

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

**PEGATRON CORPORATION
AND ITS SUBSIDIARIES**

CONSOLIDATED FINANCIAL STATEMENTS

**December 31, 2016 and 2015
(With Independent Auditors' Report Thereon)**

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

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Representation Letter

The entities that are required to be included in the combined financial statements of PEGATRON CORPORATION as of and for the year ended December 31, 2016 under the Criteria Governing the Preparation of Affiliation Reports, Consolidated Business Reports, and Consolidated Financial Statements of Affiliated Enterprises are the same as those included in the consolidated financial statements prepared in conformity with International Financial Reporting Standards No. 10 by the Financial Supervisory Commission, "Consolidated and Separate Financial Statements." In addition, the information required to be disclosed in the combined financial statements is included in the consolidated financial statements. Consequently, PEGATRON CORPORATION and its Subsidiaries do not prepare a separate set of combined financial statements.

Company name: PEGATRON CORPORATION

Chairman: Tzu-Hsien Tung

Date: March 14, 2017



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Independent Auditors' Report

To the Board of Directors of Pegatron Corporation:

Opinion

We have audited the consolidated financial statements of Pegatron Corporation and its subsidiaries (“the Group”), which comprise the consolidated statement of financial position as of December 31, 2016 and 2015, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, based on our audits and the reports of other auditors, the accompanying financial statements present fairly, in all material respects, the consolidated financial position of the Group as at December 31, 2016 and 2015, and its financial performance and its cash flows for the years then ended in accordance with the Regulations Governing the Preparation of Financial Reports by Securities Issuers and with the International Financial Reporting Standards (“IFRSs”), International Accounting Standards (“IASs”), interpretations as well as related guidance endorsed by the Financial Supervisory Commission of the Republic of China.

Basis for Opinion

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

Key Audit Matters

Based on our professional judgment, key audit matters pertain to the most important matters in the audit of consolidated financial statements for the year ended December 31, 2016 of the Group. Those matters have been addressed in our audit opinion on the said consolidated financial statements and during the formation of our audit opinion. However, we do not express an opinion on these matters individually. The key audit matters that, in our professional judgment, should be communicated are as follows:

1. Revenue recognition

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

(a) Key audit matters:

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

Therefore, the test of sales and sales returns and allowances recognition was one of the key audit matters in the audit of consolidated financial reports for the years ended December 31, 2016 and 2015 of the Group.

(b) Auditing procedures performed:

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

2. Inventory valuation

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

(a) Key audit matters:

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

(b) Auditing procedures performed:

- Analyze the amount of obsolete inventory and inventory market price decline between 2016 and 2015 and understand reasons of the difference. Discuss and resolve those differences with management.
- Obtain an inventory aging analysis and randomly select items to verify the correctness for age of inventory.
- Obtain last selling price for finished goods and replacement cost for raw material, and recalculate net realizable value with selling expense rate to check whether or not the method of inventory measurement adopted by the Group is reasonable.

Other Matter

We did not audit the financial statements of certain consolidated subsidiaries with total assets representing 11.72% and 14.33% and net sales representing 3.47% and 4.50% of the related consolidated total as of and for the years ended December 31, 2016 and 2015, respectively. Also, we did not audit the long-term investments in other companies representing 0.03% and 0.05% of consolidated total assets as of December 31, 2016 and 2015, respectively, and the related investment loss thereon representing (0.24)% and (0.11)% of consolidated net income before tax for the years ended December 31, 2016 and 2015, respectively. The financial statements of these subsidiaries and investees accounted for under the equity method were audited by other auditors, whose reports have been furnished to us, and our opinion, insofar as it relates to the amounts for these companies, were based solely on the reports of other auditors.

We have also audited the non-consolidated financial statements of Pegatron Corporation as of and for the years ended December 31, 2016 and 2015 and have issued an unqualified and a modified unqualified audit report thereon, respectively.

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

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

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

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

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

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

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

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

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

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

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

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

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

KPMG

Taipei, Taiwan (Republic of China)
March 14, 2017

Notes to Readers

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

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

PEGATRON CORPORATION AND ITS SUBSIDIARIES

Consolidated Statements of Comprehensive Income

For the years ended December 31, 2016 and 2015

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

		For the year ended December 31			
		2016		2015	
		Amount	%	Amount	%
4110	Sales revenue (Notes 6(x) and 7)	\$ 1,163,923,241	101	1,218,853,846	100
4170	Less: Sales returns and allowances	<u>6,213,128</u>	<u>1</u>	<u>5,140,870</u>	<u>-</u>
	Operating revenue, net	1,157,710,113	100	1,213,712,976	100
5000	Cost of sales (Notes 6(d), 6(q), 6(r) and 7)	<u>1,094,642,996</u>	<u>95</u>	<u>1,138,437,983</u>	<u>94</u>
	Gross profit from operations	63,067,117	5	75,274,993	6
6000	Operating expenses (Notes 6(q), 6(r) and 7):				
6100	Selling expenses	5,946,930	-	9,646,871	1
6200	General and administrative expenses	10,620,127	1	11,280,211	1
6300	Research and development expenses	<u>14,086,091</u>	<u>1</u>	<u>14,673,367</u>	<u>1</u>
	Total operating expenses	30,653,148	2	35,600,449	3
	Results from operating activities	32,413,969	3	39,674,544	3
	Non-operating income and expenses:				
7010	Other income (Note 6(z))	3,172,133	-	3,605,179	-
7020	Other gains and losses (Notes 6(o) and 6(z))	(5,247,487)	-	(2,848,776)	-
7050	Finance costs (Notes 6(o) and 6(z))	(1,005,006)	-	(852,951)	-
7060	Share of loss of associates and joint ventures accounted for using equity method (Note 6(f))	(3,131)	-	(12,854)	-
7590	Miscellaneous disbursements	<u>(250,808)</u>	<u>-</u>	<u>(379,128)</u>	<u>-</u>
		<u>(3,334,299)</u>	<u>-</u>	<u>(488,530)</u>	<u>-</u>
	Profit from continuing operations before tax	29,079,670	3	39,186,014	3
7950	Less: Tax expense (Note 6(s))	<u>6,942,278</u>	<u>1</u>	<u>10,314,155</u>	<u>1</u>
	Profit for the year	22,137,392	2	28,871,859	2
8300	Other comprehensive income (Notes 6(t) and 6(aa)):				
8310	Components of other comprehensive income that will not be reclassified to profit or loss				
8311	Remeasurement effect on net defined benefit liability	4,265	-	1,277	-
8349	Income tax related to components of other comprehensive income that will not be reclassified to profit or loss	<u>(1,286)</u>	<u>-</u>	<u>(1,085)</u>	<u>-</u>
		<u>2,979</u>	<u>-</u>	<u>192</u>	<u>-</u>
8360	Other components of other comprehensive income that may be reclassified to profit or loss				
8361	Exchange differences on translation of foreign financial statements	(8,597,708)	(1)	(1,191,862)	-
8362	Unrealized gains (losses) on valuation of available-for-sale financial assets	124,524	-	(124,493)	-
8370	Share of other comprehensive income of associates and joint ventures accounted for using equity method	(48,217)	-	(24,066)	-
8399	Income tax related to components of other comprehensive income that may be reclassified to profit or loss	<u>(96,953)</u>	<u>-</u>	<u>(611)</u>	<u>-</u>
		<u>(8,424,448)</u>	<u>(1)</u>	<u>(1,339,810)</u>	<u>-</u>
8300	Other comprehensive income for the year, net of tax	(8,421,469)	(1)	(1,339,618)	-
8500	Total comprehensive income for the year	\$ 13,715,923	1	27,532,241	2
	Profit attributable to:				
8610	Owners of the parent company	\$ 19,339,815	2	23,811,625	2
8620	Non-controlling interests	<u>2,797,577</u>	<u>-</u>	<u>5,060,234</u>	<u>-</u>
		<u>\$ 22,137,392</u>	<u>2</u>	<u>28,871,859</u>	<u>2</u>
	Comprehensive income attributable to:				
8710	Owners of the parent company	\$ 12,008,187	1	22,809,542	2
8720	Non-controlling interests	<u>1,707,736</u>	<u>-</u>	<u>4,722,699</u>	<u>-</u>
		<u>\$ 13,715,923</u>	<u>1</u>	<u>27,532,241</u>	<u>2</u>
	Earnings per share, net of tax (Note 6(w))				
9750	Basic earnings per share	\$	7.50	9.23	
9850	Diluted earnings per share	\$	7.42	9.10	

See accompanying notes to financial statements.

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

Consolidated Statements of Changes in Equity

For the years ended December 31, 2016 and 2015

(Expressed in Thousands of New Taiwan Dollars)

	Equity attributable to owners of the parent company														
	Share capital					Total other equity interest									
	Retained earnings					Exchange differences on translation of foreign financial statements	Unrealized gains (losses) on for-sale financial assets	Deferred compensation cost	Total other equity interest	Treasury stock	Owners of the parent company	Non-controlling interests	Total equity		
	Common stock	Advance receipts for share capital	Total share capital	Capital surplus	Legal reserve									Unappropriated retained earnings	Total retained earnings
Balance at January 1, 2015	\$23,679,105	1,477,700	25,156,805	74,295,720	3,413,566	25,911,678	29,325,244	4,788,058	177,810	(64,523)	4,901,345	(8,183)	133,670,931	41,200,299	174,871,230
Profit for the year	-	-	-	-	-	23,811,625	23,811,625	-	-	-	-	-	23,811,625	5,060,234	28,871,859
Other comprehensive income for the year	-	-	-	-	-	434	434	(1,035,041)	33,424	(1,002,517)	(1,002,517)	-	(1,002,083)	(337,535)	(1,339,618)
Total comprehensive income for the year	-	-	-	-	-	23,812,059	23,812,059	(1,035,041)	33,424	-	(1,002,517)	-	22,809,542	4,722,699	27,532,241
Appropriation and distribution of retained earnings:															
Legal reserve	-	-	-	-	1,465,814	(1,465,814)	-	-	-	-	-	-	-	-	-
Cash dividends of common stock	-	-	-	-	-	(10,509,621)	(10,509,621)	-	-	-	-	-	(10,509,621)	-	(10,509,621)
Conversion of convertible bonds	1,946,748	(1,472,500)	474,248	2,679,408	-	-	-	-	-	-	-	-	3,153,656	-	3,153,656
Disposal of the Company's share by subsidiaries treated as treasury stock transactions	-	-	-	12,029	-	-	-	-	-	-	-	6,113	18,142	-	18,142
Changes in ownership interests in subsidiaries	-	-	-	8,885	-	-	-	-	-	-	-	-	8,885	(8,885)	-
Share-based payments	13,800	(5,200)	8,600	26,488	-	-	-	-	-	-	(520)	-	35,088	-	35,088
Expiration of restricted shares of stock issued to employees	(6,228)	-	(6,228)	6,748	-	-	-	-	-	-	-	-	-	-	-
Compensation cost arising from restricted shares of stock	396,780	-	396,780	1,943,096	-	27,490	27,490	-	-	(1,173,854)	(1,173,854)	-	1,193,512	(3,955,723)	1,193,512
Changes in non-controlling interests	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Balance at December 31, 2015	26,030,205	-	26,030,205	78,972,374	4,879,380	37,775,792	42,655,172	3,752,117	211,234	(1,238,377)	2,724,974	(2,590)	150,380,135	41,998,390	192,338,525
Profit for the year	-	-	-	-	-	19,339,815	19,339,815	(7,305,056)	(27,281)	-	(7,332,337)	-	19,339,815	2,797,577	22,137,392
Other comprehensive income for the year	-	-	-	-	-	709	709	(7,305,056)	(27,281)	-	(7,332,337)	-	(7,331,628)	(1,089,841)	(8,421,469)
Total comprehensive income for the year	-	-	-	-	-	19,340,524	19,340,524	(7,305,056)	(27,281)	-	(7,332,337)	-	12,008,187	1,707,736	13,715,923
Appropriation and distribution of retained earnings:															
Legal reserve	-	-	-	-	2,381,163	(2,381,163)	-	-	-	-	-	-	-	-	-
Cash dividends of common stock	-	-	-	-	-	(12,953,501)	(12,953,501)	-	-	-	-	-	(12,953,501)	-	(12,953,501)
Conversion of convertible bonds	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Purchase of treasury stock	-	-	-	-	-	-	-	-	-	-	-	-	(2,068,328)	-	(2,068,328)
Retirement of treasury stock	(264,100)	-	(264,100)	(830,477)	-	(973,751)	(973,751)	-	-	-	-	-	(2,068,328)	-	(2,068,328)
Changes in ownership interests in subsidiaries	-	-	-	2,575	-	-	-	-	-	-	-	-	2,575	(2,575)	-
Share-based payments	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Expiration of restricted shares of stock issued to employees	(14,410)	-	(14,410)	14,066	-	-	-	-	-	-	-	344	900,522	-	900,522
Compensation cost arising from restricted shares of stock	-	-	-	55,721	-	36,306	36,306	-	-	808,495	808,495	-	900,522	-	900,522
Changes in non-controlling interests	-	-	-	-	-	-	-	-	-	-	-	-	(9,910,940)	-	(9,910,940)
Balance at December 31, 2016	\$25,751,695	-	25,751,695	78,214,259	7,260,543	40,844,207	48,104,750	(3,852,939)	183,953	(429,882)	(3,798,868)	(2,246)	148,269,590	33,752,611	182,022,201

See accompanying notes to financial statements.

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PEGATRON CORPORATION AND ITS SUBSIDIARIES

Consolidated Statements of Cash Flows
For the years ended December 31, 2016 and 2015
(Expressed in Thousands of New Taiwan Dollars)

	For the years ended December 31	
	2016	2015
Cash flows from operating activities:		
Profit before tax	\$ 29,079,670	39,186,014
Adjustments:		
Adjustments to reconcile profit (loss):		
Depreciation expense	12,770,863	13,471,400
Amortization expense	141,548	223,479
Reversal of allowance for uncollectable accounts	(36,760)	(80,476)
Net loss (gain) on financial assets or liabilities at fair value through profit or loss	(67,790)	200,625
Interest expense	912,165	672,266
Interest income	(1,057,275)	(1,396,275)
Dividend income	(20,659)	(97,677)
Compensation cost arising from employee stock options	907,285	941,827
Effect of exchange rate changes of bonds payable	-	(13,748)
Amortization of issuance costs on bonds payable	-	254
Share of loss of associates and joint ventures accounted for using equity method	3,131	12,854
Effect of exchange rate changes of long-term loans	(36,176)	115,907
Loss on disposal of property, plant and equipment	240,489	200,197
Property, plant and equipment charged to expenses	49,768	17,511
Gain on disposal of non-current assets classified as held for sale	-	(402,661)
Loss (gain) on disposal of investments	574,526	(397,657)
(Reversal of) Impairment loss	59,968	(134,852)
Long-term prepaid rent charged to expenses	95,295	95,425
Decrease in provision	(11,650)	(48,452)
Other loss	217,855	-
Total adjustments to reconcile profit (loss)	14,742,583	13,379,947
Changes in operating assets and liabilities:		
Changes in operating assets:		
Decrease in financial assets at fair value through profit or loss	424,768	1,052,032
Decrease in notes and accounts receivable	24,197,509	9,912,717
Increase in other receivables	(14,022,934)	(12,875,512)
Decrease (increase) in inventories	9,509,597	(22,535,022)
Decrease in other financial assets	150,037	1,402,108
Decrease (increase) in other current assets	8,128,167	(3,613,244)
Decrease in other non-current assets	21,285	50,607
Total changes in operating assets	28,408,429	(26,606,314)
Changes in operating liabilities:		
Decrease in financial liabilities at fair value through profit or loss	-	(8,937)
Increase (decrease) in notes and accounts payable	12,076,464	(13,620,335)
Increase (decrease) in accrued expenses	(1,648,644)	2,551,506
Decrease in other payables	(1,403,876)	(389,408)
Decrease in provisions	(24,416)	(47,601)
Decrease in deferred revenue	(69,141)	(611,895)
Increase in other current liabilities	670,573	2,907,337
Increase in other non-current liability	22,830	94,645
Total changes in operating liabilities	9,623,790	(9,124,688)
Net changes in operating assets and liabilities	38,032,219	(35,731,002)
Net adjustments	52,774,802	(22,351,055)
Cash provided by operating activities	81,854,472	16,834,959
Interest received	1,069,904	1,425,566
Dividends received	70,384	139,496
Interest paid	(919,565)	(806,348)
Income taxes paid	(10,244,344)	(7,621,888)
Net cash flows from operating activities	71,830,851	9,971,785

See accompanying notes to financial statements.

