 2011	
	Amount	Income Tax Effect	Amount	Income Tax Effect
Unrealized foreign exchange (gain) loss: (taxable) deductible	\$ (117,006)	(19,891)	409,543	69,622
Allowance for loss on inventory market decline and obsolescence: deductible	284,760	48,409	263,071	44,722
Unrealized sales return and sales discount: deductible	59,239	10,071	-	-
Deferred employee benefits for tax: deductible	-	-	100	17
Warranty reserve: deductible	117,937	20,049	46,339	7,878
Unrealized intercompany profits: deductible	102,505	17,426	57,611	9,794
Investment tax credits: deductible	-	249,624	-	508,659
Valuation allowance		(291,575)		(363,422)
Net deferred income tax assets — current		\$ 34,113		277,270

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Temporary differences of deferred income tax assets (liabilities) — noncurrent	December 31, 2012		December 31, 2011	
	Amount	Income Tax Effect	Amount	Income Tax Effect
Unrealized impairment loss on assets: deductible	\$ 3,911	665	8,038	1,366
Unrealized interest expenses on bonds payable: deductible	120,232	20,440	-	-
Unrealized foreign exchange gain on bonds payable: taxable	(156,066)	(26,531)	-	-
Unrealized gain on foreign investments including cumulative translation adjustments: taxable	(1,325,062)	(225,261)	(1,325,062)	(225,261)
Reserve for foreign investment losses: taxable	(595,791)	(101,285)	(648,527)	(110,250)
Net deferred income tax liabilities— noncurrent		\$ (331,972)		(334,145)

(v) The Company's tax returns through 2010 have been assessed and approved by the Tax Authority. However, the tax return for 2008 is still under review.

(vi) In accordance with Statute for Industrial Innovation, the Company is allowed to avail of tax credit from R&D expenditures, but this tax credit cannot exceed 30% of the business income tax payable in a given year. Pursuant to Statute for Upgrading Industries, the Company can credit up to 50% of the amount of funds invested for R&D expenditures against the amount of business income tax payable within five years commencing from the year subsequent to the tax credit application, however, such limit for the tax credit application shall not apply to the final year. The Company was granted investment tax credits from funds invested in equipment for automation of production, equipment for pollution control, R&D and personnel training, and newly emerging, important and strategic industries which are deemed tax credit under the statute. As of December 31, 2012, unused investment tax credits which may be applied to offset against income tax payable in the future were as follows:

Year of loss	Unused amount	Year of expiration
2009	\$ 219,702	2013
2011 (estimated)	29,922	2011
	\$ 249,624	

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- (vii) Due to the increase in its investments in new equipment, the Company was granted several income tax exemptions for its manufacturing and sales of “motherboard” out of the new equipment purchased from the proceeds of capital increase. As of December 31, 2012, the details of the five year income tax exemption period were as follows:

<u>Description</u>	<u>Exemption</u>
Eleventh capital increase used for investment in new equipment.	04/30/2007 ~ 04/29/2012

- (viii) Stockholders’ imputation tax credit account and tax rate:

<u>Undistributed earnings:</u>	<u>December 31, 2012</u>	<u>December 31, 2011</u>
Accumulated in 1997 and prior years	\$ -	-
Accumulated in 1998 and thereafter	9,829,896	144,466
Total	<u>\$ 9,829,896</u>	<u>144,466</u>
Stockholders’ imputation tax credit account	<u>\$ 211,593</u>	<u>3,448</u>
	<u>2012 (Expected)</u>	<u>2011 (Actual)</u>
Expected or actual deductible tax ratio	<u>5.67%</u>	<u>0.09%</u>

I. Stockholders’ Equity

- (i) Capital Stock

As of January 1, 2010, authorized capital of the Company amounted to \$25,000,000 and the total outstanding capital amounted to \$22,860,539, divided into 2,286,054 thousand shares with par value of \$10 per share.

In order to enhance own-brand business and boost productivity, the board of directors of ASUSTeK Computer Inc. (“ASUSTek”) resolved on December 11, 2009 but revised it on January 1, 2010, to spin-off or cede its OEM group (Pegatron Corporation (the “Company”)) to Pegatron International Investment Co., Ltd. (“Pegatron Investment”), which is being held by ASUSTeK. Pegatron Investment will issue new shares to ASUSTeK and all shareholders of ASUSTek, for which, ASUSTek and all other shareholders of ASUSTek will acquire 25% ownership and 75% ownership, respectively, of the equity of Pegatron Investment. The record

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date of this spin-off was June 1, 2010. Following the spin-off, the Company merged with Pegatron Investment. The Company issued 10 thousands new shares, resulting in additional capital of \$100. Thereafter, the total outstanding capital amounted to \$22,860,639, divided into 2,286,064 thousand shares with par value of \$10 per share.

