

GCS HOLDINGS, INC. AND SUBSIDIARIES
CONSOLIDATED FINANCIAL STATEMENTS AND
REVIEW REPORT OF INDEPENDENT
ACCOUNTANTS
DECEMBER 31, 2018 AND 2017

For the convenience of readers and for information purpose only, the 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. In the event of any discrepancy between the English version and the original Chinese version or any differences in the interpretation of the two versions, the Chinese-language auditors' report and consolidated financial statements shall prevail.

REPORT OF INDEPENDENT ACCOUNTANTS TRANSLATED FROM CHINESE

PWCR18000232

To GCS Holdings, Inc.

Opinion

We have audited the accompanying consolidated balance sheets of GCS Holdings, Inc. and its subsidiaries (the “Group”) as at December 31, 2018 and 2017, and the related consolidated statements of comprehensive income, of changes in equity and of cash flows for the years then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at December 31, 2018 and 2017, and its consolidated financial performance and its consolidated cash flows for the years then ended in accordance with the “Regulations Governing the Preparations of Financial Reports by Securities Issuers” and the International Financial Reporting Standards, International Accounting Standards, IFRIC Interpretations, and SIC Interpretations as endorsed by the Financial Supervisory Commission.

Basis for opinion

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

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole and, in forming our opinion thereon, we do not provide a separate opinion on these matters.



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Key audit matters for the Group's consolidated financial statements for the year ended December 31, 2018 are stated as follows:

Key Audit Matter – Sales revenue recognition

Description

Please refer to Note 4(26) for accounting policies of revenue recognition. Please refer to Note 6(20) for description of revenue.

The Group primarily engages in the manufacturing and selling of compound semiconductor wafers and advanced optoelectronics technology products. From the operating revenue of NT\$1,952,411 thousands for the year ended December 31, 2018, sales revenue generated from manufacturing of compound semiconductor wafers and advanced optoelectronics technology products amounted to NT\$1,908,547 thousands, representing 98% of total operating revenue. The Group's customers include wireless devices and fiber-optic communication providers in China, U.S.A., Taiwan and etc., and sales terms vary based on market conditions and customer needs in different regions. Considering that sales revenue are the main transactions of the Group, which has significant effect on the consolidated financial statements and requires substantial amount of time and resources for validation, we identified the audit of sales revenue recognition as one of the key audit matters.

How our audit addressed the matter

The major audit procedures regarding sales revenue recognition were as follows:

1. Evaluated the design, and operating effectiveness of internal controls relevant to sales revenue recognition.
2. Sampled and tested sales transactions by inspecting customers' purchase orders, documents regarding transfer of control, invoices and subsequent collection of accounts receivable to validate the occurrence and accuracy of sales transactions.
3. Performed test of sales transactions within a defined period before and after the balance sheet date in order to verify whether the sales transactions were recorded in the appropriate periods.
4. Performed confirmation procedures for sampled accounts receivable and inspected significant sales return and discount transactions that occurred in the subsequent period to verify the authenticity of sales transactions, the accuracy of sales amounts recognized and the appropriate timing for recording sales transactions.

Key Audit Matter – Assessment of allowance for valuation of inventory

Description

Please refer to Note 4(10) for description of accounting policies on allowance for inventory valuation. Please refer to Note 5(2) for accounting estimates and assumption uncertainty on evaluation of inventory. Please refer to Note 6(3) for description of allowance for inventory valuation.

The Group primarily engages in the manufacturing and selling of compound semiconductor wafers and advanced optoelectronics technology products. Due to rapid technological innovations, intense market competition and fluctuations in market prices, there is a higher risk of inventory losses due from market value decline or obsolescence. The Group used net realizable value to make provisions for estimated loss related to inventories aged over a certain period and individually identified as obsolete. The aforementioned identification of obsolete inventories and net realizable value are subject to management's judgment. Considering the Group's inventory and allowance for inventory valuation have a significant impact on the Group's consolidated financial statements, we identified the assessment of allowance for valuation of inventory as one of the key audit matters.

How our audit addressed the matter

Our audit procedures performed in respect of the above area included the following:

1. Ensured consistent application of accounting policies in relation to allowance for inventory valuation and assessed the reasonableness of these policies.
2. Validated the appropriateness of inventory aging report used by management to ensure that the information in the inventory aging report is consistent with the corresponding accounting policies.
3. Obtained net realizable value calculation report prepared by management, sampled inventory items and checked whether purchase or sales documents corresponded to records and recalculated the net realizable value calculation for accuracy. Performed the aforementioned audit procedures to assess the reasonableness of recognized inventory valuation fluctuations.

Responsibilities of management and those charged with governance for the consolidated financial statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with the "Regulations Governing the Preparations of Financial Reports by Securities Issuers" and the International Financial Reporting Standards, International Accounting Standards, IFRIC Interpretations, and SIC Interpretations as endorsed by the Financial Supervisory Commission, and for such internal controls as management determines are necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.



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

Those charged with governance, including Audit Committee, are responsible for overseeing the Group's financial reporting process.

Responsibilities of independent accountants for the audit of the consolidated financial statements

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

As part of an audit in accordance with ROC GAAS, we exercise professional judgement and maintain professional skepticism throughout the audit. We also:

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



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

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

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

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

LI, TIEN-YI

Li, Tien-Yi

Chih-Cheng Hsieh

Hsieh, Chih-Cheng

For and on behalf of PricewaterhouseCoopers, Taiwan

March 15, 2019

The accompanying consolidated financial statements are not intended to present the financial position and results of operations and cash flows in accordance with accounting principles generally accepted in countries and jurisdictions other than the Republic of China. The standards, procedures and practices in the Republic of China governing the audit of such financial statements may differ from those generally accepted in countries and jurisdictions other than the Republic of China. Accordingly, the accompanying consolidated financial statements and report of independent accountants are not intended for use by those who are not informed about the accounting principles or auditing standards generally accepted in the Republic of China, and their applications in practice.

GCS HOLDINGS, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(EXPRESSED IN THOUSANDS OF NEW TAIWAN DOLLARS)

| Assets | Notes | December 31, 2018 | | December 31, 2017 | | |
|---------------------------|--|-------------------|---------------------|-------------------|---------------------|------------|
| | | AMOUNT | % | AMOUNT | % | |
| Current assets | | | | | | |
| 1100 | Cash and cash equivalents | 6(1) | \$ 1,512,863 | 44 | \$ 1,119,712 | 38 |
| 1150 | Notes receivable, net | | 127 | - | 594 | - |
| 1170 | Accounts receivable, net | 6(2) | 212,806 | 6 | 296,921 | 10 |
| 1200 | Other receivables | | 19,026 | 1 | 15,254 | - |
| 1220 | Current income tax assets | | 28,459 | 1 | 1,791 | - |
| 130X | Inventories | 6(3) | 330,694 | 10 | 329,834 | 11 |
| 1410 | Prepayments | | 14,813 | - | 7,590 | - |
| 1470 | Other current assets | 8 | 92,571 | 3 | 29,760 | 1 |
| 11XX | Total current assets | | <u>2,211,359</u> | <u>65</u> | <u>1,801,456</u> | <u>60</u> |
| Non-current assets | | | | | | |
| 1550 | Investment accounted for using equity method | 6(4) | - | - | 14,520 | - |
| 1600 | Property, plant and equipment | 6(5) and 8 | 723,641 | 21 | 700,655 | 24 |
| 1780 | Intangible assets | 6(6)(27) | 185,489 | 6 | 183,654 | 6 |
| 1840 | Deferred income tax assets | 6(25) | 171,323 | 5 | 164,924 | 6 |
| 1900 | Other non-current assets | 6(7) and 8 | 110,472 | 3 | 116,146 | 4 |
| 15XX | Total non-current assets | | <u>1,190,925</u> | <u>35</u> | <u>1,179,899</u> | <u>40</u> |
| 1XXX | Total assets | | <u>\$ 3,402,284</u> | <u>100</u> | <u>\$ 2,981,355</u> | <u>100</u> |

(Continued)

GCS HOLDINGS, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(EXPRESSED IN THOUSANDS OF NEW TAIWAN DOLLARS)

| Liabilities and Equity | | Notes | December 31, 2018 | | December 31, 2017 | |
|---|---|-----------|---------------------|------------|---------------------|------------|
| | | | AMOUNT | % | AMOUNT | % |
| Current liabilities | | | | | | |
| 2100 | Short-term borrowings | 6(8) | \$ 20,300 | 1 | \$ 20,000 | 1 |
| 2120 | Financial liabilities at fair value through profit or loss, current | 6(9) | - | - | 31,204 | 1 |
| 2130 | Current contract liabilities | 6(20) | 16,302 | - | - | - |
| 2170 | Accounts payable | | 19,423 | - | 17,867 | - |
| 2200 | Other payables | 6(12) | 164,280 | 5 | 139,249 | 5 |
| 2230 | Current income tax liabilities | | - | - | 2,469 | - |
| 2320 | Long-term borrowings, current portion | 6(10)(11) | 20,818 | 1 | 79,372 | 3 |
| 2399 | Other current liabilities | 6(13) | 6,185 | - | 33,498 | 1 |
| 21XX | Total current liabilities | | <u>247,308</u> | <u>7</u> | <u>323,659</u> | <u>11</u> |
| Non-current liabilities | | | | | | |
| 2540 | Long-term borrowings | 6(11) | 57,424 | 2 | 75,797 | 3 |
| 2570 | Deferred income tax liabilities | 6(25) | 84,451 | 2 | 39,466 | 1 |
| 2600 | Other non-current liabilities | 6(13) | 316 | - | 4,864 | - |
| 25XX | Total non-current liabilities | | <u>142,191</u> | <u>4</u> | <u>120,127</u> | <u>4</u> |
| 2XXX | Total liabilities | | <u>389,499</u> | <u>11</u> | <u>443,786</u> | <u>15</u> |
| Equity | | | | | | |
| Equity attributable to owners of the parent | | | | | | |
| Share capital | | | | | | |
| 3110 | Common stock | 6(16) | 821,691 | 24 | 804,389 | 27 |
| Capital surplus | | | | | | |
| 3200 | Capital surplus | 6(17) | 1,092,635 | 32 | 958,751 | 32 |
| Retained earnings | | | | | | |
| 3320 | Special reserve | 6(18) | 6,821 | - | 6,821 | - |
| 3350 | Unappropriated retained earnings | | 1,143,944 | 34 | 902,702 | 30 |
| Other equity interest | | | | | | |
| 3400 | Other equity interest | 6(19) | 27,805 | 1 | (44,224) | (1) |
| 3500 | Treasury stocks | 6(16) | (90,870) | (3) | (90,870) | (3) |
| 31XX | Equity attributable to owners of the parent | | <u>3,002,026</u> | <u>88</u> | <u>2,537,569</u> | <u>85</u> |
| 36XX | Non-controlling interest | 6(27) | <u>10,759</u> | <u>1</u> | <u>-</u> | <u>-</u> |
| 3XXX | Total equity | | <u>3,012,785</u> | <u>89</u> | <u>2,537,569</u> | <u>85</u> |
| Significant contingent liabilities and unrecognised contract commitments | | | | | | |
| Significant events after the reporting period | | | | | | |
| 3X2X | Total liabilities and equity | | <u>\$ 3,402,284</u> | <u>100</u> | <u>\$ 2,981,355</u> | <u>100</u> |

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

GCS HOLDINGS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(EXPRESSED IN THOUSANDS OF NEW TAIWAN DOLLARS, EXCEPT FOR EARNINGS PER SHARE)

| Items | Notes | Year ended December 31 | | | |
|-------|-------|------------------------|---|--------|---|
| | | 2018 | | 2017 | |
| | | AMOUNT | % | AMOUNT | % |
| 4000 | | | | | |
| 5000 | | | | | |
| 5900 | | | | | |
| | | | | | |
| 6100 | | | | | |
| 6200 | | | | | |
| 6300 | | | | | |
| 6450 | | | | | |
| 6000 | | | | | |
| 6900 | | | | | |
| 7010 | | | | | |
| 7020 | | | | | |
| 7050 | | | | | |
| 7060 | | | | | |
| 7000 | | | | | |
| 7900 | | | | | |
| 7950 | | | | | |
| 8200 | | | | | |
| | | | | | |
| 8361 | | | | | |
| | | | | | |
| 8362 | | | | | |
| 8399 | | | | | |
| 8300 | | | | | |
| 8500 | | | | | |
| 8610 | | | | | |
| 8620 | | | | | |
| | | | | | |
| 8710 | | | | | |
| 8720 | | | | | |
| | | | | | |
| 9750 | | | | | |
| 9850 | | | | | |

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

GCS HOLDINGS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY
(EXPRESSED IN THOUSANDS OF NEW TAIWAN DOLLARS)

| | Notes | Equity Attributable to Owners of The Parent | | | | | | | Non-Controlling Interest | Total Equity | |
|--|-------------------|---|-----------------|-----------------------|----------------------------------|--|-----------------|-----------|--------------------------|--------------|---|
| | | Retained Earnings | | Other Equity Interest | | | Treasury Stocks | Total | | | |
| | | Common stock | Capital Surplus | Special Reserve | Unappropriated Retained Earnings | Financial Statements Translation Differences of Foreign Operations | | | | | Unrealized Gain (Loss) on Available-for-Sale Financial Assets |
| 2017 | | | | | | | | | | | |
| Balance at January 1, 2017 | | \$ 744,023 | \$ 644,626 | \$ 6,821 | \$ 618,930 | \$ 122,002 | \$ 14,166 | \$ 3,548 | \$ 77,915 | \$ 2,069,105 | \$ 2,069,105 |
| Consolidated net income for 2017 | | - | - | - | 357,047 | - | - | - | - | 357,047 | 357,047 |
| Other comprehensive loss for 2017 | 6(19) | - | - | - | - | (157,466) | (14,166) | - | - | (171,632) | (171,632) |
| Total comprehensive income (loss) for 2017 | | - | - | - | 357,047 | (157,466) | (14,166) | - | - | 185,415 | 185,415 |
| Distribution of 2016 earnings: | | | | | | | | | | | |
| Cash dividends | 6(18) | - | - | - | (73,275) | - | - | - | - | (73,275) | (73,275) |
| Compensation costs of share-based payment | 6(15)(17)(19) | - | - | - | - | - | - | 7,446 | - | 7,446 | 7,446 |
| Issuance of restricted stocks to employees | 6(15)(16)(17)(19) | 1,800 | 11,562 | - | - | - | - | (13,368) | - | 6 | 6 |
| Retirement of restricted stocks to employees | 6(16)(17)(19) | (110) | (600) | - | - | - | - | 710 | - | - | - |
| Exercise of employee stock options | 6(15)(16)(17) | - | - | - | - | - | - | - | - | - | - |
| Conversion of convertible bonds | 6(16)(17) | 4,186 | 7,775 | - | - | - | - | - | - | 11,961 | 11,961 |
| Purchase of treasury stocks | 6(16) | 54,490 | 276,940 | - | - | - | - | - | (12,955) | 331,430 | 331,430 |
| Balance at December 31, 2017 | | \$ 804,389 | \$ 958,751 | \$ 6,821 | \$ 902,702 | \$ 35,464 | \$ 8,760 | \$ 8,760 | \$ 90,870 | \$ 2,537,569 | \$ 2,537,569 |
| 2018 | | | | | | | | | | | |
| Balance at January 1, 2018 | | \$ 804,389 | \$ 958,751 | \$ 6,821 | \$ 902,702 | \$ 35,464 | \$ 8,760 | \$ 8,760 | \$ 90,870 | \$ 2,537,569 | \$ 2,537,569 |
| Consolidated net income for 2018 | | - | - | - | 320,302 | - | - | - | - | 320,302 | 320,302 |
| Other comprehensive income for 2018 | 6(19) | - | - | - | - | 78,469 | - | - | - | 78,469 | 78,469 |
| Total comprehensive income (loss) for 2018 | | - | - | - | 320,302 | 78,469 | - | - | - | 398,771 | 398,771 |
| Distribution of 2017 earnings: | | | | | | | | | | | |
| Cash dividends | 6(18) | - | - | - | (79,060) | - | - | - | - | (79,060) | (79,060) |
| Compensation costs of share-based payment | 6(15)(17)(19) | - | - | - | - | - | - | 28,928 | - | 28,928 | 28,928 |
| Issuance of restricted stocks to employees | 6(15)(16)(17)(19) | 4,260 | 31,500 | - | - | - | - | (35,760) | - | - | - |
| Retirement of restricted stocks to employees | 6(16)(17)(19) | (50) | (342) | - | - | - | - | 392 | - | - | - |
| Exercise of employee stock options | 6(15)(16)(17) | 2,231 | 3,736 | - | - | - | - | - | - | 5,967 | 5,967 |
| Conversion of convertible bonds | 6(16)(17) | 10,861 | 78,300 | - | - | - | - | - | - | 89,161 | 89,161 |
| Non-controlling interest-acquisition of a subsidiary | 6(27) | - | - | - | - | - | - | - | - | - | - |
| Balance at December 31, 2018 | | \$ 821,691 | \$ 1,092,635 | \$ 6,821 | \$ 1,143,944 | \$ 43,005 | \$ 15,200 | \$ 15,200 | \$ 90,870 | \$ 3,002,026 | \$ 3,012,785 |

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

GCS HOLDINGS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(EXPRESSED IN THOUSANDS OF NEW TAIWAN DOLLARS)

| | Notes | Years ended December 31, | |
|--|-----------|--------------------------|---------------------|
| | | 2018 | 2017 |
| CASH FLOWS FROM OPERATING ACTIVITIES | | | |
| Profit before tax | | \$ 391,014 | \$ 424,053 |
| Adjustments | | | |
| Adjustments to reconcile profit (loss) | | | |
| Bad debt expense | 12(4) | - | 1,117 |
| Net impairment (income) loss on financial assets | 12(2) | (515) | - |
| Depreciation | 6(5)(23) | 113,693 | 81,824 |
| Amortisation | 6(6)(23) | 5,489 | 8,102 |
| Interest expense | 6(22) | 5,137 | 21,690 |
| Interest income | | (5,988) | (3,647) |
| Compensation cost of share-based payment | 6(15) | 49,618 | 25,894 |
| Net (gain) loss on financial liabilities at fair value through profit or loss | 6(9)(21) | (2,322) | 8,985 |
| Gain on disposal of property, plant and equipment | 6(21) | - | (456) |
| Gain on disposal of investments | 12(4) | - | (29,276) |
| Share of net loss of associates and joint ventures accounted for using equity method | 6(4) | 756 | 746 |
| Changes in operating assets and liabilities | | | |
| Changes in operating assets | | | |
| Notes receivable | | 467 | (594) |
| Accounts receivable | | 91,849 | (52,914) |
| Other receivables | | (3,232) | (3,046) |
| Inventories | | 8,534 | 63,948 |
| Prepayments | | (1,584) | 3,616 |
| Changes in operating liabilities | | | |
| Contract liabilities | | (8,467) | - |
| Accounts payable | | 1,066 | (2,750) |
| Other payables | | (742) | (5,335) |
| Other current liabilities | | (1,662) | 4,073 |
| Cash inflow generated from operations | | 643,111 | 546,030 |
| Interest received | | 5,989 | 3,594 |
| Interest paid | | (4,367) | (5,629) |
| Income tax paid | | (61,134) | (60,973) |
| Net cash flows from operating activities | | <u>583,599</u> | <u>483,022</u> |
| CASH FLOWS FROM INVESTING ACTIVITIES | | | |
| Acquisition of investment accounted for using equity method | 6(4) | - | (14,906) |
| Acquisition of property, plant and equipment | 6(29) | (155,995) | (197,225) |
| Proceeds from disposal of property, plant and equipment | | 35 | 456 |
| Acquisition of intangible assets | 6(6) | (5,197) | (1,450) |
| Acquisition of a subsidiary | 6(27) | (2,442) | (395,070) |
| Proceeds from disposal of available-for-sale financial assets | | - | 36,883 |
| Decrease in refundable deposits | | - | 5 |
| Increase in other current assets | | (404) | (30,430) |
| Decrease in other non-current assets | | 47 | - |
| Cash inflows from business combination | 6(27) | 27,263 | - |
| Net cash flows used in investing activities | | (136,693) | (601,737) |
| CASH FLOWS FROM FINANCING ACTIVITIES | | | |
| Increase in prepayments | | (5,792) | - |
| Proceeds from short-term borrowings | | 20,300 | 20,000 |
| Repayments of short-term borrowings | | (20,000) | - |
| Repayments of bonds payable | 6(10)(30) | (2,800) | - |
| Repayments of long-term borrowings | 6(30) | (19,621) | (19,017) |
| Payments of cash dividends | 6(29) | (79,060) | (73,275) |
| Proceeds from exercise of employee stock options | | 5,967 | 11,961 |
| Treasury stocks repurchased | | - | (12,955) |
| Net cash flows used in financing activities | | (101,006) | (73,286) |
| Effect of changes in exchange rates | | 47,251 | (70,181) |
| Net increase (decrease) in cash and cash equivalents | | 393,151 | (262,182) |
| Cash and cash equivalents at beginning of year | 6(1) | 1,119,712 | 1,381,894 |
| Cash and cash equivalents at end of year | 6(1) | <u>\$ 1,512,863</u> | <u>\$ 1,119,712</u> |

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

GCS HOLDINGS, INC. AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2018 AND 2017
(EXPRESSED IN THOUSANDS OF NEW TAIWAN DOLLARS,
EXCEPT AS OTHERWISE INDICATED)

1. HISTORY AND ORGANISATION

GCS Holdings Inc. (the “Company”) was incorporated in the Cayman Islands on November 30, 2010, as a holding company for the purpose of registering its shares with the Taipei Exchange. The Company was approved by the Financial Supervisory Commission to be listed on the Taipei Exchange. The Company's common shares have been traded on the Taipei Exchange since September 15, 2014.