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PEGATRON CORPORATION AND ITS SUBSIDIARIES

Consolidated Statements of Cash Flows(CONT'D)

For the years ended December 31, 2016 and 2015

(Expressed in Thousands of New Taiwan Dollars)

	For the years ended December 31	
	2016	2015
Cash flows from investing activities:		
Proceeds from disposal of available-for-sale financial assets	-	935,224
Acquisition of financial assets carried at cost	-	(15,450)
Proceeds from disposal of financial assets carried at cost	653	200,584
Acquisition of investments accounted for using equity method	-	(10,000)
Proceeds from disposal of subsidiaries	(3,674,323)	-
Proceeds from capital reduction of investments accounted for using equity method	-	161,086
Proceeds from disposal of non-current assets classified as held for sale	-	603,037
Acquisition of property, plant and equipment	(12,453,467)	(11,461,700)
Proceeds from disposal of property, plant and equipment	529,241	594,520
Acquisition of intangible assets	(224,591)	(143,249)
Decrease (increase) in other financial assets	(110,298)	254,418
Increase in prepayments on purchase of equipment	(4,317,635)	(3,415,970)
Increase in long-term prepaid rentals	(180,965)	(455,788)
Net cash flows used in investing activities	<u>(20,431,385)</u>	<u>(12,753,288)</u>
Cash flows from financing activities:		
Increase (decrease) in short-term loans	(13,919,128)	18,286,520
Proceeds from long-term loans	14,200,000	16,636,681
Repayments of long-term loans	(24,020,366)	(23,539,410)
Cash dividends paid	(15,172,473)	(12,840,060)
Capital reduction payments to shareholders	-	(1,664,408)
Exercise of employee stock options	-	39,794
Purchase of treasury stock	(2,068,328)	(32,885)
Proceeds from sale of treasury stock	-	46,521
Issuance of restricted stock	-	396,780
Redemption of restricted stock	(15,057)	(26,254)
Change in non-controlling interests	125,000	3,520
Net cash flows used in financing activities	<u>(40,870,352)</u>	<u>(2,693,201)</u>
Effect of exchange rate fluctuations on cash held	<u>(4,377,148)</u>	<u>347,418</u>
Net increase (decrease) in cash and cash equivalents	6,151,966	(5,127,286)
Cash and cash equivalents, beginning of the year	<u>102,561,346</u>	<u>107,688,632</u>
Cash and cash equivalents, end of the year	<u>\$ 108,713,312</u>	<u>102,561,346</u>

See accompanying notes to financial statements.

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

Notes to the Consolidated Financial Statements

For the years ended December 31, 2016 and 2015

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

(1) Company history

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

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

The consolidated financial statements of the Company as of and for the years ended December 31, 2016 and 2015 comprise the Company and its subsidiaries (together referred to as the "Group" and individually as "Group entities") and the Group's interest in associates entities.

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

The accompanying consolidated financial statements for the year ended December 31, 2016 were authorized for issue by the Board of Directors on March 14, 2017.

(3) New standards, amendments and interpretations adopted:

- (a) Impact of not yet adopted International Financial Reporting Standards ("IFRSs") endorsed by the Financial Supervisory Commission, R.O.C. ("FSC")

According to Ruling No. 1050026834 issued on July 18, 2016, by the FSC, public entities are required to conform to the IFRSs which were issued by the International Accounting Standards Board (IASB) before January 1, 2016, and were endorsed for adoption by the FSC in preparing their financial statements effective January 1, 2017. The related new standards, interpretations and amendments are as follows:

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

(Continued)

PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

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

Except for the following items, the Group believes that the adoption of the above IFRSs would not have a material impact on the consolidated financial statements:

(i) Amendments to IAS 36 "Recoverable Amount Disclosures for Non-Financial Assets"

Under the amendments, the recoverable amount is required to be disclosed only when an impairment loss has been recognized or reversed. In such cases, the amendments also require that the following be disclosed if the recoverable amount is based on fair value less costs of disposal:

- 1) the level of the fair value hierarchy within which the fair value measurement is categorized; and
- 2) the valuation technique(s) used for fair value measurements categorized within Levels 2 and 3 of the fair value hierarchy, and the key valuation assumptions made.

The Group expects the aforementioned amendments will result in a broader disclosure of the recoverable amount for non-financial assets.

(b) Newly released or amended standards and interpretations not yet endorsed by the FSC

The following is a summary of the new standards and amendments issued by the IASB but not yet endorsed by the FSC. The FSC announced that the Group should apply IFRS 9 and IFRS 15 starting January 1, 2018. As of the issuance date the Group's financial statements, the FSC has yet to announce the effective dates of the other IFRSs.

<u>New, Revised or Amended Standards and Interpretations</u>	<u>Effective date per IASB</u>
IFRS 9 "Financial Instruments"	January 1, 2018

(Continued)

PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

<u>New, Revised or Amended Standards and Interpretations</u>	<u>Effective date per IASB</u>
Amendments to IFRS 10 and IAS 28 "Sale or Contribution of Assets Between an Investor and Its Associate or Joint Venture"	Effective date to be determined by IASB
IFRS 15 "Revenue from Contracts with Customers"	January 1, 2018
IFRS 16 "Leases"	January 1, 2019
Amendment to IFRS 2 "Clarifications of Classification and Measurement of Share-based Payment Transactions"	January 1, 2018
Amendment to IFRS 15 "Clarifications of IFRS 15"	January 1, 2018
Amendment to IAS 7 "Disclosure Initiative"	January 1, 2017
Amendment to IAS 12 "Recognition of Deferred Tax Assets for Unrealized Losses"	January 1, 2017
Amendments to IFRS 4 "Insurance Contracts" (Applicable for IFRS 9 "Financial Instruments" and IFRS 4 "Insurance Contracts")	January 1, 2018
Annual Improvements to IFRS Standards 2014-2016 Cycle:	
IFRS 12 "Disclosure of Interests in Other Entities"	January 1, 2017
IFRS 1 "First-time Adoption of International Financial Reporting Standards" and IAS 28 "Investments in Associates and Joint Ventures"	January 1, 2018
IFRIC 22 "Foreign Currency Transactions and Advance Consideration"	January 1, 2018
Amendments to IAS 40 Investment Property	January 1, 2018

Relevant standards applicable to the Group were as follows:

<u>Issuance / Release Dates</u>	<u>Standards or Interpretations</u>	<u>Content of amendment</u>
May 28, 2014 April 12, 2016	IFRS 15 "Revenue from Contracts with Customers"	IFRS 15 establishes a five-step model for recognizing revenue that applies to all contracts with customers, and will supersede IAS 18 "Revenue," IAS 11 "Construction Contracts," and a number of revenue-related interpretations. Final amendments issued on April 12, 2016, clarify how to (i) identify performance obligations in a contract; (ii) determine whether a company is a principal or an agent; (iii) account for a license for intellectual property (IP); and (iv) apply transition requirements.

(Continued)

PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

<u>Issuance / Release Dates</u>	<u>Standards or Interpretations</u>	<u>Content of amendment</u>
November 19, 2013 July 24, 2014	IFRS 9 "Financial Instruments"	<p>The standard will replace IAS 39 "Financial Instruments: Recognition and Measurement", and the main amendments are as follows:</p> <ul style="list-style-type: none"> • Classification and measurement: Financial assets are measured at amortized cost, fair value through profit or loss, or fair value through other comprehensive income, based on both the entity's business model for managing the financial assets and the financial assets' contractual cash flow characteristics. Financial liabilities are measured at amortized cost or fair value through profit or loss. Furthermore, there is a requirement that "own credit risk" adjustments be measured at fair value through other comprehensive income. • Impairment: The expected credit loss model is used to evaluate impairment. • Hedge accounting: Hedge accounting is more closely aligned with risk management activities, and hedge effectiveness is measured based on the hedge ratio.
January 13, 2016	IFRS 16 "Leases"	<p>The new standard of accounting for lease is amended as follows:</p> <ul style="list-style-type: none"> • For a contract that is, or contains, a lease, the lessee shall recognize a right-of-use asset and a lease liability in the balance sheet. In the statement of profit or loss and other comprehensive income, a lessee shall present interest expense on the lease liability separately from the depreciation charge for the right-of use asset during the lease term. • A lessor classifies a lease as either a finance lease or an operating lease, and therefore, the accounting remains similar to IAS 17.

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

(Continued)

PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

(4) Summary of significant accounting policies:

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

(a) Statement of compliance

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

(b) Basis of preparation

(i) Basis of measurement

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

- 1) Financial instruments measured at fair value through profit or loss are measured at fair value (including derivative financial instruments) ;
- 2) Available-for-sale financial assets are measured at fair value;
- 3) Liabilities for cash-settled share-based payment arrangements are measured at fair value; and
- 4) The net defined benefit liability is recognized as the present value of the defined benefit obligation less the fair value of plan assets and the effect of the asset ceiling.

(ii) Functional and presentation currency

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

(c) Basis of consolidation

(i) Principle of preparation of the consolidated financial statements

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

(Continued)

PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

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

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

(ii) Acquisition of non-controlling interests

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

(iii) Subsidiaries

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

(iv) Business combination under common control

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

(v) Losing control

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

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

Investor	Subsidiary	Nature of business	Shareholding ratio		Notes
			December 31, 2016	December 31, 2015	
THE COMPANY AND ASUSPOWER INVESTMENT	ABILITY ENTERPRISE CO., LTD. (Ability (TW))	Selling computer peripherals, office automation equipment, digital cameras, retailing and wholesaling, of food products and leasing	11.73 %	11.72 %	Note 1
Ability (TW)	ABILITY ENTERPRISE (BVI) CO., LTD.(ABILITY)	Investing activities	100.00 %	100.00 %	Note 1

(Continued)

PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

Investor	Subsidiary	Nature of business	Shareholding ratio		Notes
			December 31, 2016	December 31, 2015	
Ability (TW)	ACTION PIONEER INTERNATIONAL LTD.	Trading activities	100.00 %	100.00 %	Note 1
Ability (TW)	VIEWQUEST TECHNOLOGIES INTERNATIONAL INC.	Selling computer peripherals, digital cameras and electronic components	100.00 %	100.00 %	Note 1
Ability (TW)	VIEWQUEST TECHNOLOGIES (BVI) INC.(VQ(BVI))	Manufacturing and trading computer peripherals, digital cameras and electronic components	100.00 %	100.00 %	Note 1
Ability (TW)	Ability International Investment Co., Ltd.(ABILITY INVESTMENT)	Investing activities	100.00 %	100.00 %	Note 1
Ability (TW)	E-PIN OPTICAL INDUSTRY CO., LTD.(E-PIN)	Selling electronic components of optical products	53.01 %	53.01 %	Note 1
ABILITY	Ability Technology (Dongguan) Co., Ltd.	Manufacturing and selling digital cameras	100.00 %	100.00 %	Note 1
ABILITY	Jiujiang Viewquest Electronics Inc.	Manufacturing and selling digital cameras	100.00 %	100.00 %	Note 1
VQ(BVI)	VIEWQUEST TECHNOLOGIES (DONGGUAN) CO., LTD.	Manufacturing and selling digital cameras	100.00 %	100.00 %	Note 1
E-PIN	E-PIN OPTICAL INDUSTRY CO., LTD.	Trading activities	100.00 %	100.00 %	Note 1
E-PIN	E-PIN OPTICAL INDUSTRY(M.)SDN BHD.	Manufacturing precision lenses	100.00 %	100.00 %	Note 1
E-PIN	ALL VISION TECHNOLOGY SDN BHD.	Manufacturing precision lenses	100.00 %	100.00 %	Note 1
E-PIN	ALL VISION HOLDING LTD.(AV)	Investing activities	100.00 %	100.00 %	Note 1
AV	EVERLIGHT DEVELOPMENT CORPORATION(ED)	Investing activities	100.00 %	100.00 %	Note 1
AV	E-SKY HOLDING LTD.(ES)	Investing activities	73.04 %	73.04 %	Note 1
ED	NANJING CHANGMING PHOTOELECTRIC TECHNOLOGY CO., LTD.	Manufacturing and developing precision optical lenses	55.45 %	55.45 %	Note 1
ES	ZHONGSHAN SANXIN PRECISION INDUSTRY CO., LTD.	Manufacturing and developing precision optical lenses	100.00 %	100.00 %	Note 1
ES	NANJING E-PIN OPTOTECH CO., LTD.	Manufacturing and developing precision optical lenses	72.22 %	72.22 %	Note 1
THE COMPANY	UNIHAN HOLIDNG LTD. (UNIHAN HOLDING)	Investing activities	100.00 %	100.00 %	
UNIHAN HOLDING	CASETEK HOLDINGS LIMITED (CASETEK HOLDINGS)	Investing and trading activities	100.00 %	100.00 %	

(Continued)

PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

Investor	Subsidiary	Nature of business	Shareholding ratio		Notes
			December 31, 2016	December 31, 2015	
CASETEK HOLDINGS	SLITEK HOLDINGS LIMITED	Investing and trading activities	100.00 %	100.00 %	
CASETEK HOLDINGS	CASETEK COMPUTER (SUZHOU) CO., LTD.	Manufacturing, developing and selling computers, computer parts, application systems, and providing after-sales service	100.00 %	100.00 %	
CASETEK HOLDINGS	KAEDAR HOLDINGS LIMITED (KAEDAR HOLDINGS)	Investing and trading activities	100.00 %	100.00 %	
KAEDAR HOLDINGS	KAEDAR ELECTRONICS (KUNSHAN) CO., LTD.	Tooling molds of stainless steel computer cases	100.00 %	100.00 %	
CASETEK HOLDINGS	KAEDAR TRADING LTD.	Investing and trading activities	100.00 %	100.00 %	
CASETEK HOLDINGS	CORE-TEK (SHANGHAI) LIMITED	Researching and producing spare parts for notebook computers, designing nonmetal tooling, electronic specific equipment and related products, repairing and producing precision equipment and providing after-sales service	100.00 %	100.00 %	
CASETEK HOLDINGS	KAI-CHUAN ELECTRONICS (CHONGQING) CO., LTD.	Manufacturing, developing and inspecting computers and application systems, designing and manufacturing nonmetal and metal tooling, developing plastic and electronic component, selling self-manufactured products.	100.00 %	100.00 %	
THE COMPANY, ASUSPOWER INVESTMENT AND ASUSTEK INVESTMENT	AZURE WAVE TECHNOLOGIES, INC. (AZURE WAVE)	Manufacturing office machinery, electronic parts and computer peripherals and selling precision equipment, and digital cameras	38.08 %	38.08 %	Note 2
AZURE WAVE	EMINENT STAR CO., LTD. (Eminent)	Investing activities	- %	100.00 %	Notes 2 and 6
Eminent	Jade Technologies Limited(Jade)	Investing activities	- %	100.00 %	Notes 2 and 4
AZURE WAVE	EZWAVE TECHNOLOGIES, INC.	Manufacturing office machinery, electronic parts and computer peripherals	100.00 %	100.00 %	Note 2
AZURE WAVE	Azwave Holding (Samoa) Inc.(Azwave Samoa)	Investing activities	100.00 %	100.00 %	Note 2
AZURE WAVE	Azurewave Technologies (USA) Inc.	Developing market	100.00 %	100.00 %	Note 2
AZURE WAVE	AZURE LIGHTING TECHNOLOGIES, INC.	Selling electronic parts	100.00 %	100.00 %	Note 2
Azwave Samoa	AZURE WAVE TECHNOLOGIES (SHANGHAI) INC.	Designing, manufacturing and selling computer products	100.00 %	100.00 %	Note 2
Azwave Samoa	AZURE LIGHTING TECHNOLOGIES, INC. (YANGZHOU)	Manufacturing and selling LED and relevant lighting products	100.00 %	100.00 %	Note 2
Azwave Samoa	AIGALE CORPORATION (SHANGHAI)	Designing and selling communication equipment and electronic products	100.00 %	100.00 %	Note 2

(Continued)

PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

Investor	Subsidiary	Nature of business	Shareholding ratio		Notes
			December 31, 2016	December 31, 2015	
THE COMPANY	AMA PRECISION INC.(AMA PRECISION)	Designing and developing computer parts	100.00 %	100.00 %	
AMA PRECISION	AMA Holdings Limited(AMA)	Investing activities	100.00 %	100.00 %	
AMA	EXTECH LTD.	Trading electronic parts	90.51 %	90.51 %	
EXTECH LTD.	GRANDTECH PRECISION (TONGZHOU) CO., LTD.	Manufacturing, developing and selling electronic parts	100.00 %	100.00 %	
AMA	TOPTEK PRECISION INDUSTRY(SUZHOU) CO., LTD.	Manufacturing and selling new electronic parts and premium hardware	100.00 %	100.00 %	
THE COMPANY	PEGATRON HOLLAND HOLDING B.V.(PHH)	Investing activities	100.00 %	100.00 %	
PHH	PEGATRON Czech s.r.o.	Installing, repairing and selling electronic products	100.00 %	100.00 %	
PHH	Pegatron Service Holland B.V.	Sales and repair service center in Europe	100.00 %	100.00 %	
THE COMPANY	PEGATRON HOLDING LTD. (PEGATRON HOLDING)	Investing activities	100.00 %	100.00 %	
PEGATRON HOLDING	POWTEK HOLDINGS LIMITED (POWTEK)	Investing and trading activities	100.00 %	100.00 %	
POWTEK	POWTEK (SHANGHAI) LTD.	Selling main boards, computer peripherals, note books, servers and software, and providing after-sales service	100.00 %	100.00 %	
PEGATRON HOLDING KINSUS SAMOA	PIOTEK HOLDINGS LTD. (CAYMAN) (PIOTEK CAYMAN)	Investing activities	100.00 %	100.00 %	
PIOTEK CAYMAN	PIOTEK HOLDING LIMITED (PIOTEK HOLDING)	Investing activities	100.00 %	100.00 %	
PIOTEK HOLDING	PIOTEK COMPUTER (SUZHOU) CO., LTD.	Developing, manufacturing and selling new electronic components, circuit boards and relevant products, and providing after-sales service	100.00 %	100.00 %	
PIOTEK HOLDING	PIOTEK(H.K.) TRADING LIMITED	Trading activities	100.00 %	100.00 %	
PEGATRON HOLDING	GRAND UPRIGHT TECHNOLOGY LIMITED	Investing and trading activities	100.00 %	100.00 %	
PEGATRON HOLDING	ASLINK PRECISION CO., LTD. (ASLINK)	Investing and trading activities	100.00 %	100.00 %	
ASLINK	PEGAGLOBE (KUNSHAN) CO.,LTD.	Manufacturing GPS, computer electronic devices, mobile phone, high-end server, disk drive, and other related components	100.00 %	100.00 %	
PEGATRON HOLDING	DIGITEK GLOBAL HOLDINGS LIMITED (DIGITEK)	Investing and trading activities	100.00 %	100.00 %	
DIGITEK	DIGITEK (CHONGQING) LTD.	Manufacturing, developing, and selling GPS, computer electronic devices, and after-sales services	100.00 %	100.00 %	