In November, 2010, the Company had retired treasury stock of 29,697 thousand shares of stock valued at \$296,970. In 2012, the Company had issued 33,938 thousand shares of restricted Company shares of stock to employees. As of December 31, 2012 and 2011, the authorized capital of the Company consisted of 3,000,000 and 2,500,000 thousand shares, respectively, with par value of \$10 per share, and its outstanding capital consisted of 2,290,305 thousand shares and 2,256,367 thousand shares of stock, respectively.

ASUSTeK GDR holders who surrender 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 Pegatron common shares and deliver them to ASUSTeK GDR holders pursuant to the "Issuer of Overseas Securities Offering and Issued Guidelines." As of December 31, 2012, the Company has listed, in total, 9,769 thousand units of GDR on the Euro MTF market of the Luxembourg Stock Exchange. As each unit of these GDRs represents 5 shares, the Company has listed Company shares totaling 48,844 thousand shares. 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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(ii) Share-based payment transactions — employee stock option plan

1. Information on equity-settled share-based payment transaction as of December 31, 2012 were as follows:

Employee stock option	For the Years Ended December 31	
	2012	2011
Grant date	04/02/2012	07/01/2011
Thousand units granted	8,053	40,679
Contractual life	3 years	3 years
Vesting period	2 years	2 years
Actual turnover rate of employees	8.96%	20.48%
Estimated future turnover rate of employees	19.01%	19.88%
Restricted stock to employee	For the Year Ended December 31	
	2012	
Grant date	11/09/2012	
Thousand units granted	34,167	
Contractual life	3 years	
Vesting period	Note	
Actual turnover rate of employees	0.19%	
Estimated future turnover rate of employees	14.28%, 22.84%, 28.85%	

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

The Company obtained the approval from the Financial Supervisory Commission and issued 50,000 units of Employee Stock Options with an exercisable right of 1,000 shares of the Company's common shares per unit on April 14, 2011. The Company will issue its own new common shares on settlement, and the exercise price of all stock options shall be equal to the closing price of the Company's common stock at grant date. The expected life of the stock options is estimated to be 3 years, and stock option granted to an employee is not transferable to any person. If the exercise period expires, the employee forfeits his/her right to exercise the option and purchase the shares. Except for the forfeiture of vested options, all stock options shall vest from the second year of the grant date, and the employees should exercise the right to apply for shares against the stock option vested in them pursuant to the stock option plan.

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On October 19, 2012, the Company obtained the approval from the Financial Supervisory Commission to issue restricted Company shares of stock to employees for total number limited up to 40,000 thousand shares. On the grant date of November 9, 2012, the Board of Directors approved the list of eligible employees and resolved to issue 34,167 thousand shares effective December 20, 2012. The actual number of new issuance shares was 33,938 thousand shares with a par value of \$10 per share. The procedure for the registration of change of capital stock has been completed. Unless the vesting conditions have been 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.

2. 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:

Employee stock option	For the Years Ended December 31	
	2012	2011
Exercise price (Note A)	\$ 44.85	30
Current market price	44.85	30
Expected dividend yield rate (Note A)	- %	- %
Expected volatility	44.41%	37.0531%
Risk-free interest rate	0.95%	1.0838%
Expected life of the option	3 years	3 years

Restricted stock to employee	For the Year Ended December 31	
	2012	
Exercise price (Note A)	\$	10.00
Current market price		39.45
Expected dividend yield rate (Note A)		- %
Expected volatility		38.49%
Risk-free interest rate		Note B
Expected life of the option		3 years

Note A: After the issuance of the employee stock option, if the Company increases its capital through the surplus and/or capital reserve, the exercise price will be adjusted accordingly. Therefore, the expected dividend yield rate is excluded in calculating the fair value of the stock option.

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Note B: The risk-free interest rate is 0.6953% for the 1st year, 0.7363% for the 2nd year, and 0.7873% for the 3rd year.

3. The components of employee stock option plan and the weighted-average exercise price as of December 31, 2012 were as follows:

A. For the year ended December 31, 2012

	Issued in 2012	
	Number of Exercisable Thousand Shares	Weighted-average Exercise Price
Balance, beginning of the period	-	\$ -
Granted	8,053	44.85
Exercised	-	-
Forfeited	664	-
Expired	-	-
Balance, end of the period	<u>7,389</u>	44.85
Exercisable, end of the period	<u>7,389</u>	
Weighted-average fair value of options granted	<u>13.8</u>	
Exercise price of share option outstanding, end of the period	<u>44.85</u>	
Remaining contractual life	<u>1.25</u>	
Expenses incurred in share-based payment transactions	<u>22,016</u>	