The Company and subsidiaries (collectively referred herein as the “Group”) are engaged in the manufacturing of compound semiconductor wafer and foundry related services as well as licensing of intellectual property. The Company and its subsidiaries are also engaged in the research, development, manufacture and sales of advanced optoelectronics technology products.

2. THE DATE OF AUTHORIZATION FOR ISSUANCE OF THE CONSOLIDATED FINANCIAL STATEMENTS AND PROCEDURES FOR AUTHORISATION

These consolidated financial statements were authorized for issuance by the Board of Directors on March 15, 2019.

3. APPLICATION OF NEW STANDARDS, AMENDMENTS AND INTERPRETATIONS

(1) Effect of the adoption of new issuances of or amendments to International Financial Reporting Standards (“IFRSs”) as endorsed by the Financial Supervisory Commission (“FSC”)

New standards, interpretations and amendments endorsed by FSC effective from 2018 are as follows:

| New Standards, Interpretations and Amendments | Effective date by International Accounting Standards Board (“IASB”) |
|---|---|
| Amendments to IFRS 2, ‘Classification and measurement of share-based payment transactions’ | January 1, 2018 |
| Amendments to IFRS 4, ‘Applying IFRS 9, Financial instruments with IFRS 4, Insurance contracts’ | January 1, 2018 |
| IFRS 9, ‘Financial instruments’ | January 1, 2018 |
| IFRS 15, ‘Revenue from contracts with customers’ | January 1, 2018 |
| Amendments to IFRS 15, ‘Clarifications to IFRS 15, Revenue from contracts with customers’ | January 1, 2018 |
| Amendments to International Accounting Standards (“IASs”) 7, ‘Disclosure initiative’ | January 1, 2017 |

| New Standards, Interpretations and Amendments | Effective date by IASB |
|---|------------------------|
| Amendments to IAS 12, 'Recognition of deferred tax assets for unrealised losses' | January 1, 2017 |
| Amendments to IAS 40, 'Transfers of investment property' | January 1, 2018 |
| International Financial Reporting Interpretations Committee ("IFRICs") 22, 'Foreign currency transactions and advance consideration' | January 1, 2018 |
| Annual improvements to IFRSs 2014-2016 cycle - Amendments to IFRS 1, 'First-time adoption of International Financial Reporting Standards' | January 1, 2018 |
| Annual improvements to IFRSs 2014-2016 cycle - Amendments to IFRS 12, 'Disclosure of interests in other entities' | January 1, 2017 |
| Annual improvements to IFRSs 2014-2016 cycle - Amendments to IAS 28, 'Investments in associates and joint ventures' | January 1, 2018 |

Except for the following, the above standards and interpretations have no significant impact to the Group's financial condition and financial performance based on the Group's assessment.

A. IFRS 9, 'Financial instruments' ("IFRS 9")

- (a) Classification of debt instruments is driven by the entity's business model and the contractual cash flow characteristics of the financial assets, which would be classified as financial asset at fair value through profit or loss, financial asset measured at fair value through other comprehensive income or financial asset at amortized cost. Equity instruments would be classified as financial asset at fair value through profit or loss, unless an entity makes an irrevocable election at inception to present in other comprehensive income subsequent changes in the fair value of an investment in an equity instrument that is not held for trading.
- (b) The impairment losses of debt instruments are assessed using an 'expected credit loss' approach. An entity assesses at each balance sheet date whether there has been a significant increase in credit risk on that instrument since initial recognition to recognize 12-month expected credit losses or lifetime expected credit losses (interest revenue would be calculated on the gross carrying amount of the asset before impairment losses occurred); or if the instrument that has objective evidence of impairment, interest revenue after the impairment would be calculated on the book value of net carrying amount (i.e., net of credit allowance). The Group shall always measure the loss allowance at an amount equal to lifetime expected credit losses for trade receivables that do not contain a significant financing component.
- (c) The Group has elected not to restate prior period financial statements using the modified retrospective approach under IFRS 9. Since the Group does not hold any debt instruments or equity instruments, the application of this requirement is not expected to materially impact the Group's financial condition and financial performance. Further, the Group has a completed assessment in respect of the expected credit loss for trade receivables under IFRS 9, and the application of this requirement has no material impact on the Group's accounts receivable and unappropriated retained earnings as of January 1, 2018.

B. IFRS 15, 'Revenue from contracts with customers' ("IFRS 15") and amendments

- (a) IFRS 15, 'Revenue from contracts with customers' replaces IAS 11, 'Construction contracts', IAS 18, 'Revenue' and relevant interpretations. According to IFRS 15, revenue is recognized when a customer obtains control of promised goods or services. A customer obtains control of goods or services when a customer has the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset.

The core principle of IFRS 15 is that an entity recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. An entity recognizes revenue in accordance with that core principle by applying the following steps:

Step 1: Identify contracts with customer.

Step 2: Identify separate performance obligations in the contract(s).

Step 3: Determine the transaction price.

Step 4: Allocate the transaction price.

Step 5: Recognize revenue when the performance obligation is satisfied.

Further, IFRS 15 includes a set of comprehensive disclosure requirements that requires an entity to disclose sufficient information to enable users of financial statements to understand the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers.

- (b) The Group has elected not to restate prior period financial statements and recognized the cumulative effect of initial application as retained earnings at January 1, 2018, using the modified retrospective approach under IFRS 15. In line with the regulations of IFRS 15, the Group changed the presentation of certain accounts in the balance sheets as of January 1, 2018 as follows:
- i. Under IFRS 15, refund liabilities in relation to expected sales discounts and allowances were previously presented as accounts receivable - allowance for sales discounts in the balance sheet. As of January 1, 2018, the balance amounted to \$888.
 - ii. Under IFRS 15, liabilities in relation to contracts with customers are recognized as contract liabilities, but were previously presented as advance sales receipts in the balance sheet. As of January 1, 2018, the balance amounted to \$24,149.
- (c) Please refer to Note 12(5) for other disclosures in relation to the first application of IFRS 15.

C. Amendments to IAS 7, 'Disclosure initiative'

This amendment requires that an entity shall provide more disclosures related to changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes.

Please refer to Note 6(30) for additional disclosures to explain the changes in liabilities arising from financing activities.

(2) Effect of new issuances of or amendments to IFRSs as endorsed by the FSC but not yet adopted by the Group

New standards, interpretations and amendments endorsed by the FSC effective from 2019 are as follows:

| New Standards, Interpretations and Amendments | Effective date by IASB |
|--|------------------------|
| Amendments to IFRS 9, 'Prepayment features with negative compensation' | January 1, 2019 |
| IFRS 16, 'Leases' | January 1, 2019 |
| Amendments to IAS 19, 'Plan amendment, curtailment or settlement' | January 1, 2019 |
| Amendments to IAS 28, 'Long-term interests in associates and joint ventures' | January 1, 2019 |
| IFRIC 23, 'Uncertainty over income tax treatments' | January 1, 2019 |
| Annual improvements to IFRSs 2015-2017 cycle | January 1, 2019 |

Except for the following, the above standards and interpretations have no significant impact to the Group's financial condition and financial performance based on the Group's assessment.

IFRS 16, 'Leases'

IFRS 16, 'Leases', replaces IAS 17, 'Leases' and related interpretations and Standing Interpretations Committee ("SICs"). The standard requires lessees to recognize a 'right-of-use asset' and a 'lease liability' (except for those leases with terms of 12 months or less and leases of low-value assets). The accounting stays the same for lessors, which is to classify their leases as either finance leases or operating leases and account for those two types of leases differently. IFRS 16 only requires enhanced disclosures to be provided by lessors.

The Group expects to recognize the lease contract of lessees in line with IFRS 16. However, the Group does not intend to restate the financial statements of prior period, and on January 1, 2019, it is expected that 'right-of-use asset' and 'lease liability' will be increased by \$38,722 and \$38,722, respectively.

(3) IFRSs issued by IASB but not yet endorsed by the FSC

New standards, interpretations and amendments issued by IASB but not yet included in the IFRSs as endorsed by the FSC are as follows:

| New Standards, Interpretations and Amendments | Effective date by IASB |
|---|--------------------------|
| Amendment to IAS 1 and IAS 8, 'Disclosure Initiative-Definition of Material' | January 1, 2020 |
| Amendments to IFRS 3, 'Definition of a business' | January 1, 2020 |
| Amendments to IFRS 10 and IAS 28, 'Sale or contribution of assets between an investor and its associate or joint venture' | To be determined by IASB |
| IFRS 17, 'Insurance contracts' | January 1, 2021 |

The above standards and interpretations have no significant impact to the Group's financial condition and financial performance based on the Group's assessment.

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the periods presented, unless otherwise stated.

(1) Compliance statement

The consolidated financial statements of the Group have been prepared in accordance with the “Regulations Governing the Preparations of Financial Reports by Securities Issuers”, International Financial Reporting Standards, International Accounting Standards, IFRIC Interpretations, and SIC Interpretations as endorsed by the FSC (collectively referred herein as the “IFRSs”).

(2) Basis of preparation

- A. Except for the financial liabilities at fair value through profit or loss and available-for-sale financial assets measured at fair value, the consolidated financial statements have been prepared under the historical cost convention.
- B. The preparation of financial statements in conformity with IFRSs requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group’s accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 5.
- C. In adopting IFRS 9 and IFRS 15 effective January 1, 2018, the Group has elected to apply modified retrospective approach whereby the cumulative impact of the adoption was recognized as retained earnings or other equity as of January 1, 2018 and the financial statements for the year ended December 31, 2017 were not restated. The financial statements for the year ended December 31, 2017 were prepared in compliance with International Accounting Standard 39 (‘IAS 39’), International Accounting Standard 18 (‘IAS 18’) and related financial reporting interpretations. Please refer to Notes 12(4) and (5) for details of significant accounting policies and details of significant accounts.

(3) Basis of consolidation

A. Basis for preparation of consolidated financial statements:

- (a) All subsidiaries are included in the Group’s consolidated financial statements. Subsidiaries are all entities (including structured entities) controlled by the Group. The Group controls an entity when the Group is exposed, or has rights, to variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. Consolidation of subsidiaries begins from the date the Group obtains control of the subsidiaries and ceases when the Group loses control of the subsidiaries.
- (b) Inter-company transactions, balances and unrealized gains or losses on transactions between companies within the Group are eliminated. Accounting policies of subsidiaries have been adjusted where necessary to ensure consistency with the policies adopted by the Group.

B. Subsidiaries included in the consolidated financial statements:

| Name of investor | Name of subsidiary | Main business activities | Ownership (%) | | Note |
|--|--|--|-------------------|-------------------|--------|
| | | | December 31, 2018 | December 31, 2017 | |
| The Company | Global Communication Semiconductors, LLC | 1. Manufacturing of compound semiconductor wafer and foundry related services as well as granting royalty rights for intellectual property 2. Manufacturing and selling of advanced optoelectronics technology products | 100 | 100 | - |
| The Company | GCS Device Technologies, Co., Ltd. | Product design and research development services | 100 | 100 | - |
| The Company | Xiamen Global Advanced Semiconductor Co., Ltd. | Developing, manufacturing and selling of mobile phone radio frequency, filter, optical communication chip, power management and optical fiber | 51 | - | (Note) |
| Global Communication Semiconductors, LLC | D-Tech Optoelectronics, Inc. | Developing, manufacturing and selling of positive, intrinsic, negative components and avalanche photo diodes for telecommunication systems and data communication networks | 100 | 100 | - |
| D-Tech Optoelectronics, Inc. | D-Tech Optoelectronics (Taiwan) Corporation | Manufacturing and selling of optical chips | 100 | 100 | - |

Note: The Group completed the acquisition of an additional 2% shareholding of Xiamen Global Advanced Semiconductor Co., Ltd. ('Xiamen Global') in September 2018. Through the completion of the acquisition, the Group has obtained control over Xiamen Global, therefore, Xiamen Global was included in the Group's consolidated financial statements.

C. Subsidiaries not included in the consolidated financial statements: None.

D. Adjustments for subsidiaries with different balance sheet dates: None.

E. Significant restrictions: None.

F. Subsidiaries that have non-controlling interests that are material to the Group: None.

(4) Foreign currency translation

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). The Company's functional currency is United States dollars; however, the consolidated financial statements are presented in New Taiwan dollars in accordance with the regulations of the country where the consolidated financial statements are reported to the regulatory authorities.

A. Foreign currency transactions and balances

(a) Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions or valuation where items are remeasured. Foreign exchange gains and losses resulting from the settlement of such transactions are recognized in profit or loss in the period in which they arise.

(b) Monetary assets and liabilities denominated in foreign currencies at the period end are re-translated at the exchange rates prevailing at the balance sheet date. Exchange differences

arising upon re-translation at the balance sheet date are recognized in profit or loss.

- (c) Non-monetary assets and liabilities denominated in foreign currencies held at fair value through profit or loss are re-translated at the exchange rates prevailing at the balance sheet date; their translation differences are recognized in profit or loss. Non-monetary assets and liabilities denominated in foreign currencies held at fair value through other comprehensive income are re-translated at the exchange rates prevailing at the balance sheet date; their translation differences are recognized in other comprehensive income. However, non-monetary assets and liabilities denominated in foreign currencies that are not measured at fair value are translated using the historical exchange rates at the dates of the initial transactions.
- (d) All foreign exchange gains and losses are presented in the statement of comprehensive income within 'other gains and losses'.

B. Translation of foreign operations

The operating results and financial position of all the group entities that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- (a) Assets and liabilities for each balance sheet presented are translated at the closing exchange rate at the date of that balance sheet;
- (b) Income and expenses for each statement of comprehensive income are translated at average exchange rates of that period; and
- (c) All resulting exchange differences are recognized in other comprehensive income.

(5) Classification of current and non-current items

- A. Assets that meet one of the following criteria are classified as current assets; otherwise they are classified as non-current assets:
 - (a) Assets arising from operating activities that are expected to be realized, or are intended to be sold or consumed within the normal operating cycle;
 - (b) Assets held mainly for trading purposes;
 - (c) Assets that are expected to be realized within twelve months from the balance sheet date;
 - (d) Cash and cash equivalents, excluding restricted cash and cash equivalents and those that are to be exchanged or used to settle liabilities more than twelve months after the balance sheet date.
- B. Liabilities that meet one of the following criteria are classified as current liabilities; otherwise they are classified as non-current liabilities:
 - (a) Liabilities that are expected to be settled within the normal operating cycle;
 - (b) Liabilities arising mainly from trading activities;
 - (c) Liabilities that are to be settled within twelve months from the balance sheet date;
 - (d) Liabilities for which the repayment date cannot be extended unconditionally to more than twelve months after the balance sheet date. Terms of a liability that could, at the option of the counterparty, result in its settlement by the issue of equity instruments do not affect its classification.

(6) Cash equivalents

Cash equivalents refer to short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

(7) Accounts and notes receivable

- A. In accordance with contracts, accounts and notes receivable entitle the Group a legal right to receive consideration in exchange for transferred goods or rendered services.

B. The short-term accounts and notes receivable without bearing interest are subsequently measured at initial invoice amount as the effect of discounting is immaterial.

(8) Impairment of financial assets

For financial assets at amortized cost, at each reporting date, the Group recognizes the impairment provision for 12 months expected credit losses if there has not been a significant increase in credit risk since initial recognition or recognizes the impairment provision for the lifetime expected credit losses (ECLs) if such credit risk has increased since initial recognition after taking into consideration all reasonable and verifiable information that includes forecasts. On the other hand, for accounts receivable that do not contain a significant financing component, the Group recognizes the impairment provision for lifetime ECLs.

(9) Derecognition of financial assets

The Group derecognizes a financial asset when the contractual rights to receive the cash flows from the financial asset expire.

(10) Inventories

Inventories are stated at the lower of cost and net realizable value. Cost is determined using the first-in, first-out (FIFO) method. The cost of finished goods and work in process comprises raw materials, direct labor, other direct costs and related production overheads (allocated based on normal operating capacity). It excludes borrowing costs. The item by item approach is used in applying the lower of cost and net realizable value. Net realizable value is the estimated selling price in the ordinary course of business, less the estimated cost of completion and applicable variable selling expenses.

(11) Investment accounted for using equity method- joint ventures

The Group accounts for its interest in a joint venture using equity method. Unrealized profits and losses arising from the transactions between the Group and its joint venture are eliminated to the extent of the Group's interest in the joint venture. However, when the investment has objective evidence of a reduction in the net realisable value of current assets or an impairment loss, all such losses shall be recognized immediately. When the Group's share of losses in a joint venture equals or exceeds its interest in the joint venture together with any other unsecured receivables, the Group does not recognise further losses, unless it has incurred legal or constructive obligations or made payments on behalf of the joint venture.

(12) Property, plant and equipment

- A. Property, plant and equipment are initially recorded at cost. Borrowing costs incurred during the construction period are capitalised.
- B. Subsequent costs are included in the asset's carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognized. All other repairs and maintenance are charged to profit or loss during the financial period in which they are incurred.
- C. Property, plant and equipment apply cost model. Land is not depreciated and other property, plant and equipment are depreciated using the straight-line method to allocate their cost over their estimated useful lives. Each significant part of an item of property, plant and equipment is required to be depreciated separately.
- D. The assets' residual values, useful lives and depreciation methods are reviewed, and adjusted if appropriate, at each balance sheet date. If expectations for the assets' residual values and useful

lives differ from previous estimates or the patterns of consumption of the assets' future economic benefits embodied in the assets have changed significantly, any change is accounted for as a change in estimate under IAS 8, 'Accounting Policies, Changes in Accounting Estimates and Errors', from the date of the change.

The estimated useful lives of property, plant and equipment are as follows:

| | |
|--------------------------------------|--------------|
| Buildings | 35 years |
| Machinery equipment | 2 ~7 years |
| Computer and communication equipment | 5 years |
| Research equipment | 5 ~7 years |
| Office equipment | 3 ~10 years |
| Leased assets | 7 years |
| Leasehold improvements | 3 ~ 15 years |

(13) Leased assets/leases (lessee)

A. Based on the terms of a lease contract, a lease is classified as a finance lease if the Group assumes substantially all the risks and rewards incidental to ownership of the leased asset.

(a) A finance lease is recognised as an asset and a liability at the lease's commencement at the lower of the fair value of the leased asset or the present value of the minimum lease payments.

(b) The minimum lease payments are apportioned between the finance charges and the reduction of the outstanding liability. The finance charges are allocated to each period over the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability.

(c) Property, plant and equipment held under finance leases are depreciated over their estimated useful lives. If there is no reasonable certainty that the Group will obtain ownership at the end of the lease, the asset shall be depreciated over the shorter of the lease term and its useful life.

B. An operating lease is a lease other than a finance lease. Payments made under an operating lease are recognized in profit or loss on a straight-line basis over the lease term.

(14) Intangible assets

A. Computer software

Computer software is stated at cost and amortized on a straight-line basis over its estimated useful life of 1 to 5 years.

B. Goodwill

Goodwill arises in a business combination accounted for by applying the acquisition method.

(15) Impairment of non-financial assets

A. The Group assesses at each balance sheet date the recoverable amounts of those assets where there is an indication that they are impaired. An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell or value in use. Except for goodwill, when the circumstances or reasons for recognizing impairment loss for an asset in prior years no longer exist, the impairment loss shall be reversed to the extent of the loss previously recognized in profit or loss.