(Continued)

PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

Investor	Subsidiary	Nature of business	Shareholding ratio		Notes
			December 31, 2016	December 31, 2015	
PEGATRON HOLDING	MAGNIFICENT BRIGHTNESS LIMITED (MAGNIFICENT)	Investing and trading activities	100.00 %	100.00 %	
MAGNIFICENT	MAINTEK COMPUTER (SUZHOU) CO., LTD.	Manufacturing, developing and selling power supply units, computer cases, computer systems, notebooks, main boards, and computer peripherals, and providing after-sales service	100.00 %	100.00 %	
PEGATRON HOLDING	PROTEK GLOBAL HOLDINGS LTD.(PROTEK)	Investing and trading activities	100.00 %	100.00 %	
PROTEK	PROTEK (SHANGHAI) LTD.	Developing, manufacturing and selling GPS, new electronic components, circuit boards and relevant products, and providing after-sales service	100.00 %	100.00 %	
PEGATRON HOLDING	COTEK HOLDINGS LIMITED(COTEK)	Investing and trading activities	100.00 %	100.00 %	
COTEK	COTEK ELECTRONICS (SUZHOU) CO., LTD.	Developing, manufacturing and selling new electronic components, circuit boards and relevant products, and providing after-sales service	100.00 %	100.00 %	
PEGATRON HOLDING	TOP QUARK LIMITED(TOP QUARK)	Investing activities	100.00 %	100.00 %	
TOP QUARK	RUNTOP (SHANGHAI) CO., LTD.	Manufacturing and selling computer parts and peripherals of digital automatic data processors, multimedia computer system accessories, power supply units, network switches, and modems	100.00 %	100.00 %	
THE COMPANY	ASUSPOWER INVESTMENT CO., LTD.	Investing activities	100.00 %	100.00 %	
THE COMPANY	ASUS INVESTMENT CO., LTD.	Investing activities	100.00 %	100.00 %	
THE COMPANY	ASUSTEK INVESTMENT CO., LTD.	Investing activities	100.00 %	100.00 %	
ASUSPOWER INVESTMENT, ASUS INVESTMENT AND ASUSTEK INVESTMENT	ASROCK INCORPORATION (ASROCK)	Data storage and processing equipment, manufacturing wired and wireless communication equipment, and whole selling of computer equipment and electronic components	58.65 %	58.65 %	
ASROCK	ASIAROCK TECHNOLOGY LIMITED (ASIAROCK)	Manufacturing and selling database storage and processing equipment	100.00 %	100.00 %	
ASIAROCK	ASROCK EUROPE B.V.	Selling database service and trading electronic components	100.00 %	100.00 %	
ASIAROCK	CalRock Holdings, LLC.	Office building leasing	100.00 %	100.00 %	
ASROCK	Leader Insight Holdings Ltd.(Leader)	Investing and holding activities	100.00 %	100.00 %	
Leader	First place International Limited (First place)	Investing and holding activities	100.00 %	100.00 %	
First place	ASRock America, Inc.	Selling database service and trading electronic components	100.00 %	100.00 %	

(Continued)

PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

Investor	Subsidiary	Nature of business	Shareholding ratio		Notes
			December 31, 2016	December 31, 2015	
ASROCK	ASRock Rack Incorporation	Manufacturing and selling computer and related peripherals	69.40 %	69.40 %	
ASUSPOWER INVESTMENT AND ASUS INVESTMENT	PEGATRON Mexico, S.A. DE C.V.	Sales and repair service center in Mexico	100.00 %	100.00 %	
ASUSPOWER INVESTMENT, ASUS INVESTMENT AND ASUSTEK INVESTMENT	KINSUS INTERCONNECT TECHNOLOGY CORP. (KINSUS)	Manufacturing electronic parts, whole selling and retailing electronic components, and providing business management consultant service	39.04 %	39.04 %	Note 2
KINSUS	KINSUS INVESTMENT CO., LTD. (KINSUS INVESTMENT)	Investing activities	100.00 %	100.00 %	Note 2
KINSUS INVESTMENT, ASUSPOWER INVESTMENT AND ASUSTEK INVESTMENT	PEGAVISION CORPORATION	Manufacturing medical appliances	54.87 %	54.87 %	Note 2
KINSUS INVESTMENT, ASUSTEK INVESTMENT AND ASUS INVESTMENT	FUYANG TECHNOLOGY CORPORATION	Manufacturing and wholesaling wires, cables, and electronic components	90.00 %	- %	Note 3
PEGAVISION CORPORATION	PEGAVISION HOLDINGS CORPORATION (PEGAVISION)	Investing activities	100.00 %	100.00 %	Note 2
PEGAVISION CORPORATION	PEGAVISION JAPAN INC.	Selling medical appliances	100.00 %	100.00 %	Note 2
FUYANG TECHNOLOGY CORPORATION	FUYANG FLEX HOLDING LTD. (FUYANG HOLDING)	Investing activities	100.00 %	- %	Notes 3 and 7
FUYANG HOLDING	FUYANG ELECTRONICS (SUZHOU) CO., LTD.	Researching, producing, inspecting, repairing and selling flexible multilayer model, computer digital signal process system and card.	100.00 %	- %	Note 3
PEGAVISION	PEGAVISION (SHANGHAI) LIMITED	Selling medical appliances	100.00 %	100.00 %	Note 2
KINSUS	KINSUS CORP. (USA)	Developing and designing new technology and products; analyzing marketing strategy and developing new customers	100.00 %	100.00 %	Note 2
KINSUS	KINSUS HOLDING (SAMOA) LIMITED (KINSUS SAMOA)	Investing activities	100.00 %	100.00 %	Note 2
KINSUS SAMOA	KINSUS HOLDING (CAYMAN) LIMITED(KINSUS CAYMAN)	Investing activities	100.00 %	100.00 %	Note 2

(Continued)

PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

Investor	Subsidiary	Nature of business	Shareholding ratio		Notes
			December 31, 2016	December 31, 2015	
KINSUS CAYMAN	KINSUS INTERCONNECT TECHNOLOGY (SUZHOU) CORP.	Manufacturing and selling circuit boards	100.00 %	100.00 %	Note 2
KINSUS CAYMAN	KINSUS TRADING (SUZHOU) CORP.	Manufacturing and selling circuit boards related products and materials	100.00 %	100.00 %	Note 2
ASUSPOWER INVESTMENT, ASUS INVESTMENT AND ASUSTEK INVESTMENT	STARLINK ELECTRONICS CORPORATION	Manufacturing electronic parts and plastic products, and manufacturing and wholesaling electronic components	100.00 %	100.00 %	
ASUSPOWER INVESTMENT, ASUS INVESTMENT AND ASUSTEK INVESTMENT	ASUSPOWER CORPORATION	Investing and trading activities	100.00 %	100.00 %	
ASUSPOWER CORPORATION	CASETEK HOLDINGS LIMITED(CAYMAN) (CASETEK CAYMAN)	Investing activities	60.73 %	60.73 %	
CASETEK CAYMAN	RIH LI INTERNATIONAL LIMITED	Investing activities	100.00 %	100.00 %	
RIH LI	RI-TENG COMPUTER ACCESSORY (SHANGHAI) CO., LTD. (RI-TENG)	Designing, manufacturing and selling electronic components and providing after-sales services , idle equipments leasing, commission agency, trading services and their relevant corresponding services	100.00 %	100.00 %	
RIH LI	RI-PRO PRECISION MODEL (SHANGHAI) CO., LTD.	Designing, manufacturing and selling electronic components and providing after-sales services , idle equipments leasing, commission agency, trading services and their relevant corresponding services	100.00 %	100.00 %	
RIH LI	RI-MING (SHANGHAI) CO., LTD.	Designing, manufacturing and selling electronic components and providing after-sales services , idle equipments leasing, commission agency, trading services and their relevant corresponding services	100.00 %	100.00 %	
RIH LI	SHENG-RUI ELECTRONIC TECHNOLOGY (SHANGHAI) LIMITED	Designing, manufacturing and selling electronic components and providing after-sales services , idle equipments leasing, commission agency, trading services and their relevant corresponding services	100.00 %	100.00 %	
RIH LI	RI PEI COMPUTER ACCESSORY (SHANGHAI) CO., LTD.	Designing, manufacturing and selling electronic components and providing after-sales services , idle equipment leasing, commission agency, trading services and their relevant corresponding services	100.00 %	100.00 %	

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

Investor	Subsidiary	Nature of business	Shareholding ratio		Notes
			December 31, 2016	December 31, 2015	
RIH LI	KAI JIA COMPUTER ACCESSORY CO., LTD.	Designing, manufacturing and selling electronic components and providing after-sales services, idle equipment leasing, commission agency, trading services, relevant corresponding services, and surface processing for the aforementioned product.	100.00 %	100.00 %	
CASETEK CAYMAN	APEX SUN LIMITED	Investing activities	100.00 %	-	Note 5
CASETEK CAYMAN	RIH KUAN METAL CORPORATION	Selling iron and aluminum products	100.00 %	100.00 %	
CASETEK CAYMAN	APLUS PRECISION LIMITED(APLUS)	Investing and trading activities	100.00 %	100.00 %	
APLUS	UNITED NEW LIMITED(UNITED)	Investing and trading activities	100.00 %	100.00 %	
UNITED	KAI HE COMPUTER ACCESSORY (SUZHOU) CO., LTD	Designing, manufacturing and selling electronic components and providing after-sales service, idle equipment leasing, commission agency, trading services, relevant corresponding services, and surface processing for the aforementioned product.	100.00 %	100.00 %	
CASETEK CAYMAN	MEGA MERIT LIMITED	Trading activities	100.00 %	100.00 %	
ASUS INVESTMENT	ASFLY TRAVEL SERVICE LIMITED	Travel agency	100.00 %	100.00 %	
ASUSPOWER INVESTMENT	PEGATRON TECHNOLOGY SERVICE INC. (PTSI)	Sales and repair service center in North America	100.00 %	100.00 %	
PTSI	PEGATRON SERVICOS DE INFORMATICA LTDA. (PCBR)	Maintenance service	100.00 %	100.00 %	
ASUSPOWER INVESTMENT	PEGA INTERNATIONAL LIMITED	Design service and sales	100.00 %	100.00 %	
ASUSPOWER INVESTMENT	PEGATRON JAPAN INC.	Sales and repair service center in Japan	100.00 %	100.00 %	
ASUSPOWER INVESTMENT	PEGATRON LOGISTIC SERVICE INC.	Sales and logistics center in North America	100.00 %	100.00 %	
ASUSPOWER INVESTMENT, ASUS INVESTMENT AND ASUSTEK INVESTMENT	Lumens Digital Optics Inc. (Lumens Optics)	Developing, manufacturing and selling computer data projectors and related peripherals	56.52 %	56.52 %	
Lumens Optics	Lumens Integration Inc.	Selling computer communication products and peripherals	100.00 %	100.00 %	
Lumens Optics	Lumens Digit Image Inc. (SAMOA)(Lumens)	Investing activities	100.00 %	100.00 %	
Lumens	Lumens (Suzhou) Digital Image Inc.	Developing, manufacturing and selling projectors, projection screens and related products, and providing after-sales service	100.00 %	100.00 %	

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Investor	Subsidiary	Nature of business	Shareholding ratio		Notes
			December 31, 2016	December 31, 2015	
ASUSPOWER INVESTMENT	Pegatron Service Singapore Pte. Ltd.(PSG)	Sales and logistics center in Singapore	100.00 %	100.00 %	
PSG	PEGATRON SERVICE KOREA LLC.	Sales and repair service center in Korea	100.00 %	- %	Note 5
ASUS INVESTMENT	HUA-YUAN INVESTMENT LIMITED	Investing activities	100.00 %	100.00 %	
THE COMPANY	PEGATRON USA, INC.	Sales and repair service center in North America	100.00 %	100.00 %	

Note 1: On June 29, 2016, the shareholders of Ability Enterprise Co., Ltd. elected new set of directors during shareholders' meeting, so that the Group lost its control over Ability Enterprise Co., Ltd. as the Group is unable to acquire more than half of the voting rights of the board of directors. Consequently, Ability Enterprise Co., Ltd. and its subsidiaries were no longer included in the consolidated financial statements from that date on.

Note 2: As of December 31, 2016, AZURE WAVE TECHNOLOGY CORP., ABILITY ENTERPRISE CO., LTD. and KINSUS INTERCONNECT TECHNOLOGY CORP., were included in the consolidated financial statements even if the Group held 38.08% and 39.04%, respectively, or less than 50% of their total issued shares because the Group has acquired more than 50% of voting shares of each of these entities and has the ability to excise control over their respective board of directors.

Note 3: It was established in the second quarter of 2016.

Note 4: It was liquidated in May 2016.

Note 5: It was established in the first quarter of 2016.

Note 6: It was liquidated in August 2016.

Note 7: In October 2016, the Group has restructured, so that the 100% equity ownership of FUYANG HOLDING was transferred from UNIHAN HOLDING to FUYANG TECHNOLOGY.

(vii) Subsidiaries excluded from consolidation: None.

(d) Foreign currency

(i) Foreign currency transaction

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

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

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

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

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

(ii) Foreign operations

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

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

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

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

An asset is classified as current when:

- (i) It is expected to be realized the asset, or intended to be sold or consumed, during the normal operating cycle;
- (ii) It is held primarily for the purpose of trading;
- (iii) It is expected to be realized within twelve months after the reporting period; or

(Continued)

PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

- (iv) The asset is cash and cash equivalent (as defined in IAS 7) unless the asset is restricted from being exchanged or used to settle a liability for at least twelve months after the reporting period.

All other assets are classified as non-current.

A liability is classified as current when:

- (i) It is expected to be settled within the Group's normal operating cycle;
- (ii) It is held primarily for the purpose of trading;
- (iii) The liability is due to be settled within twelve months after the reporting period; or
- (iv) It does not have an unconditional right to defer settlement for at least twelve months after the reporting period. Terms of a liability that could, at the option of the counterparty, result in its settlement by issuing equity instruments do not affect its classification.

All other liabilities are classified as non-current.

(f) Cash and cash equivalents

Cash comprise cash balances and call deposits with maturities within three months. Cash equivalents are assets that are readily convertible into cash, and are subject to an insignificant risk of changes in their fair value.

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

(g) Inventories

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

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

(h) Financial instruments

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

(i) Financial assets

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

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

1) Financial assets at fair value through profit or loss

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

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

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

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

2) Available-for sale financial assets

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

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

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

(Continued)

PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

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

3) Loans and receivables

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

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

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

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

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

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
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4) Impairment of financial assets

A financial asset is impaired if, and only if, there is objective evidence of impairment as a result of one or more events (a loss event) that occurred subsequent to the initial recognition of the asset and that a loss event (or events) has an impact on the future cash flows of the financial assets that can be estimated reliably.

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

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

An impairment loss in respect of a financial asset measured at cost is calculated as the difference between its carrying amount and the present value of its estimated future cash flows discounted at the asset's original effective interest rate. Such impairment loss is not reversible in subsequent periods.

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

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

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

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

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

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

5) Derecognition of financial assets

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

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

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

(ii) Financial liabilities and equity instruments

1) Classification of debt or equity instruments

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

An equity instrument represents the Group's residual interest at any contract after deducting its liabilities from assets. Equity instruments issued are recognized based on amount of consideration received less the direct issuance cost.

Preference share is classified as equity if it is non-redeemable, or redeemable only at the Company's option, and any dividends are discretionary. Discretionary dividends thereon are recognized as distributions within equity upon approval by the Group's shareholders.

