

**POU CHEN CORPORATION AND  
SUBSIDIARIES**

**Consolidated Financial Statements for the  
Years Ended December 31, 2006 and 2005 and  
Independent Auditors' Report**

## INDEPENDENT AUDITORS' REPORT

The Board of Directors and Stockholders  
Pou Chen Corporation and subsidiaries

We have audited the accompanying consolidated balance sheets of Pou Chen Corporation and subsidiaries (collectively, the "Company") as of December 31, 2006 and 2005, and the related consolidated statements of income, changes in stockholders' equity, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company as of December 31, 2006 and 2005, and the consolidated results of their operations and their cash flows for the years then ended, in conformity with the Guidelines Governing the Preparation of Financial Reports by Securities Issuers, requirements of the Business Accounting Law and Guidelines Governing Business Accounting relevant to financial accounting standards, and accounting principles generally accepted in the Republic of China.

As described in Note 3 to the consolidated financial statements, effective January 1, 2006, the Company adopted Statement of Financial Accounting Standards No. 34, "Accounting for Financial Instruments," No. 36, "Disclosure and Presentation of Financial Instruments," and the related amendments to other Statement of Financial Accounting Standards.

February 15, 2007

### Notice to Readers

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

*For the convenience of readers, the independent auditors' report and the accompanying consolidated financial statements have been translated into English from the original Chinese version prepared and used in the Republic of China. If there is any conflict between the English version and the original Chinese version or any difference in the interpretation of the two versions, the Chinese-language independent auditors' report and consolidated financial statements shall prevail. Also, as stated in Note 2 to the consolidated financial statements, the additional footnote disclosures that are not required under generally accepted accounting principles were not translated into English.*

## POU CHEN CORPORATION AND SUBSIDIARIES

### CONSOLIDATED BALANCE SHEETS DECEMBER 31, 2006 AND 2005 (In Thousands of New Taiwan Dollars)

ASSETS	2006		2005		LIABILITIES AND STOCKHOLDERS' EQUITY	2006		2005	
	Amount	%	Amount	%		Amount	%	Amount	%
<b>CURRENT ASSETS</b>					<b>CURRENT LIABILITIES</b>				
Cash and cash equivalents (Notes 2 and 4)	\$ 14,594,226	9	\$ 18,100,617	12	Short-term borrowings (Note 15)	\$ 15,433,592	9	\$ 12,014,780	8
Financial assets measured at fair value through profit or loss, current (Notes 2, 3 and 5)	5,826,810	4	3,892,205	3	Short-term bills (Note 16)	1,554,160	1	1,195,342	1
Notes receivable (Notes 2 and 6)	83,133	-	38,878	-	Notes payable	124,682	-	72,030	-
Accounts receivable (Notes 2 and 7)	24,187,905	14	18,915,717	13	Notes payable to affiliates (Note 27)	95,656	-	102,687	-
Accounts receivable from affiliates (Notes 2, 7 and 27)	2,224,619	1	3,458,267	2	Accounts payable	15,164,734	9	11,729,354	8
Other financial assets, current	3,674,758	2	2,976,144	2	Accounts payable to affiliates (Note 27)	947,953	1	1,378,983	1
Inventories (Notes 2 and 8)	19,180,012	12	17,351,485	11	Income tax payable (Notes 2 and 24)	312,263	-	332,428	-
Other current assets	3,968,818	2	4,809,237	3	Derivative financial liabilities held for hedging, current (Notes 2, 3 and 26)	26,565	-	26,382	-
Total current assets	73,740,281	44	69,542,550	46	Other payables	9,084,593	5	7,773,637	5
<b>FUNDS AND LONG-TERM INVESTMENTS</b>					Current portion of long-term liabilities (Note 17)	2,463,335	2	16,015,247	10
Long-term investments at equity method (Notes 2 and 9)	23,864,121	14	16,874,443	11	Other current liabilities	1,711,949	1	1,198,587	1
Investments in real estate (Notes 2 and 10)	172,065	-	191,743	-	Total current liabilities	46,919,482	28	51,839,457	34
Available-for-sale financial assets, noncurrent (Notes 2 and 11)	1,502,932	1	1,688,086	1	<b>LONG-TERM LIABILITIES</b>				
Financial assets carried at cost, noncurrent (Notes 2 and 12)	683,463	1	1,160,002	1	Bonds payable (Notes 2 and 18)	12,863,751	8	5,150,453	3
Total funds and long-term investments	26,222,581	16	19,914,274	13	Long-term debt (Note 19)	30,815,681	18	25,621,481	17
<b>PROPERTY, PLANT AND EQUIPMENT (Notes 2 and 13)</b>					Derivative financial liabilities held for hedging, noncurrent (Notes 2 and 26)	167,839	-	-	-
Cost	84,116,388	50	72,501,024	48	Total long-term liabilities	43,847,271	26	30,771,934	20
Revaluation increment	293,323	-	293,323	-	<b>RESERVE FOR LAND VALUE INCREMENT TAX (Note 13)</b>	142,664	-	142,664	-
	84,409,711	50	72,794,347	48	<b>OTHER LIABILITIES</b>				
Less accumulated depreciation	(32,553,624)	(19)	(28,631,130)	(19)	Accrued pension cost (Notes 2 and 20)	562,657	-	523,646	1
Less accumulated impairment	(164,021)	-	(164,021)	-	Advance deposits from customers	5,927	-	4,910	-
Construction in progress and prepayments on purchase of equipment	3,842,377	2	5,809,585	4	Total other liabilities	568,584	-	528,556	1
Property, plant and equipment, net	55,534,443	33	49,808,781	33	Total liabilities	91,478,001	54	83,282,611	55
<b>INTANGIBLE ASSETS</b>					<b>STOCKHOLDERS' EQUITY</b>				
Goodwill (Note 2)	6,927,994	4	7,141,023	5	Capital stock (Note 21)	24,426,857	15	23,057,928	15
Deferred pension cost (Notes 2 and 20)	16,451	-	15,993	-	Capital surplus (Note 2)	2,527,272	1	2,511,981	2
Total intangible assets	6,944,445	4	7,157,016	5	Retained earnings (Note 21)	13,841,558	8	12,875,934	8
<b>OTHER ASSETS (Notes 2 and 14)</b>					Cumulative translation adjustments (Note 2)	(201,358)	-	35,494	-
	5,826,945	3	5,505,814	3	Unrealized losses on financial instruments (Notes 2, 3 and 11)	(1,221,891)	(1)	(1,470,331)	(1)
					Unrealized revaluation increment	134,641	-	134,641	-
					Treasury stock (Notes 2 and 22)	(2,451,485)	(1)	(3,459,328)	(2)
					Minority interest	39,735,100	24	34,959,505	23
					Total stockholders' equity	76,790,694	46	68,645,824	45
<b>TOTAL</b>	<b>\$ 168,268,695</b>	<b>100</b>	<b>\$ 151,928,435</b>	<b>100</b>	<b>TOTAL</b>	<b>\$ 168,268,695</b>	<b>100</b>	<b>\$ 151,928,435</b>	<b>100</b>

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

(With Deloitte & Touche audit report dated February 15, 2007)

# POU CHEN CORPORATION AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF INCOME YEARS ENDED DECEMBER 31, 2006 AND 2005

(In Thousands of New Taiwan Dollars, Except Earnings Per Share)

	2006		2005	
	Amount	%	Amount	%
GROSS SALES AND REVENUES EARNED	\$187,957,902	100	\$151,085,701	100
LESS SALES RETURNS AND ALLOWANCES	<u>(463,654)</u>	<u>-</u>	<u>(282,853)</u>	<u>-</u>
NET SALES AND REVENUES EARNED	187,494,248	100	150,802,848	100
COST OF GOODS SOLD	<u>151,746,219</u>	<u>81</u>	<u>119,793,763</u>	<u>79</u>
GROSS PROFIT	<u>35,748,029</u>	<u>19</u>	<u>31,009,085</u>	<u>21</u>
OPERATING EXPENSES				
Selling expenses	6,175,519	3	5,077,977	3
General and administrative expenses	12,904,541	7	11,903,348	8
Research and development expenses	<u>4,426,310</u>	<u>2</u>	<u>4,136,307</u>	<u>3</u>
Total operating expenses	<u>23,506,370</u>	<u>12</u>	<u>21,117,632</u>	<u>14</u>
INCOME FROM OPERATIONS	<u>12,241,659</u>	<u>7</u>	<u>9,891,453</u>	<u>7</u>
NON-OPERATING INCOME				
Interest income	493,622	-	375,513	-
Long-term equity investment income (Note 9)	1,695,225	1	1,145,030	1
Dividend income	375,399	-	338,580	-
Gain on disposal of property, plant and equipment	17,801	-	19,845	-
Gain on disposal of investments	-	-	237,997	-
Rental income	8,772	-	9,507	-
Reversal of provision for bad debts	203,264	-	-	-
Reversal of provision for inventory valuation	-	-	158,339	-
Revaluation gain on financial assets (Note 5)	534,446	-	7,479	-
Others	<u>748,549</u>	<u>1</u>	<u>552,407</u>	<u>1</u>
Total non-operating income	<u>4,077,078</u>	<u>2</u>	<u>2,844,697</u>	<u>2</u>
NON-OPERATING EXPENSES				
Interest expense	2,649,355	2	1,555,828	1
Other investment losses (Notes 11 and 12)	1,071,254	1	6,074	-
Loss on disposal of property, plant and equipment	274,697	-	170,011	-
Loss on disposal of investments	29,998	-	-	-
Foreign exchange loss, net	44,909	-	594,610	1
Loss on inventory devaluation and obsolescence	242,638	-	-	-
Loss on devaluation and depreciation of idle assets	18,831	-	815	-
Impairment loss on assets	-	-	20,668	-
Revaluation loss on financial liabilities (Note 26)	26,565	-	26,382	-
Others	<u>407,038</u>	<u>-</u>	<u>292,614</u>	<u>-</u>
Total non-operating expenses	<u>4,765,285</u>	<u>3</u>	<u>2,667,002</u>	<u>2</u>

(Continued)

# POU CHEN CORPORATION AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF INCOME YEARS ENDED DECEMBER 31, 2006 AND 2005

(In Thousands of New Taiwan Dollars, Except Earnings Per Share)

	2006		2005	
	Amount	%	Amount	%
INCOME FROM CONTINUING OPERATIONS BEFORE INCOME TAX	\$ 11,553,452	6	\$ 10,069,148	7
INCOME TAX EXPENSE (Notes 2 and 24)	<u>(711,928)</u>	<u>-</u>	<u>(150,462)</u>	<u>-</u>
INCOME BEFORE CUMULATIVE EFFECT OF CHANGES IN ACCOUNTING PRINCIPLES	10,841,524	6	9,918,686	7
CUMULATIVE EFFECT OF CHANGES IN ACCOUNTING PRINCIPLES (Note 3)	<u>1,625,271</u>	<u>1</u>	<u>-</u>	<u>-</u>
CONSOLIDATED NET INCOME	<u>\$ 12,466,795</u>	<u>7</u>	<u>\$ 9,918,686</u>	<u>7</u>
ATTRIBUTED TO				
Parent Company's stockholders	\$ 5,771,971	3	\$ 4,227,942	3
Minority interest	<u>6,694,824</u>	<u>4</u>	<u>5,690,744</u>	<u>4</u>
	<u>\$ 12,466,795</u>	<u>7</u>	<u>\$ 9,918,686</u>	<u>7</u>
	2006		2005	
	Before Income Tax	After Income Tax	Before Income Tax	After Income Tax
BASIC EARNINGS PER SHARE (Notes 2 and 25)				
Income from continuing operations	<u>\$ 5.11</u>	\$ 4.80	<u>\$ 4.46</u>	\$ 4.39
Cumulative effect of changes in accounting principles		<u>0.72</u>		<u>-</u>
Included income for minority interest		<u>\$ 5.52</u>		<u>\$ 4.39</u>
Attributed to stockholders of the Parent Company		<u>\$ 2.55</u>		<u>\$ 1.87</u>
DILUTED EARNINGS PER SHARE (Notes 2 and 25)				
Income from continuing operations	<u>\$ 5.02</u>	\$ 4.71	<u>\$ 4.38</u>	\$ 4.32
Cumulative effect of changes in accounting principles		<u>0.71</u>		<u>-</u>
Included income for minority interest		<u>\$ 5.42</u>		<u>\$ 4.32</u>
Attributed to stockholders of the Parent Company		<u>\$ 2.51</u>		<u>\$ 1.84</u>

(Continued)

# POU CHEN CORPORATION AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF INCOME YEARS ENDED DECEMBER 31, 2006 AND 2005

(In Thousands of New Taiwan Dollars, Except Earnings Per Share)

Pro-forma information, assuming common shares of the Parent Company held by its subsidiaries were not treated as treasury stock:

	<b>2006</b>		<b>2005</b>	
CONSOLIDATED NET INCOME ATTRIBUTED TO STOCKHOLDERS OF THE PARENT COMPANY	<u>\$ 5,955,304</u>		<u>\$ 4,338,885</u>	
	<b>2006</b>		<b>2005</b>	
	<b>Before Income Tax</b>	<b>After Income Tax</b>	<b>Before Income Tax</b>	<b>After Income Tax</b>
BASIC EARNINGS PER SHARE (Notes 2 and 25)				
Income from continuing operations	<u>\$ 4.91</u>	\$ 4.61	<u>\$ 4.27</u>	\$ 4.20
Cumulative effect of changes in accounting principles		<u>0.68</u>		<u>-</u>
Included income for minority interest		<u>\$ 5.29</u>		<u>\$ 4.20</u>
Attributed to stockholders of the Parent Company		<u>\$ 2.49</u>		<u>\$ 1.82</u>
DILUTED EARNINGS PER SHARE (Notes 2 and 25)				
Income from continuing operations	<u>\$ 4.83</u>	\$ 4.54	<u>\$ 4.20</u>	\$ 4.13
Cumulative effect of changes in accounting principles		<u>0.67</u>		<u>-</u>
Included income for minority interest		<u>\$ 5.21</u>		<u>\$ 4.13</u>
Attributed to stockholders of the Parent Company		<u>\$ 2.45</u>		<u>\$ 1.79</u>

(Concluded)

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

(With Deloitte & Touche audit report dated February 15, 2007)

**POU CHEN CORPORATION AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY  
YEARS ENDED DECEMBER 31, 2006 AND 2005  
(In Thousands of New Taiwan Dollars)**

	Capital Surplus				Retained Earnings			Other Adjustments of Stockholders' Equity					Total	
	Capital Stock	Additional Paid-in Capital of Common Stock	Additional Paid-in Capital of Bonds Conversion	Treasury Stock	Long-Term Equity Investments	Legal Reserve	Special Reserve	Unappropriated Earnings	Cumulative Translation Adjustments	Unrealized Losses on Financial Instruments	Unrealized Revaluation Increment	Treasury Stock		Minority Interest
BALANCE, JANUARY 1, 2005	\$ 20,936,734	\$ 792,119	\$ 1,439,788	\$ 144,154	\$ -	\$ 2,845,193	\$ 59,232	\$ 9,950,045	\$ (1,220,643)	\$ (1,203,354)	\$ 84,989	\$ (3,459,328)	\$ 30,290,009	\$ 60,658,938
Appropriation of earnings														
Legal reserve	-	-	-	-	-	424,633	-	(424,633)	-	-	-	-	-	-
Special reserve	-	-	-	-	-	-	2,364,765	(2,364,765)	-	-	-	-	-	-
Bonuses to directors and supervisors	-	-	-	-	-	-	-	(43,708)	-	-	-	-	-	(43,708)
Bonuses to employees (Note 21)	42,397	-	-	-	-	-	-	(42,397)	-	-	-	-	-	-
Stock dividends (Note 21)	2,049,657	-	-	-	-	-	-	(2,049,657)	-	-	-	-	-	-
Cash dividends	-	-	-	-	-	-	-	(2,049,658)	-	-	-	-	-	(2,049,658)
Effect of change of ownership interest in investees	-	-	-	-	14,192	-	-	(21,058)	-	-	-	-	-	(6,866)
Cash dividends received by subsidiaries	-	-	-	110,943	-	-	-	-	-	-	-	-	-	110,943
Provision for decline in market value of available-for-sale financial assets	-	-	-	-	-	-	-	-	-	(266,977)	-	-	-	(266,977)
Execution of employee stock warrants	29,140	10,785	-	-	-	-	-	-	-	-	-	-	-	39,925
Translation adjustments on foreign long-term equity investments	-	-	-	-	-	-	-	-	1,256,137	-	-	-	-	1,256,137
Adjustments for permanent reduction of land value increment tax (Note 13)	-	-	-	-	-	-	-	-	-	-	49,652	-	-	49,652
Change of minority interest	-	-	-	-	-	-	-	-	-	-	-	-	(1,021,248)	(1,021,248)
Consolidated net income for 2005	-	-	-	-	-	-	-	4,227,942	-	-	-	-	5,690,744	9,918,686
BALANCE, DECEMBER 31, 2005	23,057,928	802,904	1,439,788	255,097	14,192	3,269,826	2,423,997	7,182,111	35,494	(1,470,331)	134,641	(3,459,328)	34,959,505	68,645,824
Adjustments from first adoption of new and amended Financial Accounting Standards (Note 3)	-	-	-	-	-	-	-	-	-	(180,742)	-	-	-	(180,742)
Appropriation of earnings														
Legal reserve	-	-	-	-	-	422,795	-	(422,795)	-	-	-	-	-	-
Special reserve	-	-	-	-	-	-	(989,158)	989,158	-	-	-	-	-	-
Bonuses to directors and supervisors	-	-	-	-	-	-	-	(143,829)	-	-	-	-	-	(143,829)
Bonuses to employees (Note 21)	139,514	-	-	-	-	-	-	(139,514)	-	-	-	-	-	-
Stock dividends (Note 21)	1,130,751	-	-	-	-	-	-	(1,130,751)	-	-	-	-	-	-
Cash dividends	-	-	-	-	-	-	-	(3,392,253)	-	-	-	-	-	(3,392,253)
Convertible bonds transferred to common stock (Note 18)	21,884	-	38,723	-	-	-	-	-	-	-	-	-	-	60,607
Effect of changes of ownership interest in investees	-	-	-	-	17,248	-	-	-	-	-	-	-	-	17,248
Treasury stock transferred to employees (Note 22)	-	-	-	(229,163)	-	-	-	-	-	-	-	1,007,843	-	778,680
Cash dividends received by subsidiaries	-	-	-	183,333	-	-	-	-	-	-	-	-	-	183,333
Adjustments on changes of unrealized loss on cash flow hedge financial liability	-	-	-	-	-	-	-	-	-	63,511	-	-	-	63,511
Adjustments on changes of unrealized loss on available-for-sale financial assets	-	-	-	-	-	-	-	-	-	365,671	-	-	-	365,671
Execution of employee stock warrants	76,780	5,150	-	-	-	-	-	-	-	-	-	-	-	81,930
Translation adjustments on foreign long-term equity investments	-	-	-	-	-	-	-	-	(236,852)	-	-	-	-	(236,852)
Change of minority interest	-	-	-	-	-	-	-	-	-	-	-	-	(1,919,229)	(1,919,229)
Consolidated net income for 2006	-	-	-	-	-	-	-	5,771,971	-	-	-	-	6,694,824	12,466,795
BALANCE, DECEMBER 31, 2006	\$ 24,426,857	\$ 808,054	\$ 1,478,511	\$ 209,267	\$ 31,440	\$ 3,692,621	\$ 1,434,839	\$ 8,714,098	\$ (201,358)	\$ (1,221,891)	\$ 134,641	\$ (2,451,485)	\$ 39,735,100	\$ 76,790,694