- B. The recoverable amounts of goodwill, intangible assets with an indefinite useful life and intangible assets that have not yet been available for use are evaluated periodically. An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. Impairment loss of goodwill previously recognized in profit or loss shall not be reversed in the following years.
- C. For the purpose of impairment testing, goodwill is allocated to each of the cash-generating units, or groups of cash-generating units, that is/are expected to benefit from the synergies of the business combination.

(16) Borrowings

Borrowings are recognized initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognized in profit or loss over the period of the borrowings using the effective interest method.

(17) Notes and accounts payable

- A. Accounts payable are liabilities for purchases of raw materials, goods or services and notes payable are those resulting from operating and non-operating activities.
- B. The short-term notes and accounts payable without bearing interest are subsequently measured at initial invoice amount as the effect of discounting is immaterial.

(18) Convertible bonds payable

Bonds payable

Convertible corporate bonds issued by the Company contain conversion options (that is, the bondholders have the right to convert the bonds into the Company's common shares by exchanging a fixed amount of cash for a fixed number of common shares), call options and put options. The Company classifies the bonds payable and derivative features embedded in convertible corporate bonds on initial recognition as a financial asset, a financial liability or an equity instrument ('capital surplus-stock warrants') in accordance with the substance of the contractual arrangement and the definitions of a financial asset, a financial liability and an equity instrument. Convertible corporate bonds are accounted for as follows:

- (a) Call options and put options embedded in convertible corporate bonds are recognized initially at net fair value as 'financial assets or financial liabilities at fair value through profit or loss'. They are subsequently remeasured and stated at fair value on each balance sheet date; the gain or loss is recognized as 'gain or loss on valuation of financial assets or financial liabilities at fair value through profit or loss'.
- (b) Bonds payable of convertible corporate bonds is initially recognized at fair value and subsequently stated at amortized cost. Any difference between the proceeds and the redemption value is accounted for as the premium or discount on bonds payable and presented as an addition to or deduction from bonds payable, which is amortized in profit or loss as an adjustment to the 'finance costs' over the period of bond circulation using the effective interest method.
- (c) Any transaction costs directly attributable to the issuance of convertible corporate bonds are allocated to the liability and equity components in proportion to the allocation of proceeds.
- (d) When bondholders exercise conversion options, the liability component of the bonds (including 'bonds payable and 'financial assets or financial liabilities at fair value through profit or loss') shall be remeasured on the conversion date. The book value of common shares issued due to the conversion shall be based on the adjusted book value of the abovementioned liability component.

(19) Derecognition of financial liabilities

A financial liability is derecognized when the obligation under the liability specified in the contract is discharged or cancelled or expires.

(20) Employee benefits

A. Short-term employee benefits

Short-term employee benefits are measured at the undiscounted amount of the benefits expected to be paid in respect of service rendered by employees in a period and should be recognized as expense in that period when the employees render service.

B. Pensions

Defined contribution plans

For defined contribution plans, the contributions are recognized as pension expense when they are due on an accrual basis. Prepaid contributions are recognized as an asset to the extent of a cash refund or a reduction in the future payments.

C. Termination benefits

Termination benefits are employee benefits provided in exchange for the termination of employment as a result from either the Group's decision to terminate an employee's employment before the normal retirement date, or an employee's decision to accept an offer of redundancy benefits in exchange for the termination of employment. The Group recognizes termination benefits when it is demonstrably committed to a termination, when it has a detailed formal plan to terminate the employment of current employees and when it can no longer withdraw the plan.

D. Employees' compensation and directors' remuneration

Employees' compensation and directors' remuneration are recognized as expense and liability, provided that such recognition is required under legal or constructive obligation and those amounts can be reliably estimated. Any difference between the resolved amounts and the subsequently actual distributed amounts is accounted for as changes in estimates. If employee compensation is paid by shares, the Group calculates the number of shares based on the closing price at the previous day of the board meeting resolution.

(21) Employee share-based payment

A. For the equity-settled share-based payment arrangements, the employee services received are measured at the fair value of the equity instruments granted at the grant date, and are recognized as compensation cost over the vesting period, with a corresponding adjustment to equity. The fair value of the equity instruments granted shall reflect the impact of market vesting conditions and non-vesting conditions. Compensation cost is subject to adjustment based on the service conditions that are expected to be satisfied and the estimates of the number of equity instruments that are expected to vest under the non-market vesting conditions at each balance sheet date. Ultimately, the amount of compensation cost recognized is based on the number of equity instruments that eventually vest.

B. Restricted stocks

(a) Restricted stocks issued to employees are measured at the fair value of the equity instruments granted at the grant date, and are recognized as compensation cost over the vesting period.

- (b) For restricted stocks where those stocks do not restrict distribution of dividends to employees and employees are not required to return the dividends received if they resign during the vesting period, the Group recognizes the fair value of the dividends received by the employees who are expected to resign during the vesting period as compensation cost at the date of dividends declaration.

(22) Income tax

- A. The tax expense for the period comprises current and deferred tax. Tax is recognized in profit or loss, except to the extent that it relates to items recognized in other comprehensive income or items recognized directly in equity, in which cases the tax is recognized in other comprehensive income or equity.
- B. The current income tax expense is calculated on the basis of the tax laws enacted or substantively enacted at the balance sheet date in the countries where the Company and its subsidiaries operate and generate taxable income. Management periodically evaluates positions taken in tax returns with respect to situations in accordance with applicable tax regulations. It establishes provisions where appropriate based on the amounts expected to be paid to the tax authorities. An additional tax is levied on the unappropriated retained earnings and is recorded as income tax expense in the year the stockholders resolve to retain the earnings.
- C. Deferred tax is recognized, using the balance sheet liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated balance sheet. Deferred tax is provided on temporary differences arising on investments in subsidiaries, except where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred tax asset is realized or the deferred tax liability is settled.
- D. Deferred tax assets are recognized only to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilized. At each balance sheet date, unrecognized and recognized deferred tax assets are reassessed.
- E. Current income tax assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis or realize the asset and settle the liability simultaneously. Deferred tax assets and liabilities are offset on the balance sheet when the entity has the legally enforceable right to offset current tax assets against current tax liabilities and they are levied by the same taxation authority on either the same entity or different entities that intend to settle on a net basis or realize the asset and settle the liability simultaneously.
- F. If a change in tax rate is enacted or substantively enacted, the Group recognizes the effect of the change immediately in the period in which the change occurs. The effect of the change on items recognized outside profit or loss is recognized in other comprehensive income or equity while the effect of the change on items recognized in profit or loss is recognized in profit or loss.

(23) Share capital

- A. Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new shares or stock options are shown in equity as a deduction, net of tax, from the proceeds.
- B. Where the Company repurchases the Company's equity share capital that has been issued, the consideration paid, including any directly attributable incremental costs (net of income taxes) is deducted from equity attributable to the Company's equity holders. Where such shares are

subsequently reissued, the difference between their book value and any consideration received, net of any directly attributable incremental transaction costs and the related income tax effects, is included in equity attributable to the Company's equity holders.

(24) Dividends

Dividends are recorded in the Company's financial statements in the period in which they are approved by the Company's shareholders. Cash dividends are recorded as liabilities.

(25) Revenue recognition

Sales of goods

- (a) The Group engages in the manufacturing and selling of compound semiconductor wafer and advanced optoelectronics technology products. Sales are recognized when control of the products has transferred, being when the products are delivered to the customer and there is no unfulfilled obligation that could affect the customer's acceptance of the products. Delivery occurs when the products have been shipped to the specific location, the risks of obsolescence and loss have been transferred to the customer, and either the customer has accepted the products in accordance with the sales contract, or the Group has objective evidence that all criteria for acceptance have been satisfied.
- (b) Revenue from these sales is recognized based on the price specified in the contract. A refund liability is recognized for expected sales discounts and allowances payable to customers in relation to sales made through the end of the reporting period.
- (c) A receivable is recognized when the goods are delivered as this is the point in time that the consideration is unconditional because only the passage of time is required before the payment is due.

Service revenue

- (a) The Group provides transfer services of wafer manufacturing process to the customers. Revenue from providing services is recognized in the accounting period in which the services are rendered. For fixed-price contracts, revenue is recognized based on the actual service provided to the end of the reporting period as a proportion of the total services to be provided. This is determined based on the actual cost relative to the total expected cost. The customer pays at the time specified in the payment schedule. If the services rendered exceed the payment, a contract asset is recognized. If the payments exceed the services rendered, a contract liability is recognized.
- (b) Some contracts include multiple deliverables. As the services provided by the Group are highly correlated and not distinct, they are identified to be one performance obligation.
- (c) The Group's estimate about revenue, costs and progress towards completion of a performance obligation is subject to revision whenever there is a change in circumstances. Any increase or decrease in revenue or costs due to an estimate revision is reflected in profit or loss during the period when management becomes aware of the changes in circumstances.

Royalty revenue

Some contracts require sales-based royalty in exchange for a licence of intellectual property. The Group recognizes revenue when the performance obligation has been satisfied and the subsequent sale occurs.

Financing components

The Group does not expect to have any contracts where the period between the transfer of the promised goods or services to the customer and payment by the customer exceeds one year. As a

consequence, the Group does not adjust any of the transaction prices for the time value of money.

(26) Business combinations

- A. The Group uses the acquisition method to account for business combinations. The consideration transferred for an acquisition is measured as the fair value of the assets transferred, liabilities incurred or assumed and equity instruments issued at the acquisition date, plus the fair value of any assets and liabilities resulting from a contingent consideration arrangement. All acquisition-related costs are expensed as incurred. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. For each business combination, the Group measures at the acquisition date components of non-controlling interests in the acquiree that are present ownership interests and entitle their holders to the proportionate share of the entity's net assets in the event of liquidation at either fair value or the present ownership instruments' proportionate share in the recognised amounts of the acquiree's identifiable net assets. All other non-controlling interests should be measured at the acquisition-date fair value.
- B. The excess of the consideration transferred, the amount of any non-controlling interest in the acquiree and the fair value of any previous equity interest in the acquiree over the fair value of the identifiable assets acquired and the liabilities assumed is recorded as goodwill at the acquisition date. If the total of consideration transferred, non-controlling interest in the acquiree recognized and the fair value of previously held equity interest in the acquiree is less than the fair value of the identifiable assets acquired and the liabilities assumed, the difference is recognized directly in profit or loss on the acquisition date.

(27) Operating segments

Operating segments are reported in a manner consistent with the internal reporting provided to the Chief Operating Decision-Maker. The Group's Chief Operating Decision-Maker, who is responsible for allocating resources and assessing performance of the operating segments, has been identified as the Board of Directors that makes strategic decisions.

5. CRITICAL ACCOUNTING JUDGMENTS, ESTIMATES AND KEY SOURCES OF ASSUMPTION UNCERTAINTY

The preparation of these consolidated financial statements requires management to make critical judgements in applying the Group's accounting policies and make critical assumptions and estimates concerning future events. Assumptions and estimates may differ from the actual results and are continually evaluated and adjusted based on historical experience and other factors. Such assumptions and estimates have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year; and the related information is addressed below:

(1) Critical judgements in applying the Group's accounting policies

None.

(2) Critical accounting estimates and assumptions

The Group makes estimates and assumptions based on the expectation of future events that are believed to be reasonable under the circumstances at the end of the reporting period. The resulting accounting estimates might be different from the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are addressed below:

Evaluation of inventories

As inventories are stated at the lower of cost and net realizable value, the Group must determine the net realizable value of inventories on balance sheet date using judgements and estimates. Due to the rapid technology innovation, the Group evaluates the amounts of normal inventory consumption, obsolete inventories or inventories without market selling value on balance sheet date, and writes down the cost of inventories to the net realizable value. Such an evaluation of inventories is principally based on the selling prices of sales orders. Therefore, there might be material changes to the evaluation.

As of December 31, 2018, the carrying amount of inventories was \$330,694.

6. DETAILS OF SIGNIFICANT ACCOUNTS

(1) Cash and cash equivalents

| | <u>December 31, 2018</u> | <u>December 31, 2017</u> |
|---------------------------------------|--------------------------|--------------------------|
| Cash on hand | \$ 117 | \$ 117 |
| Checking accounts and demand deposits | 1,512,746 | 1,119,595 |
| | <u>\$ 1,512,863</u> | <u>\$ 1,119,712</u> |

A. The Group transacts with a variety of financial institutions with high credit quality to disperse credit risk and expects that the probability of counterparty default is remote.

B. The Group has no cash and cash equivalents pledged to others.

(2) Accounts receivable, net

| | <u>December 31, 2018</u> | <u>December 31, 2017</u> |
|---|--------------------------|--------------------------|
| Accounts receivable | \$ 213,433 | \$ 298,926 |
| Less: Allowance for doubtful accounts | (627) | (1,117) |
| Allowance for sales returns and discounts | - | (888) |
| | <u>\$ 212,806</u> | <u>\$ 296,921</u> |

Information relating to credit risk of accounts receivable is provided in Note 12(2).

(3) Inventories

| | <u>December 31, 2018</u> | | |
|------------------|--------------------------|--------------------|-------------------|
| | <u>Cost</u> | <u>Allowance</u> | <u>Book value</u> |
| Raw materials | \$ 145,388 | (\$ 31,297) | \$ 114,091 |
| Work in progress | 185,761 | (31,979) | 153,782 |
| Finished goods | 66,146 | (3,325) | 62,821 |
| | <u>\$ 397,295</u> | <u>(\$ 66,601)</u> | <u>\$ 330,694</u> |

| | December 31, 2017 | | |
|------------------|-------------------|--------------------|-------------------|
| | Cost | Allowance | Book value |
| Raw materials | \$ 146,696 | (\$ 33,957) | \$ 112,739 |
| Work in progress | 197,836 | (37,208) | 160,628 |
| Finished goods | 67,519 | (11,052) | 56,467 |
| | <u>\$ 412,051</u> | <u>(\$ 82,217)</u> | <u>\$ 329,834</u> |

Expenses and costs incurred as cost of operating revenue for the years ended December 31, 2018 and 2017 were as follows:

| | Years ended December 31, | |
|--|--------------------------|---------------------|
| | 2018 | 2017 |
| Cost of inventories sold | \$ 1,111,241 | \$ 1,056,375 |
| (Recovery of) loss on market price decline | (17,714) | 5,213 |
| Revenue from sale of scraps | (38,828) | (31,659) |
| | <u>\$ 1,054,699</u> | <u>\$ 1,029,929</u> |

The Group recognized recovery of loss on market price decline for the year ended December 31, 2018 because some of the inventories previously written down were sold.

(4) Investment accounted for using equity method

| | 2018 | 2017 |
|---|-------------|------------------|
| At January 1 | \$ 14,520 | \$ - |
| Acquisition of investment accounted for using equity method | - | 14,906 |
| Share of net loss of investment accounted for using equity method | (756) | (746) |
| Translation differences of foreign operation | (2,363) | 360 |
| Disposal of investment accounted for using equity method | (11,401) | - |
| At December 31 | <u>\$ -</u> | <u>\$ 14,520</u> |

A. The basic information of the joint venture that is material to the Group is as follows:

| Company name | Principal place of business | Shareholding ratio (Note) | | Nature of relationship | Method of measurement |
|--------------|--------------------------------|---|--|---------------------------|--------------------------|
| | | December 31, 2018 | December 31, 2017 | | |
| | | Xiamen Global Advanced Semiconductor Co., Ltd. | Xiamen City, Fujian Province, China | | |

Note: In September 2018, the Company obtained the control over Xiamen Global Advanced Semiconductor Co., Ltd, through acquisition of an additional 2% shareholding of Xiamen Global Advanced Semiconductor Co., Ltd in cash, and amendment of the original Joint Venture Agreement entered into with Xiamen San'an Integrated Circuit Co., Ltd. Please refer to Note 6(27).

B. The summarized financial information of the joint venture that is material to the Group is as follows:

Balance sheet

| | Xiamen Global Advanced Semiconductor Co., Ltd. | |
|--------------------------------------|---|-------------------|
| | December 31, 2018 | December 31, 2017 |
| Cash and cash equivalents | \$ - | \$ 29,642 |
| Current assets | - | 29,642 |
| Total assets | - | 29,642 |
| Other current liabilities | - | 10 |
| Current liabilities | - | 10 |
| Total liabilities | - | 10 |
| Total net assets | \$ - | \$ 29,632 |
| Share in joint venture's net assets | \$ - | \$ 14,520 |
| Carrying amount of the joint venture | \$ - | \$ 14,520 |

Statement of comprehensive income

| | Xiamen Global Advanced Semiconductor Co., Ltd. | |
|---------------------------------------|---|-----------------|
| | Years ended December 31, | |
| | 2018 (Note) | 2017 |
| Administrative expenses | \$ 2,324 | \$ 909 |
| Interest income | (39) | (26) |
| Net foreign exchange (gains) losses | (754) | 639 |
| Other losses | 12 | - |
| Net loss / total comprehensive loss | <u>\$ 1,543</u> | <u>\$ 1,522</u> |
| Dividends received from joint venture | <u>\$ -</u> | <u>\$ -</u> |

Note: Xiamen Global Advanced Semiconductor Co., Ltd, became a subsidiary of the Group in September 2018, and was included in the Group's consolidated financial statements from the date the Group obtained control over it. Please refer to Note 6(27) for details.

(5) Property, plant and equipment

| | Land | Buildings | Machinery equipment | Computer and communication equipment | Research equipment | Office equipment | Leased assets | Leasehold improvements | Total |
|---------------------------------------|-------------------|------------------|---------------------|--------------------------------------|--------------------|------------------|------------------|------------------------|-------------------|
| At January 1, 2018 | | | | | | | | | |
| Cost | \$ 137,045 | \$ 91,363 | \$ 1,020,035 | \$ 10,103 | \$ 116,587 | \$ 11,545 | \$ 41,826 | \$ 292,911 | \$ 1,721,415 |
| Accumulated depreciation | - | (6,308) | (725,444) | (7,081) | (33,730) | (8,156) | (23,265) | (216,776) | (1,020,760) |
| <u>2018</u> | <u>\$ 137,045</u> | <u>\$ 85,055</u> | <u>\$ 294,591</u> | <u>\$ 3,022</u> | <u>\$ 82,857</u> | <u>\$ 3,389</u> | <u>\$ 18,561</u> | <u>\$ 76,135</u> | <u>\$ 700,655</u> |
| Opening net book amount | \$ 137,045 | \$ 85,055 | \$ 294,591 | \$ 3,022 | \$ 82,857 | \$ 3,389 | \$ 18,561 | \$ 76,135 | \$ 700,655 |
| Acquired through business combination | | | | | | | | | |
| Additions | - | - | 87,426 | 52 | - | - | - | - | 52 |
| Disposals | - | - | - | 438 | 26,465 | - | - | 427 | 114,756 |
| Reclassifications | - | - | 42,663 | - | - | (35) | - | - | (35) |
| Depreciation charges | - | (2,645) | (79,708) | (1,287) | (8,346) | (1,102) | (6,053) | (14,552) | (113,693) |
| Net exchange differences | 4,421 | 2,693 | 9,950 | 68 | 2,040 | 73 | 484 | 2,177 | 21,906 |
| <u>Closing net book amount</u> | <u>\$ 141,466</u> | <u>\$ 85,103</u> | <u>\$ 354,922</u> | <u>\$ 2,293</u> | <u>\$ 60,353</u> | <u>\$ 2,325</u> | <u>\$ 12,992</u> | <u>\$ 64,187</u> | <u>\$ 723,641</u> |
| At December 31, 2018 | | | | | | | | | |
| Cost | \$ 141,466 | \$ 94,310 | \$ 1,174,986 | \$ 10,547 | \$ 100,089 | \$ 11,738 | \$ 43,175 | \$ 300,876 | \$ 1,877,187 |
| Accumulated depreciation | - | (9,207) | (820,064) | (8,254) | (39,736) | (9,413) | (30,183) | (236,689) | (1,153,546) |
| | <u>\$ 141,466</u> | <u>\$ 85,103</u> | <u>\$ 354,922</u> | <u>\$ 2,293</u> | <u>\$ 60,353</u> | <u>\$ 2,325</u> | <u>\$ 12,992</u> | <u>\$ 64,187</u> | <u>\$ 723,641</u> |

| | Land | Buildings | Machinery equipment | Computer and communication equipment | Research equipment | Office equipment | Leased assets | Leasehold improvements | Total |
|---------------------------------------|-------------------|------------------|---------------------|--------------------------------------|--------------------|------------------|------------------|------------------------|-------------------|
| At January 1, 2017 | | | | | | | | | |
| Cost | \$ 148,511 | \$ 99,008 | \$ 780,103 | \$ 11,852 | \$ 57,524 | \$ 5,346 | \$ 45,325 | \$ 218,033 | \$ 1,365,702 |
| Accumulated depreciation | - | (4,008) | (620,858) | (7,356) | (29,790) | (3,468) | (18,736) | (194,183) | (878,399) |
| | <u>\$ 148,511</u> | <u>\$ 95,000</u> | <u>\$ 159,245</u> | <u>\$ 4,496</u> | <u>\$ 27,734</u> | <u>\$ 1,878</u> | <u>\$ 26,589</u> | <u>\$ 23,850</u> | <u>\$ 487,303</u> |
| 2017 | | | | | | | | | |
| Opening net book amount | \$ 148,511 | \$ 95,000 | \$ 159,245 | \$ 4,496 | \$ 27,734 | \$ 1,878 | \$ 26,589 | \$ 23,850 | \$ 487,303 |
| Acquired through business combination | - | - | 47,781 | - | - | 2,495 | - | 52,891 | 103,167 |
| Additions | - | - | 153,364 | 172 | 64,261 | 28 | - | 16,392 | 234,217 |
| Depreciation charges | - | (2,669) | (50,543) | (1,369) | (6,247) | (859) | (6,110) | (14,027) | (81,824) |
| Net exchange differences | (11,466) | (7,276) | (15,256) | (277) | (2,891) | (153) | (1,918) | (2,971) | (42,208) |
| Closing net book amount | <u>\$ 137,045</u> | <u>\$ 85,055</u> | <u>\$ 294,591</u> | <u>\$ 3,022</u> | <u>\$ 82,857</u> | <u>\$ 3,389</u> | <u>\$ 18,561</u> | <u>\$ 76,135</u> | <u>\$ 700,655</u> |
| At December 31, 2017 | | | | | | | | | |
| Cost | \$ 137,045 | \$ 91,363 | \$ 1,020,035 | \$ 10,103 | \$ 116,587 | \$ 11,545 | \$ 41,826 | \$ 292,911 | \$ 1,721,415 |
| Accumulated depreciation | - | (6,308) | (725,444) | (7,081) | (33,730) | (8,156) | (23,265) | (216,776) | (1,020,760) |
| | <u>\$ 137,045</u> | <u>\$ 85,055</u> | <u>\$ 294,591</u> | <u>\$ 3,022</u> | <u>\$ 82,857</u> | <u>\$ 3,389</u> | <u>\$ 18,561</u> | <u>\$ 76,135</u> | <u>\$ 700,655</u> |

A. Amount of borrowing costs capitalized as part of property, plant and equipment for the years ended December 31, 2018 and 2017: None.