	Issued in 2011	
	Number of Exercisable Thousand Shares	Weighted-average Exercise Price
Balance, beginning of the period	37,648	\$ 28.38
Granted	-	-
Exercised	-	-
Forfeited	4,739	-
Expired	-	-
Balance, end of the period	<u>32,909</u>	28.38
Exercisable, end of the period	<u>32,909</u>	
Weighted-average fair value of options granted	<u>7.9</u>	
Exercise price of share option outstanding, end of the period	<u>28.38</u>	
Remaining contractual life	<u>0.50</u>	
Expenses incurred in share-based payment transactions	<u>92,456</u>	

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B. For the year ended December 31, 2011

	Issued in 2011	
	Number of Exercisable Thousand Shares	Weighted-average Exercise Price
Balance, beginning of the period	-	\$ -
Granted	40,679	28.38
Exercised	-	-
Forfeited	3,031	-
Expired	-	-
Balance, end of the period	37,648	28.38
Exercisable, end of the period	37,648	
Weighted-average fair value of options granted	7.9	
Exercise price of share option outstanding, end of the period	28.38	
Remaining contractual life	1.50	
Expenses incurred in share-based payment transactions	49,513	

4. For the year ended December 31, 2012, the Company issued restricted shares of stock to employees of 33,938 thousand shares, which resulted in a capital surplus — restricted employee stock of \$478,366 and salary expense of \$65,091. Also, as of December 31, 2012, deferred compensation arising from issuance of restricted stock of \$497,698 was accounted for under other adjustments to shareholders' equity.

(iii) Share-based payment transactions — stock appreciation rights plan

Information on cash-settled share-based payment transaction as of December 31, 2012 were as follows:

	Stock Appreciation Right
Grant date	04/02/2012
Vesting condition	EPS performance target
Exercise period	07/01/2013~06/30/2014
Vesting period	1.25 years
Actual turnover rate of employees	8.27%
Estimated future turnover rate of employees	8.97%

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In order to encourage employees to stay and contribute their skills to the Company, the Board of Directors resolved on March 19, 2012 to issue 30,000,000 units of Employee Stock Appreciation Rights. The Company will pay the stock appreciation rights as employee bonus in cash based on the difference between the base price and the settlement price of the stock appreciation right where the base price on settlement of the right is the closing price of the Company's common stock on grant date, and the settlement price is the closing price of the Company's common share on exercise date.

The previously recognized compensation cost was reversed due to the award fails to meet the vesting condition on December 31, 2012.

(iv) Legal reserve and capital surplus

According to the ROC Company Law, as amended in January 2012, and the Company's Articles of Incorporation, a company shall first set aside 10% of its net income as legal reserve. Where the balance of such legal reserve reaches an amount that is equal to the paid-in capital, the appropriation to legal reserve is discontinued. Where a company incurs no loss, it may, pursuant to a resolution to be adopted by a shareholders' meeting distribute its legal reserve by issuing new shares or by cash. Where legal reserve is distributed by issuing new shares or by cash, only the portion of legal reserve which exceeds 25% of the paid-in capital may be distributed.

In accordance with the ROC Company Law, as amended in January 2012, capital surplus is initially used to cover accumulated deficit and the balance, if any, can be distributed as dividends in cash or shares. The realized capital surplus includes donation and premium derived from the issuance of capital stock in excess of par value. In accordance with the Regulations Governing the Offering and Issuance of Securities by Securities Issuers, when capital reserve is capitalized, the combined amount of any portions capitalized in any one year can not exceed 10 % of paid-in capital.

Dividends yield by the trust of the shareholders of parent company were distributed to the employees of the Company as bonuses. These bonuses both amounted to \$409,917 for the years ended December 31, 2012 and 2011, which were credited to capital surplus — others. Also, the Company issued restricted shares of stock to employees, which resulted in capital surplus — restricted employee stock of \$478,366 for the year ended December 31, 2012.

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(v) Treasury Stock

1. In accordance with Securities and Exchange Act, the number of treasury shares shall not exceed ten percent of the total number of issued and outstanding common shares of the Company. Also, the total amount of treasury shares issued may not exceed the amount of retained earnings plus premium on capital stock plus realized capital reserve. The repurchased shares shall not exceed the amount of retained earnings plus premium on capital stock plus realized capital reserve. The repurchased shares held by the Company amounted to \$1,006,862, divided into 29,697 thousand shares as of December 31, 2010 which conformed to Securities and Exchange Act. The number of shares the Company can repurchase from the active market is limited to up to 228,605 thousand shares amounting to \$66,221,050 which is calculated according to financial reports for the latest accounting period prior to a resolution of a meeting of the board of directors.
2. In accordance with Securities and Exchange Act, treasury shares cannot be pledged. Also, treasury shares do not bear the shareholder's right prior to being sold to third parties.
3. As of December 31, 2012, the Company's shares held by its subsidiaries were 1,700 thousand shares amounting to \$63,835 at fair value.