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

(With Deloitte & Touche audit report dated February 15, 2007)

# POU CHEN CORPORATION AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF CASH FLOWS YEARS ENDED DECEMBER 31, 2006 AND 2005 (In Thousands of New Taiwan Dollars)

	2006	2005
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Consolidated net income	\$ 12,466,795	\$ 9,918,686
Adjustments to reconcile net income to net cash provided by operating activities		
Cumulative effect of changes in accounting principles	(1,625,271)	-
Depreciation and amortization	6,435,606	6,720,196
Gain on redeemed and repurchased Euro Convertible Bonds	(166,855)	(103,083)
Revaluation gain on financial assets	(534,446)	(7,479)
Revaluation loss on financial liabilities	26,565	26,382
(Recovery from) provision for doubtful accounts	(203,264)	256,594
Provision for (recovery from) inventory devaluation and obsolescence	242,638	(158,339)
Investment income recognized under equity method	(1,695,225)	(1,145,030)
Cash dividends received from investees under equity method	821,647	504,482
Net gain on disposal of long-term equity investments	(6,391)	(18,734)
Loss on asset impairment	-	20,668
Net loss on disposal of property, plant and equipment	256,896	150,166
Loss on devaluation and depreciation of idle assets	18,831	815
Other investment losses	1,071,254	6,074
Net changes in operating assets and liabilities		
Notes receivable	(44,255)	43,544
Accounts receivable	(4,940,170)	(4,130,482)
Accounts receivable from affiliates	1,133,256	(1,654,371)
Other financial assets, current	(726,975)	(763,506)
Inventories	(2,071,165)	(2,511,030)
Other current assets	840,419	(2,074,388)
Deferred pension cost	(458)	(15,652)
Deferred income tax asset, noncurrent	156,395	(90,671)
Long-term accounts receivable	(54,872)	(46,146)
Other assets	1,306	(2,317)
Notes payable	52,652	(29,481)
Notes payable to affiliates	(7,031)	3,779
Accounts payable	3,435,380	3,799,663
Accounts payable to affiliates	(431,030)	359,260
Income tax payable	(20,165)	229,935
Other payables	1,403,876	829,864
Other current liabilities	513,362	(1,290,384)
Foreign exchange adjustment on Euro Convertible Bonds	(11,586)	789,358
Interest compensation payable	108,261	246,579
Reserve for retirement plan	39,011	99,601
Minority interest	(1,919,229)	(1,021,248)
Net cash provided by operating activities	<u>14,565,762</u>	<u>8,943,305</u>

(Continued)

# POU CHEN CORPORATION AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF CASH FLOWS YEARS ENDED DECEMBER 31, 2006 AND 2005 (In Thousands of New Taiwan Dollars)

	2006	2005
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Decrease in financial assets measured at fair value through profit or loss, current	\$ 699,609	\$ 1,290,069
Increase in long-term equity investments	(5,880,683)	(2,249,633)
Increase in available-for-sale financial assets, noncurrent	(110,233)	-
Increase in financial assets carried at cost, noncurrent	(686,286)	-
Acquisition of property, plant and equipment	(12,934,521)	(11,259,298)
Proceeds from disposal of property, plant and equipment	564,090	334,565
Decrease in investment in real estate	10,163	66,071
Decrease (increase) in refundable deposits	209,386	(29,937)
Decrease (increase) in goodwill	17,961	(184,873)
Increase in deferred charges	<u>(296,865)</u>	<u>(150,385)</u>
Net cash used in investing activities	<u>(18,407,379)</u>	<u>(12,183,421)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Increase (decrease) in short-term borrowings	3,418,812	(129,541)
Increase in short-term bills	358,818	96,594
Redeemed and repurchased overseas convertible bonds	(5,902,478)	(10,396,507)
Remuneration to directors and supervisors	(143,829)	(43,708)
Payment of cash dividend	(3,204,970)	(1,936,123)
Increase in long-term borrowings	5,149,830	10,889,415
Increase (decrease) in advance deposits from customers	1,018	(311)
Execution of employee stock warrants	81,930	39,925
Transfer treasury stock to employees	<u>778,680</u>	<u>-</u>
Net cash provided by (used in) financing activities	<u>537,811</u>	<u>(1,480,256)</u>
EFFECT OF EXCHANGE RATE CHANGES ON CASH	<u>(202,585)</u>	<u>(395,477)</u>
NET DECREASE IN CASH AND CASH EQUIVALENTS	(3,506,391)	(5,115,849)
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	<u>18,100,617</u>	<u>23,216,466</u>
CASH AND CASH EQUIVALENTS, END OF YEAR	<u>\$ 14,594,226</u>	<u>\$ 18,100,617</u>
<b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION</b>		
Cash paid during the year		
Interest (excluding interest capitalized)	<u>\$ 2,546,043</u>	<u>\$ 1,275,532</u>
Income tax	<u>\$ 993,389</u>	<u>\$ 326,436</u>

(Continued)

# POU CHEN CORPORATION AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF CASH FLOWS YEARS ENDED DECEMBER 31, 2006 AND 2005 (In Thousands of New Taiwan Dollars)

	2006	2005
SUPPLEMENTAL DISCLOSURES OF NONCASH OPERATING, INVESTING AND FINANCING ACTIVITIES		
Adjustments of stockholders' equity from first adoption of new and amended Financial Accounting Standards	<u>\$ (180,742)</u>	<u>\$ -</u>
Recovery from unrealized loss on cash flow hedge financial liabilities	<u>\$ 63,511</u>	<u>\$ -</u>
Unrealized gain (loss) on available-for-sale financial assets	<u>\$ 365,671</u>	<u>\$ (266,977)</u>
Effect of changes in ownership interest in investees	<u>\$ 17,248</u>	<u>\$ (6,866)</u>
Cash dividends received by subsidiaries	<u>\$ 183,333</u>	<u>\$ 110,943</u>
Translation adjustments on foreign long-term equity investments	<u>\$ (236,852)</u>	<u>\$ 1,256,137</u>
Long-term liabilities, current portion	<u>\$ 2,463,335</u>	<u>\$ 16,015,247</u>
Convertible bonds transferred to common stock	<u>\$ 60,607</u>	<u>\$ -</u>
Treasury stock transferred to employees	<u>\$ (229,163)</u>	<u>\$ -</u>
Cash paid during the year for acquisition of property, plant and equipment		
Fair value of property, plant and equipment acquired	\$ 13,174,031	\$ 11,374,737
Add payables for acquisition of property, plant and equipment, beginning of year	185,957	70,518
Less payables for acquisition of property, plant and equipment, end of year	<u>(425,467)</u>	<u>(185,957)</u>
Cash paid during the year for acquisition of property, plant and equipment	<u>\$ 12,934,521</u>	<u>\$ 11,259,298</u>

(Concluded)

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

(With Deloitte & Touche audit report dated February 15, 2007)

# POU CHEN CORPORATION AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

YEARS ENDED DECEMBER 31, 2006 AND 2005

(In Thousands of New Taiwan Dollars, Unless Stated Otherwise)

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### 1. ORGANIZATION AND OPERATIONS

Pou Chen Corporation (“Pou Chen”) was incorporated in September 1969 in the Republic of China (the “ROC”). Pou Chen is located in Changhwa County and currently has three factories and nine trade departments. Pou Chen’s business activities include manufacturing and sales of various kinds of shoes and electronic peripheral components, and import and export of related products and materials. Pou Chen also invests significantly in shoes and electronic industries to diversify its business operation.

Pou Chen invested in Yue Yuen Industrial (Holdings) Limited and other footwear related companies through Wealthplus Holdings Limited.

Pou Chen has its stock traded on the Taiwan Stock Exchange Corporation since January 1990.

In addition to Pou Chen, the consolidated financial statements include the following subsidiaries:

Name	Location of Incorporation	Pou Chen and its Subsidiaries’ Ownership Percentage
Wealthplus Holdings Limited	British Virgin Islands	100.00
Win Fortune Investments Limited	British Virgin Islands	100.00
Ming Wang Investments Co., Ltd.	ROC	100.00
Windsor Entertainment Co., Ltd. (Original known as: Yue Yuen Entertainment Development Co., Ltd.)	ROC	100.00
Yun Yang Investments Co., Ltd.	ROC	100.00
Pou Shine Investments Co., Ltd.	ROC	100.00
Pan Asia Insurance Services Co., Ltd. (Original known as: Pan Asia Insurance Consulting Ltd.)	ROC	99.98
Barits Development Corporation	ROC	98.46
Pou Yuen Technology Co., Ltd.	ROC	99.10
Pro Arch Technology Inc.	ROC	99.93
Global Brands Manufacture Ltd.	ROC	51.77

Wealthplus Holdings Limited (“Wealthplus”), a British Virgin Islands registered corporation, is an investment holding company. Wealthplus commenced its operations in 1991 and invests in companies which are engaged in the design and sale of footwear and electronic peripheral products. As at December 31, 2006, Wealthplus has an outstanding common stock of US\$169,222 thousand.

The information of Wealthplus' subsidiaries is as follows:

<b>Name</b>	<b>Location of Incorporation</b>	<b>Ownership Percentage</b>	<b>Primary Operation Activities</b>
Yue Yuen Industrial (Holdings) Limited	Bermuda	48.17	Manufacturing and sale of athletic and casual footwear and sports apparel
GBM Manufacturing Co., Ltd.	British Virgin Islands	100.00	Property management in the People's Republic of China (PRC)
Upmost Smart Limited	British Virgin Islands	100.00	Manufacturing of electronic components
Gao Chen Technology Co., Ltd.	PRC	79.60	Manufacturing and sale of plastic products and electronic components
Mindtech Display Co., Ltd.	PRC	100.00	Assembly and sale of TFT-LCD module
Digital Decade Limited	British Virgin Islands	100.00	Assembly and sale of TFT-LCD module
Pou Qiao Electronic Limited	PRC	100.00	Assembly of backlight units
China Lion Associates Limited	British Virgin Islands	51.00	Sale of backlight units
Yuen Lim Metal Industrial Limited	PRC	68.75	Manufacturing of electronic components
Go-Cheery Industrial Limited	Hong Kong	100.00	Management and office administration service
Crown Master Investments Limited	British Virgin Islands	100.00	Investment holding
Exotic Developments Limited	British Virgin Islands	100.00	Investment holding
Tetor Ventures Ltd.	British Virgin Islands	100.00	Investment holding
Star Eagle Consultants Limited	British Virgin Islands	100.00	Insurance agent
Diverse Consultants Limited	British Virgin Islands	65.00	Construction and consulting service

Win Fortune Investments Limited ("Win Fortune"), a British Virgin Islands registered corporation, is an investment holding company. Win Fortune commenced its operations in 1994 and invests in Yue Yuen Industrial (Holdings) Limited (as at December 31, 2006, the ownership percentage is 0.93%). As at December 31, 2006, Win Fortune has an outstanding common stock of US\$100 thousand.

Ming Wang Investments Co., Ltd. ("Ming Wang"), a corporation incorporated in the ROC, is an investment holding company. Ming Wang commenced its operations in 1996. It is engaged in investing activities. As at December 31, 2006, Ming Wang has an outstanding common stock of \$427,291 thousand.

Windsor Entertainment Co., Ltd. ("Windsor Entertainment"), a corporation incorporated in the ROC, commenced its operations in 2003. It is engaged in hotel and resort operation. As at December 31, 2006, Windsor Entertainment has an outstanding common stock of \$210,000 thousand.

Yun Yang Investments Co., Ltd. ("Yun Yang") is a corporation incorporated in the ROC. Yun Yang commenced its operations in 1997. It is engaged in investment activities. As at December 31, 2006, Yun Yang has an outstanding common stock of \$75,000 thousand.

Pou Shine Investments Co., Ltd. ("Pou Shine") is a corporation incorporated in the ROC. Pou Shine commenced its operations in 1990. It is engaged in investing activities. As at December 31, 2006, Pou Shine has an outstanding common stock of \$573,632 thousand.

Pan Asia Insurance Services Co., Ltd. (“Pan Asia Insurance Services”) is a corporation incorporated in the ROC. Pan Asia Insurance Services commenced its operations in 1999. It is engaged in agency of property and casualty insurance. As at December 31, 2006, Pan Asia Insurance Services has an outstanding common stock of \$3,000 thousand.

Barits Development Corporation (“Barits Development”), a corporation incorporated in the ROC. It is engaged in leather manufacturing and investing activities. As at December 31, 2006, Barits Development has an outstanding common stock of \$913,000 thousand.

The information of Barits Development’s subsidiaries is as follows:

<b>Name</b>	<b>Location of Incorporation</b>	<b>Ownership Percentage</b>	<b>Primary Operation Activities</b>
Top Score Investments Ltd.	British Virgin Islands	100.00	Investment holding
Song Ming Investment Corporation	ROC	100.00	Investment holding
Ming Chi Investments Ltd.	ROC	99.99	Investment holding
Ming Shun Investments Ltd.	ROC	100.00	Investment holding
Wang Yi Construction Co., Ltd.	ROC	89.75	Construction
Pou Yii Development Co., Ltd.	ROC	75.00	Rental and sale of real estate

Top Score Investments Ltd. invests in Yue Yuen Industrial (Holdings) Limited. As at December 31, 2006, the ownership percentage is 0.44%.

Pou Yuen Technology Co., Ltd. (“Pou Yuen Technology”), a corporation incorporated in the ROC, is engaged in designing, manufacturing and trading mold, magnesium alloy casing and data processing and storage equipment. As at December 31, 2006, Pou Yuen Technology has an outstanding common stock of \$600,000 thousand.

The information of Pou Yuen Technology’s subsidiaries is as follows:

<b>Name</b>	<b>Location of Incorporation</b>	<b>Ownership Percentage</b>	<b>Primary Operation Activities</b>
Kleine Developments Ltd.	British Virgin Islands	100.00	Manufacturing and sale of electronic components
Dong Guan Pou Yuen Digital Technologic Ltd.	PRC	100.00	Manufacturing and sale of digital control and software
Kunshan Yuanying Electronics Technology Co., Ltd.	PRC	100.00	Manufacturing and sale of magnalium products

Pro Arch Technology Inc. (“Pro Arch Technology”), a corporation incorporated in the ROC, is engaged in manufacturing and sale of computer peripheral equipment and related spare parts. As at December 31, 2006, Pro Arch Technology has an outstanding common stock of \$301,000 thousand.

The information of Pro Arch Technology’s subsidiary is as follows:

<b>Name</b>	<b>Location of Incorporation</b>	<b>Ownership Percentage</b>	<b>Primary Operation Activities</b>
Pro Arch Technology BVI Inc.	British Virgin Islands	100.00	Investment holding

Global Brands Manufacture Ltd. (“Global Brands Manufacture”), a corporation incorporated in the ROC, is engaged in the manufacturing, assembly and sale of printed circuit boards. Its stock has been traded on the Over-the-Counter Exchange in Taiwan since February 1991. As at December 31, 2006, Global Brands Manufacture has an outstanding common stock of \$2,717,794 thousand.

The information of Global Brands Manufacture’s subsidiaries is as follows:

Name	Location of Incorporation	Ownership Percentage	Primary Operation Activities
Chuan Yi Computer (Shenzhen) Co., Ltd.	PRC	100.00	Manufacturing and sale of PCB
Yi Kuan Electronics (Shenzhen) Co., Ltd.	PRC	100.00	Manufacturing and sale of PCB
PC Asia Limited	British Virgin Islands	100.00	Sale of PCB
CMK Global Brands Manufacture Ltd.	British Virgin Islands	51.00	Manufacturing and sale of PCB
Atlantic Gateway Ltd.	British Virgin Islands	100.00	Rental of machinery
Dynamic Skyline Ltd.	British Virgin Islands	100.00	Assembly of PCB
Success Ocean Investments Ltd.	British Virgin Islands	100.00	Investing in business of electronic peripheral products
Cheng Cheng Enterprise Co., Ltd.	ROC	100.00	Rental and development of real estate
Solar Link Technologies, Inc.	USA	100.00	Assembly of TFT-LCD and Liquid Crystal on Silicon

As at December 31, 2006 and 2005, there were 305,059 and 289,250 employees in Pou Chen and subsidiaries referred above, respectively.

Pou Chen and its consolidated subsidiaries are hereafter collectively referred to as the “Company.”

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### Basis of Presentation

The accompanying consolidated financial statements have been prepared in conformity with the Guidelines Governing the Preparation of Financial Reports by Securities Issuers, requirements of the Business Accounting Law and Guidelines Governing Business Accounting relevant to financial accounting standards, and accounting principles generally accepted in the ROC. Under these guidelines, law and principles, the Company is required to make certain estimates and assumptions that could affect the amounts of allowance for doubtful accounts, loss on inventory devaluation, depreciation expenses and impairment, amortization expenses, and pension expenses, etc. Actual results could differ from these estimates.