B. Information about the property, plant and equipment that were pledged to others as collateral is provided in Note 8.

(6) Intangible assets

| | <u>Software</u> | <u>Goodwill</u> | <u>Total</u> |
|---|------------------|-------------------|-------------------|
| <u>At January 1, 2018</u> | | | |
| Cost | \$ 56,744 | \$ 176,569 | \$ 233,313 |
| Accumulated amortisation and impairment | (49,659) | - | (49,659) |
| | <u>\$ 7,085</u> | <u>\$ 176,569</u> | <u>\$ 183,654</u> |
| <u>2018</u> | | | |
| At January 1 | \$ 7,085 | \$ 176,569 | \$ 183,654 |
| Additions | 5,197 | - | 5,197 |
| Amortization charges | (5,489) | - | (5,489) |
| Net exchange differences | 210 | 1,917 | 2,127 |
| At December 31 | <u>\$ 7,003</u> | <u>\$ 178,486</u> | <u>\$ 185,489</u> |
| <u>At December 31, 2018</u> | | | |
| Cost | \$ 62,791 | \$ 178,486 | \$ 241,277 |
| Accumulated amortisation and impairment | (55,788) | - | (55,788) |
| | <u>\$ 7,003</u> | <u>\$ 178,486</u> | <u>\$ 185,489</u> |
| | | | |
| | <u>Software</u> | <u>Goodwill</u> | <u>Total</u> |
| <u>At January 1, 2017</u> | | | |
| Cost | \$ 58,774 | \$ - | \$ 58,774 |
| Accumulated amortisation and impairment | (44,103) | - | (44,103) |
| | <u>\$ 14,671</u> | <u>\$ -</u> | <u>\$ 14,671</u> |
| <u>2017</u> | | | |
| At January 1 | \$ 14,671 | \$ - | \$ 14,671 |
| Acquired through business combination | - | 176,569 | 176,569 |
| Additions | 1,450 | - | 1,450 |
| Amortization charges | (8,102) | - | (8,102) |
| Net exchange differences | (934) | - | (934) |
| At December 31 | <u>\$ 7,085</u> | <u>\$ 176,569</u> | <u>\$ 183,654</u> |
| <u>At December 31, 2017</u> | | | |
| Cost | \$ 56,744 | \$ 176,569 | \$ 233,313 |
| Accumulated amortisation and impairment | (49,659) | - | (49,659) |
| | <u>\$ 7,085</u> | <u>\$ 176,569</u> | <u>\$ 183,654</u> |

A. Details of amortization on intangible assets are as follows:

| | Years ended December 31, | |
|-------------------------------------|--------------------------|-----------------|
| | 2018 | 2017 |
| Cost of operating revenue | \$ 5,293 | \$ 7,906 |
| General and administrative expenses | 196 | 196 |
| | <u>\$ 5,489</u> | <u>\$ 8,102</u> |

B. The Group carried out the impairment testing of goodwill on the balance sheet date. The recoverable amount of the cash-generating units is determined based on the value-in-use calculated using cash flow projections discounted from financial budgets approved by management covering a five-year period. The discount rate used by management is 13.93%. The calculation of value-in-use for the cash-generating unit is mainly based on the future growth rates of operating revenues, historical information on gross margins and operating expenses ratios, and the future trend of industrial economy.

As a result of the analysis, the Group did not identify any impairment for the goodwill in 2018 due to the recoverable amount was higher than the carrying amount of goodwill.

(7) Non-current assets

| Item | December 31, 2018 | December 31, 2017 |
|---------------------------|-------------------|-------------------|
| Time deposits (Note) | \$ 371 | \$ 59,828 |
| Prepayments for equipment | 106,676 | 52,857 |
| Refundable deposits | 3,425 | 3,234 |
| Other non-current assets | - | 227 |
| | <u>\$ 110,472</u> | <u>\$ 116,146</u> |

Note: Pledged assets, please refer to Note 8.

(8) Short-term borrowings

| Type of borrowings | December 31, 2018 | December 31, 2017 | Interest rate range | Collateral |
|--------------------|-------------------|-------------------|---------------------|---------------------|
| Bank borrowings | | | | |
| Secured borrowings | \$ 20,300 | \$ 20,000 | 1.75%~2.22% | Time deposit (Note) |

Note: Please refer to Note 8 for the information of the Group's assets pledged to secured borrowings.

(9) Financial liabilities at fair value through profit or loss

| Item | December 31, 2018 | December 31, 2017 |
|--|-------------------|-------------------|
| Current items: | | |
| Financial liabilities held for trading | | |
| Call options, put options and conversion options embedded in convertible bonds | \$ - | \$ 10,565 |
| Valuation adjustment | - | 20,639 |
| | <u>\$ -</u> | <u>\$ 31,204</u> |

- A. The Group recognized net gains (losses) of \$2,322 and (\$8,985), respectively, on financial liabilities at fair value through profit or loss for the years ended December 31, 2018 and 2017.
- B. In accordance with Article 9 of the “Regulations For Issuance of Secured Convertible Bonds in the R.O.C.” and Article 9 of the “Regulations For Issuance of Unsecured Convertible Bonds in the R.O.C.”, the Group announced that the last conversion date for bondholders to exercise conversion right was March 15, 2018 in preparation for holding the Group’s 2018 shareholders’ meeting. As of December 31, 2018, the Group recognized the remaining unconverted balances of financial liabilities at fair value through profit or loss by last conversion date as net profit (loss).

(10) Bonds payable

| Item | December 31, 2018 | December 31, 2017 |
|--|-------------------|-------------------|
| Convertible bonds | | |
| First secured convertible bonds | \$ 300,000 | \$ 300,000 |
| Second unsecured convertible bonds | 300,000 | 300,000 |
| | 600,000 | 600,000 |
| Less: Bonds converted | (597,200) | (538,500) |
| Less: Repayment of principal at maturity | (2,800) | - |
| Less: Discount on bonds payable | - | (1,494) |
| | - | 60,006 |
| Less: Current portion (Note) | - | (60,006) |
| | \$ - | \$ - |

Note: The bondholders may request the Company to redeem the bonds, in whole or in part, with an added interest rate on the carrying amount as the premium after two years from the issue date. As a result, the convertible bonds are recognised as “Long-term borrowings, current portion”.

- A. On May 13, 2015, the Company issued the first secured domestic convertible bonds. Key terms and conditions of bonds are as follows:
- (a) Issue amount: \$300,000.
 - (b) Issue price: Issued at 100% of par value; \$100 in thousands.
 - (c) Issue period: Three years; from May 13, 2015 to May 13, 2018
 - (d) Coupon rate: 0% per annum
 - (e) Repayment date and method: The bonds will be redeemed at par at maturity if the bonds are not converted into common stocks at maturity, or redeemed early by the Company, or resold early to the Company by the bondholders, or redeemed from the Company’s underwriter and cancelled by the Company.
 - (f) Conversion period: Except that the bonds are in the lock-up period, or redeemed early by the Company, the conversion right can be exercised at any time from June 14, 2015 through May 13, 2018 in accordance with the terms of the bonds and relevant regulations.

- (g) Conversion price and price reset: The conversion price was set at NT\$79.3 (in dollars) per share on the issue date. The conversion price is subject to adjustments on the ex-right date of new shares issuance based on the formula specified in the terms of the bonds, due to changes in the number of the Company's common shares. The conversion price was subsequently adjusted to NT\$53.6 (in dollars) per share due to aforementioned rationale.
 - (h) The converted shares have the same rights as common shares.
 - (i) Call options of the Company: The bonds may be called, in whole or in part, at the option of the Company after one month from the issue date (June 14, 2015) to forty days before the maturity date (April 3, 2018) at 100% of their principal amount, provided the closing price of the Company's common shares on the Taipei Exchange exceeds 130% (inclusive) of the then-current conversion price of the bonds over 30 (inclusive) trading days during 30 consecutive trading days, or when over 90% (inclusive) of the bonds have been redeemed, converted, called and retired.
 - (j) Put options of the holders: The bondholders may request the Company to redeem the bonds, in whole or in part, with an added interest rate on the carrying amount as the premium, which is equivalent to 102.516% (real yield rate is 1.25%) of their principal amount, after two years from the issue date. The non-equity conversion options, call options, put options embedded in bonds payable were separated from their host contracts and were recognised in "financial assets or liabilities at fair value through profit or loss" in net amount in accordance with IAS 39 because the economic characteristics and risks of the embedded derivatives were not closely related to those of the host contracts. The effective interest rate of the bonds payable after such separation was 7.2%.
 - (k) Through December 31, 2018, convertible bonds amounting to \$297,600 was converted to 5,300,002 ordinary shares.
 - (l) Please refer to Note 8 for the information of the Group's assets pledged for secured domestic convertible bonds.
- B. On May 14, 2015, the Company issued the second unsecured domestic convertible bonds. Key terms and conditions of bonds are as follows:
- (a) Issue amount: \$300,000.
 - (b) Issue price: Issued at 100% of par value; \$100 in thousands.
 - (c) Issue period: Three years; from May 14, 2015 to May 14, 2018
 - (d) Coupon rate: 0% per annum
 - (e) Repayment date and method: The bonds will be redeemed at par at maturity if the bonds are not converted into common stocks at maturity, or redeemed early by the Company, or resold early to the Company by the bondholders, or redeemed from the Company's underwriter and cancelled by the Company.
 - (f) Conversion period: Except that the bonds are in the lock-up period, or redeemed early by the Company, the conversion right can be exercised at any time from June 15, 2015 through May 14, 2018 in accordance with the terms of the bonds and relevant regulations.
 - (g) Conversion price and price reset: The conversion price was set at NT\$81.2 (in dollars) per share on the issue date. The conversion price is subject to adjustments on the ex-right date of new shares issuance based on the formula specified in the terms of the bonds, due to changes in the number of the Company's common shares. The conversion price was subsequently adjusted to NT\$54.9 (in dollars) per share due to the aforementioned rationale.

- (h) The converted shares have the same rights as common shares.
- (i) Call options of the Company: The bonds may be called, in whole or in part, at the option of the Company after one month from the issue date (June 15, 2015) to forty days before the maturity date (April 4, 2018) at 100% of their principal amount, provided the closing price of the Company's common shares on the Taiwan Exchange exceeds 130% (inclusive) of the then-current conversion price of the bonds during 30 consecutive trading days, or when over 90% (inclusive) of the bonds have been redeemed, converted, called and retired.
- (j) Put options of the holders: The bondholders may request the Company to redeem the bonds, in whole or in part, with an added interest rate on the carrying amount as the premium, which is equivalent to 103.023% (real yield rate is 1.5%) of their principal amount, after two years from the issue date. The non-equity conversion options, call options, and put options embedded in bonds payable were separated from their host contracts and were recognised in "financial assets or liabilities at fair value through profit or loss" in net amount in accordance with IAS 39 because the economic characteristics and risks of the embedded derivatives were not closely related to those of the host contracts. The effective interest rate of the bonds payable after such separation was 5.66%.
- (k) Through December 31, 2018, convertible bonds amounting to \$299,600 was converted to 4,948,016 ordinary shares.

(11) Long-term borrowings

| Type of borrowings | Borrowing period and repayment term | Interest rate | Collateral | December 31, 2018 | December 31, 2017 |
|--------------------------------|--|------------------|-----------------------|-------------------|-------------------|
| Long-term bank borrowings | | | Land and buildings | | |
| Secured borrowings (Note 1) | (Note 2) | 4% | (Note 3) | \$ 78,242 | \$ 95,163 |
| Less: Current portion | | | | (20,818) | (19,366) |
| | | | | \$ 57,424 | \$ 75,797 |

Note 1: According to the secured loan contract, the Group was required to comply with certain financial covenants by maintaining certain financial ratios, such as debt coverage ratio, on an annual basis. As of December 31, 2018 and 2017, the Group had not violated any of the required financial covenants.

Note 2: Borrowing period is from August 6, 2015 to August 6, 2022; interest and principal are repayable monthly.

Note 3: Please refer to Note 8 for the information of the Group's assets pledged for secured borrowings.

(12) Other payables

| | <u>December 31, 2018</u> | <u>December 31, 2017</u> |
|--|--------------------------|--------------------------|
| Accrued salaries and bonuses | \$ 48,852 | \$ 46,811 |
| Accrued employees' compensation and directors' remuneration | 29,431 | 31,761 |
| Payables for equipment | 27,460 | 5,703 |
| Accrued unused compensated absences | 27,117 | 25,171 |
| Accrued professional service fees | 7,179 | 464 |
| Accrued outsourcing manufacturing services charges | 2,885 | 7,373 |
| Accrued utilities | 2,089 | 2,101 |
| Accrued rental expenses | 503 | 269 |
| Accrued miscellaneous tools | - | 1,611 |
| Other accrued expenses | 18,764 | 17,985 |
| | <u>\$ 164,280</u> | <u>\$ 139,249</u> |

(13) Finance lease liabilities

The Group leases machinery equipment under finance lease. Based on the terms of the lease contracts, the Group has the option to purchase the leased machinery equipment at a price which is expected to be sufficiently lower than fair value at the date the option becomes exercisable when the leases expire. Future minimum lease payments and present value as of December 31, 2018 and 2017 are as follows:

| | <u>December 31, 2018</u> | | |
|---|--|-----------------------------------|---|
| | <u>Total finance lease liabilities</u> | <u>Future finance charges</u> | <u>Present value of finance lease liabilities</u> |
| <u>Current</u> | | | |
| No later than one year (shown as "Other current liabilities") | <u>\$ 4,793</u> | <u>(\$ 98)</u> | <u>\$ 4,695</u> |

| | December 31, 2017 | | |
|---|------------------------------------|---------------------------|--|
| | Total finance lease liabilities | Future finance charges | Present value of finance lease liabilities |
| <u>Current</u> | | | |
| No later than one year (shown as “Other current liabilities”) | \$ 9,684 | (\$ 360) | \$ 9,324 |
| <u>Non-current</u> | | | |
| Later than one year but not later than five years (shown as “Other non-current liabilities”) | 4,643 | (95) | 4,548 |
| | <u>\$ 14,327</u> | <u>(\$ 455)</u> | <u>\$ 13,872</u> |

(14) Pension plan

- A. The Group’s US subsidiary has established a 401(K) pension plan (the “Plan”) covering substantially all employees. The Plan provides voluntary salary reduction contributions by eligible participants in accordance with Section 401(K) of the Internal Revenue Code (IRC), as well as discretionary matching contributions below 15% of employees’ salaries from the Company’s subsidiary to its employees’ individual pension accounts.
- B. The Group’s Taiwan subsidiaries have established a defined contribution pension plan (the “New Plan”) under the Labor Pension Act (the “Act”), covering all regular employees with R.O.C. nationality. Under the New Plan, the Company’s Taiwan subsidiaries contribute monthly an amount based on 6% of the employees’ monthly salaries and wages to the employees’ individual pension accounts at the Bureau of Labor Insurance. The benefits accrued are paid monthly or in lump sum upon termination of employment.
- C. The pension costs under the above pension plans of the Group for the years ended December 31, 2018 and 2017 amounted to \$19,073 and \$16,005, respectively.

(15) Share-based payment-employee compensation plan

- A. Through December 31, 2018 and 2017, the Company’s share-based payment transactions are set forth below:

| Type of arrangement | Grant date | Quantity granted | Contract period | Vesting condition |
|---|----------------|------------------|-----------------|-------------------|
| Employee stock options | April 2013 | 1,538,000 shares | 10 years | (Note 1) |
| Employee stock options | August 2013 | 7,830 shares | 10 years | (Note 1) |
| Employee stock options | October 2013 | 538,000 shares | 10 years | (Note 1) |
| Employee stock options | February 2014 | 60,000 shares | 10 years | (Note 1) |
| Employee stock options | November 2014 | 75,000 shares | 10 years | (Note 1) |
| Employee stock options | January 2015 | 30,000 shares | 10 years | (Note 1) |
| Employee stock options | February 2015 | 652,200 shares | 10 years | (Note 1) |
| Employee stock options | March 2016 | 5,000 shares | 10 years | (Note 1) |
| Employee stock options | August 2016 | 895,000 shares | 10 years | (Note 1) |
| Employee stock options | November 2016 | 34,000 shares | 10 years | (Note 1) |
| Employee stock options | February 2017 | 15,000 shares | 10 years | (Note 1) |
| Employee stock options | August 2017 | 215,000 shares | 10 years | (Note 1) |
| Employee stock options | January 2018 | 13,000 shares | 10 years | (Note 1) |
| Employee stock options | February 2018 | 355,000 shares | 10 years | (Note 1) |
| Employee stock options | August 2018 | 27,000 shares | 10 years | (Note 1) |
| Employee stock options | November 2018 | 5,000 shares | 10 years | (Note 1) |
| Restricted stocks to employees (Note 3) | July 2015 | 297,300 shares | 2 years | (Note 2) |
| Restricted stocks to employees (Note 3) | November 2015 | 22,000 shares | 2 years | (Note 2) |
| Restricted stocks to employees (Note 3) | January 2016 | 93,700 shares | 2 years | (Note 2) |
| Restricted stocks to employees (Note 3) | March 2016 | 8,000 shares | 2 years | (Note 2) |
| Restricted stocks to employees (Note 3) | August 2017 | 180,000 shares | 2 years | (Note 2) |
| Restricted stocks to employees (Note 3) | February 2018 | 398,000 shares | 2 years | (Note 2) |
| Restricted stocks to employees (Note 3) | September 2018 | 28,000 shares | 2 years | (Note 2) |

Note 1: Employee stock options shall be vested and become exercisable up to 50% of the shares after fulfilling two years of service, and in accordance with the agreement, the remaining 50% of such options will be vested ratably in equal installments as of the last day of each of the succeeding 24 months.

Note 2: Restricted stocks to employees shall be vested up to 50% of the shares after one year of service, and the remaining 50% of such shares to be vested after fulfilling two years of service.

Note 3: The restricted stocks to employees are restricted from transferring within vesting period, but are allowed for voting rights and rights to receive dividends. The Company will recover restricted stocks at no consideration and cancel registration if employees resign or die not due to occupational hazards. However, employees do not need to return

dividends already received.