(vi) Earnings Distribution and Dividend Policy

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, is distributed as follows:

1. No less than 10% as employees' bonuses which are distributable in cash or shares of stock. In the event that the employee bonus is distributed in the form of shares of stock, employees qualifying for such distribution may include the employees of subsidiaries of the Company who meet certain specific requirements. Such qualified employees and distribution ratio are decided by the Board of Directors.

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2. Up to 1% as remuneration to directors and supervisors.
3. The remaining earnings, if any, are appropriated according to a resolution of a stockholders' meeting.

Pursuant to the Regulations of Securities and Futures Bureau Commission, a special reserve is set aside from the current year's net income after tax and prior year's unappropriated earnings at an amount equal to the debit balance of contra accounts in the shareholders' equity such as the unrealized loss on financial instruments and cumulative translation adjustments. When the debit balance of any of these contra accounts in the shareholders' equity is reversed, the related special reserve can be reversed.

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, the Company distributes cash dividends of at least 10% of the aggregate dividends, if the distributions include cash dividends.

On June 27, 2012 and June 24, 2011, the Company's shareholders' meetings resolved to appropriate the 2011 and 2010 earnings. Except for the appropriation for 2011 directors' and supervisors' remuneration which is yet to be resolved by the shareholders, these earnings were distributed as dividends and employee bonuses and remuneration to directors and supervisors as follows:

	<u>2011</u>	<u>2010</u>
Common stock dividends per share (dollars)		
-Cash	<u>\$ -</u>	<u>1.45</u>
Employee bonus — cash	\$ 12,100	127,000
Remuneration to directors and supervisors	-	12,000
Total	<u>\$ 12,100</u>	<u>139,000</u>

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The approved earnings distribution for 2010 agreed with those accrued and reflected in the financial statements for the year ended December 31, 2010. The approved earnings distributions for 2011 were as follows:

	Actual distribution approved by the shareholders'	Distribution recognized in the financial report	Difference
Employee bonus - cash \$	12,100	12,100	-
Remuneration of directors and supervisors	-	1,000	(1,000)
	\$ 12,100	13,100	(1,000)

The difference between the actual amounts of earnings distribution for 2011 and those recognized in the financial statements was due mainly to the board of directors' resolution to change the amount of directors' and supervisors' remuneration to \$0. Such difference was accounted for under a change in accounting estimate and charged to profit or loss.

For the year ended December 31, 2012, employee bonuses of \$299,000 and directors' and supervisors' remuneration of \$29,000 were estimated and recognized as current expenses. Management is expecting that the differences between the amounts which are yet to be approved in the shareholders' meeting and those recognized in the financial statements, if any, will be treated as changes in accounting estimates and charged to profit or loss.

The earnings distribution for the year ended December 31, 2012 has not been approved through shareholders' meeting. Related information can be accessed from the Market Observation Post System on the web site.

m. Earnings per Share (EPS)

For the years ended December 31, 2012 and 2011, the primary earnings per share, diluted earnings per share and the retroactively adjusted primary and diluted earnings per share were computed as follows:

(Note: shares in thousands)

	For the Years Ended December 31			
	2012		2011	
	Before income tax	After income tax	Before income tax	After income tax
Net income	\$ 6,541,353	6,103,796	58,514	111,365
Effect of potentially dilutive common shares	182,163	151,195	-	-
Diluted net income	\$ 6,723,516	6,254,991	58,514	111,365

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For the Years Ended December 31

	2012		2011	
	Before income tax	After income tax	Before income tax	After income tax
Weighted-average common shares outstanding	2,255,780	2,255,780	2,255,192	2,255,192
Potentially dilutive common shares	217,920	217,920	7,981	7,981
Diluted shares	2,473,700	2,473,700	2,263,173	2,263,173
Primary earnings per share	\$ 2.90	2.71	0.03	0.05
Diluted earnings per share	\$ 2.72	2.53	0.03	0.05

Pro forma result from assuming the Company's shares held by its subsidiaries do not count as treasury stock

For the Years Ended December 31

	2012		2011	
	Before income tax	After income tax	Before income tax	After income tax
Net income	\$ 6,541,353	6,103,796	58,514	111,365
Effect of potentially dilutive common shares	182,163	151,195	-	-
Diluted net income	\$ 6,723,516	6,254,991	58,514	111,365
Weighted-average common shares outstanding	2,257,480	2,257,480	2,256,367	2,256,367
Potentially dilutive common shares	217,920	217,920	7,981	7,981
Diluted shares	2,475,400	2,475,400	2,264,348	2,264,348
Primary earnings per share	\$ 2.90	2.70	0.03	0.05
Diluted earnings per share	\$ 2.72	2.53	0.03	0.05

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n. Financial Instruments

(i) Fair value of financial instruments

The fair value of short-term financial instruments is determined by their face value on balance sheet date. As this type of financial instrument has a short maturity period, the face value is adopted as a reasonable basis for establishing its fair value. This method is applied to cash, accounts receivable, accounts payable, short-term loans, accrued expenses, and other payables.