For the convenience of readers, the accompanying consolidated financial statements have been translated into English from the original Chinese version prepared and used in the ROC. If there is any conflict between the English version and the original Chinese version or any difference in the interpretation of the two versions, the Chinese-language financial statements shall prevail. However, the accompanying consolidated financial statements do not include English translation of the additional footnote disclosures that are not required under generally accepted accounting principles but are required by the Securities and Futures Bureau for their oversight purposes.

The Company's significant accounting policies and basis of measurement are summarized as follows:

### **Principles of Consolidation**

The accompanying consolidated financial statements include the accounts of Pou Chen and its controlled subsidiaries. All significant intercompany balances and transactions have been eliminated upon consolidation. Minority interest presented in gross amount is included in "stockholders' equity."

Wealthplus, Win Fortune, Top Score Investments Ltd. and Kleine Developments Ltd. have their accounting year from October 1 of the preceding year to September 30 of the year.

### **Current/Noncurrent Assets and Liabilities**

Cash or cash equivalents, assets held for operating purposes and assets expected to be converted into cash, or consumed in 12 months after balance sheet date are recorded as current assets. Property, plant and equipment, intangible assets and other assets not being recorded as current assets are recorded as noncurrent assets. Liabilities incurred for operating purposes and expected to be liquidated in 12 months after balance sheet date are recorded as current liabilities. Liabilities not being recorded as current liabilities are recorded as noncurrent liabilities.

### **Cash and Cash Equivalents**

Cash includes unrestricted cash and bank deposits. Cash equivalents refer to short-term commercial papers whose carrying values approximate fair values.

### **Financial Instruments Measured at Fair Value through Profit or Loss**

Financial instruments measured at fair value through profit or loss include financial assets or financial liabilities classified as held for trading and designated by the Company as at fair value through profit or loss upon initial recognition. Those financial instruments are initially recorded at fair value at the transaction date and continuously recorded at fair value with unrealized gains or losses reported as part of net income. Related transaction costs are expensed currently. Cash dividends are recognized as income when received.

Derivative financial instruments which do not qualify for hedge accounting are classified as financial instruments measured at fair value through profit or loss and are recorded as financial assets if their fair value is positive; otherwise are recorded as financial liabilities.

The fair value of listed and over-the-counter stocks and open-end fund are determined at their closing prices, and net asset values, respectively.

### **Allowance for Doubtful Accounts**

The allowance for doubtful accounts is provided on the basis of management's evaluation of the collectibility and past loss experience of notes and accounts receivable and other pertinent factors.

### **Inventories**

Inventories are stated at the lower of cost or market, with cost determined using the weighted-average method. Market values of raw materials are determined by averaging the unit purchase prices during the last month, while those of merchandise, finished goods and work-in-process are determined at their net realizable values.

Revenues, costs and profits arising from real estate development projects and construction contracts that will take longer than one year to complete and can be reasonably estimated, are accounted for using the percentage-of-completion method. The percentage of completion is measured by comparing actual costs incurred in a period with the total estimated costs to be incurred on the project. All other real estate development projects and construction contracts are accounted for using the completed-contract method.

Construction in progress and advance construction receipts related to the same construction contract should be netted. If the netted amount is a debit balance, then it should be recorded as construction in progress, whereas a credit balance should be recorded as advance construction receipts.

### **Long-Term Investments at Equity Method**

Investments in companies where the Company's ownership interest is 20% or more or the Company can exercise significant influence over the investees are accounted for by the equity method.

When the equity method is first adopted or the investment is first acquired, the difference between the underlying equity in net assets of the investee and the cost of the investment is amortized on a straight line basis over 10 years. However, effective January 1, 2006, the cost of the investment in excess of the fair value of investee's identifiable net assets is considered as goodwill in accordance with the amended Statement of Financial Accounting Standards (SFAS). Goodwill is not amortized but impairment loss on goodwill should be evaluated periodically and not allowed to be reversed.

If an investee company issues new shares and the Company does not purchase new shares proportionately, then the ownership percentage and the equity in net assets of the investee will be changed. Such difference will be adjusted in the additional paid-in capital and the long-term equity investments accounts. If the adjustment stated above is to debit the additional paid-in capital account and the balance of additional paid-in capital from long-term equity investments is not enough to be offset, retained earnings will be debited for the remaining amount.

Investment is evaluated for impairment on the balance sheet date and loss is recognized if there is objective evidence showing that the investment is impaired. The impairment losses of those investments in which the Company exercises significant influence but without controlling power are evaluated based on their respective carrying amount.

Effective from January 1, 2002, common shares of Pou Chen held by its subsidiaries are treated as treasury stock.

### **Investments in Real Estate**

Depreciation of buildings under investments in real estate is provided over 55 years. Impairment loss is recognized immediately for any significant decline in the value of real estate investments. If the loss is reversed, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, such that the increased carrying amount should not exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset in prior years. A reversal of an impairment loss is immediately recognized as a gain.

### **Available-for-Sale Financial Assets**

Available-for-sale financial assets are initially recorded at fair value at the transaction date plus related transaction costs and continuously recorded at fair value with unrealized gains or losses recorded as a separate component of stockholders' equity until realized.

Cash dividends are recognized as income at the ex-dividend date but cash dividends resulting from net income before the investment date should be recorded as a decrease in the investment cost. Stock dividends received are not recognized as income; they are instead reflected as an increase in the number of shares held.

When a decline in the fair value of an available-for-sale financial asset has been recognized directly in equity and there is objective evidence showing that the asset is impaired, the cumulative loss that had been recognized directly in equity shall be removed from equity and recognized in profit or loss.

### **Financial Assets Carried at Cost, Noncurrent**

Equity investments without reliable fair value are carried at their original cost. Cash dividends are recognized as income at the ex-dividend date but cash dividends resulting from net income before the investment date should be recorded as a decrease in the investment cost. Stock dividends received are not recognized as income; they are instead reflected as an increase in the number of shares held. If there is objective evidence showing that the asset is impaired, the impairment loss shall be recognized and not allowed to be reversed.

### **Property, Plant, Equipment and Leased Asset**

Property, plant, equipment and leased assets are stated at cost with revalued appreciation less accumulated depreciation. Expenditures that would increase the value or extend the useful lives of property, plant and equipment are capitalized. Interest costs are capitalized starting with the first expenditure related to construction of asset, and capitalization continues until such asset is substantially completed and ready for its intended use.

Depreciation is provided on the straight-line basis over the following estimated useful lives of the related assets, with an additional year for salvage:

<b>Items</b>	<b>Estimated Useful Lives</b>
Buildings and improvements	15~55 years
Machinery and equipment	2~13 years
Transportation equipment	3~5 years
Furniture, fixtures and office equipment	3~8 years
Other equipment	2~11 years

An additional service life and a new residual value will be determined for any depreciable asset which is still in use after the end of its initially prescribed useful life. Depreciation is computed using the straight-line method.

When assets are retired or disposed of, their costs and related accumulated depreciation are removed from the accounts. Any resulting gain or loss is credited to non-operating income or charged to non-operating expense.

Impairment loss is recognized immediately for any significant decline in recoverable value below carrying amount of property, plant, equipment and leased asset. If the loss is reversed, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, such that the increased carrying amount should not exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset in prior years. A reversal of an impairment loss is immediately recognized as a gain.

## **Goodwill**

Goodwill on consolidated subsidiaries is amortized over five to ten years. Effective January 1, 2006, goodwill is not amortized (negative goodwill is still amortized over five to ten years) but evaluated periodically for impairment.

## **Deferred Charges**

Deferred charges are amortized on a straight-line basis over three to five years. However, the issue costs of convertible bonds issued before January 1, 2006 are amortized between the issue date and the expiration date of redemption option.

## **Euro-Dollar Convertible Bonds**

The convertible bonds, issued by the Company before January 1, 2006, contain put right. Each holder has the right, at the holder's option, to request the Company to repurchase all or any portion of such holder's bonds, in amounts of US\$1,000 (dollars) or any integral multiples. The interest compensation, which is the amount of agreed put price over face value of such bonds, will be recognized as a liability under the effective interest rate method from the issue date to the date the put right expires. As at the balance-sheet-date, the convertible bonds are classified as either current liabilities or long-term liabilities based on the repurchase date and the maturity date, whichever is earlier.

When the holder exercises the conversion right, the net written-off amount of the unamortized issuing costs, accrued interest, accrued interest compensation and face value of convertible bonds will be the cost basis of entitlement certificates. The difference of the net written-off carrying amount of the convertible bonds over the par value of the entitlement certificates should be recognized as capital surplus.

## **Retirement Plan**

The Labor Pension Act (the "Act"), which took effect on July 1, 2005, provides for a new defined contribution pension plan. Employees who were subject to the Labor Standards Law before the enforcement of this Act and still work for the Company after the enforcement of this Act may choose to remain to be subject to the pension mechanism under the Labor Standards Law. If they choose to be subject to the Act, their service years before the enforcement of this Act will be retained. Employees who start to work for the Company after July 1, 2005 are only subject to the Act.

Pou Chen, Barits Development, Pou Yuen Technology, Pro Arch Technology, and Global Brands Manufacture each has retirement plan covering all eligible employees. The benefits are primarily based upon an employee's years of service and average compensation for the last six months before retirement.

Pou Chen and its subsidiaries each has defined contribution pension plan under the Act. Pension costs are recorded based on actual contributions made to employees' individual pension accounts in amounts equal to 6% of monthly salaries and wages after July 1, 2005.

Pou Chen, Barits Development, Pou Yuen Technology, Pro Arch Technology, and Global Brands Manufacture, adopted the provisions of SFAS No. 18, "Accounting for Pensions," which require that pension expense shall be computed on actuarial basis.

## **Foreign Currency Transactions**

Foreign-currency transactions (except derivative transactions) are recorded in New Taiwan dollars at the exchange rates prevailing on the transaction date. Gains or losses resulting from the application of prevailing exchange rates when foreign-currency receivables and payables are settled are credited or charged to income. Assets and liabilities denominated in foreign currencies (except those on foreign long-term investments) are translated at the balance sheet date exchange rates, and resulting gains or losses are credited or charged to current income.

## **Cumulative Translation Adjustments**

Long-term equity investments accounted for under the cost method and denominated in foreign currencies are restated to New Taiwan dollars at the balance-sheet-date exchange rates. The related translation adjustments are reported as a separate component of stockholders' equity. For consolidated subsidiaries and equity method investees denominated in foreign currency, assets and liabilities denominated in foreign currencies are translated at the balance-sheet-date exchange rates. Stockholders' equity accounts should be translated at the historical rate except for the beginning balance of the retained earnings, which is carried by the translated amount of the preceding period. Dividends are translated at the spot rate of the declared date. Income statement accounts are translated at the current rate or weighted-average rate of the current period.

## **Treasury Stock**

Treasury stock is the Company's own stocks acquired according to the Stock Exchange Law. Treasury stock is recorded at purchasing cost, while fair value is adopted when stocks are received from donation. When the Company does not dispose or write off these stocks, their cost is listed as a deduction of stockholders' equity.

Effective from January 1, 2002, common shares of the Company held by its subsidiaries are treated in compliance with the provisions of SFAS No. 30, "Accounting for Treasury Stock."

When treasury stock is retired, the book value of the treasury stock and the proportionate part of capital surplus - stock issuance premium are written-off. If the book value of the treasury stock is more than the total of the par value and related stock issuance premium, the difference is charged to the capital surplus of the same class of stock. If the capital surplus is not sufficient, debit is made to retained earnings for the remaining amount. If the book value of the treasury stock is less than the total of the par value and related stock issuance premium, the difference is credited to the capital surplus of the same class of stock.

When treasury stock is disposed, if the disposal value is more than the book value of the treasury stock, the difference is credited to the capital surplus - treasury stock, while capital surplus - treasury stock is debited if the disposal value is less than the book value. If the capital surplus is not sufficient, debit is made to retained earnings for the remaining amount.

## **Revenue Recognition**

Sales are recognized when title to the products and the risks of ownership are transferred to customers, primarily upon shipment. Sales returns and allowances are subtracted from sales when they occur and the related inventory costs are subtracted from cost of goods sold.

Service revenue is recognized when service is rendered and the collection is reasonably assured.

## **Income Tax**

The Company adopted the provisions of SFAS No. 22, "Accounting for Income Tax," which requires an asset and liability approach to account for income tax. Deferred income tax assets and liabilities are computed for differences between the financial statement and tax bases of assets and liabilities that will result in taxable or deductible amounts in the future based on enacted tax laws and rates applicable to the periods in which the differences are expected to affect taxable income. Valuation allowances are provided for deferred tax assets with uncertain realizability. Income tax expense or benefit is the tax payable or refundable for the period plus or minus the change during the period in deferred tax assets and liabilities.

Under the Amended Income Tax Law of the ROC, undistributed earnings of the Company from 1998 onward are subject to 10% additional income tax which will be shown as income tax expense in the following year when the decision to retain the earnings is made by the shareholders in their meeting.

The ROC government enacted the Alternative Minimum Tax Act (the "AMT Act"), which became effective on January 1, 2006. The alternative minimum tax imposed under the AMT Act is a supplemental tax levied at a rate of 10% which is payable if the income tax payable determined pursuant to the Income Tax Law is below the minimum amount prescribed under the AMT Act. The taxable income for calculating the alternative minimum tax includes most of the income that is exempted from income tax under various laws and statutes. The Company has considered the impact of the AMT Act in the determination of its tax liabilities.

## **Earnings Per Share**

Basic earnings per common share are calculated by dividing net earnings applicable to common stock by the weighted average number of common stocks outstanding.

On a diluted basis, both net earnings and shares outstanding are adjusted to assume the conversion of convertible bonds from the date of issuance, and adopt the treasury stock method to calculate the stock warrants' dilutive potential common shares. However, if the convertible bonds contain an anti-dilutive effect, they will be excluded from the calculation.

## **Derivative Financial Instruments Held for Hedging**

Financial instruments held for hedging are evaluated at fair value and changes in fair value shall be recognized in profit or loss or recognized as adjustments to stockholders' equity.

## **Reclassifications**

Certain accounts in the consolidated financial statements for the year ended December 31, 2005 have been reclassified to be consistent with the presentation of the consolidated financial statements for the year ended December 31, 2006.

### **3. REASON AND EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE**

Effective January 1, 2006, the Company adopted SFAS No. 34, "Accounting for Financial Instruments," No. 36, "Disclosure and Presentation of Financial Instruments," and related amendments to other SFASs.

## Effect of Adoption of the New and Amended Financial Accounting Standards

The financial assets and liabilities (including derivative financial instruments) had been reclassified in accordance with the new and amended SFASs. The adjustments to the original carrying amount of financial instruments categorized as financial assets or financial liabilities at fair value through profit or loss are included in the cumulative effect of changes in accounting principle in the income statement; on the other hand, the adjustments to the original carrying amount of available-for-sale financial assets are recognized as adjustments to stockholders' equity.

The adjustment of the initial adoption of the newly released SFASs is summarized as follows:

	<b>Recognized As Cumulative Effect of Changes in Accounting Principles (After Tax)</b>	<b>Recognized As Adjustment of Parent Company's Stockholders' Equity</b>
Financial assets measured at fair value through profit or loss, current	\$ 1,625,271	\$ -
Available-for-sale financial assets, noncurrent	-	50,608
Derivative financial liabilities held for hedging, noncurrent	-	(231,350)
	<u>\$ 1,625,271</u>	<u>\$ (180,742)</u>

The change in accounting principle above increased the income from operation by \$507,881 thousand, the consolidated net income by \$2,133,152 thousand, basic earnings per share after tax by \$0.94 dollar and the adjustments of parent company stockholders' equity by \$94,924 thousand. The parent company stockholders' equity totally decreased by \$85,818 thousand as at December 31, 2006.

## Reclassifications Due to Adoption of the New and Amended Financial Accounting Standards

According to the accounting pronouncement declared in 2005, the 2005 accounts should be reclassified to be consistent with the presentation of 2006 financial statements without retroactive adjustments. The valuation methods in 2005 that were changed in 2006 due to the new SFASs are as follows:

### Short-Term Investments

Short-term investments are stated at the lower of aggregate cost or market. The cost of short-term investments sold is determined on the weighted-average method. Stock dividends received are not recognized as income, they are instead reflected as an increase in the number of shares held.

### Long-Term Equity Investments

Long-term equity investments in listed or over-the-counter companies, in which the Company's ownership is less than 20% and the Company can not exercise significant influence, are stated at the lower of cost or market value with the unrealized loss reflected as a separate component of stockholders' equity. Market values of marketable equity securities are determined by averaging the daily market closing prices during the last month of the fiscal year.

## Forward Exchange Contracts

Forward exchange contracts that are designated and effective as a hedge of net foreign assets or liabilities positions are recorded on the respective transaction date. The discounts or premiums (the differences between the contract rates and the spot rates on the date of purchase multiplied by principal amount of foreign currencies) involved in all forward contracts are separately accounted for and amortized to income over the duration of the contracts.

Losses, caused by forward exchange contracts which are effective as a hedge of recognizable foreign commitments, should be recognized in the current period. On the other hand, gain can be deferred to adjust strike price at the time the transactions are executed. If the principal amounts of forward exchange contracts are larger than recognizable foreign commitments, any excess is reflected directly to current income.

Receivables and payables from forward exchange contracts are shown on the accompanying balance sheets in net balance.