B. Details of the employee stock options are set forth below:

| Year ended December 31, 2018 | | | |
|--|------------------|----------|------------------------------------|
| | No. of options | Currency | Weighted average exercise price |
| | | | (in dollars) |
| Options outstanding at beginning of the year | 1,912,541 | NTD | \$ 50.44 |
| Options granted | 400,000 | NTD | 81.95 |
| Options exercised | (223,084) | NTD | 26.49 |
| Options forfeited | (60,000) | NTD | 77.77 |
| Options outstanding at end of the year | <u>2,029,457</u> | NTD | 58.48 |
| Options exercisable at end of the year | <u>1,178,924</u> | NTD | 48.61 |
| Year ended December 31, 2017 | | | |
| | No. of options | Currency | Weighted average exercise price |
| | | | (in dollars) |
| Options outstanding at beginning of the year | 2,178,139 | NTD | \$ 44.84 |
| Options granted | 230,000 | NTD | 65.89 |
| Options exercised | (418,638) | NTD | 28.46 |
| Options forfeited | (76,960) | NTD | 57.54 |
| Options outstanding at end of the year | <u>1,912,541</u> | NTD | 50.44 |
| Options exercisable at end of the year | <u>668,190</u> | NTD | 26.98 |

C. The weighted-average stock price of stock options at exercise dates for the years ended December 31, 2018 and 2017 was \$77.60 (in dollars) and \$65.19 (in dollars), respectively.

D. As of December 31, 2018 and 2017, the range of exercise prices of stock options outstanding are as follows:

| Grant date | Expiry date | December 31, 2018 | | |
|---------------|---------------|-------------------|----------|--|
| | | No. of Shares | Currency | Stock options exercise price (in dollars) |
| April 2013 | April 2023 | 170,396 | NTD | \$ 11.35 |
| October 2013 | October 2023 | 33,335 | NTD | 17.63 |
| November 2014 | November 2024 | 54,188 | NTD | 32.65 |
| January 2015 | January 2025 | 7,500 | NTD | 42.09 |
| February 2015 | February 2025 | 313,038 | NTD | 41.21 |
| March 2016 | March 2026 | 5,000 | NTD | 71.01 |
| August 2016 | August 2026 | 840,000 | NTD | 65.73 |
| November 2016 | November 2026 | 26,000 | NTD | 64.40 |
| February 2017 | February 2027 | 15,000 | NTD | 57.10 |
| August 2017 | August 2027 | 205,000 | NTD | 66.50 |
| January 2018 | January 2028 | 13,000 | NTD | 86.70 |
| February 2018 | February 2028 | 315,000 | NTD | 83.60 |
| August 2018 | August 2028 | 27,000 | NTD | 64.00 |
| November 2018 | November 2028 | 5,000 | NTD | 49.50 |
| | | <u>2,029,457</u> | | |

| | | December 31, 2017 | | |
|---------------|---------------|-------------------|----------|---|
| Grant date | Expiry date | No. of Shares | Currency | Stock options exercise price (in dollars) |
| April 2013 | April 2023 | 224,896 | NTD | \$ 11.35 |
| October 2013 | October 2023 | 95,002 | NTD | 17.63 |
| February 2014 | February 2024 | 7,500 | NTD | 19.20 |
| November 2014 | November 2024 | 58,667 | NTD | 32.65 |
| January 2015 | January 2025 | 10,000 | NTD | 42.09 |
| February 2015 | February 2025 | 405,476 | NTD | 41.21 |
| March 2016 | March 2026 | 5,000 | NTD | 71.01 |
| August 2016 | August 2026 | 850,000 | NTD | 65.73 |
| November 2016 | November 2026 | 26,000 | NTD | 64.40 |
| February 2017 | February 2027 | 15,000 | NTD | 57.10 |
| August 2017 | August 2027 | 215,000 | NTD | 66.50 |
| | | <u>1,912,541</u> | | |

E. Details of the restricted stocks to employees are set forth below:

| Employee restricted stocks | Years ended December 31, | |
|--------------------------------------|--------------------------|----------------|
| | 2018 | 2017 |
| | No. of shares | No. of shares |
| Outstanding at beginning of the year | 215,850 | 244,850 |
| Granted (Notes 1 and 2) | 426,000 | 180,000 |
| Vested | (125,850) | (196,000) |
| Retired | (5,500) | (13,000) |
| Outstanding at end of the year | <u>510,500</u> | <u>215,850</u> |

Note 1: For the restricted stocks granted with the compensation cost accounted for using the fair value method, the fair values on the grant date are calculated based on the closing price on the grant date.

Note 2: The fair value of restricted stocks granted in February and September 2018 was \$83.60 (in dollars) and \$55.40 (in dollars), respectively.

F. For the stock options granted with the compensation cost accounted for using the fair value method, their fair value on the grant date is estimated using the Black-Scholes option-pricing model and discounted cash flow valuation. The parameters used in the estimation of the fair value are as follows:

| Type of arrangement | Grant date | Currency | Fair value (in dollars) | Exercise price (in dollars) | Expected price volatility | Expected option period (years) | Expected dividend yield rate | Risk-free interest rate | Weighted average fair value (in dollars) |
|------------------------|---------------|----------|----------------------------|--------------------------------|---------------------------|-----------------------------------|------------------------------|-------------------------|---|
| Employee stock options | February 2017 | NTD | \$ 57.98 | \$ 57.10 | 34.41% | 6.26 | 1.00% | 1.19% | \$ 29.14 |
| Employee stock options | August 2017 | NTD | 64.90 | 66.50 | 36.37% | 6.26 | 1.00% | 1.10% | 32.53 |
| Employee stock options | January 2018 | NTD | 86.43 | 86.70 | 42.83% | 6.26 | 1.00% | 0.97% | 45.74 |
| Employee stock options | February 2018 | NTD | 84.61 | 83.60 | 45.43% | 6.26 | 1.00% | 0.97% | 46.31 |
| Employee stock options | August 2018 | NTD | 67.41 | 64.00 | 32.93% | 6.26 | 1.00% | 0.90% | 38.38 |
| Employee stock options | November 2018 | NTD | 50.24 | 49.50 | 58.84% | 6.26 | 1.00% | 0.89% | 34.22 |

G. Expenses incurred on share-based payment transactions are shown below:

| | Years ended December 31, | |
|----------------|--------------------------|-----------|
| | 2018 | 2017 |
| Equity-settled | \$ 49,618 | \$ 25,894 |

(16) Common stock

A. As of December 31, 2018, the Company's paid-in capital was \$821,691, consisting of 82,169,126 shares with a par value of \$10 (in dollars) per share.

Movements in the number of the Company's ordinary shares outstanding are as follows:

| | Unit: Numbers of shares | |
|---|-------------------------|------------|
| | 2018 | 2017 |
| At January 1 | 79,059,886 | 73,275,266 |
| Exercise of employee stock options | 223,084 | 418,638 |
| Conversion of convertible bonds | 1,086,156 | 5,448,982 |
| Issuance of restricted stocks to employees | 426,000 | 180,000 |
| Retirement of restricted stocks to employees | (3,000) | (11,000) |
| Restricted stocks to employees retrieved, not yet retired | (2,500) | (2,000) |
| Purchase of treasury stocks | - | (250,000) |
| At December 31 | 80,789,626 | 79,059,886 |

- B. On May 15, 2015, the shareholders adopted a resolution to issue 600,000 employee restricted stocks with par value of \$10 (in dollars) per share, with the effective date set on July 13, 2015. The subscription price is \$0 (in dollars) per share. The employee restricted stocks issued are subject to certain transfer restrictions before their vesting conditions are met. Other than these restrictions, the rights and obligations of these shares issued are the same as other issued ordinary shares. On July 27, 2015, November 5, 2015, January 14, 2016 and March 2, 2016, the Board of Directors adopted resolutions to grant 297,300, 22,000, 93,700 and 8,000 employee restricted stocks, respectively. For the years ended December 31, 2017 and 2016, the Company had retrieved 13,000 and 16,000 employee restricted stocks, respectively, due to the employees' resignation and the retrieved shares have been retired.
- C. On June 1, 2017, the shareholders adopted a resolution to reserve 1,000,000 shares for the purpose of granting employee restricted stocks with par value of \$10 (in dollars) per shares, with the effective date filed with the regulator on August 8, 2017. The subscription price is \$0 (in dollar) per share. The employee restricted stocks issued are subject to certain transfer restrictions before their vesting conditions are met. Other than these restrictions, the rights and obligations of these shares issued are the same as other issued ordinary shares. On August 21, 2017 and February 27, 2018, the Board of Directors adopted a resolution to grant 180,000 and 398,000 employee restricted stocks, respectively. In April 2018, the Company had retrieved 3,000 employee restricted stocks due to the employees' resignation and the retrieved shares have been retired. Further, in October 2018 and for the period from January 1 to March 15, 2019, the Company retrieved 2,500 and 8,000 employee restricted stocks, respectively, due to the employee's resignation, which have not been retired.
- D. On May 15, 2018, the shareholders adopted a resolution to reserve 1,000,000 shares for the purpose of granting employee restricted stocks with par value of \$10 (in dollars) per shares, with the effective date filed with the regulator on August 16, 2018. The subscription price is \$0 (in dollar) per share. The employee restricted stocks issued are subject to certain transfer restrictions before their vesting conditions are met. Other than these restrictions, the rights and obligations of these shares issued are the same as other issued ordinary shares. On August 2, 2018, the Board of Directors adopted a resolution to grant 28,000 employee restricted stocks.
- E. On April 2, 2018, the Board of Directors resolved to increase cash capital by issuing ordinary shares for participating in issuance of Global Depositary Receipts ("GDRs") in order to fund the purchase of plant, machinery and equipment, and overseas purchases of raw materials. On July 31, 2018, the Company received the official letter No. 1070326367 from the FSC of approval of the issuance of ordinary shares for participating in issuance of GDRs, while on October 31, 2018, the Company received another official letter No.1070118798 for the extension of three months to complete the aforementioned issuance. On December 19, 2018, the Board of Directors resolved to adjust the number of shares to be issued from the range of 15,000,000 to 25,000,000 ordinary shares to 8,000,000 to 25,000,000 ordinary shares. The aforementioned adjustment was approved by the FSC with the receipt of the official letter No.1070121974. The Company's GDRs began trading on the Luxembourg Stock Exchange on January 21, 2019. The actual units of GDRs for this offering were 1,600,000 and each GDR represents five of the Company's ordinary shares, which in the aggregate representing 8,000,000 ordinary shares. The offering price per GDR was US\$8.20 (in dollars). The actual cash received was US\$12,989 thousand (approximately NT\$400,717 thousand) after deducting issuance costs. The fundraising had been fully collected by the Company as of January 22, 2019, and the change registration of

this capital increase had been completed.

The terms of GDR are as follows:

Voting rights

- (a) The voting right of GDR holders may, pursuant to the Depositary Agreement and the relevant laws and regulations of the R.O.C., exercise the voting rights pertaining to the underlying common shares represented by the GDRs.

Dividends, stocks warrants and other rights

- (b) GDR holders and common shareholders are all entitled to receive dividends, stock warrants and other rights.

F. Treasury stocks

- (a) Reason for share repurchase and the number of the Company's treasury stocks are as follows:

| | | <u>December 31, 2018</u> | |
|---|------------------------------|--------------------------|------------------------|
| <u>Name of company holding the shares</u> | <u>Reason for repurchase</u> | <u>Number of shares</u> | <u>Carrying amount</u> |
| The Company | To be reissued to employees | 1,377,000 | \$ 90,870 |

| | | <u>December 31, 2017</u> | |
|---|------------------------------|--------------------------|------------------------|
| <u>Name of company holding the shares</u> | <u>Reason for repurchase</u> | <u>Number of shares</u> | <u>Carrying amount</u> |
| The Company | To be reissued to employees | 1,377,000 | \$ 90,870 |

- (b) Pursuant to the R.O.C. Securities and Exchange Act, the number of shares repurchased as treasury shares should not exceed 10% of the number of the Company's issued and outstanding shares and the amount bought back should not exceed the sum of retained earnings, paid-in capital in excess of par value and realised capital surplus.
- (c) Pursuant to the R.O.C. Securities and Exchange Act, treasury stocks should not be pledged as collateral and is not entitled to dividends before it is reissued.
- (d) Pursuant to the R.O.C. Securities and Exchange Act, treasury stocks should be reissued to the employees within three years from the date of repurchase, and shares not reissued within the three-year period are to be retired. Treasury stocks to enhance the Company's credit rating and the shareholders' equity should be retired within six months of repurchase.

(17) Capital surplus

Capital surplus can be used to cover accumulated deficit or distributed as dividend as proposed by the Board of Directors and resolved by the shareholders.

| | 2018 | | | | |
|--|-------------------|------------------------|----------------------------|------------------|---------------------|
| | Share premium | Employee stock options | Employee restricted stocks | Others | Total |
| At January 1 | \$ 843,765 | \$ 46,693 | \$ 37,550 | \$ 30,743 | \$ 958,751 |
| Compensation costs of share-based payment | - | 20,690 | - | - | 20,690 |
| Issuance of restricted stocks to employees | - | - | 31,500 | - | 31,500 |
| Restricted stocks to employees vested | 30,251 | - | (30,251) | - | - |
| Retrieve restricted stocks from employees | - | - | (342) | - | (342) |
| Exercise of employee stock options | 12,854 | (9,118) | - | - | 3,736 |
| Conversion of convertible bonds | 78,300 | - | - | - | 78,300 |
| Forfeiture of employee stock options | - | (809) | - | 809 | - |
| At December 31 | <u>\$ 965,170</u> | <u>\$ 57,456</u> | <u>\$ 38,457</u> | <u>\$ 31,552</u> | <u>\$ 1,092,635</u> |
| | 2017 | | | | |
| | Share premium | Employee stock options | Employee restricted stocks | Others | Total |
| At January 1 | \$ 541,476 | \$ 46,850 | \$ 26,588 | \$ 29,712 | \$ 644,626 |
| Compensation costs of share-based payment | - | 18,448 | - | - | 18,448 |
| Issuance of restricted stocks to employees | - | - | 11,562 | - | 11,562 |
| Retrieve restricted stocks from employees | - | - | (600) | - | (600) |
| Exercise of employee stock options | 25,349 | (17,574) | - | - | 7,775 |
| Conversion of convertible bonds | 276,940 | - | - | - | 276,940 |
| Forfeiture of employee stock options | - | (1,031) | - | 1,031 | - |
| At December 31 | <u>\$ 843,765</u> | <u>\$ 46,693</u> | <u>\$ 37,550</u> | <u>\$ 30,743</u> | <u>\$ 958,751</u> |

(18) Retained earnings

- A. Under the Company's Articles of Incorporation, the current year's earnings, if any, shall first be used to pay all taxes and offset losses incurred in previous years and then a special reserve as required by the applicable securities authority under the applicable public company rules in Taiwan. After combining accumulated undistributed earnings in the previous years and setting aside a certain amount of remaining profits of such financial year as a reserve or reserves for development purposes as the Board of Directors may from time to time deem appropriate, subject to the compliance with the Cayman Islands Companies Law, the Company shall distribute no less than 10% of the remaining profit as dividends to the shareholders.
- B. The Company's dividend policy is as follows: As the Company operates in a capital intensive industry and in the stable growth stage, the residual dividend policy is adopted taking into consideration the Company's operation scale, cash flow demand and future expansion plans, and cash dividends shall account for at least 10% of the total dividends distributed.
- C. The appropriations of 2018 earnings had been proposed by the Board of Directors on March 15, 2019 and the appropriations of 2017 earnings had been resolved by the shareholders' meeting on May 15, 2018. Details are summarised below:

| | 2018 (Note) | | 2017 | |
|----------------|-------------------|--|------------------|--|
| | Amount | Dividends per share (in dollars) | Amount | Dividends per share (in dollars) |
| Cash dividends | <u>\$ 106,561</u> | <u>\$ 1.20</u> | <u>\$ 79,060</u> | <u>\$ 1.00</u> |

Note: The appropriations of 2018 earnings had not been resolved by the shareholders' meeting.

- D. For the information relating to employees' compensation and directors' remuneration, please refer to Note 6(24).

(19) Other equity interest

| | 2018 | | |
|---|--|--------------------------------------|------------------|
| | Currency translation differences | Unearned employee compensation | Total |
| At January 1 | (\$ 35,464) | (\$ 8,760) | (\$ 44,224) |
| Currency translation differences | 78,469 | - | 78,469 |
| Compensation costs of share-based payment | - | 28,928 | 28,928 |
| Issuance of restricted stocks to employees | - | (35,760) | (35,760) |
| Retrieve restricted stocks from employees | - | 392 | 392 |
| At December 31 | <u>\$ 43,005</u> | <u>(\$ 15,200)</u> | <u>\$ 27,805</u> |

| | 2017 | | | |
|--|----------------------------------|--------------------------------|-------------------------------------|--------------------|
| | Currency translation differences | Unearned employee compensation | Available-for-sale financial assets | Total |
| At January 1 | \$ 122,002 | (\$ 3,548) | \$ 14,166 | \$ 132,620 |
| Currency translation differences | (157,466) | - | - | (157,466) |
| Compensation costs of share-based payment | - | 7,446 | - | 7,446 |
| Issuance of restricted stocks to employees | - | (13,368) | - | (13,368) |
| Retrieve restricted stocks from employees | - | 710 | - | 710 |
| Changes of fair value in financial instruments | | | | |
| - Transfer out of revaluation - gross | - | - | (31,076) | (31,076) |
| - Transfer out of revaluation - tax | - | - | 12,378 | 12,378 |
| - Revaluation - gross | - | - | 7,534 | 7,534 |
| - Revaluation - tax | - | - | (3,002) | (3,002) |
| At December 31 | <u>(\$ 35,464)</u> | <u>(\$ 8,760)</u> | <u>\$ -</u> | <u>(\$ 44,224)</u> |

(20) Operating revenue

| | Year ended December 31, 2018 |
|---------------------------------------|---------------------------------|
| Revenue from contracts with customers | <u>\$ 1,952,411</u> |

A. Disaggregation of revenue from contracts with customers

The Group derives revenue from the transfer of goods and services over time and at a point in time in the following major product lines and geographical regions:

| | Year ended December 31, 2018 | | | |
|---------------|------------------------------|------------------|------------------|---------------------|
| | Sales revenue | Service revenue | Royalty revenue | Total |
| China | \$ 935,495 | \$ 15,075 | \$ 2,132 | \$ 952,702 |
| United States | 724,517 | - | 38 | 724,555 |
| Taiwan | 180,477 | - | 26,619 | 207,096 |
| Others | 68,058 | - | - | 68,058 |
| | <u>\$ 1,908,547</u> | <u>\$ 15,075</u> | <u>\$ 28,789</u> | <u>\$ 1,952,411</u> |

B. Contract liabilities

The Group has recognized the following revenue-related contract liabilities:

| | December 31, 2018 |
|---|-------------------|
| Contract liabilities – advance sales receipts | <u>\$ 16,302</u> |

Revenue recognized that was included in the contract liability balance at the beginning of the year:

| | Year ended December 31, 2018 |
|---|---------------------------------|
| Contract liabilities – advance sales receipts | \$ 21,582 |

C. Related disclosures for operating revenue for the year ended December 31, 2017 are provided in Note 12(5) B.

(21) Other gains and losses

| | Years ended December 31, | |
|--|--------------------------|-------------------|
| | 2018 | 2017 |
| Gain on disposal of property, plant and equipment | \$ - | \$ 456 |
| Gain on disposal of investments | - | 29,276 |
| Net currency exchange gains (losses) | 1,523 (| 28,043) |
| Net gains on financial liabilities at fair value through profit or loss | 2,322 (| 8,985) |
| Other losses | (1,749) | - |
| | <u>\$ 2,096</u> | <u>(\$ 7,296)</u> |

(22) Finance costs

| | Years ended December 31, | |
|------------------|--------------------------|-----------|
| | 2018 | 2017 |
| Interest expense | \$ 5,137 | \$ 21,690 |

(23) Expenses by nature

| | Years ended December 31, | |
|--|--------------------------|------------|
| | 2018 | 2017 |
| Employee benefit expenses | \$ 780,081 | \$ 669,452 |
| Depreciation charges on property, plant and equipment | \$ 113,693 | \$ 81,824 |
| Amortization charges on intangible assets (recognized as cost of operating revenue and operating expenses) | \$ 5,489 | \$ 8,102 |

(24) Employee benefit expenses

| | Years ended December 31, | |
|--|--------------------------|-------------------|
| | 2018 | 2017 |
| Wages and salaries | \$ 647,967 | \$ 569,599 |
| Compensation costs of share-based payments | 49,618 | 25,894 |
| Insurance expenses | 59,969 | 55,470 |
| Pension costs | 19,073 | 16,005 |
| Other personnel expenses | 3,454 | 2,484 |
| | <u>\$ 780,081</u> | <u>\$ 669,452</u> |

- A. According to the Articles of Incorporation of the Company, when distributing earnings, an amount equal to the ratio of distributable profit of the current year, after covering accumulated losses, shall be distributed as employees' compensation and directors' remuneration. The ratio shall not be higher than 15% and lower than 5% for employees' compensation, and shall not be higher than 2% for directors' remuneration.
- B. For the years ended December 31, 2018 and 2017, employees' compensation was accrued at \$21,022 and \$22,687, respectively; directors' remuneration was accrued at \$8,409 and \$9,075, respectively. The aforementioned amounts were recognized in wages and salaries. The employees' compensation and directors' remuneration were estimated and accrued based on 5% and 2% of distributable profit of 2018. Employees' compensation and directors' remuneration of 2017 as resolved by the Board of Directors were in agreement with those amount recognized in the 2017 financial statements. The employees' compensation will be distributed in the form of cash.
- C. Information about employees' compensation and directors' remuneration of the Company as proposed by the Board of Directors and resolved by the shareholders will be posted in the "Market Observation Post System" at the website of the Taiwan Stock Exchange.