As of December 31, 2012 and 2011, except for the financial assets and liabilities described above, the Company's other financial assets and liabilities were as follows:

Financial Liabilities	December 31, 2012		December 31, 2011	
	Book Value	Fair Value	Book Value	Fair Value
Financial liabilities report at fair value through profit or loss	\$ 6,275	6,275	-	-
Bank loans	17,975,760	17,975,760	18,286,100	18,286,100
Bonds payable	8,403,406	8,403,406	-	-

(ii) Methods and assumptions used by the Company to evaluate the fair value of financial instruments were as follows:

1. The fair market value of long-term loans is determined by the present value of future cash flow. As the present value derived by using interest rate in discounting future cash flow is close to the book value, the book value is adopted as the fair market value.
2. The fair market value of bonds payable is determined by the present value of future cash flow. The discount rate adopted calculating the said present value is estimated based on similar corporate bond's market interest rate.
3. The fair value of derivative financial instruments, which are reported at fair value through profit or loss and traded in active markets, is based on quoted market prices. If the financial instruments are not traded in an active market, then the fair value is determined by using valuation techniques, under which, the estimates and assumptions used are consistent with prevailing market conditions.

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(iii) Financial risks

1. Market risk

The Company's purchases and sales are denominated mainly in US dollars. Consequently, it is exposed to the current and future foreign currency fluctuation risk that arises from cash flows of foreign currency assets and liabilities. However, this risk may be regarded as insignificant, because foreign currency losses from sales are subsequently offset by foreign currency gain from purchases.

2. Credit risk

The primary potential credit risk is from financial instruments like cash, equity securities, and accounts receivable. However, the Company deposits cash in different financial institutions. Also, the Company 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 Company only transacted with approved third parties with good financial conditions and reputation. For those customers with poor financial situation, the Company would transfer the risk by acquiring guarantees or transacting by L/C. In compliance with the Company's customer credit evaluation policies, the Company 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 Company are concentrated in the high-tech computer industry. As the customers of the Company have good credits and profit records, the Company evaluates the financial conditions of these customers continually to reduce credit risk from accounts receivable. Moreover, the Company periodically evaluates the customers' financial positions and the possibility of collecting trade receivables. Thus, management is not expecting any significant issue on credit risk.

3. Liquidity risk

The capital and working funds of the Company are sufficient to meet its entire contractual obligations; therefore, management is not expecting any significant issue on liquidity risk.

4. Cash flow and interest rate risk

The Company'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.

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(iv) Financial Instruments with Off-Balance Sheet Credit Risk:

As of December 31, 2012 and 2011, guarantees and endorsements provided by the Company for bank loans obtained by related parties, were discussed in Note 5.

o. Others

The Company's significant foreign financial assets and liabilities were as follows:

	December 31, 2012			December 31, 2011		
	Foreign Currency	Exchange Rate	NTD	Foreign Currency	Exchange Rate	NTD
Financial Assets						
<u>Monetary Items</u>						
USD	\$6,976,283	29.04	202,591,258	3,853,347	30.275	116,660,080
<u>Long-term Equity Investments</u>						
USD	1,038,854	29.04	30,168,324	971,608	30.275	29,415,421
EUR	53,635	38.49	2,064,406	35,320	39.18	1,383,843
Financial Liabilities						
<u>Monetary Items</u>						
USD	7,173,487	29.04	208,318,062	4,042,144	30.275	122,375,910

5. Related-Party Transactions

a. Names and relationships of related parties with the Company

Name of Related Party	Relationship with the Company
ASUSTEK COMPUTER INC. (ASUSTEK)	An investor company accounting its investment in the Company under the equity method
ASKEY COMPUTER CORP.(ASKEY)	An investee company accounted for under the equity method by ASUSTeK Computer Inc.
ASUS TECHNOLOGY INC.	//
ASMEDIA TECHNOLOGY INC.	//
ASUSTEK COMPUTER (SHANGHAI) CO., LTD.	//
ASUS COMPUTER (SHANGHAI) CO., LTD.	//
SHINEWAVE INTERNATIONAL INC.	//
UNIMAX ELECTRONICS INC.	//
ASUS COMPUTER INTERNATIONAL (ACI)	//
ENERTRONIX, INC.	//
ASHINE TECHNOLOGY (SUZHOU) LTD.	//
ASKEY TECHNOLOGY (JIANG SU) LTD. (ASKEY (JIANG SU))	//
POWTEK (SHANGHAI) CO., LTD. (POWTEK)	An investee company accounted for under the equity method