The following were the accounts in the consolidated financial statements for the year ended December 31, 2005 reclassified to be consistent with the new and amended SFASs effective January 1, 2006:

	<b>2005 (Before Reclassification)</b>	<b>2005 (After Reclassification)</b>
<u>Balance Sheets</u>		
Short-term investments	\$ 3,826,132	\$ -
Long-term equity investments at cost method	2,914,161	-
Financial assets measured at fair value through profit or loss, current	-	3,892,205
Available-for-sale financial assets, noncurrent	-	1,688,086
Financial assets carried at cost, noncurrent	-	1,160,002
Other payables	7,800,019	7,773,637
Derivative financial liabilities held for hedging, current	-	26,382
Provision for decline in market value of long-term equity investments	(1,470,331)	-
Unrealized losses on financial instruments	-	(1,470,331)
<u>Income Statements</u>		
Foreign exchange loss, net	\$ 620,992	\$ 594,610
Revaluation loss on financial liabilities	-	26,382

Effective January 1, 2006, the Company adopted amended SFAS No. 1, "Conceptual Framework for Financial Accounting and Preparation of Financial Statements," No. 5, "Long-term Investments under Equity Method," and No. 25, "Business Combinations." The major amendments in these SFASs include the requirement that goodwill should not be amortized thereafter and the difference between the underlying equity in net assets of the investee and the cost of the investment should be analyzed first and the portion attributed to goodwill is not amortized but evaluated periodically for impairment. As a result, the Company's income from operations for the year ended December 31, 2006 increased by \$1,013,339 thousand, basic earnings per share after tax by \$0.45 dollar and there was no cumulative effect of changes in accounting principle.

#### 4. CASH AND CASH EQUIVALENTS

Cash and cash equivalents as at December 31, 2006 and 2005 consist of the following:

	<b>2006</b>	<b>2005</b>
Cash on hand	\$ 72,099	\$ 47,821
Checking accounts	26,544	10,801
Savings accounts	1,703,727	1,053,797
Foreign-currency savings deposit	10,418,584	15,504,272
Time deposits	1,623,587	728,376
Commercial papers	<u>749,685</u>	<u>755,550</u>
	<u>\$ 14,594,226</u>	<u>\$ 18,100,617</u>

The time deposits of \$28,601 thousand and \$27,902 thousand, included in other assets - refundable deposits were pledged for employment of foreign labors and for tax appealing on additional tax assessment as at December 31, 2006 and 2005, respectively.

#### 5. FINANCIAL ASSETS MEASURED AT FAIR VALUE THROUGH PROFIT OR LOSS, CURRENT

Financial assets measured at fair value through profit or loss, current as at December 31, 2006 and 2005 were summarized as follows:

	<b>2006</b>	<b>2005</b>
Financial assets at fair value through profit or loss		
Marketable equity securities	\$5,431,735	\$2,773,810
Open-ended mutual funds	<u>395,075</u>	<u>1,118,395</u>
	<u>\$5,826,810</u>	<u>\$3,892,205</u>

The net gain from financial assets measured at fair value through profit or loss, current for the year ended December 31, 2006 amounted to \$534,446 thousand.

#### 6. NOTES RECEIVABLE

Notes receivable as at December 31, 2006 and 2005 consist of the following:

	<b>2006</b>	<b>2005</b>
Notes receivable	\$84,033	\$39,778
Less allowance for doubtful accounts	<u>(900)</u>	<u>(900)</u>
	<u>\$83,133</u>	<u>\$38,878</u>

## 7. ACCOUNTS RECEIVABLE

Accounts receivable as at December 31, 2006 and 2005 consist of the following:

	<b>2006</b>	<b>2005</b>
Accounts receivable	\$ 24,710,990	\$ 19,844,921
Less allowance for doubtful accounts	<u>(523,085)</u>	<u>(929,204)</u>
	<u>24,187,905</u>	<u>18,915,717</u>
Accounts receivable from affiliates (Note 27)	2,333,734	3,475,957
Less allowance for doubtful accounts	<u>(109,115)</u>	<u>(17,690)</u>
	<u>2,224,619</u>	<u>3,458,267</u>
	<u>\$ 26,412,524</u>	<u>\$ 22,373,984</u>

## 8. INVENTORIES

Inventories as at December 31, 2006 and 2005 consist of the following:

	<b>2006</b>	<b>2005</b>
Raw materials and supplies	\$ 8,885,082	\$ 8,361,301
Work-in-process	3,333,136	2,676,297
Finished goods	7,038,931	6,854,461
Merchandise	15,249	15,253
Goods in transit	462,310	96,825
Land for development	140,072	140,248
Land, buildings and improvements for sale	96,855	123,724
Construction in process	<u>53,035</u>	<u>52,469</u>
	20,024,670	18,320,578
Less valuation allowance	<u>(844,658)</u>	<u>(969,093)</u>
	<u>\$ 19,180,012</u>	<u>\$ 17,351,485</u>

Land for development and land, buildings and improvements for sale belong to Pou Yii Development Co., Ltd.

Construction in process belongs to Wang Yi Construction Co., Ltd.

## 9. LONG-TERM INVESTMENTS AT EQUITY METHOD

Long-term investments at equity method as at December 31, 2006 and 2005 are comprised of the following:

	2006			2005	
	Original Cost	Carrying Value	Ownership Percentage	Carrying Value	Ownership Percentage
<u>Shoes, shoe materials and athletic products companies</u>					
All Saints Enterprises Limited	\$ 79,597	\$ 134,833	37.00	\$ 120,038	37.00
Eagle Nice (Int'l) Holdings Ltd.	1,331,966	1,473,149	44.96	1,462,623	44.96
Nan Pao Resins (Holdings) Limited	71,920	294,462	35.00	287,975	35.00
Pine Wood Industrial Limited	92,863	81,454	37.00	93,588	37.00
Prosperous Industrial (Holdings) Ltd.	586,710	721,210	30.00	668,609	30.00
Rising Sun Associates Limited	36,180	86,027	37.00	84,118	37.00
Best Focus Holdings Ltd.	325,950	397,490	50.00	322,672	50.00
Blessland Enterprises Limited	26,330	85,267	50.00	90,797	50.00
Central Honour Limited	5,215	6,864	50.00	5,583	50.00
Great Skill Industrial Limited	34,323	80,381	50.00	71,720	50.00
Up Front Technology Ltd.	162,975	87,880	50.00	137,842	50.00
Willpower Industries Limited	104,304	106,699	40.00	97,840	40.00
Smart Shine Industries Limited	-	358,618	50.00	328,500	50.00
Din Tsun Holding Co., Ltd.	203,597	222,414	50.00	-	-
Profit Land Limited	68,450	67,886	35.00	-	-
Texas Clothing Holdings Corp.	1,955,700	1,852,420	49.40	-	-
China Ocean Resources Limited	586,710	544,585	50.00	-	-
I-Tech Enterprises Ltd.	10,186	9,761	50.00	-	-
Bigfoot Limited	179,426	163,821	48.76	205,204	48.76
Natural Options Limited	11,201	12,319	38.30	19,952	38.30
Original Designs Developments Limited	40,360	133,754	47.00	125,272	47.00
Cohen Enterprises Inc.	157,618	417,116	50.00	430,246	50.00
Ever Atlantic Investments Limited	214,755	125,618	50.00	146,067	50.00
Hua Jian Industrial Holding Co., Limited	775,125	1,428,449	50.00	1,174,203	50.00
Ka Yuen Rubber Factory Limited	78,976	518,545	50.00	416,258	50.00
Topmost Industries Limited	26,573	92,578	50.00	86,719	50.00
Twinways Investments Limited	88,681	224,450	50.00	214,105	50.00
Yuen Thai Industrial Company Limited	86,181	-	50.00	-	50.00
Oftenrich Holdings Limited	1,547,817	1,918,868	45.00	-	-
New Peak Services Limited	250,418	264,210	50.00	-	-
PT. GF Indonesia Ltd.	73,339	53,877	45.00	-	-
Just Lucky Investments Limited	44,459	48,566	38.30	47,677	38.30
High Style Investments Limited	26,076	40,642	50.00	41,189	50.00
Pou Thane Enterprise Co., Ltd.	5,627	8,498	50.00	8,793	50.00
Precise Zone Investments Limited	41,874	38,876	47.65	51,645	47.65
PYGF Co., Ltd.	32,595	42,559	50.00	40,965	50.00
Liberty Bell Investments Limited	102,753	88,272	49.00	-	-
Evermore Chemical Industry Co., Ltd.	240,202	240,202	20.31	-	-
San Fang Chemical Industrial Co., Ltd.	2,655,068	2,731,559	44.34	2,548,942	41.55
Envopro Technology Limited	-	-	-	16	50.00
<u>Electronic companies</u>					
Haicheng Information Technology Co., Ltd.	195,570	165,115	50.00	117,575	50.00
Silver Island Trading Ltd.	130,380	69,468	50.00	130,746	50.00
Venture Well Holdings Ltd.	334,331	305,442	43.08	315,797	43.08
Prime World International Ltd.	110,823	111,535	34.34	-	-
Digital Sun Investments Ltd.	318,108	199,905	25.93	-	-
Centralian Investments Limited	650,993	632,300	49.64	-	-
Elitegroup Computer Systems Co., Ltd.	6,033,250	4,707,190	17.98	4,928,354	30.21
Techview International Technology Inc.	665,348	752,064	48.84	430,815	49.48

	2006			2005	
	Original Cost	Carrying Value	Ownership Percentage	Carrying Value	Ownership Percentage
<u>Investment holding and other companies</u>					
Asia Air Tech Industrial (Pte) Ltd.	83,117	70,957	30.00	81,181	30.00
Enthroned Group Limited	159	159	48.76	160	48.76
Coprosects Holdings Ltd.	7,317	9,234	50.00	7,014	50.00
Eagle Great Investments Limited	78,840	73,102	40.00	73,375	40.00
Optiyield Industrial Limited	36	-	50.00	53	50.00
Well Success Investments Limited	257,675	984,423	40.00	1,256,184	40.00
Rising Developments Ltd.	5,053	68,494	50.00	111,988	50.00
Supplyline Ltd.	105,994	-	46.12	80,669	46.12
Talent Pool Management Ltd.	-	2,388	30.00	2,040	30.00
Partner Alliance Limited	3,887	5,931	50.00	6,659	41.25
Prolik Properties Management Co., Ltd.	2,329	2,751	30.00	2,675	30.00
Yusong Chateau Enterprise Co., Ltd.	1,500	896	50.00	-	-
Zhong Ao Multiplex Management Limited	526,095	498,588	47.50	-	-
	<u>\$ 21,872,905</u>	<u>\$ 23,864,121</u>		<u>\$ 16,874,443</u>	

The Company's long-term equity investment income (loss) under equity method for the years ended December 31, 2006 and 2005 are summarized as follows:

	2006	2005
<u>Shoes, shoe materials and athletic products companies</u>		
All Saints Enterprises Limited	\$ 11,559	\$ (6,846)
Eagle Nice (Int'l) Holdings Ltd.	111,466	148,696
Nan Pao Resins (Holdings) Limited	68,471	41,169
Pine Wood Industrial Limited	(11,442)	-
Prosperous Industrial (Holdings) Ltd.	56,876	61,273
Rising Sun Associates Limited	2,569	25,471
Best Focus Holdings Ltd.	78,675	60,908
Blessland Enterprises Limited	11,506	11,098
Central Honour Limited	1,329	1,164
Great Skill Industrial Limited	25,590	25,956
Up Front Technology Ltd.	(49,035)	-
Willpower Industries Limited	9,646	(6,975)
Smart Shine Industries Limited	421,471	-
Din Tsun Holding Co., Ltd.	18,873	-
Profit Land Limited	(565)	-
Texas Clothing Holdings Corp.	(102,160)	-
China Ocean Resources Limited	(40,001)	-
I-Tech Enterprise Ltd.	(426)	-
Bigfoot Limited	(7,978)	11,775
Natural Options Limited	(3,598)	4,028
Original Designs Developments Limited	37,138	33,766
Cohen Enterprises Inc.	35,948	16,528
Ever Atlantic Investments Limited	17,834	(38,031)
Hua Jian Industrial Holdings Co., Limited	325,630	187,071
Ka Yuen Rubber Factory Limited	165,340	127,308
Topmost Industries Limited	27,800	31,992
Twinways Investments Limited	61,077	68,691
Yuen Thai Industrial Company Limited	(65,380)	(4,637)
Oftenrich Holdings Limited	372,540	-
New Peak Services Limited	13,833	-
PT. GF Indonesia Ltd.	(16,247)	-

	2006	2005
Just Lucky Investments Limited	1,262	1,344
High Style Investments Limited	7,127	11,937
Pou Thane Enterprise Co., Ltd.	1,448	1,763
Precise Zone Investments Limited	6,288	(5,162)
PYGF Co., Ltd.	5,187	(339)
Liberty Bell Investments Limited	(14,523)	-
San Fang Chemical industrial Co., Ltd.	185,655	69,458
Envopro Technology Limited	-	(11,922)
<u>Electronic companies</u>		
Haicheng Information Technology Co., Ltd.	44,872	(8,746)
Silver Island Trading Ltd.	(60,439)	(638)
Venture Well Holdings Ltd.	(6,707)	(16,082)
Prime World International Ltd.	714	-
Digital Sun Investments Ltd.	(119,294)	-
Centralian Investments Limited	(14,908)	-
Elitegroup Computer Systems Co., Ltd.	(226,221)	6,758
Techview International Technology Inc.	82,281	73,289
<u>Investment holding and other companies</u>		
Asia Air Tech Industrial (Pte) Ltd.	(11,899)	(9,496)
Coprosects Holdings Ltd.	2,281	2,022
Eagle Great Investments Ltd.	(2,220)	(5,352)
Well Success Investments Limited	354,245	231,553
Rising Developments Limited	6,286	6,247
Supplyline Ltd.	(90,233)	-
Talent Pool Management Ltd.	365	569
Partner Alliance Limited	1,156	(243)
Prolik Properties Management Co., Ltd.	77	(968)
Zhong Ao Multiplex Management Limited	(35,310)	-
Yusong Chateau Enterprise Co., Ltd.	(604)	-
Global Biotech Inc.	-	(1,367)
	<u>\$ 1,695,225</u>	<u>\$ 1,145,030</u>

The names, main businesses, and place of incorporation of the equity-accounted investees are as follows:

Name	Core Operating Item	Place of Incorporation
Venture Well Holdings Ltd.	Sale of electronic parts	British Virgin Islands
All Saints Enterprises Limited	Manufacture and sale of paint	British Virgin Islands
Asia Air Tech Industrial (Pte) Ltd.	Manufacture and sale of air conditioner	Singapore
Eagle Nice (Int'l) Holdings Ltd.	Manufacture and sale of apparel	Cayman Islands
Enthroned Group Limited	Investment holding	British Virgin Islands
Nan Pao Resins (Holdings) Limited	Manufacture and sale of paint	British Virgin Islands
Pine Wood Industrial Limited	Manufacture and sale of paint	British Virgin Islands
Prosperous Industrial (Holdings) Ltd.	Manufacture and sale of	Cayman Islands

<b>Name</b>	<b>Core Operating Item</b>	<b>Place of Incorporation</b>
Rising Sun Associates Limited	sports bags Manufacture and sale of paint	British Virgin Islands
Best Focus Holdings Ltd.	Manufacture and sale of cartons	British Virgin Islands
Blessland Enterprises Limited	Manufacturing and sale of shoe pads	British Virgin Islands
Central Honour Limited	Shoe injection	British Virgin Islands
Coprosects Holdings Ltd.	Investment holding	British Virgin Islands
Great Skill Industrial Limited	Manufacture and sale of plastic shoe injection	British Virgin Islands
Optiyield Industrial Limited	Investment holding	British Virgin Islands
Up Front Technology Ltd.	Manufacture and sale of shoe injection	British Virgin Islands
Well Success Investments Limited	Investment holding	British Virgin Islands
Willpower Industries Limited	Manufacture and sale of cartons	British Virgin Islands
Smart Shine Industries Limited	Manufacture and sale of shoes and apparel	British Virgin Islands
Eagle Great Investments Limited	Investment holding	British Virgin Islands
Din Tsun Holding Co., Ltd.	Manufacture and sales of apparel	British Virgin Islands
Profit Land Limited	Manufacture and sale of shoe material	British Virgin Islands
Texas Clothing Holdings Corp.	Manufacture and sale of apparel	British Virgin Islands
China Ocean Resources Limited	Sales of sports goods	British Virgin Islands
Prime World International Ltd.	Sale of electronic parts	British Virgin Islands
I-Tech Enterprises Ltd.	Manufacture and sale of shoe material	British Virgin Islands
Bigfoot Limited	Cloth product trading / cloth dyeing & processing cloth shoe material binding	British Virgin Islands
Natural Options Limited	Manufacture of foamed cotton	British Virgin Islands
Original Designs Developments Limited	Manufacture of shoe lasts	British Virgin Islands
Cohen Enterprises Inc.	Manufacture and sales of leather products for shoes	British Virgin Islands
Ever Atlantic Investments Limited	Manufacture of apparel	British Virgin Islands
Hua Jian Industrial Holding Co., Limited	Manufacture and sale of ladies shoes	British Virgin Islands
Ka Yuen Rubber Factory Limited	Manufacture and sale of rubber soles	British Virgin Islands
Topmost Industries Limited	Manufacture of counters for shoes	British Virgin Islands
Twinways Investments Limited	Manufacture of injection moulds for shoe components	British Virgin Islands
Yuen Thai Industrial Company Limited	Manufacture and trading of sports and active wear	Hong Kong
Oftenrich Holdings Limited	Manufacture and sale of shoes	Bermuda
New Peak Services Limited	Manufacture and sale of	British Virgin Islands

<b>Name</b>	<b>Core Operating Item</b>	<b>Place of Incorporation</b>
PT. GF Indonesia Ltd.	shoes Manufacture and sale of shoes	Indonesia
Just Lucky Investments Limited	Manufacture and sale of shoes material	British Virgin Islands
High Style Investments Limited	Manufacture halftone, printing ink	British Virgin Islands
Pou Thane Enterprise Co., Ltd.	Sales of plastic grain	British Virgin Islands
Precise Zone Investments Limited	Manufacture and processing of ironware and plastic products	British Virgin Islands
PYGF Co., Ltd.	Processing rubber	British Virgin Islands
Liberty Bell Investments Limited	Manufacture of composed gum	British Virgin Islands
Envopro Technology Limited	Manufacture glues, plastics, and chemical products	British Virgin Islands
Haicheng Information Technology Co., Ltd.	Developing and manufacture of software and electronic parts	Shanghai City
Silver Island Trading Ltd.	Sale of electronic parts	British Virgin Islands
Digital Sun Investments Ltd.	Sale of printed circuit boards	British Virgin Islands
Centralian Investments Ltd.	Assembly of printed circuit boards	British Virgin Islands
Rising Developments Ltd.	Trading of diesel / petroleum	British Virgin Islands
Supplyline Ltd.	Provision of logistic service	Hong Kong
Talent Pool Management Ltd.	Provision of school service	British Virgin Islands
Partner Alliance Limited	Sale of tobacco and liquor	British Virgin Islands
Prolik Properties Management Co., Ltd.	Properties management	British Virgin Islands
Zhong Ao Multiplex Management Limited	Properties management	Beijing City

The fiscal year end of the above-listed companies is September 30. The Company accounted for the long-term investment income (loss) from these companies based on these companies' financial results for the years ended September 30, 2006 and 2005 as permitted under the accounting principles generally accepted in the ROC.