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

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

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

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

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

2) Financial liabilities at fair value through profit or loss

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

- a) Such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise from measuring assets or liabilities or recognizing the gains and losses thereon on different basis;
- b) Performance of the financial liabilities is evaluated on a fair value basis;
- c) Hybrid instrument contains one or more embedded derivatives.

Attributable transaction costs are recognized in profit or loss as incurred. Financial liabilities at fair value through profit or loss are measured at fair value and changes therein, which takes into account any interest expense, are recognized in profit or loss, under “non-operating income and expenses.”

Financial liabilities at fair value through profit or loss is measured at cost if it sells borrowed unquoted equity investment whose fair value cannot be reliably measured and if it is to be delivered to the obligator of the equity investment. This type of financial instrument is classified as financial liabilities measured at cost.

Financial guarantee contract and loan commitments are classified as financial liabilities at fair value through profit or loss, any gains and losses thereon are recognized in profit or loss.

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
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3) Other financial liabilities

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

4) Derecognition of financial liabilities

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

5) Offsetting of financial assets and liabilities

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

6) Financial guarantee contract

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

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

(iii) Derivative financial instruments, including hedge accounting

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

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

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

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

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

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

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

1) Fair value hedge

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

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

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

2) Cash flow hedge

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

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

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

(i) Non-current assets held-for-sale

Non-current assets, or disposal groups comprising assets and liabilities, that are expected to be recovered primarily through sale or distribution rather than through continuing use, are reclassified as held-for-sale or distribution. Immediately before classification as held-for-sale or distribution, the assets, or components of a disposal group, are re-assessed for impairment in accordance with the Group's accounting policies. Thereafter, generally the assets or disposal group, are measured at the lower of their carrying amount and fair value less costs to sell.

Any impairment loss on a disposal group is first allocated to goodwill, and then the remaining balance of impairment loss is apportioned to assets and liabilities on a pro rata basis, except that no loss is allocated to inventories, financial assets, deferred tax assets, employee benefit assets, investment property and biological assets, which are assessed for impairment in accordance with the Group's accounting policies. Impairment losses on initial classification of noncurrent assets held-for-sale or distribution and subsequent gains or losses on re-measurement are recognized in profit or loss. Gains are not recognized in excess of any cumulative impairment loss.

Once classified as held-for-sale or distribution, intangible assets and property, plant and equipment are no longer amortized or depreciated, and any equity-accounted investee is no longer equity accounted.

(j) Investment in associates

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

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

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

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

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

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(k) Investment property

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

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

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

Buildings	20-60 years
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When the use of an investment property changes such that it is reclassified as property, plant and equipment, its fair value at the date of reclassification becomes its cost for subsequent accounting.

(l) Property, plant and equipment

(i) Recognition and measurement

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

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

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

(ii) Reclassification to investment property

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

(Continued)

PEGATRON CORPORATION AND ITS SUBSIDIARIES
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(iii) Subsequent cost

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

(iv) Depreciation

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

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

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

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

Buildings	1-60 years
Machinery	1-10 years
Instrument equipment	3-10 years
Office and other equipment	2-10 years
Miscellaneous equipment	1-25 years

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

(m) Leased assets

(i) Lessor

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

(Continued)

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

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

(ii) Lessee

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

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

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

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

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

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

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

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

(Continued)

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

(n) Intangible assets

(i) Goodwill

1) Recognition

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

2) Measurement

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

(ii) Other Intangible Assets

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

(iii) Subsequent Expenditure

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

(iv) Amortization

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

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

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

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

(Continued)

PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

(o) Revenue

(i) Goods sold

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

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

(ii) Service

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

(p) Impairment – Non-financial assets

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

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

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

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

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

(Continued)

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

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

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

Reversal of an impairment loss for goodwill is prohibited.

(q) Provisions

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

(r) Treasury stock

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

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

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

(s) Employee benefits

(i) Defined contribution plans

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

(Continued)

PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

(ii) Defined benefit plans

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

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

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

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

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

(iii) Short-term employee benefits

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

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

(t) Share-based payment

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

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

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

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

(u) Income Taxes

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

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

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

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

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

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

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

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

(v) Business combination

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

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

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

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

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

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

(w) Government grant

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

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

(Continued)

PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

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

(x) Earnings per share

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

(y) Operating segments

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

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

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

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

(a) Judgment regarding control of subsidiaries

Due to significant judgments involved and material impact on recognized amounts for consolidated financial report, please refer to Note 6(g) for details.

(b) Valuation of inventories

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

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Notes to Consolidated Financial Statements

(6) Explanation of significant accounts:

(a) Cash and cash equivalents

	December 31, 2016	December 31, 2015
Cash on hand	\$ 16,143	37,507
Cash in banks	34,381,705	47,415,722
Time deposits	74,218,714	55,108,117
Cash equivalents-repurchase bonds	96,750	-
	<u>\$ 108,713,312</u>	<u>102,561,346</u>

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

(b) Investment in financial assets and liabilities

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

	December 31, 2016	December 31, 2015
Financial assets at fair value through profit or loss—current:		
Held-for-trading		
Shares of stock of listed companies	\$ 270,926	246,679
Beneficiary certificates	4,096,921	4,485,982
Total	<u>\$ 4,367,847</u>	<u>4,732,661</u>
Available-for-sale financial assets — current:		
Shares of stock of overseas listed companies	<u>\$ 266,523</u>	<u>857,820</u>
Available-for-sale financial assets — noncurrent:		
Shares of stock of listed companies	\$ 610,702	765,744
Equity securities — common stock	178,920	195,840
Total	<u>\$ 789,622</u>	<u>961,584</u>
Financial assets carried at cost — noncurrent:		
Equity securities — common stock	\$ 165,450	263,118
Equity securities — preferred stock	205,632	205,632
Total	<u>\$ 371,082</u>	<u>468,750</u>

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
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- 1) For the years ended December 31, 2016 and 2015, the Group recognized a net gain (loss) on financial assets (liabilities) reported at fair value through profit or loss of \$67,790 and \$(200,625), respectively.
 - 2) For the years ended December 31, 2016 and 2015, the unrealized gain (loss) on available-for-sale financial assets amounted to \$124,524 and \$(124,493), respectively.
 - 3) Considering that the range of reasonable fair value estimates is large and the probability for each estimate cannot be reasonably determined, the Group management believes the fair value cannot be measured reliably. Therefore, the aforementioned investments held by the Group are measured at amortized cost less impairment at each reporting date. The Group evaluated the carrying value and the recoverable amount of the investments and recognized impairment loss of \$0 and \$11,247 for the years ended December 31, 2016 and 2015, respectively. As of December 31, 2016 and 2015, the Group had accumulated impairment loss of \$254,811 and \$266,188, respectively.
 - 4) The convertible bond issued by the Group was treated as a compound financial instrument, for which the liability and equity components were accounted for separately. The call and put option embedded in bonds payable were separated from bonds payable, and were measured at fair value.” For the year ended December 31, 2015, the Group recognized a loss on financial liability reported at fair value through profit or loss of \$238,997. Please refer to Note 6(o) for detail.
 - 5) Refer to Note 6(z) for further discussion on gains and losses on disposal of investments.
 - 6) Refer to Note 6(ab) for the Group’s information on financial instruments risk management.
 - 7) As of December 31, 2016 and 2015, the aforesaid financial assets were not pledged as collateral.
- (ii) Fair value sensitivity analysis

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

	For the years ended December 31			
	2016		2015	
	Comprehensive Income (Loss) (net of tax)	Net Income (Loss) (net of tax)	Comprehensive Income (Loss) (net of tax)	Net Income (Loss) (net of tax)
Increase 3%	\$ 31,684	131,035	54,582	141,980
Decrease 3%	\$ (31,684)	(131,035)	(54,582)	(141,980)

(Continued)

PEGATRON CORPORATION AND ITS SUBSIDIARIES
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(iii) Foreign equity investments

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

(Unit: Foreign currency/NTD in Thousands)

	December 31, 2016			December 31, 2015		
	Foreign Currency	Exchange Rate	NTD	Foreign Currency	Exchange Rate	NTD
USD	\$ 10,992	32.250	354,492	28,121	32.825	923,072
CNY	57,329	4.6490	266,523	58,849	5.0550	297,482

(iv) Derivative not used for hedging

Derivative financial instruments are used to hedge certain foreign exchange and interest risk the Group is exposed to, arising from its operating, investing and financial activities. As of December 31, 2016 and 2015, the Group did not have related transactions that do not qualify for hedge accounting presented as held-for-trading financial assets and financial liability.

As of December 31, 2016 and 2015, the Group did not have related transactions that do not qualify for hedge accounting are presented as held-for-trading financial assets and financial liabilities.

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

	December 31, 2016	December 31, 2015
Notes receivable	\$ 96,170	170,001
Accounts receivable	95,115,492	121,973,316
Other receivables	42,605,518	27,709,682
Less: Allowance for impairment	(1,910,613)	(2,127,925)
	\$ 135,906,567	147,725,074

(i) Refer to Note 6(ab) for the Group's notes receivable, accounts receivable and other receivables exposure to credit risk and currency risk, and the impairment evaluation of notes receivable, accounts receivable and other receivables.

(ii) Accounts receivable which are transferred in accordance with derecognition standards of IFRS are deemed as sale of accounts receivable. As of December 31, 2016 and 2015, the Company sold its accounts receivable without recourse as follows:

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

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
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December 31, 2015						
Purchaser	Assignment Facility	Factoring Line	Advanced Amount	Collateral	Significant Factoring Terms	Derecognition Amount
SMBC	\$ -	USD 300,000,000	USD -	None	The accounts receivable factoring is without recourse but the seller still bears the risks except for eligible obligor's insolvency.	\$ -
ANZ (Note)	\$ 23,524,575	USD 1,400,000,000	USD -	None	"	\$ 23,524,575

Note: In October 2015, the Company signed a one year joint accounts receivable factoring agreement with ANZ Bank and six other banks where each bank will factor on pro-rata basis.

For the years ended December 31, 2016 and 2015, the Company recognized a loss of \$66,988 and \$159,497, respectively, from the factoring of accounts receivable, which was accounted under financial costs in the statement of comprehensive income. Also, the difference of \$38,700,000 and \$23,524,575 between the carrying value of factored accounts receivable and the amount advanced was accounted under other receivables as of December 31, 2016 and 2015, respectively.

- (iii) As of December 31, 2016 and 2015, KINSUS INTERCONNECT TECHNOLOGY CORP. sold its accounts receivable without recourse as follows:

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

December 31, 2015						
Purchaser	Assignment Facility	Factoring Line (thousands)	Advanced Amount	Collateral	Significant Factoring Terms	Derecognition Amount
Mega International Commercial Bank	\$ 251,600	USD 30,000	\$ -	None	The accounts receivable factoring is without recourse	\$ 251,600

(d) Inventories

	December 31, 2016	December 31, 2015
Merchandise	\$ 629,690	1,551,835
Finished goods	65,797,600	67,260,261
Work in process	17,624,217	20,917,494
Raw materials	28,203,409	35,083,914
Subtotal	112,254,916	124,813,504
Less: Allowance for inventory market decline and obsolescence	(4,935,514)	(6,648,044)
Total	<u>\$ 107,319,402</u>	<u>118,165,460</u>

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For the years ended December 31, 2016 and 2015, the components of cost of goods sold were as follows:

	For the years ended December 31	
	2016	2015
Cost of goods sold	1,067,674,727	1,099,548,746
(Reversal of) Provision on inventory market price decline	(1,519,661)	863,182
Loss on disposal of inventory	27,187,138	37,215,635
Unallocated manufacturing overhead	1,254,990	819,130
(Gain) Loss on physical inventory	<u>45,802</u>	<u>(8,710)</u>
	<u>1,094,642,996</u>	<u>1,138,437,983</u>

In 2016, the Group recognized reversal of provision on inventory market price decline of \$1,519,661 and included it in cost of goods sold because of adjusting inventory value to net realize value. The provision arising from destocking in 2015 of \$863,182 was recognized. Such gain was deducted from cost of goods sold.

As of December 31, 2016 and 2015, the aforesaid inventories were not pledged as collateral.

(e) Non-current assets classified as held for sale (net)

	December 31, 2016	December 31, 2015
Property, plant, and equipment	<u>\$ -</u>	<u>-</u>

(i) On February 16, 2015, Casetek Holdings sold its equity ownership in Indeed Holdings Limited for \$431,211 to non-related parties. As of December 31, 2014, the investments in Indeed Holdings Limited were accounted under non-current assets classified as held for sale. The transfer of equity ownership was completed in May 2015. A disposal gain of \$335,878 has been recognized thereon.

(ii) In December 2014, Ability (TW) and its subsidiaries sold part of the land and property of E-PIN's office in Taipei for \$158,280 in a sale-lease back arrangement. In February 2015, the process for the transfer of title of ownership to these assets was completed, when the payment for the assets sold is received, as required under the sales contract. In December 2014, Ability (TW) also sold its E-PIN's equipments in Nanjing for \$16,529 to a non-related party. The process for the transfer of title of ownership to those non-current assets has been completed during the reporting period. A disposal gain of \$66,783 has been recognized thereon.

(Continued)

PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

(f) Investments accounted for using equity method

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

	December 31, 2016	December 31, 2015
Individually insignificant associates	\$ 362,909	424,191
	For the years ended December 31	
	2016	2015
The Group's share of profit (loss) of the associates		
Loss for the year	\$ (3,131)	(12,854)
Other comprehensive income	(48,217)	(24,066)
Total comprehensive income	\$ (51,348)	(36,920)

- (ii) As of December 31, 2016 and 2015, the aforesaid investments accounted for using equity method were not pledged as collateral.

(g) Loss of control of a subsidiary

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

The derecognition amount of Ability's assets and liabilities as of June 29, 2016, were as follows:

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

(Continued)

PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

(h) Subsidiaries that have material non-controlling interest

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

Subsidiaries	Country of registration	Equity Ownership of non-controlling interest	
		December 31, 2016	December 31, 2015
KINSUS and its subsidiaries	Taiwan	60.96 %	60.96 %
ABILITY and its subsidiaries	Taiwan	-	88.28 %
ASROCK and its subsidiaries	Taiwan	41.35 %	41.35 %
CASETEK CAYMAN	Taiwan/ Cayman	39.27 %	39.27 %

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

(i) Information regarding KINSUS and its subsidiaries

	December 31, 2016	December 31, 2015
Current assets	\$ 21,615,555	23,471,368
Non-current assets	19,638,160	19,167,364
Current liabilities	(8,639,797)	(10,318,448)
Non-current liabilities	(1,599,149)	(1,492,483)
Net assets	<u>\$ 31,014,769</u>	<u>30,827,801</u>
Non-controlling interest	<u>\$ 18,151,995</u>	<u>17,777,750</u>
	For the years ended December 31	
	2016	2015
Operating revenue	<u>\$ 23,165,066</u>	<u>23,061,311</u>
Net income for the period	\$ 2,073,028	2,729,526
Other comprehensive loss	(326,985)	(137,614)
Comprehensive income	<u>\$ 1,746,043</u>	<u>2,591,912</u>
Net income attribute to non-controlling interest	<u>\$ 1,446,006</u>	<u>1,809,591</u>
Comprehensive income attribute to non-controlling interest	<u>\$ 1,325,193</u>	<u>1,767,315</u>

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

	<u>For the years ended December 31</u>	
	<u>2016</u>	<u>2015</u>
Cash flows from operating activities	\$ 5,752,676	6,938,575
Cash flows from investing activities	(4,971,181)	(4,961,460)
Cash flows from financing activities	<u>(2,312,646)</u>	<u>(783,229)</u>
Net (decrease) increase in cash and cash equivalents	<u>\$ (1,531,151)</u>	<u>1,193,886</u>
 (ii) Information regarding ABILITY and its subsidiaries		
	<u>December 31,</u>	<u>December 31,</u>
	<u>2016</u>	<u>2015</u>
Current assets	\$ -	8,795,084
Non-current assets	-	5,222,319
Current liabilities	-	(5,180,123)
Non-current liabilities	-	<u>(102,557)</u>
Net assets	<u>\$ -</u>	<u>8,734,723</u>
Non-controlling interest	<u>\$ -</u>	<u>7,745,320</u>
	<u>2016 Jan.-June</u>	<u>2015 Jan.-Dec.</u>
	<u>(Note)</u>	<u></u>
Operating revenue	<u>\$ 5,758,572</u>	<u>19,254,208</u>
Net income for the period	\$ 48,287	867,444
Other comprehensive income (loss)	<u>30,123</u>	<u>(150,734)</u>
Comprehensive income	<u>\$ 78,410</u>	<u>716,710</u>
Net income attribute to non-controlling interest	<u>\$ 48,655</u>	<u>788,449</u>
Comprehensive income attribute to non-controlling interest	<u>\$ 74,224</u>	<u>655,092</u>
Cash flows from operating activities	\$ 213,863	989,459
Cash flows from investing activities	(205,297)	290,330
Cash flows from financing activities	<u>(11,498)</u>	<u>(2,366,148)</u>
Net decrease in cash and cash equivalents	<u>\$ (2,932)</u>	<u>(1,086,359)</u>