(25) Income tax

A. Income tax expense

(a) Components of income tax expense:

| | Years ended December 31, | |
|---|--------------------------|------------------|
| | 2018 | 2017 |
| Current tax: | | |
| Current tax on profit for the year | \$ 38,836 | \$ 38,966 |
| Effect from alternative minimum tax | - | 2,055 |
| Tax on undistributed surplus earnings | 776 | - |
| Prior year income tax overestimation | (4,773) | (205) |
| Total current tax | <u>34,839</u> | <u>40,816</u> |
| Deferred tax: | | |
| Origination and reversal of temporary differences | 40,085 | (38,190) |
| Impact of change in tax rate (Note 1) | (1,499) | 64,380 |
| Total deferred tax | <u>38,586</u> | <u>26,190</u> |
| Income tax expense | <u>\$ 73,425</u> | <u>\$ 67,006</u> |

(b) The income tax charged relating to components of other comprehensive income is as follows:

| | Years ended December 31, | |
|--|--------------------------|-----------------|
| | 2018 | 2017 |
| Unrealized gain / loss on valuation of available-for-sale financial assets | <u>\$ -</u> | <u>\$ 9,376</u> |

B. Reconciliation between income tax expense and accounting profit:

| | Years ended December 31, | |
|---|--------------------------|------------------|
| | 2018 | 2017 |
| Tax calculated based on profit before tax and statutory tax rate (Note 2) | \$ 121,819 | \$ 177,456 |
| Expenses disallowed by tax regulation | 361 | 490 |
| Tax exempt income by tax regulation | (15,685) | - |
| Effect from loss carryforwards | (27,278) | - |
| Change in assessment of realization of deferred tax assets | 7,685 (| 177,170) |
| Impact of change in tax rate (Note 1) | (1,499) | 64,380 |
| Tax on undistributed surplus earnings | 776 | - |
| Prior year income tax overestimation | (4,773) (| 205) |
| Utilization of foreign tax credit | (7,981) | - |
| Effect from alternative minimum tax | - | 2,055 |
| Income tax expense | <u>\$ 73,425</u> | <u>\$ 67,006</u> |

Note 1: The impact of change in tax rate was due to the amendments to the Income Tax Act which was promulgated by the President of Republic of China on February 7, 2018, the applicable corporate income tax rate was raised from 17% to 20%; and due to the Tax Cuts and Jobs Act, which was enacted by the U.S. government on December 22, 2017 (Taiwan time), the Federal statutory corporate income tax rate was reduced from 35% to 21%.

Note 2: The basis for computing the applicable tax rate are the rates applicable in the respective countries where the Group entities operate.

C. Amounts of deferred tax assets or liabilities as a result of temporary differences and loss carryforward are as follows:

| | 2018 | | | |
|---|--------------------|---------------------------------|---|--------------------|
| | January 1 | Recognized in profit or loss | Recognized in other comprehensive income | December 31 |
| <u>Deferred tax assets:</u> | | | | |
| Temporary differences: | | | | |
| Unrealized allowance for inventory decline in market value | \$ 21,089 | (\$ 4,422) | \$ - | \$ 16,667 |
| State tax paid | 8,508 | (1,010) | - | 7,498 |
| Accrued unused compensated absences | 5,682 | 920 | - | 6,602 |
| Other | 18,959 | 6,377 | - | 25,336 |
| Loss carryforwards - U.S. Federal tax | 88,915 | (569) | - | 88,346 |
| Loss carryforwards - Taiwan tax | 8,636 | 4,679 | - | 13,315 |
| Alternative minimum tax - U.S. Federal tax | 13,135 | 424 | - | 13,559 |
| Subtotal | <u>\$ 164,924</u> | <u>\$ 6,399</u> | <u>\$ -</u> | <u>\$ 171,323</u> |
| <u>Deferred tax liabilities:</u> | | | | |
| Temporary differences: | | | | |
| Depreciation - U.S. Federal tax | (\$ 29,617) | (\$ 43,271) | \$ - | (\$ 72,888) |
| Depreciation - U.S. state tax | (9,849) | (1,681) | - | (11,530) |
| Other | - | (33) | - | (33) |
| Subtotal | <u>(\$ 39,466)</u> | <u>(\$ 44,985)</u> | <u>\$ -</u> | <u>(\$ 84,451)</u> |
| Total | <u>\$ 125,458</u> | <u>(\$ 38,586)</u> | <u>\$ -</u> | <u>\$ 86,872</u> |

| | | 2017 | | | |
|--|---------|-----------|---------------------------------|---|-------------|
| | | January 1 | Recognized in profit or loss | Recognized in other comprehensive income | December 31 |
| <u>Deferred tax assets:</u> | | | | | |
| Temporary differences: | | | | | |
| Unrealized allowance for inventory decline in market value | \$ | - | \$ 21,089 | \$ - | \$ 21,089 |
| State tax paid | - | - | 8,508 | - | 8,508 |
| Accrued unused compensated absences | - | - | 5,682 | - | 5,682 |
| Other | - | - | 18,959 | - | 18,959 |
| Loss carryforwards - U.S. Federal tax | 212,819 | (| 123,904) | - | 88,915 |
| Loss carryforwards - Taiwan tax | - | - | 8,636 | - | 8,636 |
| Alternative minimum tax - U.S. Federal tax | - | - | 13,135 | - | 13,135 |
| Subtotal | \$ | 212,819 | (\$ 47,895) | \$ - | \$ 164,924 |
| <u>Deferred tax liabilities:</u> | | | | | |
| Temporary differences: | | | | | |
| Depreciation - U.S. Federal tax | (\$ | 52,212) | \$ 22,595 | \$ - | (\$ 29,617) |
| Depreciation - U.S. state tax | (| 8,959) | (890) | - | (9,849) |
| Unrealized gain on valuation of available-for-sale financial assets | (| 9,376) | - | 9,376 | - |
| Subtotal | (\$ | 70,547) | \$ 21,705 | \$ 9,376 | (\$ 39,466) |
| Total | \$ | 142,272 | (\$ 26,190) | \$ 9,376 | \$ 125,458 |

D. Expiration dates of unused net operating loss carryforward and amounts of unrecognized deferred tax assets are as follows:

Federal tax:

| December 31, 2018 | | | | |
|--|-----------------|------------------|-------------------------------|--|
| Year incurred (fiscal year end of tax returns) | Amount filed | Unused amount | Unrecognized amount (Note) | Usable until year (fiscal year end of tax returns) |
| 2005.6.30 | \$ 166,885 | 26,144 | - | 2024.12.31 |
| 2006.6.30 | 154,447 | 154,447 | - | 2025.12.31 |
| 2007.6.30 | 112,840 | 112,840 | - | 2026.12.31 |
| 2008.6.30 | 67,030 | 67,030 | - | 2027.12.31 |
| 2011.12.31 | 6,045 | 6,045 | - | 2031.12.31 |
| 2012.12.31 | 54,191 | 54,191 | - | 2032.12.31 |
| | \$ 561,438 | \$ 420,697 | \$ - | |

December 31, 2017

| Year incurred (fiscal year end of tax returns) | Amount filed | Unused amount | Unrecognized amount (Note) | Usable until year (fiscal year end of tax returns) |
|--|-------------------|-------------------|-------------------------------|--|
| 2005.6.30 | \$ 161,670 | \$ 41,183 | \$ - | 2024.12.31 |
| 2006.6.30 | 149,621 | 149,621 | - | 2025.12.31 |
| 2007.6.30 | 109,313 | 109,313 | - | 2026.12.31 |
| 2008.6.30 | 64,936 | 64,936 | - | 2027.12.31 |
| 2011.12.31 | 5,856 | 5,856 | - | 2031.12.31 |
| 2012.12.31 | 52,498 | 52,498 | - | 2032.12.31 |
| | <u>\$ 543,894</u> | <u>\$ 423,407</u> | <u>\$ -</u> | |

E. As of December 31, 2018, the assessment of income tax returns of the Taiwan subsidiaries are as follows:

| Name of subsidiary | Assessment of income tax returns |
|---|----------------------------------|
| Global Device Technologies, Co., Ltd. | Assessed and approved up to 2016 |
| D-Tech Optoelectronics (Taiwan) Corporation | Assessed and approved up to 2015 |

F. Under the amendments to the Income Tax Act which was promulgated by the President of the Republic of China on February 7, 2018, the Company's applicable income tax rate was raised from 17% to 20% effective from January 1, 2018. The Group has assessed the impact of the change in income tax rate.

(26) Earnings per share (EPS)

The basic EPS is determined by the net income divided by the weighted average number of outstanding stocks. The diluted EPS is under the assumption that all potential ordinary stocks have been converted into ordinary stocks at the beginning of the year. The revenue and expense generated from the conversion shall be included in the computation.

Details of ordinary stocks per share are as follows:

| | <u>Year ended December 31, 2018</u> | | |
|--|-------------------------------------|-----------------------|---------------------|
| | <u>Amount</u> | <u>Weighted</u> | <u>Earnings</u> |
| | <u>after tax</u> | <u>average</u> | <u>per share</u> |
| | | <u>outstanding</u> | <u>(in dollars)</u> |
| | | <u>stocks</u> | |
| | | <u>(in thousands)</u> | |
| <u>Basic earnings per share</u> | | | |
| Profit attributable to ordinary shareholders of the parent | <u>\$ 320,302</u> | <u>79,880</u> | <u>\$ 4.01</u> |
| <u>Diluted earnings per share</u> | | | |
| Profit attributable to ordinary shareholders of the parent | \$ 320,302 | 79,880 | |
| Assumed conversion of all dilutive potential ordinary shares | | | |
| Employees' bonus | - | 452 | |
| Employee stock options | - | 340 | |
| Employee restricted stocks | - | 262 | |
| Profit attributable to ordinary shareholders of the parent plus assumed conversion of all dilutive potential ordinary stocks | <u>\$ 320,302</u> | <u>80,934</u> | <u>\$ 3.96</u> |

| | Year ended December 31, 2017 | | |
|--|------------------------------|--|---------------------------------------|
| | Amount after tax | Weighted average outstanding stocks (in thousands) | Earnings per share (in dollars) |
| <u>Basic earnings per share</u> | | | |
| Profit attributable to ordinary shareholders of the parent | \$ 357,047 | 74,867 | \$ 4.77 |
| <u>Diluted earnings per share</u> | | | |
| Profit attributable to ordinary shareholders of the parent | \$ 357,047 | 74,867 | |
| Assumed conversion of all dilutive potential ordinary shares | | | |
| Employees' bonus | - | 313 | |
| Employee stock options | - | 202 | |
| Employee restricted stocks | - | 38 | |
| Profit attributable to ordinary shareholders of the parent plus assumed conversion of all dilutive potential ordinary stocks | \$ 357,047 | 75,420 | \$ 4.73 |

(27) Business combinations

The Acquisition of D-Tech Optoelectronics, Inc.

- A. The Company's Board of Directors approved on July 13, 2017 for its wholly owned subsidiary, Global Communication Semiconductors, LLC, to enter into an Acquisition Agreement with D-Tech Optoelectronics, Inc. ("D-Tech") to acquire all of the outstanding shares of D-Tech at an aggregate consideration of US\$13 million in cash. The above acquisition transaction has been completed on July 20, 2017 (USA time). With the completion of the acquisition, the Company acquired 100% shareholding of the wholly-owned subsidiary of D-Tech, D-Tech Optoelectronics (Taiwan) Corporation. The Group expects that the acquisition will allow the Group and D-Tech to further integrate research technology, manufacturing capabilities and workforce to enhance their product offering at an accelerated pace, optimize their product integration, and provide customers with better services and products. The main goal of the acquisition is to gain a competitive advantage, and enhance market and margin expansion opportunities with greater scale.
- B. The following table summarises the consideration paid for D-Tech and the fair values of the assets acquired and liabilities assumed at the acquisition date:

| | <u>July 20, 2017</u> |
|--|----------------------|
| Consideration | |
| Cash paid (US\$ 13 million) | \$ <u>395,070</u> |
| Fair value of the identifiable assets acquired and liabilities assumed | |
| Notes receivable and accounts receivable | 65,216 |
| Other receivables and prepayments | 3,828 |
| Other current assets | 308 |
| Inventories | 71,621 |
| Property, plant and equipment | 103,167 |
| Other non-current assets | 9,329 |
| Accounts payable | (16,216) |
| Other payables | (18,270) |
| Other current liabilities | (174) |
| Other non-current liabilities | (308) |
| Total identifiable net assets | <u>218,501</u> |
| Goodwill (US\$ 5.81 million) | \$ <u>176,569</u> |

C. The operating revenue and profit before income tax included in the 2017 consolidated statement of comprehensive income since July 20, 2017 contributed by D-Tech was \$154,615 and \$10,232, respectively. Had D-Tech been consolidated from January 1, 2017, the consolidated statement of comprehensive income would show an increase in operating revenue of \$412,544 and a decrease in profit before income tax of \$11,455.

The Acquisition of Xiamen San'an Integrated Circuit Co., Ltd.

A. The Company's Board of Directors approved on June 25, 2018 that the Company enter into an Equity Interest Transfer Agreement (the "Agreement") with Xiamen San'an Integrated Circuit Co., Ltd. ("San'an") to acquire the 2% shareholding of Xiamen Global Advanced Semiconductor Co., Ltd. ("Xiamen Global") in the amount of US\$80 thousand. After the completion of the transfer, Xiamen Global became a subsidiary of the Group. After the 2% shareholding of Xiamen Global was transferred to the Company, the Company will invest US\$2.04 million and San'an will invest US\$1.96 million in Xiamen Global, which represents 51% and 49% of the registered capital, respectively. The purpose of this equity transfer is to speed up the manufacturing transfer process, enabling the Group to accelerate the application of advanced production process in connection with 5th generation wireless system and other smartphones.

B. The following table summarises the consideration paid for Xiamen Global and the fair values of the assets acquired and liabilities assumed at the acquisition date:

| | <u>September 30, 2018</u> |
|---|---------------------------|
| Consideration | |
| Cash paid (US\$80 thousand) | \$ 2,442 |
| | <u>2,442</u> |
| Fair value of equity interest in Xiamen Global held before the business combination | 11,401 |
| Fair value of the non-controlling interest | <u>13,300</u> |
| | <u>27,143</u> |
| Fair value of the identifiable assets acquired and liabilities assumed | |
| Cash | 27,263 |
| Property, plant and equipment | 52 |
| Other payables | (168) |
| Other current liabilities | <u>(4)</u> |
| Total identifiable net assets | <u>27,143</u> |
| Goodwill | <u>\$ -</u> |

C. The operating revenue and profit before income tax included in the consolidated statement of comprehensive income since September 2018 contributed by Xiamen Global were \$0 and (\$5,319), respectively. Had Xiamen Global been consolidated from January 1, 2018, the consolidated statement of comprehensive income would show an increase in operating revenue of \$0 and a decrease in profit before income tax of (\$6,862).

(28) Operating lease commitments

The Group leases property and plant under non-cancellable operating lease agreements. Most of the lease agreements can be renewed based on the market prices upon termination of the leases. The future aggregate minimum lease payments under non-cancellable operating leases are as follows:

| | <u>December 31, 2018</u> | <u>December 31, 2017</u> |
|---|--------------------------|--------------------------|
| Not later than one year | \$ 11,602 | \$ 9,897 |
| Later than one year but not later than five years | <u>30,811</u> | <u>26,486</u> |
| | <u>\$ 42,413</u> | <u>\$ 36,383</u> |

(29) Supplemental cash flow information

A. Investing activities with partial cash payments:

| | Years ended December 31, | |
|--|--------------------------|-------------------|
| | 2018 | 2017 |
| Acquisition of property, plant and equipment | \$ 114,756 | \$ 234,217 |
| Add: Ending balance of prepayments for equipment (Note) | 106,676 | 52,857 |
| Less: Beginning balance of prepayments for equipment (Note) | (52,857) | (118,721) |
| Less: Prepayments for equipment - Acquired through business combinations | - | (7,461) |
| Less: Ending balance of finance lease liabilities | (4,695) | (13,872) |
| Add: Beginning balance of finance lease liabilities | 13,872 | 26,636 |
| Less: Ending balance of payables for equipment | (27,460) | (5,703) |
| Add: Beginning balance of payables for equipment | 5,703 | 29,272 |
| Cash paid during the period | <u>\$ 155,995</u> | <u>\$ 197,225</u> |

Note: Shown as "Other non-current assets".

B. Financing activities with no cash flow effect:

| | Years ended December 31, | |
|---|--------------------------|-------------------|
| | 2018 | 2017 |
| Convertible bonds being converted to capital stocks | <u>\$ 89,161</u> | <u>\$ 331,430</u> |

(30) Changes in liabilities from financing activities

| | Short-term borrowings | Bonds payable | Long-term borrowings (Note) | Liabilities from financing activities |
|--|-----------------------|---------------|-----------------------------|---------------------------------------|
| At January 1, 2018 | \$ 20,000 | \$ 60,006 | \$ 95,163 | \$ 175,169 |
| Changes in cash flow from financing activities | 300 | (2,800) | (19,621) | (22,121) |
| Bonds converted | - | (58,700) | - | (58,700) |
| Discount on bonds payable | - | 1,494 | - | 1,494 |
| Impact of changes in foreign exchange rate | - | - | 2,700 | 2,700 |
| At December 31, 2018 | <u>\$ 20,300</u> | <u>\$ -</u> | <u>\$ 78,242</u> | <u>\$ 98,542</u> |

Note: Current portion is included.

7. RELATED PARTY TRANSACTIONS

Key management compensation

| | Years ended December 31, | |
|---|--------------------------|------------------|
| | 2018 | 2017 |
| Salaries and other short-term employee benefits | \$ 85,692 | \$ 69,435 |
| Post-employment benefits | 2,593 | 2,038 |
| Compensation costs of share-based payment | 21,283 | 11,611 |
| | <u>\$ 109,568</u> | <u>\$ 83,084</u> |

8. PLEGDED ASSETS

As of December 31, 2018 and 2017, the Group's assets pledged as collateral were as follows:

| Assets | December 31, 2018 | December 31, 2017 | Purpose |
|---|-------------------|-------------------|---|
| Land | \$ 141,466 | \$ 137,045 | Long-term borrowings |
| Buildings | 85,103 | 85,055 | Long-term borrowings |
| Time deposits (Shown as "Other current assets") | 31,131 | 29,760 | Short-term borrowings |
| Time deposits (Shown as "Other non-current assets") | 371 | 59,828 | Custom guarantee for imported goods and secured convertible bonds |
| Refundable deposits (Shown as "Other non-current assets") | 3,425 | 3,234 | Deposits for office rental and waste water treatment |

9. SIGNIFICANT CONTINGENT LIABILITIES AND UNRECOGNIZED CONTRACT COMMITMENTS

(1) Please refer to Note 6(28) for the operating lease commitments.

(2) Capital expenditures contracted for at the balance sheet date but not yet incurred and are cancellable without cause are as follows:

| | December 31, 2018 | December 31, 2017 |
|-------------------------------|-------------------|-------------------|
| Property, plant and equipment | <u>\$ 16,491</u> | <u>\$ 15,590</u> |

10. SIGNIFICANT DISASTER LOSS

None.