Techview International Technology Inc. ("Techview International") is engaged in development, sale and assembly of TFT-LCD display. It has an outstanding common stock of \$1,191,999 thousand as at December 31, 2006.

Elitegroup Computer Systems Co., Ltd. ("Elitegroup Computer") is engaged in designing, manufacturing and sale of computer peripheral equipment. The shares of Elitegroup Computer are listed on the Taiwan Stock Exchange Corporation. It has an outstanding common stock of \$12,551,891 thousand as at December 31, 2006. In January 2006, Elitegroup Computer issued additional 314,001 thousand common stocks, to exchange the desktop department of Tatung Co. In addition, Elitegroup Computer merged with Uniwill Computer Corp. by issuing additional 184,931 thousand common stock in December 2006. As at December 31, 2006, the Company's ownership was decreased to 17.98%.

San Fang Chemical Industrial Co., Ltd. (“San Fang”) is engaged in manufacturing and marketing leather. The shares of San Fang are listed on the Taiwan Stock Exchange Corporation. It has an outstanding capital of \$2,504,083 thousand as at December 31, 2006.

## 10. INVESTMENTS IN REAL ESTATE

Investments in real estate as at December 31, 2006 and 2005 are comprised of the following:

	2006			2005
	Cost	Accumulated Depreciation	Carrying Value	Carrying Value
Land	\$ 109,712	\$ -	\$ 109,712	\$ 175,136
Building (construction in progress)	<u>62,353</u>	<u>-</u>	<u>62,353</u>	<u>16,607</u>
	<u>\$ 172,065</u>	<u>\$ -</u>	<u>\$ 172,065</u>	<u>\$ 191,743</u>

## 11. AVAILABLE-FOR-SALE FINANCIAL ASSETS, NONCURRENT

Available-for-sale financial assets, noncurrent as at December 31, 2006 and 2005 are as follows:

	2006			2005	
	Original Investment Cost	Carrying Value	Ownership Percentage	Carrying Value	Ownership Percentage
Taiwan marketable equity securities					
Asia Vital Components Co., Ltd.	\$ 388,553	\$ 487,555	9.78	\$ -	-
Taiwan Paiho Limited	137,038	130,787	3.61	138,110	3.61
Quanta Display Inc.	-	-	-	427,264	0.88
Foreign marketable equity securities					
Luen Thai Holdings Ltd.	1,113,997	525,663	8.98	1,122,712	9.90
Symphony Holdings Ltd.	296,636	355,009	5.05	-	-
Foreign mutual funds					
Investar Excelsus Venture Capital	<u>3,918</u>	<u>3,918</u>		<u>-</u>	<u>-</u>
	<u>\$ 1,940,142</u>	<u>\$ 1,502,932</u>		<u>\$ 1,688,086</u>	

Asia Vital Components Co., Ltd. is engaged in manufacturing and selling of semiconductors electronic connectors, computer connectors and communication products. The shares of Asia Vital Components are listed on the Taiwan Stock Exchange Corporation. It has an outstanding common stock of \$2,512,121 thousand as at December 31, 2006.

Quanta Display Inc. is engaged in manufacturing and sale of TFT-LCD products. The shares of Quanta Display are listed on the Taiwan Stock Exchange Corporation. Quanta Display merged with AU Optronics Corporation (“AUO”), the survivor entity. The merger took effect on October 1, 2006. The Company acquired on October 1, 2006 the AUO shares at share swap ratio of 3.5 Quanta Display shares for 1 AUO share, and the AUO shares were reclassified to “financial assets measured at fair value through profit or loss, current” in accordance with the market closing price on October 1, 2006. Therefore, the Company recognized loss of \$378,972 thousand for the year ended December 31, 2006, which was recorded as other investment losses.

Luen Thai Holdings Ltd. is engaged in manufacturing ready-made garments. The shares of Luen Thai Holdings Ltd. are listed on the Hong Kong Exchange and Clearing Limited. It has an outstanding common stock of US\$9,023 thousand as at December 31, 2006.

Symphony Holdings Ltd. is engaged in manufacturing and sales of footwear. The shares of Symphony Holdings Ltd. are listed on the Hong Kong Exchange and Clearing Limited. It has an outstanding common stock of US\$35,683 thousand as at December 31, 2006.

## 12. FINANCIAL ASSETS CARRIED AT COST, NONCURRENT

Financial assets carried at cost, noncurrent as at December 31, 2006 and 2005 were as follows:

	2006			2005	
	Original Investment Cost	Carrying Value	Ownership Percentage	Carrying Value	Ownership Percentage
Chiang Yei Precision Industrial Co., Ltd.	\$ 8,153	\$ 8,153	15.27	\$ 8,153	15.27
Golden Brands Developments Ltd.	728,107	272,516	5.88	733,803	6.35
L&C Aluminium Corp.	1,200	831	3.33	831	3.33
Media Reality Technologies, Inc.	88	88	0.41	88	0.41
Shey Yu Co., Ltd.	320	320	1.07	320	1.07
Hwiang Shei Co., Ltd.	200	-	1.00	-	1.00
View Sonic Corporation	96,231	96,231	0.42	96,231	0.42
Taichung International Country Club	1,905	1,905	0.09	1,905	0.09
Redsun Electronic Co., Ltd.	14,000	-	5.40	-	-
Bizlink Holding Inc.	108,904	108,904	3.06	109,756	3.06
Great Team Backend Foundry Inc.	79,021	79,021	15.52	79,639	19.86
Eic Enterprise Ltd. - preferred stock	63,082	1,412	1.78	63,576	1.78
Asia Pacific Genesis Venture Capital Fund	114,082	114,082	-	65,700	-
	<u>\$ 1,215,293</u>	<u>\$ 683,463</u>		<u>\$ 1,160,002</u>	

The stocks and foreign mutual funds mentioned above do not have open pricing and reliable fair values, thus they are carried at cost. Due to the continuing operation losses of Golden Brands Developments Ltd. and Eic Enterprise Ltd., the Company recognized a loss of \$518,769 thousand for the year ended December 31, 2006, which was recorded as other investment losses.

## 13. PROPERTY, PLANT AND EQUIPMENT

A summary of property, plant and equipment as at December 31, 2006 and 2005 is as follows:

	2006				2005	
	Cost	Reassessed Value Increment	Accumulated Depreciation	Accumulated Impairment	Carrying Value	Carrying Value
Land	\$ 2,463,191	\$ 248,261	\$ -	\$ 162,739	\$ 2,548,713	\$ 2,437,167
Buildings and improvements	36,695,358	45,062	8,915,362	1,282	27,823,776	22,180,417
Machinery and equipment	38,969,880	-	19,846,159	-	19,123,721	17,400,532
Transportation equipment	1,036,084	-	701,067	-	335,017	298,772
Furniture, fixtures and office equipment	4,338,324	-	2,839,312	-	1,499,012	1,380,987
Other equipment	613,551	-	251,724	-	361,827	301,321
Construction in progress and prepayments on purchase of equipment	3,842,377	-	-	-	3,842,377	5,809,585
	<u>\$87,958,765</u>	<u>\$ 293,323</u>	<u>\$32,553,624</u>	<u>\$ 164,021</u>	<u>\$55,534,443</u>	<u>\$49,808,781</u>

The Company recorded land value increment in 1987 and 1991 to reflect the value appraised and published by the government. Reserve for land value increment tax, payable upon sale of land, is presented under long-term liabilities. Furthermore, in accordance with the amended Land Tax Law, the Company decreased its reserve for land value increment tax by \$49,652 thousand with a corresponding increase in property, plant and equipment revaluation increment for the year ended December 31, 2005.

Two parcels of land located in Changhwa County were purchased by the Company for \$22,187 thousand in June 1990 and for \$33,668 thousand in April 1997. According to related laws, the ownership for these two parcels of land should be transferred to the Company. However, due to certain restrictions under the land regulations, the ownership for these two parcels of land resides with a trustee through a trust agreement which prohibits the trustee from selling, pledging or hypothecating the property. Consequently, the two parcels of land amounted to \$55,855 thousand as at December 31, 2006 and 2005 are included in "other assets - land held by trustee" (see Note 14).

In 2006, the construction of Pou Chen International Building was completed. The total price of land was \$907,582 thousand and the building was \$3,486,744 thousand, or total of \$4,394,326 thousand.

The interest expense for the years ended December 31, 2006 and 2005 amounted to \$2,657,361 thousand and \$1,557,175 thousand, respectively. Interest costs capitalized as part of the costs of property, plant and equipment for the years ended December 31, 2006 and 2005 amounted to \$8,006 thousand and \$1,347 thousand, respectively. Interest rate for capitalization was 2.50% for both years.

#### 14. OTHER ASSETS

Other assets as at December 31, 2006 and 2005 consist of the following:

	2006	2005
Leased-out assets		
Cost and revaluation increment	\$ 1,810,313	\$ 1,206,590
Less accumulated depreciation	<u>(108,835)</u>	<u>(111,381)</u>
	<u>1,701,478</u>	<u>1,095,209</u>
Refundable deposits	<u>72,596</u>	<u>281,982</u>
Deferred charges	<u>3,615,682</u>	<u>3,584,049</u>
Long-term receivables	<u>265,023</u>	<u>210,151</u>
Deferred tax assets (Note 24)	<u>68,350</u>	<u>224,745</u>
Land held by trustee (Note 13)	<u>55,855</u>	<u>55,855</u>
Idle asset	85,604	65,342
Less		
Accumulated depreciation	(44,405)	(38,489)
Allowance for valuation loss of idle asset	<u>(41,199)</u>	<u>(22,345)</u>
	<u>-</u>	<u>4,508</u>
Prepaid pension cost (Note 20)	36,467	14,955
Others - land and building for sale	5,574	5,622
Temporary tax payments	<u>5,920</u>	<u>28,738</u>
	<u>\$ 5,826,945</u>	<u>\$ 5,505,814</u>

## 15. SHORT-TERM BORROWINGS

Short-term borrowings as at December 31, 2006 and 2005 consist of the following:

	2006		2005	
	Annual Interest Rate %	Balance	Annual Interest Rate %	Balance
Short-term borrowings				
Procurement loans	1.17~6.88	\$ 1,414,160	3.79~5.64	\$ 3,084,069
Unsecured loans	1.65~8.30	<u>14,019,432</u>	0.70~5.22	<u>8,930,711</u>
		<u>\$ 15,433,592</u>		<u>\$ 12,014,780</u>

## 16. SHORT-TERM BILLS

Short-term bills as at December 31, 2006 and 2005 consist of the following:

	2006		2005	
	Annual Interest Rate %	Balance	Annual Interest Rate %	Balance
Short-term bills				
Commercial paper, credit	1.37~2.31	\$ 1,560,000	1.03~1.51	\$ 1,200,000
Less discount on commercial paper		<u>(5,840)</u>		<u>(4,658)</u>
		<u>\$ 1,554,160</u>		<u>\$ 1,195,342</u>

## 17. CURRENT PORTION OF LONG-TERM LIABILITIES

Current portion of long-term liabilities as at December 31, 2006 and 2005 consists of the following:

	2006	2005
Bonds payable (see Note 18)	\$ -	\$ 13,507,542
Long-term debt (see Note 19)	<u>2,463,335</u>	<u>2,507,705</u>
	<u>\$ 2,463,335</u>	<u>\$ 16,015,247</u>

## 18. BONDS PAYABLE

Bonds payable as at December 31, 2006 and 2005 consist of the following:

	2006	2005
Euro Convertible Bonds	\$ 7,568,526	\$ 12,379,745
Add interest compensation and income tax payable	<u>295,225</u>	<u>1,278,250</u>
	7,863,751	13,657,995
Less current portion	<u>-</u>	<u>(13,507,542)</u>
	7,863,751	150,453
Domestic secured bonds	<u>5,000,000</u>	<u>5,000,000</u>
	<u>\$ 12,863,751</u>	<u>\$ 5,150,453</u>

In 2006, the Company repurchased and redeemed at maturity its Euro Convertible Bonds with par value of US\$143,125 thousand from open market at cost of \$5,902,479 thousand and the Company recognized a gain of \$166,855 thousand. Furthermore, the holders of Euro Convertible Bonds converted Euro Convertible Bonds with par value US\$1,850 thousand into 2,188 thousand shares of Pou Chen's common stock in 2006.

In 2005, the Company repurchased its Euro Convertible Bonds with par value of US\$305,825 thousand from open market at cost of \$10,396,507 thousand and the Company recognized a gain of \$103,083 thousand.

### **Euro-Dollar Convertible Bonds**

First Issue by Pou Chen

- (a) Date of issuance: June 24, 1999
- (b) Par value: US\$1,000 (dollars)
- (c) Location of issuance: Luxemburg
- (d) Price of issuance: 100%
- (e) Total amount: US\$125,000 thousand issued, all are redeemed at maturity or repurchased as at June 15, 2006.

Second Issue by Pou Chen

- (a) Date of issuance: November 4, 2003
- (b) Par value: US\$1,000 (dollars)
- (c) Location of issuance: Luxemburg
- (d) Price of issuance: 100%
- (e) Total amount: US\$300,000 thousand issued; there are US\$730 thousand outstanding as at December 31, 2006.
- (f) Interest rate: 0%
- (g) Date of maturity: November 4, 2008
- (h) Conversion Price:  
The initial price at which shares will be issued upon conversion is \$47.285 per share at the issue date. The above conversion price will be adjusted accordingly if there is a capital increase in cash or dividend distribution by Pou Chen. As at December 31, 2006, the current adjusted conversion price is \$28.70 dollars per share.
- (i) Redemption at maturity:  
Unless previously redeemed, repurchased and cancelled, or converted, the Bonds will be redeemed on November 4, 2008 at a price equal to 99.501% of the unpaid principal amount.

- (j) Redemption at the option of Pou Chen:
- (i) The Bonds may be redeemed, in whole or from time to time in part (in the principal amount of US\$1,000 (dollars) or any integral multiple thereof), at the option of Pou Chen at any time on or after November 4, 2005, at a price equal to 100% of the unpaid principal amount thereof; provided that the closing price of the common shares (translated into US dollars at the prevailing rate) on each of 20 consecutive trading days, the last of which occurs not more than five days prior to the date on which notice of such redemption is given, is at least 130% of the conversion price (translated into US dollars at the fixed rate). Notwithstanding the foregoing, the Bonds may be redeemed in whole at the option of Pou Chen at any time at a price equal to 100% of the unpaid principal amount thereof if at least 95% in aggregate principal amount of the Bonds has already been redeemed, repurchased and cancelled, or converted.
  - (ii) The Bonds may also be redeemed in whole at any time at the option of Pou Chen at a price equal to 100% of the unpaid principal amount thereof in the event of certain changes relating to taxation in the Republic of China or such other jurisdiction in which Pou Chen is then organized.
- (k) Repurchase at the option of holders:
- (i) Each holder has the right to require Pou Chen to repurchase all or any portion (in the principal amount of US\$1,000 (dollars) or any integral multiple thereof) of such holder's bonds on November 4, 2005 at a price equal to 99.80% of the unpaid principal amount thereof.
  - (ii) If the common shares cease to be listed or admitted to trading on the TSE for a period exceeding five consecutive trading days, then each holder will have the right, at such holder's option, to require Pou Chen to repurchase all of such holder's bonds at a price equal to 100% of the unpaid principal amount.
  - (iii) Upon the occurrence of a change of control, each holder shall have the right, at such holder's option, to require Pou Chen to repurchase all of such holder's bonds at a price equal to 100% of the unpaid principal amount thereof on the date set by Pou Chen which is not less than 30 days nor more than 60 days following the date on which Pou Chen notifies the trustee of the change of control.  
A change of control means any of the following events:
    - any person or persons, other than the Tsai Family or its affiliates, acting together, acquires or acquire legal or beneficial ownership of at least 50% of Pou Chen's capital stock; or
    - Pou Chen consolidates with or merges into or sells or transfers all or substantially all of its assets to any other person or persons (other than the Tsai Family or its affiliates), unless the consolidation, merger, sale or transfer will not result in the other person or persons acquiring control over Pou Chen or the successor entity.
  - (iv) If Pou Chen ceases to hold, directly or indirectly, at least 33% of the outstanding capital stock of Yue Yuen or if Pou Chen, together with the Tsai Family and its affiliates, ceases to hold, directly or indirectly, at least 51% of the outstanding capital stock of Yue Yuen, then each holder shall have the right, at such holder's option, to require Pou Chen to repurchase all of such holder's bonds at a price equal to 100% of the unpaid principal amount.

### **Domestic Secured Bonds**

The first secured bonds of 2003:

- (a) Pou Chen issued \$5,000,000 thousand secured bonds from June 10, 2003 to June 13, 2003, for the purpose of repaying bank loan. The bonds were separated into 19 types (from "A" to "S"). The issued amount of type A, B, C, D, E, F, K, L, M, N, P, Q was \$300,000 thousand and the other types was \$200,000 thousand. The par value of all types was \$10,000 thousand.
- (b) Date of maturity and price of issuance: from June 10, 2008 to June 13, 2008 and 100%

(c) Interest rate:

Type A, F, K, P: 4.000%, minus floating rate

Type B, G, L, Q: 4.001%, minus floating rate

Type C, H, M, R: 4.002%, minus floating rate

Type D, I, N, S: 4.003%, minus floating rate

Type E, J, O: 4.004%, minus floating rate

The nominal interest rate of all types should be greater than 0%.

The floating rate is determined on the Fixing Rate of USD 6-month LIBOR at 11:00 AM on the second London business day before the first day of each interest period on "LIBOR" page on the Reuters screen.