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<u>Name of Related Party</u>	<u>Relationship with the Company</u>
ADVANSUS CORP. (ADVANSUS)	An investee company which ceased to be accounted for under the equity method effective January 1, 2012.
ASROCK INC.	An investee company accounted for under the equity method
ABILITY ENTERPRISE CO., LTD.	"
PEGA INTERNATIONAL LTD.	"
UNIHAN CORPORATION (UNIHAN)	"
AMA PRECISION INC.	"
STARLINK ELECTRONICS CORP.	"
ASFLY TRAVEL SERVICE LTD.	"
AZUREWAVE TECHNOLOGIES INC.	"
PROTEK (SHANGHAI) LTD. (PROTEK)	"
SHANGHAI INDEED TECHNOGLY CO., LTD. (SHANGHAI INDEED)	"
KAEDAR ELECTRONICS (KUNSHAN) CO., LTD. (KAEDAR ELECTRONICS)	"
MAINTEK COMPUTER (SUZHOU) CO., LTD. (MAINTEK)	"
BOARDTEK COMPUTER (SUZHOU) CO., LTD.	"
CASETEK COMPUTER (SUZHOU) CO., LTD. (CASETEK)	"
AVY PRECISION ELECTROPLATING (SUZHOU) CO., LTD. (AVY)	"
CORE-TEK (SHANGHAI) LTD.	"
PEGAVISION CORP.	An investee company accounted for under the equity method by Kinsus Interconnect Technology Corp.
RUNTOP(SHANGHAI) CO., LTD. (RUNTOP)	An investee company accounted for under the equity method
LUMENS DIGITAL OPTICS INC.	"
HOLD JUMPER PACKING (SUZHOU) CO., LTD.	"
HOLD JUMPER PACKING (SHANGHAI) CO., LTD.	"
SUZHOU DELUXE PACKING PRODUCTION CO., LTD.	"
COTEK ELECTRONICS (SUZHOU) CO., LTD.	"
RI-TENG COMPUTER ACCESSORY (SHANGHAI) CO., LTD. (RI-TENG)	"
RI-KUAN METAL CORP.(RI-KUAN)	"

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<u>Name of Related Party</u>	<u>Relationship with the Company</u>
RIH LI INTERNATIONAL LIMITED	An investee company accounted for under the equity method
GREEN PACKING LIMITED	//
DIGITEK (CHONGQING) LTD.	//
KINSUS INTERCONNECT CORP.	//
ASUS INVESTMENT CO., LTD.	//
PEGATRON SERVICOS DE INFORMATICA LTDA. (PCBR)	//
KAEDAR TRADING LTD.	//
ASUSPOWER CORP. (ASUSPOWER)	//
PEGATRON CZECH S.R.O (PCZ)	//
PEGATRON JAPAN INC. (PCJ)	//
PEGATRON MEXICO, S.A. DE C.V.(PCM)	//
PEGATRON TECHNOLOGY SERVICE INC. (PTSI)	//
PEGATRON USA, INC.	//
BLACKROCK MARYLAND INT'L CORP.	//
VIEWQUEST TECHNOLOGIES (BVI) INC.	//
UNITED NEW LIMITED	//
MEGA MERIT LIMITED	//
ASIAROCK TECHNOLOGY LTD.	//

b. Significant Transactions with Related Parties

(i) Sales

Name of Related Party	For the Years Ended December 31					
	2012			2011		
	Amount	% of Net Sales	The collection term	Amount	% of Net Sales	The collection term
ASUSTEK	\$ 132,338,189	20.72	Open account 60 days	168,460,748	45.32	Open account 60 days
PCZ	6,733,693	1.05	120 days from receipt of goods	5,239,652	1.41	120 days from receipt of goods
POWTEK	3,902,538	0.61	45 days from receipt of goods	3,485,967	0.94	45 days from receipt of goods
Others	370,585	0.06	30~90 days from receipt of goods Open account 30~90 days	718,062	0.19	30~90 days from receipt of goods Open account 30~90 days
Total	\$ 143,345,005	22.44		177,904,429	47.86	

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The collection term with third-party customer is L/C, T/T or 7 to 120 days from receipt of goods.

For the years ended December 31, 2012 and 2011, the Company adjusted the double recording of sales to and purchases from related parties, which amounted to \$527,057,811 and \$309,257,679, respectively.

As of December 31, 2012 and 2011, unrealized profits on intercompany transactions were \$102,505 and \$57,611, respectively.