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

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Notes to Consolidated Financial Statements

(iii) Information regarding ASROCK and its Subsidiaries

	December 31, 2016	December 31, 2015
Current assets	\$ 7,751,292	7,812,156
Non-current assets	330,798	319,077
Current liabilities	(2,438,731)	(2,244,410)
Non-current liabilities	<u>(15,879)</u>	<u>(30,284)</u>
Net assets	<u>\$ 5,627,480</u>	<u>5,856,539</u>
Non-controlling interest	<u>\$ 2,309,248</u>	<u>2,425,260</u>
	For the years ended December 31	
	2016	2015
Operating revenue	<u>\$ 7,120,620</u>	<u>7,217,149</u>
Net income for the period	\$ 123,375	206,131
Other comprehensive (loss) income	<u>(64,830)</u>	<u>144,199</u>
Comprehensive income	<u>\$ 58,545</u>	<u>350,330</u>
Net income attribute to non-controlling interest	<u>\$ 29,750</u>	<u>65,427</u>
Comprehensive income attribute to non-controlling interest	<u>\$ 340</u>	<u>125,804</u>
Cash flows from operating activities	\$ 541,030	1,305,366
Cash flows from investing activities	8,117	1,980,973
Cash flows from financing activities	<u>(287,604)</u>	<u>(460,137)</u>
Net increase in cash and cash equivalents	<u>\$ 261,543</u>	<u>2,826,202</u>

(iv) Information regarding CASETEK CAYMAN

	December 31, 2016	December 31, 2015
Current assets	\$ 28,863,585	28,893,035
Non-current assets	21,739,451	19,927,861
Current liabilities	(19,445,716)	(15,581,629)
Non-current liabilities	<u>(2,412,077)</u>	<u>(2,237,693)</u>
Net assets	<u>\$ 28,745,243</u>	<u>31,001,574</u>
Non-controlling interest	<u>\$ 11,287,107</u>	<u>12,173,078</u>

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
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	For the years ended December 31	
	2016	2015
Operating revenue	\$ 32,763,310	38,614,914
Net income for the period	\$ 2,801,624	5,635,891
Other comprehensive loss	(2,340,299)	(537,953)
Comprehensive income	\$ 461,325	5,097,938
Net income attribute to non-controlling interest	\$ 1,100,086	2,212,989
Comprehensive income attribute to non-controlling interest	\$ 176,272	2,001,754
Cash flows from operating activities	\$ 5,188,093	10,819,513
Cash flows from investing activities	(6,529,986)	(5,513,822)
Cash flows from financing activities	2,075,656	(3,554,164)
Net increase in cash and cash equivalents	\$ 733,763	1,751,527

(i) Property, plant and equipment

The movements in the cost, depreciation, and impairment of the property, plant and equipment of the Group for the years ended December 31, 2016 and 2015 were as follows:

	Land	Buildings	Machinery and equipment	Instrument equipment	Other facilities	Construction in progress	Total
Cost or deemed cost:							
Balance on January 1, 2016	\$ 5,580,222	41,312,837	58,970,443	1,559,813	25,442,907	6,164,893	139,031,115
Additions	-	1,201,866	2,507,628	115,842	1,696,725	7,095,931	12,617,992
Disposals and obsolescence	-	(683,866)	(3,907,119)	(112,741)	(2,508,785)	-	(7,212,511)
Reclassifications	4,642	4,398,938	4,180,183	11,438	1,986,181	(6,254,585)	4,326,797
Effect of movement in exchange rate	(15,462)	(2,818,941)	(3,587,843)	(102,931)	(1,490,261)	(339,203)	(8,354,641)
Loss of control of a subsidiary	(1,248,948)	(1,429,646)	(2,570,728)	-	(2,460,056)	(526,728)	(8,236,106)
Balance on December 31, 2016	\$ 4,320,454	41,981,188	55,592,564	1,471,421	22,666,711	6,140,308	132,172,646
Balance on January 1, 2015	\$ 5,567,180	41,446,276	58,742,688	1,670,643	25,178,826	2,982,725	135,588,338
Additions	10,766	662,997	2,724,897	77,359	1,987,509	5,768,819	11,232,347
Disposals and obsolescence	(179,496)	(1,142,042)	(4,026,148)	(157,911)	(2,177,467)	-	(7,683,064)
Reclassifications	191,374	1,173,279	2,518,969	-	949,097	(2,516,768)	2,315,951
Effect of movement in exchange rate	(9,602)	(827,673)	(989,963)	(30,278)	(495,058)	(69,883)	(2,422,457)
Balance on December 31, 2015	\$ 5,580,222	41,312,837	58,970,443	1,559,813	25,442,907	6,164,893	139,031,115

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	<u>Land</u>	<u>Buildings</u>	<u>Machinery and equipment</u>	<u>Instrument equipment</u>	<u>Other facilities</u>	<u>Construction in progress</u>	<u>Total</u>
Depreciation and impairment loss :							
Balance on January 1, 2016	\$ -	13,083,979	36,019,984	1,145,084	17,744,290	-	67,993,337
Depreciation for the year	-	2,218,989	6,852,364	242,630	3,448,286	-	12,762,269
(Reversal of) Impairment loss	-	141	56,564	(50)	3,313	-	59,968
Reclassifications	-	288,821	639	-	(193,829)	-	95,631
Disposals and obsolescence	-	(621,287)	(3,423,598)	(111,091)	(2,286,805)	-	(6,442,781)
Effect of movement in exchange rate	-	(938,862)	(2,260,504)	(87,297)	(1,088,449)	-	(4,375,112)
Loss of control of a subsidiary	-	(499,879)	(1,933,444)	-	(2,348,152)	-	(4,781,475)
Balance on December 31, 2016	<u>\$ -</u>	<u>13,531,902</u>	<u>35,312,005</u>	<u>1,189,276</u>	<u>15,278,654</u>	<u>-</u>	<u>65,311,837</u>
Balance on January 1, 2015	\$ 50,054	11,823,017	33,554,418	1,026,774	16,235,791	-	62,690,054
Depreciation for the year	-	2,556,168	6,614,194	292,840	3,996,928	-	13,460,130
(Reversal of) Impairment loss	(50,054)	(2)	(120,249)	(79)	482	-	(169,902)
Reclassifications	-	(4,220)	106,359	-	(146,758)	-	(44,619)
Disposals and obsolescence	-	(1,039,963)	(3,684,264)	(153,693)	(2,010,427)	-	(6,888,347)
Effect of movement in exchange rate	-	(251,021)	(450,474)	(20,758)	(331,726)	-	(1,053,979)
Balance on December 31, 2015	<u>\$ -</u>	<u>13,083,979</u>	<u>36,019,984</u>	<u>1,145,084</u>	<u>17,744,290</u>	<u>-</u>	<u>67,993,337</u>
Carrying amounts :							
Balance on December 31, 2016	<u>\$ 4,320,454</u>	<u>28,449,286</u>	<u>20,280,559</u>	<u>282,145</u>	<u>7,388,057</u>	<u>6,140,308</u>	<u>66,860,809</u>
Balance on December 31, 2015	<u>\$ 5,580,222</u>	<u>28,228,858</u>	<u>22,950,459</u>	<u>414,729</u>	<u>7,698,617</u>	<u>6,164,893</u>	<u>71,037,778</u>

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

	For the years ended December 31	
	2016	2015
Impairment loss (reversal gain)	<u>\$ 59,968</u>	<u>(169,902)</u>

- (ii) For the years ended December 31, 2016 and 2015, impairment losses on damaged equipment of \$16,571 and \$14,257, respectively, were recognized by CASETEK CAYMAN and its subsidiaries. CASETEK CAYMAN and its subsidiaries sold damaged equipment at selling price exceeding its carrying amount by \$2,959 which was recognized as a reversal gain for the year ended December 31, 2016. In 2015, CASETEK CAYMAN and its subsidiaries retested the impairment of the production line and the result thereof disclosed an excess of \$127,157 in the recoverable amount of the production line over its carrying value, which was recognized as reversal gain.
- (iii) KINSUS INTERCONNECT TECHNOLOGY CORP. completed a series of farm land purchases covering a total land area of 36,287.15 square meters in the name of KINSUS's chairman instead of KINSUS, due to the restriction imposed by the local government.
- (iv) In September 2015, a fire accident occurred at RI PEI COMPUTER ACCESSORY (SHANGHAI) CO., LTD.. The equipment loss and the related repair cost arising from this accident amounted to RMB 16,198 thousand (NTD 82,534), which was recognized in its books by RI PEI COMPUTER ACCESSORY (SHANGHAI) CO., LTD..

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Notes to Consolidated Financial Statements

- (v) Please refer to Note 6(z) for details of gain and loss on disposal of property, plant and equipment.
- (vi) Please refer to Note 8 for details of the property, plant and equipment pledged as collateral.
- (j) Investment property

	<u>Land</u>	<u>Buildings</u>	<u>Total</u>
Cost or deemed cost:			
Balance on January 1,2016	\$ 281,945	610,253	892,198
Effect of movement in exchange rate	-	(5,684)	(5,684)
Loss of control of a subsidiary	<u>(281,945)</u>	<u>(539,483)</u>	<u>(821,428)</u>
Balance on December 31, 2016	<u>\$ -</u>	<u>65,086</u>	<u>65,086</u>
Balance on January 1,2015	\$ 281,945	539,483	821,428
Reclassifications	-	72,341	72,341
Effect of movement in exchange rate	-	(1,571)	(1,571)
Balance on December 31, 2015	<u>\$ 281,945</u>	<u>610,253</u>	<u>892,198</u>
Depreciation and impairment loss :			
Balance on January 1,2016	\$ 9,617	178,450	188,067
Depreciation for the year	-	8,594	8,594
Effect of movement in exchange rate	-	(553)	(553)
Loss of control of a subsidiary	<u>(9,617)</u>	<u>(178,626)</u>	<u>(188,243)</u>
Balance on December 31, 2016	<u>\$ -</u>	<u>7,865</u>	<u>7,865</u>
Balance on January 1,2015	\$ 9,617	163,059	172,676
Depreciation for the year	-	11,270	11,270
Reclassifications	-	4,220	4,220
Effect of movements in exchange rate	-	(99)	(99)
Balance on December 31, 2015	<u>\$ 9,617</u>	<u>178,450</u>	<u>188,067</u>
Carrying amounts :			
Balance on December 31, 2016	<u>\$ -</u>	<u>57,221</u>	<u>57,221</u>
Balance on December 31, 2015	<u>\$ 272,328</u>	<u>431,803</u>	<u>704,131</u>

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

- (i) Rental income and direct operating expenses arising from investment property that generate rental income were as follows:

	For the years ended December 31	
	2016	2015
Rental income	\$ 18,047	31,685
Direct operating expenses arising from investment property that generate rental income	\$ 8,594	11,270

- (ii) As of December 31, 2016 and 2015 the fair value of investment property of the Group was \$87,564 and \$1,166,415, respectively. The fair value of investment property was evaluated based on the recent market transaction on arm's length terms.
- (iii) As of December 31, 2016 and 2015, the aforesaid investment properties were not pledged as collateral.

(k) Intangible assets

The movements in the costs of intangible assets, amortization, and impairment loss of the Group for the years ended December 31, 2016 and 2015 were as follows:

	Goodwill	Customer relationship	Technology	Others	Total
Costs:					
Balance on January 1, 2016	\$ 1,984,574	-	-	986,670	2,971,244
Additions	-	-	-	224,591	224,591
Disposals	-	-	-	(49,585)	(49,585)
Reclassifications	-	-	-	2,697	2,697
Effect of movement in exchange rate	(20,082)	-	-	(21,294)	(41,376)
Loss of control of a subsidiary	(164,859)	-	-	(53,025)	(217,884)
Balance on December 31, 2016	\$ 1,799,633	-	-	1,090,054	2,889,687
Balance on January 1, 2015	\$ 1,943,538	380,175	813,972	909,737	4,047,422
Additions	-	-	-	143,249	143,249
Disposals	-	(380,175)	(813,972)	(87,819)	(1,281,966)
Reclassifications	-	-	-	3,172	3,172
Effect of movement in exchange rate	41,036	-	-	18,331	59,367
Balance on December 31, 2015	\$ 1,984,574	-	-	986,670	2,971,244

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	<u>Goodwill</u>	<u>Customer relationship</u>	<u>Technology</u>	<u>Others</u>	<u>Total</u>
Amortization and Impairment Loss:					
Balance on January 1, 2016	\$ 671,792	-	-	744,365	1,416,157
Amortization for the year	-	-	-	141,548	141,548
Disposals	-	-	-	(49,585)	(49,585)
Reclassifications	-	-	-	1,185	1,185
Effect of movement in exchange rate	-	-	-	(15,224)	(15,224)
Loss of control of a subsidiary	-	-	-	(43,580)	(43,580)
Balance on December 31, 2016	<u>\$ 671,792</u>	<u>-</u>	<u>-</u>	<u>778,709</u>	<u>1,450,501</u>
Balance on January 1, 2015	\$ 671,792	380,175	813,972	580,224	2,446,163
Amortization for the year	-	-	-	223,479	223,479
Disposals	-	(380,175)	(813,972)	(87,819)	(1,281,966)
Reclassifications	-	-	-	10,656	10,656
Effect of movement in exchange rate	-	-	-	17,825	17,825
Balance on December 31, 2015	<u>\$ 671,792</u>	<u>-</u>	<u>-</u>	<u>744,365</u>	<u>1,416,157</u>
Carrying amounts:					
Balance on December 31, 2016	<u>\$ 1,127,841</u>	<u>-</u>	<u>-</u>	<u>311,345</u>	<u>1,439,186</u>
Balance on December 31, 2015	<u>\$ 1,312,782</u>	<u>-</u>	<u>-</u>	<u>242,305</u>	<u>1,555,087</u>

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

	<u>For the years ended December 31</u>	
	<u>2016</u>	<u>2015</u>
Operating costs	\$ 38,802	30,094
Operating expenses	102,746	193,385
	<u>\$ 141,548</u>	<u>223,479</u>

- (ii) Goodwill impairment

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

	<u>December 31, 2016</u>	<u>December 31, 2015</u>
Mechanics	\$ 1,081,452	1,100,733
Consumer electronic	44,867	210,527
Others	1,522	1,522
	<u>\$ 1,127,841</u>	<u>1,312,782</u>

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At the end of each reporting period, the Group assess whether there is any indication of impairment loss on goodwill. There were no impairment loss recognized on goodwill in 2016 and 2015. The key assumptions used in determining the value in use by each cash-generating unit were as follows:

- 1) The recoverable amount of the metal casing factory cash-generating unit was based on value in use. Key assumptions used in calculating the recoverable amount were as follows:
 - a) Management had projected cash flow based on a five-year financial budget which was extrapolated from historical operating results and future operating plan.
 - b) Pre-tax discount rate used in calculating the value in use was determined from weighted average cost of capital (WACC) of the Company.
 - 2) The recoverable amount of the digital camera cash-generating unit was based on value in use. Key assumptions used in calculating the recoverable amount were as follows:
 - a) Cash flow estimation was based on past experience, actual operating results and a five-year operating plan.
 - b) Projected revenue and gross profit ratio were extrapolated from management's forecast based on past operating results and future marketing development trends.
 - c) Pre-tax discount rate used in calculating the value in use was determined from weighted average cost of capital (WACC) of the Company.
 - (iii) For the years ended December 31, 2016 and 2015, the Group has not noted any indication of potential impairment loss based on the impairment testing performed.
- (I) Other financial assets and other assets

Other current and noncurrent assets were as follows:

	December 31, 2016	December 31, 2015
Other financial assets—current	\$ 479,510	785,779
Other financial assets—noncurrent	427,655	357,503
Other current assets	7,172,425	15,575,204
Other noncurrent assets	<u>46,143</u>	<u>58,896</u>
	<u>\$ 8,125,733</u>	<u>16,777,382</u>

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

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
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(m) Short-term loans

	December 31, 2016	December 31, 2015
Unsecured bank loans	<u>\$ 31,148,468</u>	<u>45,467,083</u>
Interest rate	<u>0.51%~6.85%</u>	<u>0.70%~2.03%</u>

Assets were not pledged as collateral for bank loans.