The secured bonds contain certain covenants on a yearly evaluation basis, including a covenant that requires Pou Chen to maintain a consolidated tangible net worth of not less than \$18,000,000 thousand, and the following financial ratios: (i) a ratio of consolidated total liabilities including contingent liabilities to consolidated tangible net worth of not more than 2:1, (ii) a ratio of consolidated net income before interest, taxation, depreciation and amortization to consolidated interest of no less than 3:1, and (iii) a ratio of consolidated current assets to consolidated current liabilities of not less than 0.8:1.

Additionally, the secured bonds also contain certain covenants that, among other things, limit the ability of Pou Chen, subject to certain conditions and limitations, to:

- (a) merge with any other company or spin off, unless Pou Chen being the existing company or majority lenders consent that such merger or spin off will not have a material adverse effect on Pou Chen;
- (b) change the scope or nature of its major business;
- (c) create any encumbrance over its assets, except for such encumbrance that had been made before the agreement date and disclosed to lenders;
- (d) sell, lease out, transfer or dispose of all or substantially all of its assets nor of any part of its assets with a value greater than the amount equal to 35% of the consolidated assets. Nevertheless the limitation on the preceding sentence, the following disposals shall not be taken into account under this restriction:
  - (i) disposals in the ordinary course of business,
  - (ii) the payment of cash as consideration for the acquisition of any asset at arm's length and on normal commercial terms,
  - (iii) the temporary application of funds not immediately required in the purchase or making of short-term investments, or the realization of such investments,
  - (iv) the disposal (for a consideration not exceeding a normal commercial consideration) of assets to its subsidiaries and/or Yue Yuen.
- (e) make loan, according to procedures on fund and loans, in excess of 20% of the issued capital;
- (f) trade with others in irregular course;
- (g) amend or change the contents, conditions or terms of the secured bonds, unless such amendment or change will not result in adverse effect to lenders;
- (h) provide guarantees in violation of the guidelines of endorsement and guarantees, which guidelines provide that aggregate endorsements and guarantees shall not exceed 100% of net worth as shown in the most recent audited or reviewed financial statements.

### **Euro-Dollar Convertible Bonds**

First issue by Yue Yuen Industrial (Holdings) Limited

- (a) Date of issuance: December 23, 2003
- (b) Par value: US\$1,000 thousand
- (c) Location of issuance: Luxemburg
- (d) Price of issuance: 100%

- (e) Total amount: US\$317,000 thousand issued; there are US\$231,470 thousand outstanding as at December 31, 2006
- (f) Interest rate: 0%
- (g) Date of maturity: December 23, 2008
- (h) Conversion Price:  
 HK\$27.33 dollars per share at the fixed rate of exchange of HK\$7.7622 dollars to US\$1 dollar which will be subject to adjustment for, among other things, subdivision or consolidation of shares, capital distributions, bonus issues, rights issues and other dilutive events.
- (i) Redemption at maturity:  
 Unless previously redeemed, repurchased and cancelled, or converted, the Bonds will be redeemed on December 23, 2008 at a price equal to 98.76% of the unpaid principal amount.
- (j) Redemption at the option of Yue Yuen:  
 On or at any time after December 23, 2005 (in the case of (i) below) and at any time (in the case of (ii) below) and (in either case) prior to December 16, 2008, Yue Yuen may redeem all (in the case of (ii) below) or, from time to time, some only (being US\$1,000,000 dollars in principal amount or an integral multiple thereof) of the Bonds, subject to giving not less than 30 nor more than 60 days' notice, at the Early Redemption Amount on the Redemption Date if (i) the closing price of the Share (as derived from the Daily Quotations Sheet of the Hong Kong Stock Exchange or, as the case may be, the equivalent quotation sheet of an Alternative Stock Exchange), translated into United States dollars at the prevailing rate described herein, for each of any 20 Trading Days during a 30 consecutive Trading Day period, the last day of which period occurring no more than five Trading Days prior to the date upon which such notice of redemption is given, was at least 120 per cent. of the Conversion Price in effect on each such Trading Day, translated into United States dollars at the rate of HK\$7.7622 dollars = US\$1.00 dollar or (ii) at least 90 per cent. in principal amount of the Bonds has already been converted, redeemed or purchased and cancelled.
- (k) Repurchase at the option of holders:  
 Each holder has the right to require Yue Yuen to repurchase all or any portion of such holder's bonds on December 23, 2005 at a price equal to 99.50% of the unpaid principal amount thereof.
- (l) On December 14, 2005, Yue Yuen signed a put release agreement with a financial institution and pursuant to which has agreed, on request of the holders of the Exercised Bonds, to revoke the Put Option exercised so that such CB will continue to be outstanding. In addition, Yue Yuen will make an additional payment to or to the order of the Financial Institution on maturity of the Exercised Bonds.

## 19. LONG-TERM DEBT

Long-term debt as at December 31, 2006 and 2005 consists of the following:

	2006	2005
Citibank (Lead Lender) and other banks		
Long-term debt, US\$300,000 thousand, due in semiannual installments commencing November 8, 2007 and maturing November 8, 2009. Interest rate is 5.74188%.	\$ 9,778,500	\$ 9,855,000
Bank of China		
Long-term debt, US\$420,000 thousand. The period is from June 1, 2005 to June 1, 2010. Interest rate is 5.66%. Interest is paid semiannually.	11,415,193	11,504,497

	2006	2005
China Trust Commercial Bank Long-term debt, US\$2,660 thousand, due in semiannual installments commencing September 21, 2005 and maturing September 21, 2008. Interest rate is 6.65%. Interest is paid monthly.	49,381	74,635
China Trust Commercial Bank Long-term debt, US\$2,000 thousand, the term is from February 22, 2005 to February 22, 2009. Interest rate is 4.03%. Interest is paid monthly. The principal was fully prepaid in 2006.	-	65,700
Industrial Bank of Taiwan Mid-term debt, the term is from October 26, 2005 to October 25, 2008. Interest rate is 2.6163%. Interest is paid monthly. The principal will be fully repaid upon maturity.	180,000	180,000
Citibank (Lead Lender) and other banks Long-term debt, NT\$6,500,000 thousand, due in semiannual repayments commencing April 25, 2009 and maturing October 25, 2010. Interest rates range from 2.128% to 2.196%.	6,500,000	4,500,000
China Trust Commercial Bank Long-term debt, NT\$2,500,000 thousand, due in semiannual repayments commencing December 9, 2009 and maturing June 9, 2011. Interest rate is 2.204%.	2,500,000	-
China Development Industrial Bank (Lead Lender) and other banks Long-term debt, US\$23,200 thousand, due in 5 semiannual installments commencing September 5, 2006 and maturing September 5, 2008. Interest rate is 3-month LIBOR rate plus 1%. Interest is paid monthly. The installment due in March 2007 was fully prepaid in September 2006.	453,723	762,120
Ta Chong Bank (Lead Lender) and other banks Long-term debt, US\$30,000 thousand, due in 5 semiannual installments commencing September 2, 2008 and maturing September 2, 2010. Interest rate is 1-month (2, 3 or 6-month) LIBOR rate plus 0.90%.	977,850	328,500
Standard Chartered Bank (HK) Long-term debt, US\$30,000 thousand. The term is from August 24, 2005 to August 24, 2010. Interest rate is USD 3-month LIBOR rate plus 0.90%. Interest is paid quarterly. The principal is due in semiannual installments commencing from August 24, 2008.	977,850	722,700

	2006	2005
Ta Chong Bank (Lead Lender) and other banks Long-term debt, US\$15,000 thousand. The term is from November 14, 2005 to November 14, 2010. The principal due in semiannual installments commencing from November 14, 2008. Interest rate is 3-month LIBOR rate plus 1%. Interest is paid quarterly.	130,380	131,400
Industrial Development Bureau interest-free loan	-	4,634
Cathay United Bank Long-term debt, US\$9,750 thousand, due in monthly repayments commencing June 20, 2006 and maturing May 20, 2013. Interest rate is floating. Interest is paid monthly.	<u>316,139</u>	<u>-</u>
	33,279,016	28,129,186
Less current portion	<u>(2,463,335)</u>	<u>(2,507,705)</u>
	<u>\$ 30,815,681</u>	<u>\$ 25,621,481</u>

## 20. PENSION PLAN

Pou Chen, Barits Development, Pou Yuen Technology, Pro Arch Technology and Global Brands Manufacture each has a defined benefit pension plan covering all employees. The benefits are primarily based upon an employee's years of service and average compensation for the last six months before retirement.

Net pension cost for the year 2006 consists of the following:

	Pou Chen	Barits Development	Pou Yuen Technology	Pro Arch Technology	Global Brands Manufacture	Total
Service cost	\$ 37,180	\$ 3,773	\$ 326	\$ -	\$ 854	\$ 42,133
Interest cost	37,145	2,371	335	8	1,186	41,045
Expected return on plan assets	(12,920)	(3,111)	(1,029)	(449)	(150)	(17,659)
Amortization of net transition obligation	(1,875)	646	-	27	656	(546)
Amortization of unrecognized prior service cost	-	-	204	-	-	204
Amortization of pension loss	10,111	(3,033)	(201)	-	865	7,742
Gain on curtailment of pension cost	<u>-</u>	<u>(44,033)</u>	<u>-</u>	<u>(391)</u>	<u>-</u>	<u>(44,424)</u>
	<u>\$ 69,641</u>	<u>\$ (43,387)</u>	<u>\$ (365)</u>	<u>\$ (805)</u>	<u>\$ 3,411</u>	<u>\$ 28,495</u>

Barits Development and Pro Arch Technology's gain on curtailment of pension cost of \$44,424 thousand was due to the decrease in participants in the retirement plan. It was recorded as "non-operating income."

The following table sets forth the actuarial assumptions and plan's status as at December 31, 2006:

	Pou Chen	Barits Development	Pou Yuen Technology	Pro Arch Technology	Global Brands Manufacture
Weighted-average discount rate	2.75%	2.75%	2.75%	2.75%	3.00%
Assumed rate of increase in salaries	3.00%	3.00%	3.25%	2.00%	3.00%
Expected rate of return on plan assets	2.75%	2.75%	2.75%	2.75%	4.00%

The following is pension fund distribution table as at December 31, 2006:

	Pou Chen	Barits Development	Pou Yuen Technology	Pro Arch Technology	Global Brands Manufacture	Total
Actuarial present value of benefit obligation:						
Vested benefits	\$ (116,375)	\$ (1,305)	\$ -	\$ -	\$ (2,993)	\$ (120,673)
Nonvested benefits	<u>(573,727)</u>	<u>(28,554)</u>	<u>(5,886)</u>	<u>(115)</u>	<u>(26,448)</u>	<u>(634,730)</u>
Accumulated benefit obligation	(690,102)	(29,859)	(5,886)	(115)	(29,441)	(755,403)
Additional benefits at future salaries	<u>(318,482)</u>	<u>(11,532)</u>	<u>(4,712)</u>	<u>(48)</u>	<u>(21,599)</u>	<u>(356,373)</u>
Projected benefit obligation	(1,008,584)	(41,391)	(10,598)	(163)	(51,040)	(1,111,776)
Plan assets at fair value	<u>362,654</u>	<u>93,857</u>	<u>33,614</u>	<u>14,280</u>	<u>6,425</u>	<u>510,830</u>
Projected benefit obligation in excess of plan assets	(645,930)	52,466	23,016	14,117	(44,615)	(600,946)
Net transition (asset) obligation not yet recognized	(10,248)	3,276	-	-	2,626	(4,346)
Unrecognized prior service costs	-	-	2,956	-	-	2,956
Unrecognized pension gain (loss)	116,537	(38,195)	(7,052)	(292)	27,274	98,272
Net pension gain not yet recognized	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(5,675)</u>	<u>(5,675)</u>
Accrued pension cost	<u>\$ (539,641)</u>	<u>\$ 17,547</u>	<u>\$ 18,920</u>	<u>\$ 13,825</u>	<u>\$ (20,390)</u>	<u>\$ (509,739)</u>

As at December 31, 2006, the amount of accrued pension cost of \$509,739 thousand was the net of deferred pension cost of \$16,451 thousand, prepaid pension cost of \$36,467 thousand and accrued pension cost of \$562,657 thousand.

## 21. CAPITAL STOCK AND RETAINED EARNINGS

Pou Chen's registered and issued capital as at December 31, 2006 and 2005 are summarized as follows:

	2006	2005
Registered capital		
Shares (in thousands)	<u>3,800,000</u>	<u>3,800,000</u>
Par value (in dollars)	<u>\$ 10</u>	<u>\$ 10</u>
Capital	<u>\$ 38,000,000</u>	<u>\$ 38,000,000</u>
Issued capital		
Shares (in thousands)	<u>2,442,686</u>	<u>2,305,793</u>
Par value (in dollars)	<u>\$ 10</u>	<u>\$ 10</u>
Capital	<u>\$ 24,426,857</u>	<u>\$ 23,057,928</u>

At the June 14, 2006 meeting, Pou Chen's stockholders resolved to increase capital by \$1,270,265 thousand through stock dividends and bonuses to employees. Furthermore, employee stock warrants were exercised for 7,678 thousand shares and convertible bonds were exercised for 2,188 thousand shares during 2006. As a result, Pou Chen's outstanding capital stock was increased to \$24,426,857 thousand, divided into 2,442,686 thousand common shares with a par value of \$10.00 dollars each as at December 31, 2006.

Earnings per share are based upon the weighted average number of shares of stock outstanding during the year. For the year ended December 31, 2005, the weighted average number of shares used in the calculation of earnings per share has been restated for the retroactive effect of the stock dividends issued in 2006.

At the meeting on July 15, 2002, the Board of Directors of Pou Chen resolved to issue employee stock warrants in accordance with Securities and Exchange Law Article 28-3 within the quantity of 67,600 units. Each individual employee stock warrant is granted the right to purchase new issued common share for 1,000 shares. The exercise price is the closing price of Pou Chen's common shares at the employee stock warrants' issuance date. The warrant holder can exercise the right up to one-third of the granted warrant units no earlier than two years from the granted date. After four years from the granted date, the warrants holders are eligible to exercise all the warrants owned. As of August 6, 2002 and July 24, 2003, Pou Chen has issued 66,600 units and 1,000 units of employee stock warrants, respectively to the employees with an exercise price of \$23.30 dollars and \$41.20 dollars per unit, respectively.

The exercise price of such warrant has been retroactively restated as \$10.00 dollars and \$24.7 dollars per share, respectively due to the stock dividends issued in 2006. At December 31, 2006, the employee stock warrants of 66,600 units were executed for 14,532 thousand shares of common stock.

According to the Company Law of the ROC and Pou Chen's Articles of Incorporation, 10% of Pou Chen's annual earnings, after paying tax and offsetting deficit, if any, should first be appropriated as legal reserve until such reserve equals to the amount of Pou Chen's capital, and then appropriate necessary special reserve as regulated by laws or local authorities.

Any remaining balance, unless to be retained partially by Pou Chen or resolved otherwise by the stockholders, shall then be appropriated as follows:

- a. 3% bonuses to directors and supervisors,
- b. 1%~5% as bonuses to employees, after deducting the bonuses to directors and supervisors, and
- c. the final remainder shall be distributed to stockholders unless there is deficit.

In accordance with the Approval Documents (95) Jin-Guan-Tseng (1) No. 0950000507 of Financial Supervisory Commission, Executive Yuan public companies have to appropriate earnings for special reserve according to Article 41-1 of Securities Transaction Act, in addition to the appropriation for legal reserve, in amount equal to debit balances, if any, in stockholders' equity (such as unrealized loss on financial assets and cumulative translation adjustments). The special reserve can be reversed and distributed as retained earnings if such deduction of stockholders' equity reversed.

Pou Chen's board of directors proposed and the stockholders approved the distribution from the 2005 earnings of 13,951 thousand shares to employees (represents 0.62% of the outstanding common shares at the end of 2005) and of \$143,829 thousand as bonuses to directors and supervisors. In 2005, the basic earnings per share after income tax (before retroactive adjustment for stock dividend in 2006) was \$1.98 dollars; however, if the earnings distribution to employees, directors and supervisors are accounted for as expenses, the pro-forma basic earnings per share after income tax was \$1.85 dollars. The appropriation of the 2006 retained earnings had not been proposed by the board of directors as of February 15, 2007, the date of the independent auditors' report. For the appropriation of 2005 retained earnings proposed by the board of directors and approved by the stockholders in their meetings, please refer to the Market Observation Post System ("MOPS") of the Taiwan Stock Exchange.

Wealthplus' outstanding capital stock as at September 30, 2006 and 2005 amounted to US\$169,222 thousand, with a par value of US\$1 dollar each, or 169,222 thousand shares.

Additionally, Wealthplus' board of directors approved to distribute earnings of US\$105,000 thousand in 2005.

Win Fortune's outstanding capital stock as at September 30, 2006 and 2005 amounted to US\$100 thousand, with a par value of US\$1 dollar each, 100 thousand shares.

Additionally, Win Fortune's board of directors approved to distribute earnings of US\$4,300 thousand in 2005.

Ming Wang's registered and issued capital as at December 31, 2006 and 2005 amounted to \$427,291 thousand, divided into 42,729 thousand common shares with a par value of \$10.00 dollars each.

According to the Company Law of the ROC and Ming Wang's Articles of Incorporation, 10% of Ming Wang's annual earnings, after paying tax and offsetting deficit, if any, should first be appropriated as legal reserve. From the remaining balance, if any, 3% should be appropriated as bonuses to directors and supervisors, and 1% should be appropriated as bonuses to employees after deducting the bonuses to directors and supervisors. The final remaining balance shall then be distributed in accordance with the resolution in the stockholders' meeting.

Windsor Entertainment's registered and issued capital as at December 31, 2005 amounted to \$100,000 thousand, divided into 10,000 thousand common shares with a par value of \$10.00 dollars each. Additionally, Windsor Entertainment decreased its capital to offset its accumulated deficit by \$90,000 thousand and issued additional capital stock for \$200,000 thousand at a price of \$10.00 dollars per share in October 2006. As at December 31, 2006, Windsor Entertainment's registered and issued capital amounted to \$210,000 thousand, divided into 21,000 thousand common shares with a par value of \$10.00 dollars each.