(ii) Purchases

Name of Related Party	For the Years Ended December 31					
	2012			2011		
	Amount	% of Gross Purchases	Purchase term	Amount	% of Gross Purchases	Purchase term
ASUSTeK	\$ 102,904,941	16.26	Open account 60 days	125,809,844	34.37	Open account 60 days
PROTEK	91,791,221	14.50	Open account 60 days	56,064,625	15.32	Open account 60 days
MAINTEK (Note)	4,080,331	0.64	Open account 60 days	(1,700,746)	(0.46)	Open account 60 days
CASETEK	2,176,703	0.34	Open account 60 days	1,822,673	0.50	Open account 60 days
SHANGHAI INDEED	2,131,684	0.34	Open account 60 days	2,546,870	0.70	Open account 60 days
ASKEY (JIANG SU)	1,590,694	0.25	Open account 60 days	2,333,987	0.64	Open account 60 days
RI-TENG	1,337,763	0.21	Open account 60 days	1,421,930	0.39	Open account 60 days
Others	420,027	0.07	30~90 days from receipt of goods Open account 30~120 days	2,203,519	0.58	30~90 days from receipt of goods Open account 30~120 days
Total	\$ 206,433,364	32.61		190,502,702	52.04	

Note: The Company sells raw materials to overseas factories for fabrication and buys back the finished goods for selling purposes. In order to avoid double recording of sales, the revenues and cost of goods sold are written off in proportion to the repurchase ratio. As the purchase amount is less than the sales amount for the year ended December 31, 2011, the net balance becomes a negative amount.

The purchase term with third-party vendors is 90 days from receipt of goods or open account 30 to 90 days.

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For the years ended December 31, 2012 and 2011, the Company purchased raw materials from vendors through ASUSTek.

(iii) Others

(1)	For the Years Ended December 31	
	2012	2011
<u>After-sales warranty repair expense paid to:</u>		
PCZ	\$ 65,487	52,438
PTSI	50,641	106,908
PCJ	17,224	16,531
ASUS COMPUTER (SHANGHAI) CO., LTD.	33,857	1,245
Others	1,533	1,236
Total	\$ 168,742	178,358

(2)	For the Years Ended December 31	
	2012	2011
<u>Assembling fee paid to:</u>		
ASUSPOWER	\$ 186,070	1,347,287
PCM	176,396	155,214
RUNTOP	-	47,325
Others	-	132
Total	\$ 362,466	1,549,958

(3)	For the Years Ended December 31	
	2012	2011
<u>Other income from:</u>		
ASUSTeK	\$ 493,055	527,204
UNIHAN	30,738	28,884
PCJ	17,063	26,119
Others	15,177	19,684
Total	\$ 556,033	601,891

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- (4) For the years ended December 31, 2012 and 2011, the Company incurred other related party transactions recorded as expenses such as rental expense, other expense, royalty payment, storage expense, professional service fee, etc, aggregating to \$351,207 and \$111,662, respectively.
- (5) For the years ended December 31, 2012 and 2011, the Company incurred other related party transactions recorded as rental revenue, amounting to \$64,081 and \$56,048, respectively.
- (6) For the years ended December 31, 2012 and 2011, the Company sold for \$8,656 and \$3,032 to other related party fixed assets with carrying value of \$8,099 and \$2,606, which resulted in gain on disposal of fixed assets of \$557 and \$426, respectively.
- (7) For the years ended December 31, 2012 and 2011, the Company had other related party transactions recorded as non-operating expense amounting to \$29,151 and \$31,779, respectively.
- (iv) Accounts receivable (payable)

	December 31, 2012		December 31, 2011	
	Amount	%	Amount	%
<u>Accounts Receivable:</u>				
PROTEK	\$ 81,220,882	42.25	53,627,766	48.11
DIGITEK (CHONGQING)	14,458,524	7.52	2,241,367	2.01
MAINTEK	8,840,833	4.60	2,763,233	2.48
ASUSTeK	4,746,542	2.47	9,116,587	8.18
PCZ	2,332,636	1.21	2,616,432	2.35
Others	635,846	0.34	310,758	0.28
Total	\$ 112,235,263	58.39	70,676,143	63.41
<u>Other Receivables:</u>				
UNIHAN	\$ 19,696	0.19	9,053	18.01
RI-KUAN	6,506	0.06	18	0.04
DIGITEK (CHONGQING)	1,300	0.01	-	-
Others	872	0.01	771	1.53
Total	\$ 28,374	0.27	9,842	19.58
<u>Accounts Payable:</u>				
PROTEK	\$ 72,863,923	40.25	53,236,449	53.03
DIGITEK (CHONGQING)	10,769,327	5.95	1,955,635	1.95
Others	1,591,913	0.88	2,747,526	2.74
Total	\$ 85,225,163	47.08	57,939,610	57.72

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	December 31, 2012		December 31, 2011	
	Amount	%	Amount	%
<u>Accrued Expenses:</u>				
PCM	\$ 393,676	9.67	359,402	6.10
PROTEK	-	-	362,841	6.16
ASUSPOWER	4,040	0.10	2,274,830	38.64
ASUSTeK	34,181	0.84	396,675	6.74
PCZ	39,572	0.97	13,783	0.23
Others	48,930	1.21	180,568	3.07
Total	<u>\$ 520,399</u>	<u>12.79</u>	<u>3,588,099</u>	<u>60.94</u>

As of December 31, 2012, the Company had collected \$1,349,732, on behalf of PROTEK, which was accounted for under other current liability.