(n) Long-term loans

December 31, 2016		
	Currency	Amount
Secured bank loans	NTD	\$ 171,000
Unsecured bank loans	NTD	3,787,550
Unsecured bank loans	USD	<u>1,108,597</u>
		5,067,147
Less: Fees		(8,000)
Less: Current portion		<u>(536,257)</u>
Total		<u>\$ 4,522,890</u>
Interest rate		<u>1.02%~2.59%</u>
Expiration		<u>2017.01~2021.09</u>

December 31, 2015		
	Currency	Amount
Secured bank loans	NTD	\$ 305,034
Unsecured bank loans	NTD	12,553,330
Unsecured bank loans	USD	<u>2,065,325</u>
		14,923,689
Less: Fees		(12,800)
Less: Current portion		<u>(2,604,140)</u>
Total		<u>\$ 12,306,749</u>
Interest rate		<u>1.02%~2.19%</u>
Expiration		<u>2016.01~2020.12</u>

(i) Securities for bank loans

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

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
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(ii) Loan covenants

- 1) On October 25, 2010, the Company signed a syndicated loan agreement with a total credit line of USD 400,000 thousand. According to the Company's credit loan facility agreement with the banks, during the loan repayment periods, the Company must comply with certain financial covenants based on its audited annual and reviewed semi-annual consolidated financial statements (June 30 and December 31) as follows:
- a) Current ratio (current assets/current liabilities): should not be less than 100%.
 - b) Debt ratio ((total liabilities + contingent liabilities)/tangible net assets): should not be higher than 50%.
 - c) Interest coverage ratio (EBITDA/interest expenses): should not be less than 400%.
 - d) Tangible net assets (stockholders' equity (including minority shareholders) - intangible assets): should not be less than \$90,000,000.
 - e) Factoring line of accounts receivable factoring/ net book value of accounts receivable before derecognition: less than 50%.

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

This syndicated loan agreement was due in November, 2015.

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

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

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PEGATRON CORPORATION AND ITS SUBSIDIARIES

Notes to Consolidated Financial Statements

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

The Company was in compliance with the above financial covenants as of December 31, 2016 and 2015.

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

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

CASETEK CAYMAN was in compliance with the above financial covenants as of December 31, 2016 and 2015.

(o) Bonds payable

- (i) The Company's overseas unsecured convertible bonds were as follows:

	<u>December 31, 2016</u>	<u>December 31, 2015</u>
Convertible bonds issued	\$ -	8,874,000
Accumulated amount of converted bonds	-	(8,874,000)
Bonds payable, end of the year	<u>\$ -</u>	<u>-</u>
	<u>For the years ended December 31</u>	
	<u>2016</u>	<u>2015</u>
Embedded derivative—conversion options, accounted under other gains and losses	<u>\$ -</u>	<u>238,997</u>
Interest expense	<u>\$ -</u>	<u>(65,389)</u>

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
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The put option of the bonds payable is exercisable at three years after the first day of issue (February 6, 2015).

As of February 28, 2015, all of the convertible bonds issued in 2012 have been converted into shares. Please refer to Note 6(t) for the information on capital surplus – conversion of convertible bonds generated from the conversion.

(ii) The offering information on the unsecured convertible bonds were as follows:

<u>Item</u>	<u>1st overseas unsecured convertible bonds issued in 2012</u>
1.Offering amount	USD 300 million with each unit valued at USD 200 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.
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 USD 200,000 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= USD 1.00).</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>

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
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<u>Item</u>	<u>1st overseas unsecured convertible bonds issued in 2012</u>
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>
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 any time 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\$40.11 per share effective October 7, 2013. The conversion price has been adjusted to NT\$38.28 per share effective September 15, 2014 due to the distribution of cash dividends in 2014.</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 = USD 1.00) divided by the conversion price on the conversion date.</p>

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

(p) Provisions

	<u>Warranties</u>	<u>Allowance for sales returns and discounts</u>	<u>Total</u>
Balance on January 1, 2016	\$ 233,443	191,958	425,401
Provisions made during the year	-	10,380	10,380
Provisions used during the year	(3,409)	(21,007)	(24,416)
Provisions reversed during the year	-	(19,683)	(19,683)
Effect of movement in exchange rate	(680)	(1,667)	(2,347)
Loss of control of a subsidiary	<u>(229,271)</u>	<u>-</u>	<u>(229,271)</u>
Balance on December 31, 2016	<u>\$ 83</u>	<u>159,981</u>	<u>160,064</u>
Balance on January 1, 2015	\$ 235,959	285,495	521,454
Provisions made during the year	-	107,583	107,583
Provisions used during the year	(178)	(47,423)	(47,601)
Provisions reversed during the year	(3,790)	(150,618)	(154,408)
Effect of movement in exchange rate	<u>1,452</u>	<u>(3,079)</u>	<u>(1,627)</u>
Balance on December 31, 2015	<u>\$ 233,443</u>	<u>191,958</u>	<u>425,401</u>

(i) Warranties

Warranties of Ability (TW) are recognized when the expected benefits to be derived by Ability (TW) from a contract are lower than the unavoidable cost of meeting its obligations under the contract.

(ii) Allowance for sales return and discounts

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

(q) Operating leases

(i) Leasee

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

	<u>December 31, 2016</u>	<u>December 31, 2015</u>
Less than one year	\$ 1,603,335	1,736,565
Between one and five years	1,564,062	1,900,847
More than five years	<u>206,720</u>	<u>-</u>
	<u>\$ 3,374,117</u>	<u>3,637,412</u>

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

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

For the years ended December 31, 2016 and 2015, expenses recognized in profit or loss in respect of operating leases was as follows:

	For the years ended December 31	
	2016	2015
Cost of sales	\$ 1,588,808	1,394,758
Operating expenses	496,377	441,758
	\$ 2,085,185	1,836,516

(ii) Long-term prepaid rents

	December 31, 2016	December 31, 2015
Long-term prepaid rents	\$ 4,014,064	4,348,476

- 1) Long-term prepaid rents represent land use rights under operating lease arrangement is expensed equally over 38 to 67 years.
- 2) As of December 31, 2016 and 2015, the aforesaid land use rights were not pledged as collateral.

(r) Employee benefits

(i) Defined benefit plans

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

	December 31, 2016	December 31, 2015
Present value of defined benefit obligations	\$ 230,574	331,194
Fair value of plan assets	(143,849)	(195,829)
Net defined benefit liabilities	\$ 86,725	135,365

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

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
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1) Composition of plan assets

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

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

2) Movements in present value of the defined benefit obligations

The movements in the present value of the defined benefit obligations for the years ended December 31, 2016 and 2015 were as follows:

	For the years ended December 31	
	2016	2015
Defined benefit obligation, January 1	\$ 331,194	329,749
Current service costs and interest	38,041	13,102
Re-measurements of the net defined benefit liability		
— Actuarial gains (losses) arose from changes in demographic assumptions	(2,432)	2,218
— Actuarial gains arose from changes in financial assumption	9,163	20,143
— Experience adjustments	(11,405)	(22,784)
Benefits paid by the plan	-	(11,234)
Loss of control of a subsidiary	(133,987)	-
Defined benefit obligation, December 31	<u>\$ 230,574</u>	<u>331,194</u>

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
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3) Movements in the fair value of plan assets

The movements in the fair value of the defined benefit plan assets for the years ended December 31, 2016 and 2015 were as follows:

	<u>For the years ended December 31</u>	
	<u>2016</u>	<u>2015</u>
Fair value of plan assets, January 1	\$ 195,829	192,195
Interests revenue	10,799	4,300
Re-measurements of the net defined benefit liability		
-- Experience adjustments	(409)	854
Contributions made	6,286	9,714
Benefits paid by the plan	-	(11,234)
Expected return on plan assets	(914)	-
Loss of control of a subsidiary	(67,742)	-
Fair value of plan assets, December 31	<u>\$ 143,849</u>	<u>195,829</u>

4) Expenses recognized in profit or loss

The Group's pension expenses recognized in profit or loss for the years ended December 31, 2016 and 2015 were as follows:

	<u>For the years ended December 31</u>	
	<u>2016</u>	<u>2015</u>
Current service cost	\$ 33,651	5,699
Net interest on net defined benefit liability	(6,409)	3,103
	<u>\$ 27,242</u>	<u>8,802</u>
Operating costs	\$ 841	549
Operating expenses	26,401	8,253
	<u>\$ 27,242</u>	<u>8,802</u>

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
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- 5) Re-measurement of net defined benefit liability recognized in other comprehensive income

The Group's net defined benefit liability recognized in other comprehensive income for the years ended December 31, 2016 and 2015 were as follows:

	For the years ended December 31	
	2016	2015
Cumulative amount, January 1	\$ 83,545	84,822
Recognized during the year	(4,265)	(1,277)
Cumulative amount, December 31	<u>\$ 79,280</u>	<u>83,545</u>

- 6) Actuarial assumptions

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

	December 31, 2016	December 31, 2015
Discount rate	1.35%~1.80%	1.75%~2.00%
Future salary increase rate	2.00%~3.00%	1.75%~3.00%

Based on the actuarial report, the Group is expected to make a contribution payment of \$6,286 to the defined benefit plans for the one year period after the reporting date.

The weighted-average duration of the defined benefit plans is between 9 and 25 years.

- 7) Sensitivity Analysis

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

As of December 31, 2016 and 2015, the changes in the principal actuarial assumptions will impact the present value of defined benefit obligation as follows:

	Impact on the present value of defined benefit obligation	
	Increase by 0.50%	Decrease by 0.50%
December 31, 2016		
Discount	(21,587)	24,285
Future salary increase	20,536	(18,137)

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
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	Impact on the present value of defined benefit obligation	
	Increase by 0.50%	Decrease by 0.50%
December 31, 2015		
Discount	(29,547)	33,208
Future salary increase	32,665	(29,384)

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

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

(ii) **Defined contribution plans**

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

The cost of the pension contributions to the Labor Insurance Bureau for the years ended December 31, 2016 and 2015 amounted to \$5,785,909 and \$6,180,514, respectively.

(iii) As of December 31, 2016 and 2015, the Group's short-term employee benefits liabilities were \$333,344 and \$282,590, respectively.

(s) **Income Tax**

(i) The income tax expense for the years ended December 31, 2016 and 2015 was calculated as follows:

	For the years ended December 31	
	2016	2015
Current income tax expense		
Current period incurred	\$ 6,674,459	9,712,212
Prior years income tax adjustment	(380,860)	(435,378)
10% surtax on undistributed earnings	991,507	510,783
Deferred tax expense		
The origination and reversal of temporary differences	(342,828)	526,538
Income tax expense	\$ 6,942,278	10,314,155

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
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- (ii) Income tax on pre-tax financial income was reconciled with income tax expense for the years ended December 31, 2016 and 2015 as follows:

	<u>For the years ended December 31</u>	
	<u>2016</u>	<u>2015</u>
Profit before income tax	\$ 29,079,670	39,186,014
Income tax on pre-tax financial income calculated at the domestic rates applicable to profits in the country concerned	9,655,043	12,035,798
Permanent differences	(2,591,351)	(1,621,248)
Changes in unrecognized temporary differences	(1,224,929)	(1,067,663)
Oversea dividends received	407,749	909,540
Prior years income tax adjustment	(380,860)	(435,378)
10% surtax on undistributed earnings	991,507	510,783
Others	85,119	(17,677)
Income tax expense	<u>\$ 6,942,278</u>	<u>10,314,155</u>

- (iii) Deferred tax assets and liabilities

1) Unrecognized deferred tax liabilities

As of December 31, 2016 and 2015, the temporary differences associated with investments in subsidiaries were not recognized as deferred income tax liabilities as the Group has the ability to control the reversal of these temporary differences which are not expected to reverse in the foreseeable future. The related amounts were as follows:

	<u>December 31,</u> <u>2016</u>	<u>December 31,</u> <u>2015</u>
The aggregate temporary differences associated with investments in subsidiaries	\$ 34,747,332	28,593,218
Unrecognized deferred tax liabilities	<u>\$ 5,907,046</u>	<u>4,860,847</u>

2) Unrecognized deferred tax assets

	<u>December 31,</u> <u>2016</u>	<u>December 31,</u> <u>2015</u>
Deductible temporary differences	\$ 692,807	644,663
Tax losses	810,089	1,036,963
	<u>\$ 1,502,896</u>	<u>1,681,626</u>

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

As of December 31, 2016, the Group had not recognized the prior years' loss carry-forwards as deferred tax assets, and the expiry years thereof were as follows:

<u>Company Name</u>	<u>Year of occurrence</u>	<u>Unused balance</u>	<u>Expiry year</u>
KINSUS and its subsidiaries	2010~2015	\$ 3,108,899	2017~2022
ASROCK and its subsidiaries	2007~2016	302,077	2017~2026
CASETEK CAYMAN and its subsidiaries	2015~2016	834,181	2020~2021
AZUREWAVE and its subsidiaries	2012~2014	548,248	2022~2024
AMA PRECISION	2009~2014	<u>145,080</u>	2019~2024
		<u>\$ 4,938,485</u>	

3) Recognized deferred tax assets and liabilities

The movements in deferred tax assets and liabilities for the years ended December 31, 2016 and 2015 were as follows:

	<u>Gain on foreign investments</u>	<u>Others</u>	<u>Total</u>
Deferred tax liabilities:			
Balance, January 1, 2016	\$ 2,519,429	59,552	2,578,981
Recognized in loss (profit)	(603,270)	23,505	(579,765)
Recognized in other comprehensive income	(57,119)	(39,834)	(96,953)
Exchange differences on translation	(93,039)	(1,871)	(94,910)
Loss of control of a subsidiary	-	(4,109)	(4,109)
Balance, December 31, 2016	<u>\$ 1,766,001</u>	<u>37,243</u>	<u>1,803,244</u>
Balance, January 1, 2015	\$ 2,005,973	289,108	2,295,081
Recognized in loss (profit)	597,198	(217,083)	380,115
Recognized in other comprehensive income	11,786	(12,397)	(611)
Exchange differences on translation	<u>(95,528)</u>	<u>(76)</u>	<u>(95,604)</u>
Balance, December 31, 2015	<u>\$ 2,519,429</u>	<u>59,552</u>	<u>2,578,981</u>

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	<u>Provision for Contingent Service Cost</u>	<u>Gain on valuation of inventory</u>	<u>Unrealized expenses</u>	<u>Others</u>	<u>Total</u>
Deferred tax assets:					
Balance, January 1, 2016	\$ 151,534	1,033,690	1,525,983	141,299	2,852,506
Recognized in loss (profit)	(33,089)	(354,368)	43,219	107,301	(236,937)
Recognized in other comprehensive income	-	-	-	(1,286)	(1,286)
Exchange differences on translation	(1,267)	(58,466)	(92,294)	(24,597)	(176,624)
Loss of control of a subsidiary	(32,791)	-	(43,232)	(13,703)	(89,726)
Balance, December 31, 2016	<u>\$ 84,387</u>	<u>620,856</u>	<u>1,433,676</u>	<u>209,014</u>	<u>2,347,933</u>
Balance, January 1, 2015	\$ 484,922	907,826	1,551,733	112,039	3,056,520
Recognized in loss (profit)	(327,752)	144,383	7,666	29,280	(146,423)
Recognized in other comprehensive income	-	-	-	(1,085)	(1,085)
Exchange differences on translation	(5,636)	(18,519)	(33,416)	1,065	(56,506)
Balance, December 31, 2015	<u>\$ 151,534</u>	<u>1,033,690</u>	<u>1,525,983</u>	<u>141,299</u>	<u>2,852,506</u>

(iv) Status of approval of income tax

- 1) The Company's income tax returns through 2014 have been assessed and approved by the Tax Authority, except for the income tax return for 2012, which is still under review by the Tax Authority.
- 2) The Group have income tax returns approved by the Tax Authority were as follows:

<u>Years of Approval</u>	<u>Company Name</u>
2013	ASROCK INCORPORATION, KINSUS INTERCONNECT TECHNOLOGY CORP., and UNIHAN CORPORATION
2014	PEGAVISION CORPORATION, PEGA INTERNATIONAL LIMITED, AMA PRECISION, PEGAVISION INVESTMENT, ASUSTEK INVESTMENT, ASUSPOWER INVESTMENT, ASUS INVESTMENT CO., LTD., STARLINK, LUMENS OPTICS, ASFLY TRAVEL SERVICE LTD., HUA-YUAN INVESTMENT LTD., RIH KUAN METAL, AZURE WAVE, EZWAVE, AZURE LIGHTING TECHNOLOGIES, INC., and ASROCK RACK, INC.

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(v) Five year income tax exemption period

The investments of KINSUS INTERCONNECT TECHNOLOGY CORP. and PEGAVISION CORPORATION for their establishment and expansion conform to “the Regulations Regarding Awards for Newly Emerging and Strategic Industries under Manufacturing and Technical Service Industries.” As approved by the Tax Authority, the Group is eligible for five-year income tax exemption, the details of which were as follows:

<u>Approving Office</u>	<u>Approval document number</u>	<u>Tax exemption period</u>
Industrial Development Bureau	10005112010	01/01/2013~12/31/2017
Industrial Development Bureau	10005116950	01/01/2014~12/31/2018

(vi) Stockholders' imputation tax credit account and tax rate:

	<u>December 31, 2016</u>	<u>December 31, 2015</u>
Stockholders' imputation tax credit account	\$ <u>4,734,475</u>	<u>3,296,778</u>
	<u>2016 (Expect)</u>	<u>2015 (Actual)</u>
Tax deduction ratio for earnings distributable to R.O.C. residents	<u>14.92 %</u>	<u>13.61 %</u>

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

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

(t) Capital and reserves

As of December 31, 2016 and 2015, the authorized capital of the Company consisted of 3,000,000 thousand shares, with par value of \$10 per share. The outstanding shares consisted of 2,575,169 and 2,603,020 thousand common shares, respectively, and the capital that rose from the shares had all been retrieved.