According to the Company Law of the ROC and Windsor Entertainment's Articles of Incorporation, 10% of Windsor Entertainment's annual earnings, after paying tax and offsetting deficit, if any, should first be appropriated as legal reserve. From the remaining balance, if any, 0.01% should be appropriated as bonuses to employees. The final remaining balance shall then be distributed in accordance with the resolution in the stockholders' meeting.

Yun Yang's registered and issued capital as at December 31, 2006 and 2005 amounted to \$75,000 thousand, divided into 7,500 thousand common shares with a par value of \$10.00 dollars each.

According to the Company Law of the ROC and Yun Yang's Articles of Incorporation, 10% of Yun Yang's annual earnings, after paying tax and offsetting deficit, if any, should first be appropriated as legal reserve. From the remaining balance, if any, at least 1% should be appropriated as bonuses to employees. The final remaining balance shall then be distributed in accordance with the resolution in the stockholders' meeting.

Pou Shine's registered and issued capital as at December 31, 2006 and 2005 amounted to \$573,632 thousand, divided into 57,363 thousand common shares with a par value of \$10.00 dollars each.

According to the Company Law of the ROC and Pou Shine's Articles of Incorporation, 10% of Pou Shine's annual earnings, after paying tax and offsetting deficit, if any, should first be appropriated as legal reserve. From the remaining balance, if any, 3% should be appropriated as bonuses to directors and supervisors, and 1% should be appropriated as bonuses to employees after deducting the bonuses to directors and supervisors. The final remaining balance shall then be distributed in accordance with the resolution in the stockholders' meeting.

Pan Asia Insurance Services' issued capital as at December 31, 2006 and 2005 amounted to \$3,000 thousand.

According to the Company Law of the ROC and Pan Asia Insurance Services' Articles of Incorporation, 10% of Pan Asia Insurance Services' annual earnings, after paying tax and offsetting deficit, if any, should first be appropriated as legal reserve. From the remaining balance, if any, 95% should be distributed to stockholders, 2% should be appropriated as bonuses to employees, and 3% should be appropriated as bonuses to directors and supervisors.

Barits Development's registered and issued capital as at December 31, 2006 and 2005 amounted to \$913,000 thousand, divided into 91,300 thousand common shares with a par value of \$10 dollars each.

According to the Company Law of the ROC and Barits Development's Articles of Incorporation, 10% of Barits Development's annual earnings, after paying tax and offsetting deficit, if any, should first be appropriated as legal reserve. From the remaining balance, if any, 3% should be appropriated as bonuses to directors and supervisors, and 1% should be appropriated as bonuses to employees after deducting the bonuses to directors and supervisors. The final remainder shall then be distributed in accordance with the resolution in the stockholders' meeting.

Pou Yuen Technology's registered and issued capital as at December 31, 2006 and 2005 are summarized as follows:

	<b>2006</b>	<b>2005</b>
Registered capital		
Shares (in thousands)	120,000	120,000
Par value (in dollars)	<u>\$ 10</u>	<u>\$ 10</u>
Capital	<u>\$ 1,200,000</u>	<u>\$ 1,200,000</u>
Issued capital		
Shares (in thousands)	60,000	60,000
Par value (in dollars)	<u>\$ 10</u>	<u>\$ 10</u>
Capital	<u>\$ 600,000</u>	<u>\$ 600,000</u>

According to the Company Law of the ROC and Pou Yuen Technology's Articles of Incorporation, 10% of Pou Yuen Technology's annual earnings, after paying tax and offsetting deficit, if any, should first be appropriated as legal reserve. From the remaining balance, if any, 3% should be appropriated as bonuses to directors and supervisors, and 1% should be appropriated as bonuses to employees. The final remainder shall then be distributed in accordance with the resolution in the stockholders' meeting.

Pro Arch Technology's registered and issued capital as at December 31, 2006 and 2005 are summarized as follows:

	<b>2006</b>	<b>2005</b>
Registered capital		
Shares (in thousands)	185,000	185,000
Par value (in dollars)	<u>\$ 10</u>	<u>\$ 10</u>
Capital	<u>\$ 1,850,000</u>	<u>\$ 1,850,000</u>
Issued capital		
Shares (in thousands)	30,100	117,513
Par value (in dollars)	<u>\$ 10</u>	<u>\$ 10</u>
Capital	<u>\$ 301,000</u>	<u>\$ 1,175,127</u>

Pro Arch Technology's outstanding capital stock as at December 31, 2005 amounted to \$1,175,127 thousand. In September 2006, Pro Arch Technology decreased its capital to offset its accumulated deficit by \$1,174,127 thousand and issued additional capital stock for \$300,000 thousand at a price of \$10.00 dollars per share. As at December 31, 2006, Pro Arch Technology has an outstanding common stock of \$301,000 thousand with a par value of \$10.00 dollars each.

According to the Company Law of the ROC and Pro Arch Technology's Articles of Incorporation, 10% of Pro Arch Technology's annual earnings, after paying tax and offsetting deficit, if any, should first be appropriated as legal reserve. From the remaining balance, if any, less than 12% should be appropriated as bonuses to employees, and more than 1% should be appropriated as bonuses to directors and supervisors. The final remainder shall then be distributed in accordance with the resolution in the stockholders' meeting.

Global Brands Manufacture's registered and issued capital as at December 31, 2006 and 2005 are summarized as follows:

	<b>2006</b>	<b>2005</b>
Authorized capital		
Share (in thousands)	<u>440,000</u>	<u>330,000</u>
Par value (in dollars)	<u>\$ 10</u>	<u>\$ 10</u>
Capital	<u>\$4,400,000</u>	<u>\$3,330,000</u>
Issued capital		
Share (in thousands)	<u>271,779</u>	<u>205,438</u>
Par value (in dollars)	<u>\$ 10</u>	<u>\$ 10</u>
Capital	<u>\$2,717,794</u>	<u>\$2,054,382</u>

Global Brands Manufacture was authorized to issue common stock of 30,000 thousand shares under private placement at \$40.48 dollars per share for funding operating capital in November 2003. Such private placement shares and their distributed shares (41,745 thousand shares as at December 31, 2006) are not allowed to trade in the following 3 years of issuance. The private placement shares referred above had been allowed to trade by Financial Supervisory Commission, Executive Yuan in January 2007.

Global Brands Manufacture was approved on May 27, 2005 by Financial Supervisory Commission, Executive Yuan to issue capital stock of \$350 million at \$37.50 dollars per share for paying off debt and for working capital. On June 10, 2005, Global Brands Manufacture issued additional capital of \$163,362 thousand through stockholders' dividends of \$154,102 thousand, and bonuses to employees of \$9,260 thousand. As a result, Global Brands Manufacture's outstanding capital was increased to \$2,054,382 thousand divided into 205,438 thousand common shares with a par value of \$10.00 dollars each as at December 31, 2005.

At their March 31, 2006 meeting, the Board of Directors of Global Brands Manufacture resolved to issue additional common stock of 33,000 thousand shares at \$45.50 dollars per share for funding operating capital and paying off debt. This issue was approved by the regulatory authority at April 19, 2006. On June 9, 2006, Global Brands Manufacture issued additional capital of \$333,412 thousand through stockholders' dividends of \$308,157 thousand, and bonuses to employees of \$25,255 thousand. As a result, Global Brands Manufacture's outstanding capital was increased to \$2,717,797 thousand divided into 271,779 thousand common shares with a par value of \$10.00 dollars as at December 31, 2006.

In their October 15, 2002 meeting, the Board of Directors of Global Brands Manufacture resolved to issue employee stock warrants in accordance with the Securities and Exchange Law Article 28-3 within the quantity of 5,672 units. Each stock warrant is granted the right to purchase 1,000 new issued common shares. The exercise price is the closing price of Global Brands Manufacture's common shares at the employee stock warrants' issuance date. The warrant holders can exercise the right up to one-third of the granted warrant units no earlier than two years from the granted date. After four years from the granted date, the warrants holders are eligible to exercise all the warrants owned. As of December 13, 2002 and September 22, 2003, Global Brands Manufacture issued 5,662 and 10 units, respectively, of employee stock warrants to the employees with an exercise price of \$29.50 dollars and \$64 dollars per unit. The exercise price will be adjusted according to calculating formula due to stock and cash dividends and issuance of capital stock. As at December 31, 2006, the exercise price was \$18.20 dollars and \$37.40 dollars per unit.

On their September 22, 2003 meeting, the Board of Directors of Global Brands Manufacture resolved to issue another employee stock warrants with the quantity of 10,672 units. The issuing rules are the same as the first issuance mentioned above. Global Brands Manufacture issued all the employee stock warrants with an exercise price of \$50.50 dollars per unit on November 12, 2003. The exercise price will be adjusted according to calculating formula due to stock and cash dividends and issuance of capital stock. As at December 31, 2006, the exercise price was \$31.20 dollars per unit.

Under the Company Law of the ROC and Global Brands Manufacture's Articles of Incorporation, 10% of Global Brands Manufacture's annual earnings, after paying tax and offsetting deficit, if any, should first be appropriated as legal reserve until such reserve equals the amount of Global Brands Manufacture's capital, and then appropriate necessary special reserve and return the amount of capital surplus from revaluation increment on property, plant and equipment previously used to offset accumulated deficit in prior years, if any, as regulated by laws or local authorities.

Any remaining balance, unless to be retained partially by Global Brands Manufacture or resolved otherwise by the stockholders, shall then be appropriated as follows:

- a. 2%~10% as bonuses to employees,
- b. 1% bonuses to directors and supervisors, and
- c. dividends to stockholders as proposed and approved by Global Brands Manufacture's board of directors and stockholders; nevertheless, cash dividends shall not be more than 90% of the proposed dividends.

## 22. TREASURY STOCK

The changes in treasury stock in 2006 are summarized as follows (in shares):

Reason	2006.01.01	Increase	Decrease	2006.12.31
Buy the stock back to transfer to employees	45,700,000	-	31,500,000	14,200,000
Common shares held by subsidiaries	122,147,184	6,289,231	-	128,436,415

In December 2006, the Company transferred 31,500 thousand shares of common stock to employees at a price of \$24.72 dollars per share, and the difference between the transferred value \$778,680 thousand and the book value \$1,007,843 thousand was \$229,163 thousand, which was recorded as capital surplus - treasury stock.

According to the Stock Exchange Law of the ROC, the shares of treasury stock should not be over 10% of the Company's issued and outstanding shares and the amount of treasury stock should not be over the total of retained earnings and realized additional paid-in capital. The Company held 14,200 thousand shares of treasury stock at the cost of \$396,166 thousand as at December 31, 2006.

According to the Stock Exchange Law of the ROC, the treasury stock of the Company should not be pledged and does not have the same right as the common stock does.

In 2006, after the stock dividends were received by the subsidiaries, 6,289,231 shares were added to treasury stock. Accordingly, as at December 31, 2006, the subsidiaries held 128,436,415 shares of the Company's common stock at cost of \$2,055,319 thousand in total.

The information on the subsidiaries' holdings of the Company's common stock is summarized as follows:

Company's Name	Shares	Amount
Wealthplus	23,625,009	\$ 634,410
Pou Shine	12,206,200	292,736
Ming Wang	23,268,725	495,703
Barits Development	35,217,976	844,618
Top Score	2,624,995	63,576
Ming Chi	17,375,819	416,717
Pou Yii	16,844,426	318,431

## 23. PERSONNEL, DEPRECIATION AND AMORTIZATION EXPENSES

Personnel, depreciation, and amortization expenses for the years ended December 31, 2006 and 2005 are summarized as follows:

Category \ Function	2006				2005			
	Operating Cost	Operating Expenses	Non-Operating Expenses	Total	Operating Cost	Operating Expenses	Non-Operating Expenses	Total
Personnel expense								
Salaries	17,251,497	7,953,262	-	25,204,759	13,452,222	6,734,123	-	20,186,345
Labor insurance and health insurance	495,304	313,986	-	809,290	358,481	243,872	-	602,353
Pension cost	13,129	191,024	-	204,153	84,964	84,776	-	169,740
Others	51,515	108,392	-	159,907	40,415	86,791	-	127,206
Depreciation expenses	4,281,073	1,634,235	59,997	5,975,305	3,718,530	1,457,139	11,510	5,187,179
Amortization expenses	131,247	329,054	-	460,301	26,633	1,506,384	-	1,533,017

## 24. INCOME TAX

The Company's income tax expense for the year ended December 31, 2006 is as follows:

Income tax expense, current	\$ 463,047
10% additional income tax on undistributed earnings of 2005	44,759
Investment tax credits	(24,635)
Adjustment of deferred tax asset and valuation allowance	209,404
Adjustment of prior year's income tax expense	<u>19,353</u>
Income tax expense	<u>\$ 711,928</u>

The components of deferred tax assets (liabilities) as at December 31, 2006 are as follows:

Unrealized inventory devaluation losses	\$ 28,925
Unrealized losses on disposal of property, plant and equipment	660
Unrealized bad debt losses	71,320
Unrealized maintenance and repairs expenses	400
Unrealized pension expense	143,450
Unrealized profit from inter-affiliate transactions	2,810
Unrealized loss on decline in market value of long-term equity investments	3,550
Unrealized net exchange gain	(1,990)
Unrealized provision for decline in value of idle assets	1,240
Losses carryforward	654,660
Investment tax credits	28,815
Others	(144,770)
Less valuation allowance	<u>(614,981)</u>
Deferred tax assets	174,089
Deferred tax assets, current	<u>(105,739)</u>
Deferred tax assets, noncurrent	<u>\$ 68,350</u>

The Company's income tax expense for the year ended December 31, 2006 and income tax payable as at December 31, 2006 were reconciled as follows:

Income tax expense at statutory rate of 25%	\$2,272,377
Income from long-term equity investment accounted for under equity method	(1,655,961)
Income from revaluation of financial instruments measured at fair value through profit or loss	(129,649)
Gain on disposal of security	(8,992)
Loss on reduction of capital in long-term equity investments accounted for under equity method	(192,694)
Loss on disposal of land	9,270
Amortization of operating expense for disposal of land and securities	5,235
Tax on the interest for bonds	6,500
Loss on other investment	91,414
Dividend income - tax free	(116,786)
Others	<u>182,333</u>
Current income tax expense	463,047
Provision for (reversal of) deferred income tax asset	
Unrealized bad debt losses	29,532
Unrealized inventory devaluation losses	(9,390)
Unrealized pension expense	15,780
Unrealized net exchange loss	(31,515)
Realized loss on liquidation of long-term equity investment	(18,300)
Others	<u>29,555</u>
Income tax payable	478,709
Add 10% additional income tax on unappropriated earnings of 2005	44,759
Prior year's income tax payable	13,550
Less temporary tax payment	<u>(224,755)</u>
Income tax payable as at December 31, 2006	<u>\$ 312,263</u>

The income tax returns of Pou Chen, Pou Yuen Technology, Pro Arch Technology, Global Brands Manufacture, Ming Wang, Pou Shine, Pan Asia Insurance Services, Yun Yang, Song Ming Investment, Ming Shun, Windsor Entertainment, Pou Yii Development, Ming Chi Investment and Wang Yi Construction for the years through 2004 have been examined and approved by the tax authority.

The income tax returns of Barits Development for the years through 2004 have been examined and approved by the tax authority.

Barits Development's salaries of staffs in foreign country and commission expenses in 1997 were disallowed by the tax authority. As a result, Barits Development was assessed for an additional income tax payment of approximately \$17,200 thousand. Barits Development did not agree with the assessment and has appealed on first instance. Barits Development lost the lawsuit. Additional provision has been recorded for such assessment for the year ended December 31, 2006.

As at December 31, 2006, the amount and year of expiration of deductible loss carryforward and investment deduction by individual company are as follows:

	<b>Pou Yuen Technology</b>	<b>Pro Arch Technology</b>	<b>Ming Wang</b>	<b>Windsor Entertainment</b>	<b>Global Brands Manufacture</b>
	<b>Loss Carryforward</b>	<b>Loss Carryforward</b>	<b>Investment Tax Credits</b>	<b>Loss Carryforward</b>	<b>Investment Tax Credits</b>
2007	\$ 20,000	\$ 53,100	\$ 4,180	\$ 4,200	\$ -
2008	41,600	131,300	-	-	370
2009	31,400	143,700	-	-	1,270
2010	8,820	161,800	-	-	2,490
2011	-	14,740	-	-	39,870
	<u>\$ 101,820</u>	<u>\$ 504,640</u>	<u>\$ 4,180</u>	<u>\$ 4,200</u>	<u>\$ 24,635</u>

The information of the integrated income tax system as at December 31, 2006 is as follows:

	<b>Pou Chen</b>	<b>Ming Wang</b>	<b>Windsor Entertainment</b>	<b>Pou Shine</b>	<b>Pan Asia Insurance</b>	<b>Barits Development</b>	<b>Song Ming</b>	<b>Pou Yii</b>
IC Balance of Imputation Credit Account	\$ 164,614	\$ 15,293	\$ -	\$ 16,610	\$ 85	\$ 136,124	\$ 4,213	\$ 17,077
Undistributed earnings for the years of 1997 and before	\$ 310,501	\$ -	\$ -	\$ -	\$ -	\$ 515,118	\$ -	\$ 7,176
Undistributed earnings for the years of 1998 and after	\$ 8,403,597	\$ 5,524	\$ (84,524)	\$ 383,023	\$ (221)	\$ 2,564,355	\$ 34,470	\$ (44,444)
Expected IC ratio on distributable earnings of 2006	1.96%	33.33%	-	4.81%	33.33%	5.51%	12.22%	-
Actual IC ratio of earnings distribution for the year of 2005	2.94%	-	-	14.42%	-	11.23%	-	-

  

	<b>Wang Yi</b>	<b>Ming Chi</b>	<b>Ming Shun</b>	<b>Pou Yuen</b>	<b>Yun Yang</b>	<b>Pro Arch</b>	<b>Global Brands Manufacture</b>	<b>Cheng Cheng</b>
IC Balance of Imputation Credit Account	\$ 12,891	10,151	\$ 3,200	\$ 1,792	\$ 2,014	\$ 650	\$ 305,178	\$ 195
Undistributed earnings for the years of 1997 and before	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Undistributed earnings for the years of 1998 and after	\$ (4,387)	\$ 20,596	\$ 255,008	\$ (227,387)	\$ 19,498	\$ (281,601)	\$ 2,275,724	\$ 1,030
Expected IC ratio on distributable earnings of 2006	-	33.33%	1.30%	-	10.65%	-	13.41%	18.93%
Actual IC ratio of earnings distribution for the year of 2005	-	33.33%	5.29%	-	5.33%	-	12.46%	33.60%

In the balance of imputation credit account as at December 31, 2006, the income tax payable for 2006 has been taken into account.