Other related party transactions accounted for as other assets or liabilities in balance sheets were as follows:

	December 31, 2012	December 31, 2011
<u>Assets:</u>		
Prepayments	\$ 8,150	75
Temporary payments	236	-
	<u>\$ 8,386</u>	<u>75</u>
<u>Liabilities:</u>		
Temporary receivables	<u>\$ 87,239</u>	<u>24,527</u>

(v) Endorsement Guarantee

As of December 31, 2012 and 2011, the Company provided endorsement guarantee for bank loans obtained by related parties as follows:

Name of Related Party Guaranteed	Amount of Guarantee (thousands)	
	December 31, 2012	December 31, 2011
ASUSPOWER	<u>USD 100,815</u>	<u>USD 80,000</u>
PCZ	<u>USD 10,000</u>	<u>USD 10,000</u>
PIOTEK	<u>USD 49,000</u>	<u>USD 49,000</u>
UNITED NEW LTD.	<u>USD -</u>	<u>USD 20,000</u>
RI-TENG	<u>USD -</u>	<u>USD 90,000</u>
PROTEK	<u>USD 200,000</u>	<u>USD 200,000</u>
AVY	<u>USD -</u>	<u>USD 75,000</u>

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(vi) Financing

As of December 31, 2012, the details of financing provided by a related party to the Company were as follows:

	For the Year Ended December 31, 2012			
	The Highest Balance	Ending Balance	Annual Interest	Interest Expense
ASUSPOWER	\$ (5,976,000)	(5,808,000)	0.311%~0.468%	12,405

(vii) Remuneration

For the years ended December 31, 2011 and 2010, the total remuneration paid to the members of Board of Directors and Supervisors and of Executive management were as follows:

	December 31, 2012	December 31, 2011
Salary and Bonus (including BODS remuneration)	\$ 119,916	196,127
Employee Bonus	-	20,791
	\$ 119,916	216,918

6. Pledged Assets

As of December 31, 2012 and 2011, pledged assets were as follows:

Asset	December 31		Purpose of pledge
	2012	2011	
Restricted deposits	\$ 76,204	72,003	Deposits for customs duties, provisional seizure, and accounts receivable factoring
Refundable deposits	30,650	29,271	Deposits for performance guarantee
	\$ 106,854	101,274	

7. Significant Commitments And Contingencies (Excluding Related-Party Transactions)

- (a) As of December 31, 2012 and 2011, the Company had unused letters of credit of both EUR\$ 267 thousand and USD1,000 thousand.
- (b) As of December 31, 2012 and 2011, the Company had promissory notes and certificate of deposit obtained for business purpose of both \$11,537.

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(c) Rental expense and future lease commitments arising from operating lease agreements were as follows:

	For the Year ended	Future lease commitments			
		December 31, 2012	2013	2014	2015
Rent expense	\$ 91,995	37,280	1,929	840	-

8. Significant Catastrophic Losses: None.

9. Significant Subsequent Events: None.

10. Others

a. Personnel, depreciation, and amortization expense incurred, categorized as operating cost or expense, were as follows:

Categorized as Nature	For the Year Ended December 31, 2012			For the Year Ended December 31, 2011		
	Operating Cost	Operating Expense	Total	Operating Cost	Operating Expense	Total
Personnel expense						
Salary expense	803,136	4,457,818	5,260,954	689,436	3,562,442	4,251,878
Health and labor	57,694	259,688	317,382	51,656	241,016	292,672
Insurance expense						
Pension expense	32,066	159,645	191,711	30,848	149,395	180,243
Other expense	68,885	266,545	335,430	41,823	161,138	202,961
Depreciation expense (Note A)	20,635	146,729	167,364	38,055	155,600	193,655
Amortization expense	341,858	126,848	468,706	247,913	223,448	471,361

Note A: For the years ended December 31, 2012 and 2011, the Company recognized depreciation expense (accounted for as non-operating expense), excluding those of rental assets and idle assets of \$6,959 and \$11,687, respectively.

b. Certain accounts in the financial statements as of and for the year ended December 31, 2011, were reclassified to conform to the presentation adopted in the financial statements as of and for the year ended December 31, 2012.

11. Segment Information

As segment information is disclosed in the Company's consolidated financial statements, the Company need not present such information in its stand-alone or individual financial statements.