11. SIGNIFICANT EVENTS AFTER THE REPORTING PERIOD

A. On November 2, 2018, the Board of Directors adopted a resolution to issue the 2018 employee stock option plan. The total number of new shares proposed for the issuance for exercise of options shall be 1,000,000 shares with a par value of \$10 (in dollars), which represents for a total amount of \$10,000 thousand. The subscription prices, which is the exercise price of the options, will be equal to the closing prices of the Company's common shares listed on the Taipei Exchange on the grant dates. The rights and obligations of these shares issued are same as other issued ordinary shares.

The 2018 employee stock option plan has been applied with and approved by FSC on January 7, 2019.

- B. The Company's Board of Directors approved on April 2, 2018 the issuance of common stocks for cash through the issuance of GDRs. The Company's GDRs began trading on the Luxembourg Stock Exchange on January 21, 2019. Please refer to Note 6(16) E.
- C. On January 23, 2019, the Board of Directors resolved to enter into the Strategic Cooperation Agreement with Epistar Corporation ("Epistar") that Epistar and its wholly owned subsidiary, Unikorn Semiconductor Corporation ("Unikorn") will provide 6-inch foundry services for the Company, and the Company and its subsidiaries will provide technical support of III-V compound semiconductor manufacturing process to Epistar. The Company is going to invest in Unikorn by acquiring 16,400 thousand ordinary shares representing 16.4% of Unikorn's common stock issued and outstanding 100 million shares.
- D. The appropriation of 2018 earnings had been proposed by the Board of Directors on March 15, 2019. Please refer to Note 6(18).

12. OTHERS

(1) Capital management

In order to safeguard the Group's ability to adapt to the changes in the industry and to accelerate the new product development, the Company's objective when managing capital is to maintain the sufficient financial resources to support the operating capital, capital expenditures, research and development activities, repayment of debts and dividend paid to shareholders, etc.

(2) Financial instruments

A. Financial instruments by category

| | <u>December 31, 2018</u> | <u>December 31, 2017</u> |
|---|--------------------------|--------------------------|
| <u>Financial assets</u> | | |
| Financial assets at amortized cost | | |
| /Loans and receivables | | |
| Cash and cash equivalents | \$ 1,512,863 | \$ 1,119,712 |
| Notes receivable | 127 | 594 |
| Accounts receivable | 212,806 | 296,921 |
| Other receivables | 19,026 | 15,254 |
| Guarantee deposits paid | 3,425 | 3,234 |
| Time deposits (over three-month period) | 92,942 | 89,588 |
| | <u>\$ 1,841,189</u> | <u>\$ 1,525,303</u> |
| <u>Financial liabilities</u> | | |
| Financial liabilities measured at fair value through profit or loss | | |
| | <u>\$ -</u> | <u>\$ 31,204</u> |
| Financial liabilities at amortized cost | | |
| Short-term borrowings | \$ 20,300 | \$ 20,000 |
| Accounts payable | 19,423 | 17,867 |
| Other payables | 164,280 | 139,249 |
| Finance lease liabilities (including current portion) | 4,695 | 13,872 |
| Bonds payable (including current portion) | - | 60,006 |
| Long-term borrowings (including current portion) | 78,242 | 95,163 |
| | <u>\$ 286,940</u> | <u>\$ 346,157</u> |

B. Financial risk management policies

- a) The Group's activities expose it to a variety of financial risks: market risk (including foreign exchange risk, price risk and interest rate risk), credit risk and liquidity risk.
- b) Risk management is carried out by the Group's finance team under policies approved by the Board of Directors. The Group's finance team identifies, evaluates and hedges financial risks in close cooperation with the Group's operating units.

C. Significant financial risks and degrees of financial risks

a) Market risk

Foreign exchange risk

The Group's businesses are mainly conducted in its functional currency. Therefore, the foreign exchange risk is deemed minimal.

Cash flow and fair value interest rate risk

- i. The Group's interest rate risk arises from short-term borrowings. Borrowings issued at variable rates expose the Group to cash flow interest rate risk which is partially offset by cash and cash equivalents held at variable rates. Borrowings issued at fixed rates expose the Group to fair value interest rate risk. During the years ended December 31, 2018 and 2017, the Group's borrowings at variable rate were denominated in the NTD.
- ii. Based on the simulations performed, the impact on post-tax profit of a 1% shift, with all other variables held constant, would be a maximum increase or decrease of \$160 and \$166 for the years ended December 31, 2018 and 2017, respectively, as a result of the decrease or increase in interest expense which is affected by variable rates.

b) Credit risk

- i. Credit risk refers to the risk of financial loss to the Group arising from default by the clients or counterparties of financial instruments on the contract obligations. The main factor is that counterparties could not repay in full the accounts receivable based on the agreed terms, and the credit risk of financial assets at amortized cost.
- ii. The Group manages their credit risk taking into consideration the entire group's concern. For banks and financial institutions, only independently rated parties with a minimum rating of "BBB+" are accepted. According to the Group's credit policy, each local entity in the Group is responsible for managing and analysing the credit risk for each of their new clients before standard payment and delivery terms and conditions are offered. Internal risk control assesses the credit quality of the customers, taking into account their financial position, past experience and other factors. Individual risk limits are set based on internal or external ratings in accordance with limits set by the Board of Directors. The utilization of credit limits is regularly monitored.
- iii. The Group does not hold any collateral as security for notes receivable and accounts receivable. As of December 31, 2018 and 2017, with no collateral held or other credit enhancements, the maximum exposure to credit risk in respect of the the Group's notes receivable was \$127 and \$594, respectively, and the maximum exposure to credit risk in respect of the Group's accounts receivable was \$212,806 and \$296,921, respectively.
- iv. The Group adopts the assumption under IFRS 9, that is, the default occurs when the contract payments are past due over 90 days.
- v. The Group wrote off the financial assets, which cannot be reasonably expected to be recovered, after initiating recourse procedures. However, the Group will continue executing the recourse procedures to secure their rights.
- vi. The Group classifies customers' notes receivable and accounts receivable in accordance with credit risk on trade. The Group applies the simplified approach using loss rate methodology to estimate expected credit loss.

vii. The Group used the forecastability of external research report to adjust historical and timely information for a specific period to assess the default possibility of notes receivable and accounts receivable. On December 31, 2018, the loss rate methodology is as follows:

| Notes Receivable | Not | | | | Total |
|-----------------------------|----------|--|--|--|-------|
| | past due | | | | |
| <u>At December 31, 2018</u> | | | | | |
| Expected loss rate | 0% | | | | |
| Total book value | \$ 127 | | | | |
| Loss allowance | \$ - | | | | |

| Accounts Receivable | Less than | | | Total | |
|-----------------------------|------------|------------------|---|-------------------|------------|
| | Not | Less than | More than | | |
| | past due | 90 days past due | 180 days and more than 90 days past due | 180 days past due | |
| <u>At December 31, 2018</u> | | | | | |
| Expected loss rate | 0%~1% | 1%~15% | 16%~31% | 31%~75% | |
| Total book value | \$ 173,428 | \$ 38,750 | \$ 1,255 | \$ - | \$ 213,433 |
| Loss allowance | \$ 17 | \$ 388 | \$ 222 | \$ - | \$ 627 |

viii. Movements in relation to the Group applying the simplified approach to provide loss allowance for notes and accounts receivable was as follows:

| | 2018 | |
|--------------------------------------|-------------------------------|-------|
| | Notes and accounts receivable | |
| At January 1_IAS 39 | \$ | 1,117 |
| Adjustments under new standards | | - |
| At January 1_IFRS 9 | | 1,117 |
| Reversal of provision for impairment | (| 515) |
| Effect of foreign exchange | | 25 |
| At December 31 | \$ | 627 |

The abovementioned provision amounts are made based on the easimated expected credit loss in the next 12 months.

ix. Credit risk information on December 31, 2017 is provided in Note 12(4).

c) Liquidity risk

- i. Cash flow forecasting is performed by the operating entities of the Group and aggregated by the Group's finance team. The Group's finance team monitors rolling forecasts of the Group's liquidity requirements to ensure the Group has sufficient cash to meet operational needs. Such forecasting takes into consideration the Group's debt financing plans, compliance with internal balance sheet ratio targets and, if applicable, external regulatory or legal requirements.
- ii. Surplus cash held by the operating entities over and above balance required for working capital management are managed for investment appropriately. The instruments chose

would be with appropriate maturities or sufficient liquidity to provide sufficient headroom as determined by the above-mentioned forecasts.

iii. The Group has the following undrawn borrowing facilities:

| | <u>December 31, 2018</u> | <u>December 31, 2017</u> |
|--------------------------|--------------------------|--------------------------|
| Floating rate: | | |
| Expiring within one year | \$ 25,700 | \$ 178,560 |

Note: The facilities expiring within one year are annual facilities subject to renegotiation at various dates during 2019.

iv. The table below analyses the Group's non-derivative financial liabilities and net-settled or gross-settled derivative financial liabilities into relevant maturity groupings based on the remaining period at the balance sheet date to the contractual maturity date for non-derivative financial liabilities and to the expected maturity date for derivative financial liabilities. The amounts disclosed in the table are the contractual undiscounted cash flows.

| | <u>Less than 1 year</u> | <u>Over 1 year</u> |
|---|-------------------------|--------------------|
| <u>Non-derivative financial liabilities:</u> | | |
| December 31, 2018 | | |
| Short-term borrowings | \$ 20,340 | \$ - |
| Accounts payable | 19,423 | - |
| Other payables | 164,280 | - |
| Finance lease liabilities | 4,793 | - |
| Long-term borrowings (including current portion) | 23,604 | 62,529 |
| | <u>Less than 1 year</u> | <u>Over 1 year</u> |
| <u>Non-derivative financial liabilities:</u> | | |
| December 31, 2017 | | |
| Short-term borrowings | \$ 20,062 | \$ - |
| Accounts payable | 17,867 | - |
| Other payables | 139,249 | - |
| Finance lease liabilities (including current portion) | 9,684 | 4,643 |
| Bonds payable (including current portion and financial liabilities at fair value through profit or loss) | 91,210 | - |
| Long-term borrowings (including current portion) | 22,867 | 83,442 |

(3) Fair value information

A. The different levels that the inputs to valuation techniques are used to measure fair value of financial and non-financial instruments have been defined as follows:

Level 1: Quoted prices (unadjusted in active markets for identical assets or liabilities that the entity can access at the measurement date.) A market is regarded as active where a market in which transactions for the asset or liability takes place with sufficient frequency and volume to provide pricing information on an ongoing basis.

Level 2: Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.

Level 3: Unobservable inputs for the asset or liability.

B. Financial instruments not measured at fair value

(a) Except for the item listed in the table below, the carrying amounts measured at amortized cost approximate the fair values of the Group's financial instruments, including cash and cash equivalents, notes receivable, accounts receivable, other receivables, refundable deposits, time deposits (over three-month period), short-term borrowings, current contract liabilities, accounts payable, other payables, finance lease liabilities (accounted for under 'Other current liabilities' and 'Other non-current liabilities') and long-term borrowings (including current portion):

As of December 31, 2018, the Group had no financial instruments not measured at fair value other than the aforementioned items.

| | Book value | December 31, 2017 | | |
|---------------|------------|-------------------|---------|-----------|
| | | Fair value | | |
| | | Level 1 | Level 2 | Level 3 |
| Bonds payable | \$ 60,006 | \$ - | \$ - | \$ 61,342 |

(b) The methods and assumptions of fair value measurement are as follows:

Convertible bonds payable: Regarding the convertible bonds issued by the Group, the fair value is estimated using Binomial Model.

C. The related information of financial and non-financial instruments measured at fair value by level on the basis of the nature, characteristics and risks of the assets and liabilities are as follows:

(a) The related information of natures of the assets and liabilities is as follows:

As of December 31, 2018, the Group had no financial and non-financial instruments measured at fair value.

| | <u>Level 1</u> | <u>Level 2</u> | <u>Level 3</u> |
|--|----------------|----------------|----------------|
| December 31, 2017 | | | |
| Liabilities | | | |
| <u>Recurring fair value measurements</u> | | | |
| Financial liabilities at fair value through profit or loss | \$ - | \$ - | \$ 31,204 |

For the years ended December 31, 2018 and 2017, there were no non-recurring fair value measurement financial instruments.

- D. For the years ended December 31, 2018 and 2017, there was no transfer between Level 1 and Level 2 financial instruments.
- E. The following chart is the movement of Level 3 financial instruments for the years ended December 31, 2018 and 2017:

| | <u>Financial liabilities at fair value through profit or loss</u> | |
|--|---|------------------|
| | <u>2018</u> | <u>2017</u> |
| At January 1 | \$ 31,204 | \$ 69,504 |
| Converted during the year | (28,961) | (46,981) |
| Effect of foreign exchange | 79 | (304) |
| (Gain) loss recognized in profit or loss | (2,322) | 8,985 |
| At December 31 | <u>\$ -</u> | <u>\$ 31,204</u> |

- F. The following is the quantitative information of significant unobservable inputs and sensitivity analysis of changes in significant unobservable inputs to valuation model used in Level 3 fair value measurement:

As of December 31, 2018, the Group had no financial instruments measured in Level 3 fair value measurement.

| | <u>Fair value at December 31, 2017</u> | <u>Valuation technique</u> | <u>Significant unobservable input</u> | <u>Range (weighted average)</u> | <u>Relationship of input to fair value</u> |
|--|--|--------------------------------|---|---|--|
| Call options, put options and conversion options embedded in convertible bonds | \$ 31,204 | Binomial model | Stock price volatility | 41.53% | The higher the volatility, the higher the fair value |

- G. The Group has carefully assessed the valuation models and assumptions used to measure fair value. However, use of different valuation models or assumptions may result in different measurement. The following is the effect of profit or loss or of other comprehensive income from financial assets and liabilities categorised within Level 3 if the inputs used to valuation models have changed:

As of December 31, 2018, the Group had no financial liabilities at fair value through profit or loss.

| | Input | Change | December 31, 2017 | |
|--|-------------|--------|------------------------------|---------------------|
| | | | Recognized in profit or loss | |
| | | | Favourable change | Unfavourable change |
| Financial liabilities | | | | |
| Financial liabilities at fair value through profit or loss | Stock price | ± 1% | \$ - | \$ - |
| | volatility | ± 5% | \$ - | \$ - |

(4) Effects on initial application of IFRS 9 and information in relation to the application of IAS 39 for the year ended December 31, 2017

A. The significant accounting policies adopted in the year ended December 31, 2017 are as follows:

(a) Available-for-sale financial assets

- i. Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories.
- ii. On a regular way purchase or sale basis, available-for-sale financial assets are recognized and derecognized using trade date accounting.
- iii. Available-for-sale financial assets are initially recognized at fair value plus transaction costs. These financial assets are subsequently remeasured and stated at fair value, and any changes in the fair value of these financial assets are recognized in other comprehensive income.

(b) Accounts receivable

Accounts receivable are loans and receivables originated by the entity. They are created by the entity by selling goods or providing services to customers in the ordinary course of business. Accounts receivable are initially recognized at fair value and subsequently measured at amortized cost using the effective interest method, less provision for impairment. However, since the short-term accounts receivable bear no interest, considering the discounting effects would not be significant, the Group subsequently measures those receivables at the invoice amount.

(c) Impairment of financial assets

- i. The Group assesses at each balance sheet date whether there is objective evidence that a financial asset or a group of financial assets is impaired as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.
- ii. The criteria that the Group uses to determine whether there is objective evidence of an impairment loss is as follows:
 - (i) Significant financial difficulty of the issuer or debtor;
 - (ii) A breach of contract, such as a default or delinquency in interest or principal payments;
 - (iii) It becomes probable that the borrower will enter bankruptcy or other financial reorganization; or
 - (iv) Information about significant changes with an adverse effect that have taken place in the technology, market, economic or legal environment in which the issuer operates,

and indicates that the cost of the investment in the equity instrument may not be recovered.

iii. When the Group assesses that there has been objective evidence of impairment and an impairment loss has occurred, accounting for impairment is made as follows according to the category of financial assets:

(i) Financial assets measured at amortized cost

The amount of the impairment loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate, and is recognized in profit or loss. If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment loss was recognized, the previously recognized impairment loss is reversed through profit or loss to the extent that the carrying amount of the asset does not exceed its amortized cost that would have been at the date of reversal had the impairment loss not been recognized previously. Impairment loss is recognized and reversed by adjusting the carrying amount of the asset through the use of an impairment allowance account.

(ii) Available-for-sale financial assets

The amount of the impairment loss is measured as the difference between the asset's acquisition cost (less any principal repayment and amortization) and current fair value, less any impairment loss on that financial asset previously recognized in profit or loss, and is reclassified from 'other comprehensive income' to 'profit or loss'. If, in a subsequent period, impairment loss of an investment in an equity instrument recognized in profit or loss shall not be reversed through profit or loss. Impairment loss is recognized and reversed by adjusting the carrying amount of the asset through the use of an impairment allowance account.

(d) Financial liabilities at fair value through profit or loss

i. Financial liabilities at fair value through profit or loss are financial liabilities held for trading or financial liabilities designated as at fair value through profit or loss on initial recognition. Financial liabilities are classified in this category of held for trading if acquired principally for the purpose of repurchasing in the short-term. Derivatives are also categorised as financial liabilities held for trading unless they are designated as hedges. Financial liabilities that meet one of the following criteria are designated as at fair value through profit or loss on initial recognition:

(i) Hybrid (combined) contracts;

(ii) They eliminate or significantly reduce a measurement or recognition inconsistency; or

(iii) They are managed and their performance is evaluated on a fair value basis, in accordance with a documented risk management policy.

ii. Financial liabilities at fair value through profit or loss are initially recognized at fair value. Related transaction costs are expensed in profit or loss. These financial liabilities are subsequently remeasured and stated at fair value, and any changes in the fair value of these

financial liabilities are recognized in profit or loss.

B. The significant accounts as of December 31, 2017 are as follows:

As of December 31, 2017, the Group had no available-for-sale financial assets.

- (a) The Group recognized \$7,532 in other comprehensive (loss) income for fair value change for the year ended December 31, 2017.
- (b) The Group reclassified \$18,698 from equity to profit or loss and recognized \$29,276 in gain on disposal of available-for-sale financial assets for the year ended December 31, 2017.

C. Credit risk information for the year ended December 31, 2017 are as follows:

- (a) Credit risk refers to the risk of financial loss to the Group arising from default by the clients or counterparties of financial instruments on the contract obligations. According to the Group's credit policy, each local entity in the Group is responsible for managing and analysing the credit risk for each of their new clients before standard payment and delivery terms and conditions are offered. Internal risk control assesses the credit quality of the customers, taking into account their financial position, past experience and other factors. Individual risk limits are set based on internal or external ratings in accordance with limits set by the Board of Directors. The utilisation of credit limits is regularly monitored. Credit risk arises from cash and cash equivalents, deposits with banks and financial institutions, as well as outstanding receivables.
- (b) As of December 31, 2017 the Group's maximum credit risk exposure is mainly from the carrying amount of financial asset recognized in the consolidated balance sheet.
- (c) The credit quality of accounts receivable that were neither past due nor impaired was in the following categories based on the Group's Credit Quality Control Policy:

| | <u>December 31, 2017</u> |
|---------|--------------------------|
| Group 1 | \$ 127,182 |
| Group 2 | 113,919 |
| Group 3 | 8,197 |
| | <u>\$ 249,298</u> |

Group 1: Annual sales transactions exceeding US\$2.5 million.

Group 2: Annual sales transactions exceeding US\$100 thousand, but less than US\$2.5 million.

Group 3: Annual sales transactions below US\$100 thousand.

(d) The aging analysis of accounts receivable that were past due but not impaired is as follows:

| | <u>December 31, 2017</u> |
|---------------|--------------------------|
| Up to 30 days | \$ 34,544 |
| 31 to 60 days | 8,269 |
| 61 to 90 days | 445 |
| Over 90 days | 4,365 |
| | <u>\$ 47,623</u> |

(e) Analysis of movement of impaired accounts receivable:

- i. As of December 31, 2017, the Group's accounts receivable that was impaired amounted to \$1,117.

ii. Movements on the Group's provision for impairment of accounts receivable are as follows:

| | 2017 | | |
|--|----------------------|-----------------|-----------|
| | Individual provision | Group provision | Total |
| At January 1 | \$ 20,910 | \$ - | \$ 20,910 |
| Acquired through business combination | - | 4,301 | 4,301 |
| Revaluation reversal for items acquired through business combination | - | (4,301) | (4,301) |
| Provision for impairment | - | 1,117 | 1,117 |
| Write-offs during the year | (20,910) | - | (20,910) |
| At December 31 | \$ - | \$ 1,117 | \$ 1,117 |

(5) Effects of initial application of IFRS 15 and information in relation to the adoption of IAS 18 for the year ended December 31, 2017

A. The significant accounting policies of revenue recognition for the year ended December 31, 2017 are as follows:

Revenue recognition

(a) Sales of goods

The Group engages in the manufacturing of compound semiconductor wafer and foundry services as well as manufacturing and selling of advanced optoelectronics technology products. Revenue is measured at the fair value of the consideration received or receivable taking into account value-added tax, returns, rebates and discounts for the sale of goods to external customers in the ordinary course of the Group's activities. Revenue arising from the sales of goods is recognized when the Group has delivered the goods to the customer, the amount of sales revenue can be measured reliably and it is probable that the future economic benefits associated with the transaction will flow to the entity. The delivery of goods is completed when the significant risks and rewards of ownership have been transferred to the customer, the Group retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold, and the customer has accepted the goods based on the sales contract or there is objective evidence showing that all acceptance provisions have been satisfied.