## 25. EARNINGS PER SHARE

For the years ended December 31, 2006 and 2005, earnings per share before income tax and earnings per share after income tax are as follows:

	2006								
	Amount				Weighted Average Number of Common Shares Outstanding (In Thousands)	Earnings Per Share			
	Income from Continuing Operations Before Tax	Income from Continuing Operations After Tax	Cumulative Effect of Changes in Accounting Principles	Income After Tax (Attributed to Pou Chen's Stockholders)		Income from Continuing Operations Before Tax	Income from Continuing Operations After Tax	Cumulative Effect of Changes in Accounting Principles	Income After Tax (Attributed to Pou Chen's Stockholders)
Net income	<u>\$ 11,553,452</u>	<u>\$ 10,841,524</u>	<u>\$ 1,625,271</u>	<u>\$ 5,771,971</u>					
Basic earnings per share									
Net income	\$ 11,553,452	\$ 10,841,524	\$ 1,625,271	\$ 5,771,971	2,260,894	<u>\$ 5.11</u>	<u>\$ 4.80</u>	<u>\$ 0.72</u>	<u>\$ 2.55</u>
Effect of dilutive potential common shares									
Employee stock warrants	-	-	-	-	35,661				
Convertible bonds	-	-	-	-	2,930				
Diluted earnings per share									
Net income plus the effect of dilutive potential common shares	<u>\$ 11,553,452</u>	<u>\$ 10,841,524</u>	<u>\$ 1,625,271</u>	<u>\$ 5,771,971</u>	<u>2,299,485</u>	<u>\$ 5.02</u>	<u>\$ 4.71</u>	<u>\$ 0.71</u>	<u>\$ 2.51</u>
	2005								
	Amount				Weighted Average Number of Common Shares Outstanding (In Thousands)	Earnings Per Share			
	Income from Continuing Operations Before Tax	Income from Continuing Operations After Tax	Cumulative Effect of Changes in Accounting Principles	Income After Tax (Attributed to Pou Chen's Stockholders)		Income from Continuing Operations Before Tax	Income from Continuing Operations After Tax	Cumulative Effect of Changes in Accounting Principles	Income After Tax (Attributed to Pou Chen's Stockholders)
	Net income	<u>\$ 10,069,148</u>	<u>\$ 9,918,686</u>	<u>\$ -</u>	<u>\$ 4,227,942</u>				
Basic earnings per share									
Net income	\$ 10,069,148	\$ 9,918,686	\$ -	\$ 4,227,942	2,257,170	<u>\$ 4.46</u>	<u>\$ 4.39</u>	<u>\$ -</u>	<u>\$ 1.87</u>
Effect of dilutive potential common shares									
Employee stock warrants	-	-	-	-	35,556				
Convertible bonds	-	-	-	-	5,242				
Diluted earnings per share									
Net income plus the effect of dilutive potential common shares	<u>\$ 10,069,148</u>	<u>\$ 9,918,686</u>	<u>\$ -</u>	<u>\$ 4,227,942</u>	<u>2,297,968</u>	<u>\$ 4.38</u>	<u>\$ 4.32</u>	<u>\$ -</u>	<u>\$ 1.84</u>

If the Company's common shares held by its subsidiaries were not accounted for as treasury stock, the pro-forma earnings per share for the years ended December 31, 2006 and 2005 are as follows:

	2006								
	Amount				Weighted Average Number of Common Shares Outstanding (In Thousands)	Earnings Per Share			
	Income from Continuing Operations Before Tax	Income from Continuing Operations After Tax	Cumulative Effect of Changes in Accounting Principles	Income After Tax (Attributed to Pou Chen's Stockholders)		Income from Continuing Operations Before Tax	Income from Continuing Operations After Tax	Cumulative Effect of Changes in Accounting Principles	Income After Tax (Attributed to Pou Chen's Stockholders)
Net income	<u>\$ 11,736,785</u>	<u>\$ 11,024,857</u>	<u>\$ 1,625,271</u>	<u>\$ 5,955,304</u>					
Basic earnings per share									
Net income	\$ 11,736,785	\$ 11,024,857	\$ 1,625,271	\$ 5,955,304	2,389,331	<u>\$ 4.91</u>	<u>\$ 4.61</u>	<u>\$ 0.68</u>	<u>\$ 2.49</u>
Effect of dilutive potential common shares									
Employee stock warrants	-	-	-	-	35,661				
Convertible bonds	-	-	-	-	2,930				
Diluted earnings per share									
Net income plus the effect of dilutive potential common shares	<u>\$ 11,736,785</u>	<u>\$ 11,024,857</u>	<u>\$ 1,625,271</u>	<u>\$ 5,955,304</u>	<u>2,427,922</u>	<u>\$ 4.83</u>	<u>\$ 4.54</u>	<u>\$ 0.67</u>	<u>\$ 2.45</u>

	2005				Weighted Average Number of Common Shares Outstanding (In Thousands)	Earnings Per Share			
	Amount		Cumulative Effect of Changes in Accounting Principles	Income After Tax (Attributed to Pou Chen's Stockholders)		Income from Continuing Operations Before Tax	Income from Continuing Operations After Tax	Cumulative Effect of Changes in Accounting Principles	Income After Tax (Attributed to Pou Chen's Stockholders)
Net income	\$ 10,180,091	\$ 10,029,629			\$ -	\$ 4,338,885			
Basic earnings per share									
Net income	\$ 10,180,091	\$ 10,029,629	\$ -	\$ 4,338,885	2,385,606	\$ 4.27	\$ 4.20	\$ -	\$ 1.82
Effect of dilutive potential common shares									
Employee stock warrants	-	-	-	-	35,556				
Convertible bonds	-	-	-	-	5,242				
Diluted earnings per share									
Net income plus the effect of dilutive potential common shares	\$ 10,180,091	\$ 10,029,629	\$ -	\$ 4,338,885	2,426,404	\$ 4.20	\$ 4.13	\$ -	\$ 1.79

## 26. DISCLOSURES FOR FINANCIAL INSTRUMENTS

### Fair Value of Financial Instruments

The fair value of nonderivative and derivative financial instruments as at December 31, 2006 and 2005 is summarized as follows:

Nonderivative Financial Instruments	2006		2005	
	Carrying Value	Fair Value	Carrying Value	Fair Value
<b>Assets</b>				
Cash and cash equivalents	\$ 14,594,226	\$ 14,594,226	\$ 18,100,617	\$ 18,100,617
Financial assets measured at fair value through profit of loss, current	5,826,810	5,826,810	3,892,205	5,614,218
Notes and accounts receivable	24,271,038	24,271,038	18,954,595	18,954,595
Accounts receivable from affiliates	2,224,619	2,224,619	3,458,267	3,458,267
Other financial assets, current	3,674,758	3,674,758	2,976,144	2,976,144
Long-term investments at equity method	23,864,121	23,719,858	16,874,443	17,473,281
Available-for-sale financial assets, noncurrent	1,502,932	1,502,932	1,688,086	1,688,086
Financial assets carried at cost, noncurrent	683,463	683,463	1,160,002	1,160,002
Refundable deposits	72,596	72,596	281,982	281,982
Long-term receivables	265,023	265,023	210,151	210,151
<b>Liabilities</b>				
Short-term borrowings	15,433,592	15,433,592	12,014,780	12,014,780
Short-term bills	1,554,160	1,554,160	1,195,342	1,195,342
Notes and accounts payable	15,289,416	15,289,416	11,801,384	11,801,384
Notes and accounts payable to affiliates	1,043,609	1,043,609	1,481,670	1,481,670
Other payables	9,084,593	9,084,593	7,773,637	7,773,637
Current portion of long-term liabilities	2,463,335	2,463,335	16,015,247	16,015,247
Bonds payable	12,863,751	12,863,751	5,150,453	5,150,453
Long-term debt	30,815,681	30,815,681	25,621,481	25,621,481
Advance deposits from customers	5,927	5,927	4,910	4,910
<b>Derivative Financial Instruments</b>				
Interest rate swap contracts (derivative financial liabilities held for hedging, noncurrent)	167,839	167,839	-	-
Forward exchange contracts (derivative financial liabilities held for hedging, current)	26,565	26,565	26,382	26,382

The Company adopted newly released SFAS No. 34, "Accounting for Financial Instruments," effective January 1, 2006. Please see Note 3 to the financial statements for the cumulative effect of changes in accounting principle and adjustments to stockholders' equity.

Approaches and assumptions employed in assessing the fair value of financial instruments are summarized as follows:

- (a) The fair value of cash and cash equivalents, notes and accounts receivable, short-term borrowings, short-term bills, and notes and accounts payable, approximates their carrying value due to the short-term maturities of these financial instruments.
- (b) The fair value of financial instruments at fair value through profit or loss, available-for-sale financial assets and derivative financial instruments are quoted by market price. The fair value of derivative financial instruments is measured, according to its specific contract's settlement rate, by the middle exchange rate and the discount rate quoted by Reuters.
- (c) The fair value of long-term debt and bond payables is estimated based on the net present value of expected cash flows.

The fair value of financial instruments that used the quoted market price in active market or other method of valuation is summarized as follows:

	<u>Quoted Market Price in</u> <u>Active Market</u>		<u>Other Method of</u> <u>Valuation</u>	
	2006	2005	2006	2005
<b>Assets</b>				
Financial assets measured at fair value through profit or loss, current	\$ 5,826,810	\$ 5,614,218	-	-
Available-for-sale financial assets, noncurrent	1,502,932	1,688,086	-	-
<b>Liabilities</b>				
Derivative financial liabilities held for hedging, current	-	-	26,565	26,382
Derivative financial liabilities held for hedging, noncurrent	-	-	167,839	-

As at December 31, 2006 and 2005, financial liabilities exposed to cash flow interest rate risk were \$10,550,000 thousand and \$5,000,000 thousand, respectively.

The Company recognized an unrealized gain of \$416,279 thousand in stockholder's equity for the changes in fair value of available-for-sale financial assets for the year ended December 31, 2006.

## **Financial Risk Information**

### ***Market Risk***

The risk the Company engaged in portfolios of marketable equity securities and open-ended mutual fund comes from changes of market price. One percentage decline in market rate will cause the fair value of financial instruments to decline by \$73,297 thousand.

### ***Credit Risk***

Financial instruments are evaluated for credit risk which represents the potential loss that would be incurred by the Company if the counter-parties or third-parties breached the contracts. The risk includes centralization of credit risk, components, contract figure, and its accounts receivable. Besides, the Company requires significant clients to provide guarantees or other rights to reduce credit risk of the Company effectively.

### ***Liquidity Risk***

The Company has the ability to meet its financial obligations; thus, liquidity risks virtually do not exist.

Financial assets measured at fair value through profit or loss and available-for-sale financial assets of the Company are saleable in active market; thus, they can be quickly and easily sold with price close to fair value.

### ***Cash Flow Risk on Interest Rat***

The Company engaged in floating-interest-rate long-term borrowings. Therefore, cash flows are expected to fluctuate due to changes in market interest rates. One percentage increase in market rate will cause the Company to increase its cash-out by \$382,872 thousand.

## **27. RELATED PARTY TRANSACTIONS**

Names and relationships of the related parties are as follows:

<b>Name</b>	<b>Relationship</b>
CMK Corporation (“CMK”)	CMK Corporation together with Global Brands Manufacture invest in CMK GBM and holds 49.00% ownership interest of CMK GBM
CMKC (HK) Limited (“CMKC”)	CMK Corporation holds a 100.00% ownership interest
Ka Yuen Rubber Factory Limited (“Ka Yuen Rubber”)	The Company holds a 50.00% ownership interest.
Techview International Technology Inc. (“Techview International”)	The Company holds a 48.84% ownership interest.
Digital Sun Investments Ltd. (“Digital Sun”)	The Company holds a 25.93% ownership interest
Twinways Investments Ltd. (“Twinways Investments”)	The Company holds a 50.00% ownership interest
San Fang Chemical Industrial Co., Ltd. (“San Fang”)	The Company holds a 44.34% ownership interest and seats in the board of directors
Eastlion Industrial Ltd. (“Eastlion Industrial”)	The Company holds a 35.00% ownership interest
Global Brands Manufacture Ltd. (“GBM”)	Related party in substance
PGE Corporation (“PGE”)	Related party in substance

The Company’s major transactions with the related parties are summarized as follows:

## Sales

Sales to related parties for the years ended December 31, 2006 and 2005 are summarized as follows:

	<u>2006</u>		<u>2005</u>	
	Amount	Percentage to Net Sales	Amount	Percentage to Net Sales
CMKC	\$4,254,258	2	\$3,186,110	2
PGE	1,446,111	1	1,751,360	2
GBM	343,830	-	777,448	1
Others	<u>929,856</u>	<u>1</u>	<u>2,987,377</u>	<u>1</u>
	<u>\$6,974,055</u>	<u>4</u>	<u>\$8,702,295</u>	<u>6</u>

## Cost of Sales - Purchases

Purchases from related parties for the years ended December 31, 2006 and 2005 are summarized below:

	<u>2006</u>		<u>2005</u>	
	Amount	Percentage to Net Purchases	Amount	Percentage to Net Purchases
Ka Yuen Rubber	\$1,613,644	1	\$1,355,805	-
CMKC	1,085,930	1	835,586	1
San Fang	1,072,963	1	1,116,827	1
Digital Sun	834,897	1	238,648	-
Eastlion Industrial	771,549	-	715,549	-
Twinways Investments	706,398	-	755,984	-
Techview International	89	-	1,575,035	1
Others	<u>1,958,872</u>	<u>1</u>	<u>1,891,605</u>	<u>4</u>
	<u>\$8,044,342</u>	<u>5</u>	<u>\$8,485,039</u>	<u>7</u>

## Accounts Receivable

Accounts receivable from affiliates as at December 31, 2006 and 2005 are summarized as follows:

	<u>2006</u>		<u>2005</u>	
	Amount	Percentage to Accounts Receivable	Amount	Percentage to Accounts Receivable
CMKC	\$1,021,305	4	\$1,157,535	5
PGE	975,685	4	1,480,190	7
GBM	17,629	-	101,801	1
Others	319,115	-	736,431	3
Less allowance for doubtful accounts	<u>(109,115)</u>	<u>-</u>	<u>(17,690)</u>	<u>-</u>
	<u>\$2,224,619</u>	<u>8</u>	<u>\$3,458,267</u>	<u>16</u>

## Notes and Accounts Payable

Notes and accounts payable to affiliates as at December 31, 2006 and 2005 are summarized as follows:

	<u>2006</u>		<u>2005</u>	
	<u>Amount</u>	<u>Percentage to Notes and Accounts Payable</u>	<u>Amount</u>	<u>Percentage to Notes and Accounts Payable</u>
Notes payable				
San Fang	\$ 95,656	45	\$ 102,578	59
Others	<u>-</u>	<u>-</u>	<u>109</u>	<u>-</u>
	<u>\$ 95,656</u>	<u>45</u>	<u>\$ 102,687</u>	<u>59</u>
Accounts payable				
Ka Yuen Rubber	\$ 272,786	2	\$ 283,364	2
San Fang	120,113	-	86,774	1
Twinways Investments	111,739	-	134,389	1
Digital Sun	92,619	-	-	-
Techview International	-	-	516,010	4
Others	<u>350,696</u>	<u>4</u>	<u>358,446</u>	<u>3</u>
	<u>\$ 947,953</u>	<u>6</u>	<u>\$ 1,378,983</u>	<u>11</u>

## Credit Guarantees

See Note 28.

## 28. COMMITMENTS AND CONTINGENCIES

### Loan Guarantees

As at December 31, 2006, the Company issued certificates of guarantee of \$60,000 thousand for the payment of loans.

### Letters of Credit

Outstanding letters of credit as at December 31, 2006 are as follows (unit: dollar):

U.S. Dollar	\$ 12,529,245
Euro	25,267
Japanese Yen	7,752,000

As at December 31, 2006, the Company has guaranteed the payments of credit of related parties as follows:

<b>Related Party</b>	<b>Amount</b>
Venture Well Holdings Ltd.	\$ 412,653
Alpha Leader Ltd.	92,655
Beijing Advazone Electronic Co., Ltd.	55,046
Best Focus Holdings Ltd.	488,925
Hua Jian Industrial Holding Co., Ltd.	831,173
Cohen Enterprises Inc.	488,925
Ka Yuen Rubber Factory Ltd.	41,788
Pine Wood Industries Ltd.	78,632
Yuen Thai Industrial Co., Ltd.	<u>125,365</u>
	<u>\$2,615,162</u>

## **29. SUBSEQUENT EVENTS**

On January 12, 2007, the Board of Directors of Pou Chen resolved to dispose of 7,479 thousand shares of AUO common stock for the total price of \$333,906 thousand or \$44.65 dollars per share, and the Company recognized loss on disposal of investments of \$4,893 thousand.

On January 16, 2007, the Board of Directors of Pou Chen resolved to invest in Fanchang Yue Xiang Enterprise Dev. Co., Ltd., Fanchang Yue Song Enterprise Dev. Co., Ltd. and Franchang Pou Feng Dev. Co., Ltd. US\$13,872 thousand for 100% ownership equity through a subsidiary, Yue Yuen.

On January 29, 2007, the Board of Directors of Pou Chen resolved to subscribe to 26,007 thousand shares of Pou Yuen Technology for the total price of \$260,073 thousand or \$10.00 dollars per share.

On February 15, 2007, the Board of Directors of Pou Chen resolved to invest in Sheng Dao Investments Co., Ltd. to become a holding company for the retailing of sports goods business in ROC through a subsidiary, Yue Yuen. Sheng Dao's registered capital was US\$44,000 thousand.