(Continued)

PEGATRON CORPORATION AND ITS SUBSIDIARIES
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(i) Nominal ordinary shares

The movements in ordinary shares of stock outstanding for the years ended December 31, 2016 and 2015 were as follows:

Ordinary Shares (In thousands of shares)	For the years ended December 31	
	2016	2015
Beginning balance, January 1	2,603,020	2,367,911
(Expiration of) Restricted stock issued to employees	(1,441)	39,055
Exercise of employee stock options	-	1,380
Conversion of convertible bonds	-	194,674
Retirement of treasury stock	(26,410)	-
Ending balance, December 31	<u>2,575,169</u>	<u>2,603,020</u>

In 2015, the Company issued 39,678 thousand shares of employee restricted stock. New common shares of stock totaling 860 and 47,424 thousand shares, respectively, were issued from the exercise of employee stock options and conversion of convertible bonds. The Company retired treasury stock 26,410 thousand shares to maintain shareholders' equity in 2016. For the years ended December 31, 2016 and 2015, the Company had retired 1,441 and 623 thousand shares, respectively, of restricted stock to employees. Therefore, the authorized capital of the Company consisted of both 3,000,000 thousand shares, with par value of \$10 per share, and its outstanding capital consisted of 2,575,169 and 2,603,020 thousand common shares of stock, as of December 31, 2016 and 2015, respectively.

As of December 31, 2016 and 2015, the restricted Company shares of stock issued to employees have expired, of which 225 and 259 thousand shares, respectively, have not been retired.

(ii) Global depositary receipts

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

The Company may issue new GDRs with no more than 60,819,020 of the Company's common shares and deliver them to ASUSTeK GDR holders pursuant to the "Issuer of Overseas Securities Offering and Issued Guidelines." As of December 31, 2016 and 2015, the Company has listed, in total, 6,250 and 5,994 thousand units of GDR, respectively, on the Euro MTF market of the Luxembourg Stock Exchange. As each unit of these GDRs represents 5 common shares of the Company, the Company has listed Company shares totaling 31,251 and 29,969 thousand shares of stock, respectively. Major terms and conditions for GDRs were as follows:

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
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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 Depository 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.

(iii) Capital surplus

The components of the capital surplus were as follows:

	<u>December 31,</u> <u>2016</u>	<u>December 31,</u> <u>2015</u>
From issuance of share capital	\$ 62,238,593	62,284,056
From conversion of convertible bonds	11,073,663	11,187,179
From treasury stock transactions	23,614	108,582
Difference between consideration and carrying amount of subsidiaries acquired or disposed	2,383,056	2,383,056
Changes in ownership interest in subsidiaries	741,312	738,737
Employee share options	1,304	1,304
Restricted stock to employees	1,342,800	1,859,543
Other	<u>409,917</u>	<u>409,917</u>
	<u>\$ 78,214,259</u>	<u>78,972,374</u>

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

(iv) Retained earnings

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

(Continued)

PEGATRON CORPORATION AND ITS SUBSIDIARIES
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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.

1) Legal reserve

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

2) Special reserve

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

3) Earnings Distribution

On June 21, 2016 and June 15, 2015, the Company's shareholders' meeting resolved to appropriate the 2015 and 2014 earnings. These earnings were distributed as dividends and employee bonuses and remuneration to directors and supervisors as follows:

	For the years ended December 31	
	2015	2014
Common stock dividends per share (dollars)		
—Cash	\$ 5.00	4.10

(v) Treasury stock

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

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

(Continued)

PEGATRON CORPORATION AND ITS SUBSIDIARIES
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(vi) Other equity accounts (net of tax)

	Exchange differences on translation of foreign financial statements	Available -for-sale investments	Deferred compensation arising from issuance of restricted stock	Total
Balance, January 1, 2016	\$ 3,752,117	211,234	(1,238,377)	2,724,974
Exchange differences on foreign operation	(7,263,087)	-	-	(7,263,087)
Exchange differences on associates accounted for using equity method	(48,217)	-	-	(48,217)
Unrealized loss on available-for-sale financial assets of subsidiaries accounted for using equity method	-	(14,425)	-	(14,425)
Deferred compensation cost	-	-	808,495	808,495
Disposal of subsidiaries	6,248	(12,856)	-	(6,608)
Balance, December 31, 2016	<u>\$ (3,552,939)</u>	<u>183,953</u>	<u>(429,882)</u>	<u>(3,798,868)</u>
Balance, January 1, 2015	\$ 4,788,058	177,810	(64,523)	4,901,345
Exchange differences on foreign operation	(1,011,875)	-	-	(1,011,875)
Exchange differences on associates accounted for using equity method	(24,066)	-	-	(24,066)
Unrealized gains on available-for-sale financial assets of subsidiaries accounted for using equity method	-	33,424	-	33,424
Deferred compensation cost	-	-	(1,173,854)	(1,173,854)
Balance, December 31, 2015	<u>\$ 3,752,117</u>	<u>211,234</u>	<u>(1,238,377)</u>	<u>2,724,974</u>

(Continued)

PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

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

	For the years ended December 31	
	2016	2015
Balance, January 1	\$ 41,958,390	41,200,299
Profit attributable to non-controlling interests	2,797,577	5,060,234
Other comprehensive income attributable to non-controlling interests		
Foreign currency translation differences—foreign operations	(1,243,916)	(179,376)
Unrealized (loss) gain on available-for-sale financial assets	151,805	(157,917)
Actuarial gain (loss) on defined benefit plans	2,270	(242)
Disposal of subsidiaries	(7,454,156)	-
Changes in ownership interest in subsidiaries	(2,575)	(8,885)
Changes in non-controlling interests	<u>(2,456,784)</u>	<u>(3,955,723)</u>
Balance, December 31	<u>\$ 33,752,611</u>	<u>41,958,390</u>

(u) Share-based payment

Information on share-based payment transaction as of December 31, 2016 and 2015 were as follows:

	Equity-settled share-based payment			
	Restricted stock to employee			Employee stock option
	Issued in 2014	Issued in 2013	Issued in 2012	Issued in 2012
Thousand units granted	40,000	6,062	34,167	8,053
Contractual life	3 years	3 years	3 years	3 years
Vesting period	Note A	Note B	Note B	2 years
Actual turnover rate of employees	4.94%	5.80%	9.27%	-%
Estimated future turnover rate for each or the three years of employees	10.48% · 20.18% · 34.36%	10.94% · 25.07% · 33.76%	14.28% · 22.84% · 28.85%	19.01%

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

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

(Continued)

PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

On October 19, 2012, the Company obtained the approval from the Financial Supervisory Commission to issue restricted Company shares of stock to employees for up to a limited number of 40,000 thousand shares. On 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 newly issued 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 elapsed, the restricted shares of stock may not be sold, pledged, transferred, hypothecated or otherwise disposed. Holders of restricted shares of stock are entitled to rights as the Company's existing common shareholders except for the fact that restricted shares of stock are held by the trust and have vesting conditions. Also, the Company bears the right to buy back the restricted shares of stock at the issuance price and to cancel all restricted shares of stock issued to any employee who fails to comply with the vesting condition without returning the distributed dividend.

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

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

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

(Continued)

PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

(i) Determining the fair value of equity instruments granted

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

	Equity-settled share-based payment			
	Equity-settled share-based payment Restricted stock to employee			Employee stock option
	Issued in 2014	Issued in 2013	Issued in 2012	Issued in 2012
	05/07/2015	08/12/2013	11/09/2012	04/02/2012
Fair value at grant date				
Share price at grant date	\$ 91.90	45.20	39.45	44.85
Exercise price (Note A)	10.00	10.00	10.00	44.85
Expected life of the option	3 years	3 years	3 years	3 years
Current market price	91.90	45.20	39.45	44.85
Expected volatility	33.37%	32.68%	38.49%	44.41%
Expected dividend yield rate (Note A)	-%	-%	-%	-%
Risk-free interest rate	(Note B)	(Note C)	(Note D)	0.95%

Note A : After the issuance of the employee stock options, 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.

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

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

Note D : 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.

(ii) Restricted stock to employee

For the year ended December 31, 2015, the Company issued restricted shares of stock to employees of 39,678 thousand shares, which resulted in a capital surplus — restricted employee stock of \$1,894,333. Also, for the years ended December 31, 2016 and 2015, 1,407 and 675 thousand shares of the restricted shares of stock issued to employees have expired, which were charged to capital surplus of \$14,066 and \$6,748, respectively. As of December 31, 2016 and 2015, the Company has deferred compensation cost arising from issuance of restricted stock of \$429,882 and \$1,238,377, respectively.

For the years ended December 31, 2016 and 2015, the Company recognized salary cost of \$36,306 and \$27,490 from the distribution of cash dividends to estimated non-vesting restricted shares of stock distributed to employees from prior period earnings. Such salary cost was accounted under retained earnings as it remained to be unrealized.

(Continued)

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On June 21, 2016, pursuant to the resolution of its shareholders' meeting, the Company planned to issue 40,000 thousand shares of restricted share of stock to employees with par value of \$10 per share, which was declared to Securities and Futures Bureau of the Financial Supervisory Commission, R.O.C. Share of issuance and warrant list were not yet approved by Board of Directors. Vesting conditions are in accordance with the offering information.

(iii) Employee stock options

Information on aforesaid employee stock options was as follows:

For the year ended December 31, 2015

	Issued in 2012	
	Number of Exercisable Thousand Shares	Weighted- average Exercise Price
Balance, beginning of the year	872	\$ 40.80
Exercised	(860)	40.80
Expired	(12)	-
Balance, end of the year	<u>-</u>	-
Exercisable, end of the year	<u>-</u>	
Weighted-average fair value of options granted	<u>13.8</u>	
Exercise price of share option outstanding, end of the year	<u>-</u>	
Remaining contractual life	<u>-</u>	
Expenses incurred on share-based payment transactions	<u>-</u>	

(iv) Expenses resulted from share-based payments

The Group incurred expenses from share-based payments transactions for the years ended December 31, 2016 and 2015 as follows:

	For the years ended December 31	
	2016	2015
Expenses resulting from issuance of restricted stock to employees	<u>\$ 900,522</u>	<u>892,593</u>

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Notes to Consolidated Financial Statements

(v) Subsidiary's share-based payments

- (i) For the years ended December 31, 2015, Ability (TW) has share-based payment transactions as follows:

	Equity-settled	
	Restricted stock to employee	Employee stock options
	Issued in 2014	Issued in 2008
Thousand units granted	22,000	9,500
Contractual life	3 years	7 years
Vesting period	3 years	2 years

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

- (ii) The Black-Scholes Option Valuation Model was adopted to estimate the fair value of the first batch of Ability (TW) employee stock options. The Trinomial Tree Option Valuation Model was adopted to estimate the fair value of the second batch of Ability (TW) employee stock option on the day of granted and at the end of each period.

	Equity-settled	
	Restricted stock to employee	Employee stock option
	Granted in 2014	Granted in 2008
Grant date	May 21, 2014	October 13, 2008
Stock Price at granted date	\$ 20.90	22.20
Exercise price	10.00	22.20
Expected life of the options	3 years	7 years
Current market price	20.90	22.20
Volatility factors of the expected market price	Note A	43.11%
Dividend yields	Note B	-%
Risk-free interest rate	Note C	2.2101%

Note A :The volatility factors of the expected market price are 22.22% for the 1st year, 21.15% for the 2nd year, and 25.67% for the 3rd year.

Note B :The Dividend yields are 8.22% for the 1st year, - % for the 2nd year, and - % for the 3rd year.

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

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(iii) Information on share-based payment transactions were as follows:

1) For the year ended December 31, 2015

<u>The first batch of employee stock options</u>	<u>Issued in 2008</u>	
	<u>Quantity of stock option (thousand shares)</u>	<u>Weighted- average exercise price</u>
Outstanding at the beginning of the year	428	\$ 13.6
Granted	-	-
Exercised	(346)	13.6
Expired	(82)	-
Outstanding at the end of the year	-	-
Exercisable at the end of the year	-	-
Weighted-average fair value of options granted	<u>8.88</u>	
Exercise price of share option outstanding, end of the year	-	
Remaining contractual life	-	

(iv) For the year ended December 31, 2015, the weighted-average exercise price of stock option on the date of exercise amounted to \$16.87 per share.

(v) The expenses resulting from the share-based payment transactions were as follows:

	<u>For the years ended December 31</u>	
	<u>2016 (Note)</u>	<u>2015</u>
Equity-settled	<u>\$ 10,170</u>	<u>52,277</u>

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

(vi) For the year ended December 31, 2015, Ability (TW) repurchased 1,950 thousand shares of stock for \$19,506, at \$10 per share as certain employee resigned during the vesting period. As of December 31, 2015, 153 thousand shares with total amount of \$1,533 have been retired.

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(w) Earnings per share

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

	For the years ended December 31	
	2016	2015
Basic earnings per share		
Profit attributable to ordinary shareholders	<u>\$ 19,339,815</u>	<u>23,811,625</u>
Weighted-average number of ordinary shares	<u>2,579,930</u>	<u>2,581,005</u>
	<u>\$ 7.50</u>	<u>9.23</u>
Diluted earnings per share		
Profit attributable to ordinary shareholders (diluted)	<u>\$ 19,339,815</u>	<u>23,811,625</u>
Weighted-average number of ordinary shares	<u>2,579,930</u>	<u>2,581,005</u>
Effect of potentially dilutive ordinary shares		
Employee stock bonus	<u>27,941</u>	<u>36,082</u>
Weighted-average number of ordinary shares (diluted)	<u>2,607,871</u>	<u>2,617,087</u>
	<u>\$ 7.42</u>	<u>9.10</u>

For the years ended December 31, 2016 and 2015, convertible bonds of \$0 and \$230,562, respectively, were not included in the calculation of weighted-average number of shares, due to its anti-dilutive impact on earnings per share.

(x) Revenue

	For the years ended December 31	
	2016	2015
Sale of goods	<u>\$ 1,074,052,905</u>	<u>1,145,874,263</u>
Others	<u>83,657,208</u>	<u>67,838,713</u>
	<u>\$ 1,157,710,113</u>	<u>1,213,712,976</u>

(y) Remuneration of employees and directors

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

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For the years ended December 31, 2016 and 2015, remuneration of employees and directors of \$1,734,000, \$2,072,000, \$166,000 and \$203,000, respectively, were estimated on the basis of the Company's net profit before tax, excluding the remuneration of employees and directors of each period, multiplied by the percentage of remuneration of employees and directors as specified in the Company's Articles of Incorporation. Such amounts were recognized as operating cost or operating expense for the years ended December 31, 2016 and 2015. Management is expecting that the differences, if any, between the actual distributed amounts and estimated amounts will be treated as changes in accounting estimates and charged to profit or loss. The number of shares to be distributed were calculated based on the closing price of the Company's ordinary shares, one day prior to Board of Directors meeting.

In 2015, the Company accrued recognized remuneration of employees and directors of \$2,072,000 and \$203,000, respectively. There was no difference between the amounts approved in Board of Directors meeting on March 17, 2016. For further information, please refer to Market Observation Post System.

(z) Non-operating income and expenses

(i) Other income

	<u>For the years ended December 31</u>	
	<u>2016</u>	<u>2015</u>
Interest income	\$ 1,057,275	1,396,275
Subsidy income	845,078	763,276
Rental income	253,063	268,171
Technical service income	251,385	271,333
Other income	<u>765,332</u>	<u>906,124</u>
	<u>\$ 3,172,133</u>	<u>3,605,179</u>

(ii) Other gains and losses

	<u>For the years ended December 31</u>	
	<u>2016</u>	<u>2015</u>
Gain on reversal of uncollectable account	\$ 70,336	110,963
Loss on disposal of property, plant and equipment	(150,078)	(170,100)
Gain on disposal of non-current assets classified as held for sale	-	402,661
(Loss) gain from disposal of investments	(574,526)	397,657
Foreign exchange loss	(4,383,186)	(3,524,184)
(Reversal of) Impairment loss	(59,968)	134,852
Net losses on evaluation of financial assets (liabilities) measured at fair value through profit or loss	67,790	(200,625)
Other losses	<u>(217,855)</u>	<u>-</u>
	<u>\$ (5,247,487)</u>	<u>(2,848,776)</u>

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
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(iii) Finance costs

	For the years ended December 31	
	2016	2015
Interest expenses	\$ 912,165	672,266
Finance expense – bank fees	92,841	180,685
	\$ 1,005,006	852,951

(aa) Reclassification of other comprehensive income

	For the years ended December 31	
	2016	2015
Available-for-sale financial assets		
Net change in fair value	\$ (14,425)	33,424
Reclassification to profit or loss for losing control of subsidiaries	(12,856)	-
Net fair value change recognized in other comprehensive income	\$ (27,281)	33,424
Cumulative adjustment		
Losses from current period	\$ (7,263,087)	(1,011,875)
Share of other comprehensive income of associates accounted for using equity method	(48,217)	(24,066)
Reclassification to profit or loss for losing control of subsidiaries	6,248	-
Net fair value change recognized in other comprehensive income	\$ (7,305,056)	(1,035,941)

(ab) Financial instruments

(i) Credit risk

1) Exposure to credit risk

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

2) Credit risk concentrations

As of December 31, 2016 and 2015, the accounts receivable from the Group's top three customers amounted to \$44,383,971 and \$72,039,287, representing 47% and 59% of accounts receivable, respectively, which exposes the Group to credit risk.

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
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3) Impairment losses

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

	December 31, 2016	December 31, 2015
Not past due	\$ 133,275,190	143,150,534
Past due 0 - 30 days	2,478,288	3,233,260
Past due 31 - 120 days	286,556	1,466,766
Past due 121 - 365 days	86,671	62,580
Past due more than 1 year	<u>1,690,475</u>	<u>1,939,859</u>
	<u>\$ 137,817,180</u>	<u>149,852,999</u>

The movement in the allowance for impairment with respect to the receivables during the year was as follows:

	Individually assessed impairment	Collectively assessed impairment	Total
Balance on January 1, 2016	\$ 73,559	2,054,366	2,127,925
Recognition of loss from impairment	12	-	12
Reversal of impairment loss	-	(36,772)	(36,772)
Loss of control of a subsidiary	-	(176,022)	(176,022)
Foreign exchange gain	<u>(2,228)</u>	<u>(2,302)</u>	<u>(4,530)</u>
Balance on December 31, 2016	<u>\$ 71,343</u>	<u>1,839,270</u>	<u>1,910,613</u>
Balance on January 1, 2015	\$ 72,020	2,136,108	2,208,128
Reversal of impairment loss	(212)	(80,264)	(80,476)
Written off unrecoverable amount	-	(1,159)	(1,159)
Foreign exchange loss (gain)	<u>1,751</u>	<u>(319)</u>	<u>1,432</u>
Balance on December 31, 2015	<u>\$ 73,559</u>	<u>2,054,366</u>	<u>2,127,925</u>

Based on historical default rates, the Group believes that, apart from the above, no impairment allowance is necessary in respect of trade receivables not past due. Also, the payment term of the receivables from related parties depend on the Group's capital movement, and there's no penalty interest due for late payment. The Group's management believes that there's no significant change on the credit quality of the aforesaid receivables which are past due but not impaired, thus they assess the receivables can be recovered. In addition, the Group does not hold any collateral and of other credit enhancement to mitigate the credit risk of the foresaid receivables.

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
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Allowance for bad debts or accumulated impairment are the accounts used to record bad debt expense or impairment loss. If the Group believes the related receivables cannot be recovered, the carrying amount of the financial assets will be reduced through the allowance for bad debts accounts and accumulated impairment.

(ii) Liquidity risk

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

	Carrying amount	Contractual cash flows	Within 1 year	1-2 years	More than 2 years
December 31, 2016					
Non-derivative financial liabilities					
Secured bank loans	\$ 171,000	171,000	56,000	46,625	68,375
Unsecured bank loans	36,044,615	36,044,615	31,628,725	3,180,575	1,235,315
Non-interest bearing liabilities	<u>201,926,183</u>	<u>201,926,183</u>	<u>201,926,183</u>	<u>-</u>	<u>-</u>
	<u>\$ 238,141,798</u>	<u>238,141,798</u>	<u>233,610,908</u>	<u>3,227,200</u>	<u>1,303,690</u>
December 31, 2015					
Non-derivative financial liabilities					
Secured bank loans	\$ 305,034	305,034	134,034	56,000	115,000
Unsecured bank loans	60,085,738	60,085,738	47,937,189	3,200,170	8,948,379
Non-interest bearing liabilities	<u>195,546,280</u>	<u>195,546,280</u>	<u>195,546,280</u>	<u>-</u>	<u>-</u>
	<u>\$ 255,937,052</u>	<u>255,937,052</u>	<u>243,617,503</u>	<u>3,256,170</u>	<u>9,063,379</u>

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

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

(iii) Currency risk

1) Currency risk exposure

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

(Unit: Foreign currency / NTD in Thousands)

	December 31, 2016			December 31, 2015		
	Foreign Currency	Exchange Rate	NTD	Foreign Currency	Exchange Rate	NTD
<u>Financial assets</u>						
<u>Monetary items</u>						
USD:NTD	\$10,433,545	32.25	336,481,826	8,323,160	32.825	273,207,727
USD:CNY	8,227,417	6.937	265,335,128	6,318,520	6.4936	207,406,354
USD:CZK	39,837	25.6342	1,284,759	55,187	24.8213	1,811,578
CNY:NTD	1,175,798	4.649	5,466,285	399,849	5.0550	2,021,237

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

	December 31, 2016			December 31, 2015		
	Foreign Currency	Exchange Rate	NTD	Foreign Currency	Exchange Rate	NTD
<u>Financial liabilities</u>						
<u>Monetary items</u>						
USD:NTD	\$10,062,359	32.250	324,511,078	7,794,417	32.825	255,851,738
USD:CNY	9,582,667	6.937	309,042,094	8,500,368	6.4936	279,025,838
USD:CZK	21,448	25.6342	691,706	28,825	24.8213	946,214
CNY:NTD	729,450	4.649	3,391,213	139,291	5.0550	704,116

2) Sensitivity analysis

The Group's exposure to foreign currency risk arises from the translation of the foreign currency exchange gains and losses on cash and cash equivalents, accounts receivable, other receivables, loans, accounts payable, bonds payable and other payables that are denominated in foreign currency. A 1% of appreciation of each major foreign currency against the Group's functional currency as of December 31, 2016 and 2015 would have increased the before-tax net income by \$291,494 and decreased the before-tax net income by \$516,735, respectively. This analysis is based on foreign currency exchange rate variances that the Group considered to be reasonably possible at the reporting date. The analysis assumes that all other variables remain constant. The analysis is performed on the same basis for both periods.

3) Gains or losses on monetary item

As the Group deals in diverse foreign currencies, gains or losses on foreign exchange were summarized as a single amount. For the years ended December 31, 2016 and 2015, the foreign exchange losses, including both realized and unrealized, amounted to \$4,383,186 and \$3,524,184, respectively.

(iv) Interest rate analysis

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

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

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

If the interest rate increases / decreases by 1%, the Group's net income will decrease /increase by \$97,067 and \$59,200 for the years ended December 31, 2016 and 2015, respectively, assuming all other variable factors remain constant. This is mainly due to the Group's variable rate borrowing.

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(v) Fair value of financial instruments

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

1) Categories of financial instruments

Financial Assets:

	<u>December 31, 2016</u>	<u>December 31, 2015</u>
Financial assets at fair value through profit or loss		
Held-for-trading non-derivative financial assets	\$ 4,367,847	4,732,661
Available-for-sale financial assets	1,056,145	1,819,404
Financial assets carried at cost	371,082	468,750
Deposits and receivables		
Cash and cash equivalents	108,713,312	102,561,346
Notes, accounts and other receivables	135,906,567	147,725,074
Other financial assets	907,165	1,143,282
Sub-total	<u>245,527,044</u>	<u>251,429,702</u>
Total	<u>\$ 251,322,118</u>	<u>258,450,517</u>

Financial liabilities:

	<u>December 31, 2016</u>	<u>December 31, 2015</u>
Financial liabilities carried at amortized cost		
Short-term loans	\$ 31,148,468	45,467,083
Notes, accounts, other payables and accrued expenses	201,926,183	195,546,280
Long-term borrowings (including current portion)	5,059,147	14,910,889
Guarantee deposit (recognized in other noncurrent liabilities)	527,461	519,337
Total	<u>\$ 238,661,259</u>	<u>256,443,589</u>

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

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

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

a) Financial assets measured at amortized cost

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

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

a) Non-derivative financial instruments

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

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

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

b) Derivative financial instruments

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

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

(vi) Offsetting of financial assets and financial liabilities

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

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

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

December 31, 2016						
Financial liabilities subject to offsetting agreement or contract and have legally enforceable right to set off.						
	Gross Assets (a)	Gross liabilities Offset (b)	Net amounts presented (c)=(a)-(b)	Amounts not offset (d)		
				Financial Instruments	Cash collected as pledge	Net amounts (e)=(c)-(d)
Accounts Receivable and Payable	\$ 25,397,763	25,397,763	-	-	-	-

December 31, 2015						
Financial assets subject to offsetting agreement or contract and have legally enforceable right to set off.						
	Gross Assets (a)	Gross liabilities Offset (b)	Net amounts presented (c)=(a)-(b)	Amounts not offset (d)		
				Financial Instruments	Cash collected as pledge	Net amounts (e)=(c)-(d)
Accounts Receivable and Payable	\$ 39,902,301	33,703,531	6,198,770	-	-	6,198,770

December 31, 2015						
Financial liabilities subject to offsetting agreement or contract and have legally enforceable right to set off.						
	Gross Assets (a)	Gross liabilities Offset (b)	Net amounts presented (c)=(a)-(b)	Amounts not offset (d)		
				Financial Instruments	Cash collected as pledge	Net amounts (e)=(c)-(d)
Accounts Receivable and Payable	\$ 33,703,531	33,703,531	-	-	-	-

(ac) Financial risk management

(i) Overview

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

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

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
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(ii) Risk management framework

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

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

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

(iii) Credit risk

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

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

1) Accounts receivables and other receivables

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

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

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

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

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

2) Investment

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

3) Guarantee

The Group's policies were prepared in accordance with Guidelines for Lending of Capital, Endorsements and Guarantees by Public Companies.

(iv) Liquidity risk

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

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

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

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

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

(v) Market risk

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

1) Currency risk

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

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

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

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

2) Interest rate risk

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

3) Price floating risk on equity instruments

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

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

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

(ad) Capital management

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

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

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

	December 31, 2016	December 31, 2015
Total liabilities	\$ 261,923,032	283,748,138
Less: cash and cash equivalents	<u>108,713,312</u>	<u>102,561,346</u>
Net debt	<u>\$ 153,209,720</u>	<u>181,186,792</u>
Total capital (Note)	<u>\$ 335,231,921</u>	<u>373,525,317</u>
Debt to equity ratio	<u>45.70%</u>	<u>48.51%</u>

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

Management believes that there were no changes in the Group's approach to capital management for the year ended December 31, 2016.

(ae) Non-cash transactions of financing activity

Convertible bonds payable converted into ordinary shares. Please refer to Note 6(o) for details.

(7) Related-party transactions:

(a) The ultimate parent company

The Company is the ultimate parent company of the Group.

(b) Significant Transactions with related parties

(i) Sale of Goods to Related Parties

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

	Sales		Receivables from Related Parties	
	2016	2015	December 31, 2016	December 31, 2015
Others	\$ <u>662</u>	<u>-</u>	<u>-</u>	<u>-</u>

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
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Prices charged for sales transactions with associates were not significantly different from those of non-related parties. The average sales term for notes and accounts receivables pertaining to such sales transactions ranged from one to three months. Receivables from related parties were not secured with collaterals, and did not require provisions for bad debt expenses.

(ii) Purchase of Goods from Related Parties

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

	Purchases		Payables to Related Parties	
	2016	2015	December 31, 2016	December 31, 2015
Others	\$ 41,357	61,851	4,472	10,796

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

(iii) Warranty repair expense paid to Related Parties

	For the years ended December 31	
	2016	2015
Others	\$ -	533

(c) Key management personnel compensation:

	For the years ended December 31	
	2016	2015
Short-term employee benefits	\$ 443,410	602,068
Post-employment benefits	3,527	4,584
Share-based payments	158,955	169,745
	\$ 605,892	776,397

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

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
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(8) Pledged assets:

As of December 31, 2016 and 2015, pledged assets were as follows:

<u>Asset</u>	<u>Purpose of pledge</u>	<u>December 31, 2016</u>	<u>December 31, 2015</u>
Other financial asset-restricted deposit	Post-release duty deposits customs duty, rental deposits, travel agency guarantee, etc.	\$ 46,691	44,533
Property, plant and equipment	Bank loans	249,649	1,616,838
Other financial asset-refundable deposits	Customs duty guarantee, rental deposits, and deposits for performance guarantee	37,382	24,300
		<u>\$ 333,722</u>	<u>1,685,671</u>

(9) Major commitments and contingencies:

(a) Major commitments and contingencies were as follows:

(i) Unused standby letters of credit

	<u>December 31, 2016</u>	<u>December 31, 2015</u>
EUR	\$ 2,655	3,010
JPY	1,454,932	3,262,883
USD	8,469	7,211
CNY	955	-

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

	<u>December 31, 2016</u>	<u>December 31, 2015</u>
NTD	<u>\$ 87,869</u>	<u>6,689</u>

(iii) As of December 31, 2016 and 2015, the significant contracts for purchase of properties by the Group amounted to \$11,554,587 and \$13,223,710, of which \$2,830,075 and \$6,258,950, respectively, were unpaid.

(iv) As of December 31, 2016 and 2015, the Group provided endorsement guarantee for bank loans obtained by the related parties, including Group entities, amounting to \$12,237,198 and \$9,841,287, respectively.

(v) As of December 31, 2016 and 2015 the Group issued a tariff guarantee of \$662,165 and \$276,175, respectively, to the bank for the purpose of importing goods.

(b) Significant contingent liability: None.

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(10) Losses due to major disasters: None

(11) Subsequent events: None

(12) Other:

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

By item	For the years ended December 31					
	2016			2015		
	Operating Cost	Operating expense	Total	Operating Cost	Operating expense	Total
Employee benefit						
Salary	\$ 44,130,325	16,128,396	60,258,721	45,440,684	16,965,510	62,406,194
Health and labor insurance	4,824,910	933,909	5,758,819	4,951,812	1,049,772	6,001,584
Pension	4,920,426	892,725	5,813,151	5,268,762	920,554	6,189,316
Others	1,713,449	789,294	2,502,743	2,270,572	874,115	3,144,687
Depreciation	11,438,450	1,323,819	12,762,269	12,164,759	1,295,371	13,460,130
Amortization	38,802	102,746	141,548	30,094	193,385	223,479

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

	For the years ended December 31	
	2016	2015
Depreciation in investment property	<u>\$ 8,594</u>	<u>11,270</u>

(13) Segment information:

(a) General Information

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

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
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- (b) Reportable segment profit or loss, segment assets, segment liabilities, and their measurement and reconciliations

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

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

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

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

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PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

	For the year ended December 31			
	2015			
	DMS	Strategic Investment Group	Adjustment and eliminations	Total
Revenue :				
Revenue from external customers	\$ 1,114,266,543	99,446,433	-	1,213,712,976
Intersegment revenues	<u>2,580,781</u>	<u>7,243,274</u>	<u>(9,824,055)</u>	<u>-</u>
Total revenue	<u>\$ 1,116,847,324</u>	<u>106,689,707</u>	<u>(9,824,055)</u>	<u>1,213,712,976</u>
Share of profit of associates and joint ventures accounted for using equity method	<u>\$ 4,838,315</u>	<u>10,092,787</u>	<u>(14,943,956)</u>	<u>(12,854)</u>
Other significant non-monetary items:				
Goodwill	<u>\$ -</u>	<u>1,147,923</u>	<u>164,859</u>	<u>1,312,782</u>
Reportable segment profit or loss	<u>\$ 30,324,630</u>	<u>23,808,056</u>	<u>(14,946,672)</u>	<u>39,186,014</u>
Assets:				
Investments accounted for using equity method	<u>\$ 47,585,206</u>	<u>89,508,143</u>	<u>(136,669,158)</u>	<u>424,191</u>
Reportable segment assets	<u>\$ 392,071,442</u>	<u>220,643,421</u>	<u>(136,628,200)</u>	<u>476,086,663</u>
Reportable segment liabilities	<u>\$ 241,691,277</u>	<u>42,180,763</u>	<u>(123,902)</u>	<u>283,748,138</u>

(c) Geographic information

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

(i) External Sales

Region	For the years ended December 31	
	2016	2015
Europe	\$ 332,669,838	510,430,274
USA	396,964,194	273,135,851
Taiwan	170,921,579	185,605,468
China	103,033,702	100,602,388
Japan	87,650,950	81,751,727
Others	<u>66,469,850</u>	<u>62,187,268</u>
	<u>\$ 1,157,710,113</u>	<u>1,213,712,976</u>

(Continued)

PEGATRON CORPORATION AND ITS SUBSIDIARIES
Notes to Consolidated Financial Statements

(ii) Non-current assets

<u>Region</u>	<u>December 31,</u> <u>2016</u>	<u>December 31,</u> <u>2015</u>
Taiwan	\$ 20,868,460	21,546,353
China	52,969,239	57,097,050
Others	<u>882,559</u>	<u>1,018,603</u>
Total	<u>\$ 74,720,258</u>	<u>79,662,006</u>

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

(d) Major Customer

Major customers from DMS in 2016 and 2015 were as follows:

<u>Customer</u>	<u>2016</u>	<u>2015</u>
A	\$ 691,091,107	729,205,460
B	125,455,471	122,375,001
C	<u>77,163,832</u>	<u>61,848,011</u>
	<u>\$ 893,710,410</u>	<u>913,428,472</u>