(b) Service revenue

The Group provides transfer services of wafer manufacturing process and development knowledge to other wafer foundries. Revenue from delivering services is recognized based on the percentage of the actual services performed as of the financial reporting date to the total services to be performed when the outcome of services provided can be estimated reliably. If the outcome of a service contract cannot be estimated reliably, contract revenue should be recognized only to the extent that contract costs incurred are likely to be recoverable.

(c) Royalty income

Royalty income is recognized based on substantial terms of the arrangements and when it is probable that future economic benefits will flow to the entity and these benefits can be measured reliably. The revenue is accounted for under the accrual basis.

- B. The operating revenue recognised by using previous accounting policies for the year ended December 31, 2017 are as follows:

| | <u>Year ended December 31, 2017</u> | |
|-----------------|-------------------------------------|------------------|
| Sales revenue | \$ | 1,875,619 |
| Service revenue | | 15,216 |
| Royalty revenue | | 34,997 |
| | <u>\$</u> | <u>1,925,832</u> |

- C. The effects and description of current balance sheet items if the Group continues adopting above accounting policies as of and for the year ended December 31, 2018 are as follows:

| | | <u>December 31, 2018</u> | | |
|--|--------------------|--------------------------|------------|-------------------|
| | | Balance by using | | |
| <u>Balance sheet items</u> | <u>Description</u> | Balance by using | previous | Effects from |
| | | IFRS 15 | accounting | changes in |
| | | | policies | accounting policy |
| Accounts receivable | Note 1 | \$ 212,805 | \$ 211,810 | \$ 995 |
| Refund liabilities | | | | |
| (Shown as "Other current liabilities-others") | Note 1 | (995) | - | (995) |
| Contract liabilities | Note 2 | (16,302) | - | (16,302) |
| Advance sales receipts | Note 2 | - | (16,302) | 16,302 |

Note 1: Under IFRS 15, refund liabilities in relation to expected sales discounts and allowances were previously presented as accounts receivable - allowance for sales discounts in the balance sheet.

Note 2: Under IFRS 15, liabilities in relation to contracts with customers are recognized as contract liabilities, but were previously presented as advance sales receipts in the balance sheet.

13. SUPPLEMENTARY DISCLOSURES

(1) Significant transactions information

- (a) Loans to others: Please refer to table 1.
- (b) Provision of endorsements and guarantees to others: Please refer to table 2.
- (c) Holding of marketable securities at the end of the period (not including subsidiaries, associates and joint ventures): None.
- (d) Acquisition or sale of the same security with the accumulated cost exceeding \$300 million or 20% of the Company's paid-in capital: None.
- (e) Acquisition of real estate reaching \$300 million or 20% of paid-in capital or more: None.
- (f) Disposal of real estate reaching \$300 million or 20% of paid-in capital or more: None.
- (g) Purchases or sales of goods from or to related parties reaching \$100 million or 20% of paid-in capital or more: None.
- (h) Receivables from related parties reaching \$100 million or 20% of paid-in capital or more: None.
- (i) Derivative financial instruments undertaken during the year ended December 31, 2018: Please refer to Notes 6(9) and 6(10).
- (j) Significant inter-company transactions during the year ended December 31, 2018: Please refer to table 9.

(2) Information on investees

Names, locations and other information of investee companies (not including investees in mainland China): Please refer to table 10.

(3) Information on investments in mainland China

Please refer to table 11.

14. SEGMENT INFORMATION

(1) General information

The Group operates business only in a single industry. The Chief Operating Decision-Maker, who allocates resources and assesses performance of the Group as a whole, has identified that the Group has only one reportable operating segment.

(2) Segment information

The segment information provided to the Chief Operating Decision-Maker for the reportable segments is as follows:

| | Years ended December 31, | |
|---------------------------------|--------------------------|--------------|
| | 2018 | 2017 |
| Revenue from external customers | \$ 1,952,411 | \$ 1,925,832 |
| Inter-segment revenue | - | - |
| Total segment revenue | \$ 1,952,411 | \$ 1,925,832 |
| Segment income (Note) | \$ 391,014 | \$ 424,053 |
| Segment assets | \$ 3,402,284 | \$ 2,981,355 |
| Segment liabilities | \$ 389,499 | \$ 443,786 |

Note: Exclusive of income tax.

(3) Reconciliation for segment income (loss)

The Company and subsidiaries engage in a single industry. The Chief Operating Decision-Maker assesses performance and allocates resources of the whole group. The Group is regarded as a single operating segment. Therefore, there is no inter-segment revenue. The revenue from external parties reported to the Chief Operating Decision-Maker is measured in a manner consistent with that in the consolidated statement of comprehensive income. The amount provided to the Chief Operating Decision-Maker with respect to total assets is measured in a manner consistent with that in the consolidated balance sheet.

(4) Information on products and services

Please refer to Notes 6(20) and 12(5) B for the related information.

(5) Geographical information

Geographical information for the years ended December 31, 2018 and 2017 is as follows:

| Area | Years ended December 31, | | | |
|---------------|--------------------------|--------------------|--------------|--------------------|
| | 2018 | | 2017 | |
| | Revenue | Non-current assets | Revenue | Non-current assets |
| China | \$ 951,455 | \$ 50 | \$ 954,469 | \$ - |
| United States | 724,517 | 994,688 | 633,663 | 914,984 |
| Taiwan | 205,719 | 24,864 | 314,415 | 25,951 |
| Others | 70,720 | - | 23,285 | 59,520 |
| | \$ 1,952,411 | \$ 1,019,602 | \$ 1,925,832 | \$ 1,000,455 |

(6) Major customer information

Major customer information of the Group for the years ended December 31, 2018 and 2017 is as follows:

| | Years ended December 31, | | | |
|---|--------------------------|-------------------|----------------|-------------------|
| | 2018 | | 2017 | |
| | <u>Revenue</u> | <u>% of sales</u> | <u>Revenue</u> | <u>% of sales</u> |
| H | \$ 391,603 | 20 | \$ 260,269 | 14 |

GCS HOLDINGS, INC.

Loans to others

Year ended December 31, 2018

Table 1

Expressed in thousands of NTD
(Except as otherwise indicated)

| No. (Note 1) | Creditor | Borrower | General ledger account | Is a party related | Balance at December 31, 2018 | Actual amount drawn down | Interest rate | Nature of loan (Note 2) | Amount of transactions with the borrower | Reason for short-term financing | Allowance for doubtful accounts | Collateral | Limit on loans granted to a single party (Note 3) | Ceiling on total loans granted (Note 3) | Footnote |
|-----------------|--|------------------------------------|----------------------------------|--------------------|------------------------------|--------------------------|---------------|-------------------------|--|---------------------------------|---------------------------------|------------|---|---|----------|
| | | | | | | | | | | | | | | | |
| 0 | GCS Holdings, Inc. | GCS Device Technologies, Co., Ltd. | Other receivable - related party | Yes | \$ 61,660 | \$ 61,440 | - | 2 | \$ - | Operation | \$ - | None | \$ 300,203 | \$ 1,200,810 | - |
| 1 | Global Communication Semiconductors, LLC | D-Tech Optoelectronics, Inc. | Other receivable - related party | Yes | 61,920 | 61,440 | - | 2 | - | Operation | - | None | 300,203 | 1,200,810 | - |

Note 1: The numbers filled in for the loans provided by the Company or subsidiaries are as follows:

(1) The Company is '0'.

(2) The subsidiaries are numbered in order starting from '1'.

Note 2: The column of 'Nature of loan' shall fill in 'Business transaction or 'Short-term financing'.

(1) The business transaction is '1'.

(2) The short-term financing is '2'.

Note 3: According to the Company's "Procedures for Lending Funds to Other Parties", the total amount available for lending purpose shall not exceed forty percent (40%) of the net worth of the Company. The total amount for lending to a company having business relationship with the Company shall not exceed the total transaction amount between the parties during the period of twelve (12) months prior to the time of lending (For the purpose of this Procedure, the "transaction amount" shall mean the sales or purchasing amount between the parties, whichever is higher), and shall not exceed ten percent (10%) of the net worth of the Company. The total amount for lending to a company for funding for a short-term period shall not exceed ten percent (10%) of the net worth of the Company. In addition, the total amount lendable to any one borrower shall be no more than thirty percent (30%) of the borrower's net worth, provided that this restriction will not apply to subsidiaries whose voting shares are 100% owned, directly or indirectly, by the Company. The total amount for fund-lending between the subsidiaries whose voting shares are 100% owned, directly or indirectly, by the Company will not be subject to the limit of forty percent (40%) of the net worth of the lending subsidiary.

GCS HOLDINGS, INC.

Provision of endorsements and guarantees to others

Year ended December 31, 2018

Table 2

Expressed in thousands of NTD
(Except as otherwise indicated)

| Number (Note 1) | Endorser/ guarantor | Party being endorsed/guaranteed | Relationship with the endorser/ guarantor (Note 2) | Limit on endorsements/ guarantees provided for a single party (Note 3) | Maximum outstanding endorsement/ guarantee amount for the year ended December 31, 2018 | Outstanding endorsement/ guarantee amount at December 31, 2018 | Actual amount drawn down | Amount of endorsements/ guarantees secured with collateral | Ratio of accumulated endorsement/ guarantee amount to net asset value of the endorser/ guarantor company | Ceiling on total amount of endorsements/ guarantees provided (Note 3) | Provision of endorsements/ guarantees by parent company to subsidiary | Provision of endorsements/ guarantees by subsidiary to parent company | Provision of endorsements/ guarantees to the party in Mainland China | Footnote |
|--------------------|---|--|--|---|---|---|--------------------------------|--|--|--|--|--|---|----------|
| | | | | | | | | | | | | | | |
| 0 | GCS Holdings, Inc. | GCS Device Technologies, Co., Ltd. | 2 | \$ 1,200,810 | \$ 30,960 | \$ 30,720 | \$ 20,000 | \$ 30,720 | 1.02% | \$ 1,200,810 | Y | N | N | - |
| 1 | Global Communication Semiconductors, LLC | GCS Holdings, Inc. | 4 | 1,200,810 | 175,170 | - | - | - | - | 1,200,810 | N | Y | N | - |

Note 1: The numbers filled in for the endorsements/guarantees provided by the Company or subsidiaries are as follows:

(1)The Company is '0'.

(2)The subsidiaries are numbered in order starting from '1'.

Note 2: Relationship between the endorser/guarantor and the party being endorsed/guaranteed is classified into the following seven categories; fill in the number of category each case belongs to:

(1)Having with which it does business.

(2)The endorser/guarantor parent company owns directly or indirectly more than 50% voting shares of the endorsed/guaranteed subsidiary.

(3)The endorser/guarantor parent company owns directly or indirectly more than 50% voting shares of the endorsed/guaranteed company.

(4)The endorsed/guaranteed parent company owns directly or indirectly more than jointly 90% voting shares of the endorser/guarantor company.

(5)Mutual guarantee of the trade or co-contractor as required by the construction contract.

(6)Due to joint venture, mutual shareholder provides endorsements/guarantees to the endorsed/guaranteed company in ratio to its ownership.

(7)Companies in the same industry provide among themselves joint and several security for a performance guarantee of sales contract for pre-construction homes pursuant to the Consumer Protection Act for each other.

Note 3: According to the Company's "Procedures for Endorsement and Guarantee", the total amount of endorsement/guarantee provided by the Company is limited to forty percent (40%) of the Company's net worth,

and the total amount of the guarantee provided by the Company to any individual entity is limited to ten percent of the Company's net worth. The total amount of the guarantee provided by the Company to any subsidiary whose voting shares are 100% owned, directly or indirectly, by the Company shall not exceed forty percent (40%) of the Company's net worth.

The aggregate total amount of endorsement/guarantee provided by the Company and its subsidiaries shall not exceed fifty percent (50%) of the Company's net worth.

GCS HOLDINGS, INC.

Significant inter-company transactions during the reporting period

Year ended December 31, 2018

Expressed in thousands of NTD
(Except as otherwise indicated)

Table 9

| Number (Note 1) | Company name | Counterparty | Relationship (Note 2) | Transaction | | | Percentage of consolidated total operating revenues or total assets (Note 3) |
|--------------------|--|---|--------------------------|-------------------------------------|-----------|--|---|
| | | | | General ledger account | Amount | Transaction terms | |
| 1 | D-Tech Optoelectronics, Inc. | Global Communication Semiconductors, LLC | 3 | Sales revenue | \$ 53,390 | Conducted in the ordinary course of business with terms similar to those with third parties | 2.73% |
| 1 | D-Tech Optoelectronics, Inc. | Global Communication Semiconductors, LLC | 3 | Other receivable - related party | 3,981 | Conducted in the ordinary course of business with terms similar to those with third parties | 0.12% |
| 2 | D-Tech Optoelectronics (Taiwan) Corporation | D-Tech Optoelectronics, Inc. | 3 | Service revenue | 52,632 | Conducted in the ordinary course of business with terms similar to those with third parties | 2.70% |
| 2 | D-Tech Optoelectronics (Taiwan) Corporation | D-Tech Optoelectronics, Inc. | 3 | Other receivable - related party | 1,920 | Conducted in the ordinary course of business with terms similar to those with third parties | 0.06% |

Note 1: The numbers filled in for the transaction company in respect of inter-company transactions are as follows:

(1)Parent company is '0'.

(2)The subsidiaries are numbered in order starting from '1'.

Note 2: Relationship between transaction company and counterparty is classified into the following three categories; fill in the number of category each case belongs to (If transactions between parent company and subsidiaries or between subsidiaries refer to the same transaction, it is not required to disclose twice. For example, if the parent company has already disclosed its transaction with a subsidiary, then the subsidiary is not required to disclose the transaction; for transactions between two subsidiaries, if one of the subsidiaries has disclosed the transaction, then the other is not required to disclose the transaction.):

(1)Parent company to subsidiary.

(2)Subsidiary to parent company.

(3)Subsidiary to subsidiary.

Note 3: Regarding percentage of transaction amount to consolidated total operating revenues or total assets, it is computed based on year-end balance of transaction to consolidated total assets for balance sheet accounts and based on accumulated transaction amount for the year to consolidated total operating revenues for income statement accounts.

Note 4: The Company may decide to disclose or not to disclose transaction details in this table based on the Materiality Principle.

GCS HOLDINGS, INC.

Information on investees (not including investees in mainland China)

Year ended December 31, 2018

Table 10

Expressed in thousands of NTD
(Except as otherwise indicated)

| Investor | Investee (Note 1 & 2) | Location | Main business activities | Initial investment amount | | Shares held as at December 31, 2018 | | Net profit (loss) of the investee for the year ended December 31, 2018 (Note 2(2)) | Investment income (loss) recognised by the Company for the year ended December 31, 2018 (Note 2(3)) | Footnote |
|--|---|------------------|---|---------------------------------------|---------------------------------------|-------------------------------------|---------------|---|---|----------|
| | | | | Balance as at December 31, 2018 | Balance as at December 31, 2017 | Number of shares | Ownership (%) | | | |
| GCS Holdings, Inc. | Global Communication Semiconductors, LLC | Los Angeles, USA | 1. Manufacturing of high-end radio frequency ICs, optoelectronic device compound semiconductor wafer and foundry related services as well as granting royalty rights for intellectual property. 2. Manufacturing and selling of advanced optoelectronics technology products | \$ 403,975 | \$ 403,975 | - | 100% | \$ 2,458,484 | \$ 349,479 | - |
| GCS Holdings, Inc. | GCS Device Technologies, Co., Ltd. | Taiwan | Product design and research development services | 12,000 | 12,000 | - | 100% | 28,237 | 758 | - |
| Global Communication Semiconductors, LLC | D-Tech Optoelectronics, Inc. | Los Angeles, USA | Developing, manufacturing and selling of positive, intrinsic, negative components and avalanche photo diodes for telecommunication systems and data communication networks | 393,380 | 393,380 | 360,000 | 100% | 411,321 | 12,178 | - |
| D-Tech Optoelectronics, Inc. | D-Tech Optoelectronics Corporation (Taiwan) | Taiwan | Manufacturing and selling of optical chips | 89,840 | 89,840 | 5,800,000 | 100% | 74,514 | (13,460) | (13,460) |

Note 1: If a public company is equipped with an overseas holding company and takes consolidated financial report as the main financial report according to the local law rules, it can only disclose the information of the overseas holding company about the disclosure of related overseas investee information.

Note 2: If situation does not belong to Note 1, fill in the columns according to the following regulations:

- (1) The columns of 'Investee', 'Location', 'Main business activities', 'Initial investment amount' and 'Shares held as at December 31, 2018' should fill orderly in the Company's (public company's) information on investees and every directly or indirectly controlled investee's investment information, and note the relationship between the Company (public company) and its investee each (ex. direct subsidiary or indirect subsidiary) in the 'footnote' column.
- (2) The 'Net profit (loss) of the investee for the year ended December 31, 2018' column should fill in amount of net profit (loss) of the investee for this year.
- (3) The 'Investment income (loss) recognised by the Company for the year ended December 31, 2018' column should fill in the Company (public company) recognised investment income (loss) of its direct subsidiary and recognised investment income (loss) of its investee accounted for under the equity method for this year. When filling in recognised investment income (loss) of its direct subsidiary, the Company (public company) should confirm that direct subsidiary's net profit (loss) for this year has included its investment income (loss) which shall be recognised by regulations.

GCS HOLDINGS, INC.
Information on investments to mainland China
Year ended December 31, 2018

Expressed in thousands of NT\$
(Except as otherwise indicated)

Table 11

| Investee in mainland China | Main business activities | Paid-in capital | Investment method (Note 1) | Amount remitted from Taiwan to mainland China/ Amount remitted back to Taiwan for the year ended December 31, 2018 | | Accumulated amount of remittance from Taiwan to mainland China as of January 1, 2018 | Net income of investee for the year ended December 31, 2018 | Ownership held by the Company (direct or indirect) | Investment income (loss) recognised by the Company for the year ended December 31, 2018 (Note 2) | Book value of investments in mainland China as of December 31, 2018 | Accumulated amount of investment income remitted back to Taiwan as of December 31, 2018 | Footnote |
|--|---|-----------------|----------------------------|---|--------|--|---|--|--|---|---|----------|
| | | | | Remitted to mainland China | Taiwan | | | | | | | |
| Xiamen Global Advanced Semiconductor Co., Ltd. | Developing manufacturing and selling of mobile phone radio frequency filter, optical communication chip, power management and optical fiber | 30,633 | 2 | \$ - | \$ - | \$ - | (\$ -) | 51% | \$ 3,486 | \$ 11,198 | \$ - | (Note 4) |
| Xiamen Global Advanced Semiconductor Co., Ltd. | | | | \$ - | \$ - | \$ - | \$ - | - | - | - | - | |

| Investee in mainland China | Accumulated amount of remittance from Taiwan to mainland China as of December 31, 2018 | Investment method |
|--|--|-------------------|
| Xiamen Global Advanced Semiconductor Co., Ltd. | \$ 30,633 | 2 |

| Investee in mainland China | Accumulated amount of remittance from Taiwan to mainland China as of December 31, 2018 | Investment method | Investment amount approved by the Investment Commission of the Ministry of Economic Affairs (MOEA) |
|--|--|-------------------|--|
| Xiamen Global Advanced Semiconductor Co., Ltd. | \$ - | 2 | MOEA |

Note 1: Investment methods are classified into the following three categories: fill in the number of category each case belongs to:
(1) Directly invest in a company in mainland China.
(2) Through investing in an existing company in the third area, which then invested in the investee in mainland China.
(3) Others

Note 2: In the "Investment income (loss) recognised by the Company for the year ended December 31, 2018" column:
(1) It should be indicated if the investee was still in the incorporation arrangements and had not yet any profit during this year.
(2) Indicate the basis for investment income (loss) recognition in the number of one of the following three categories:
A. The financial statements that are audited and attested by international accounting firm which has cooperative relationship with accounting firm in R.O.C.
B. The financial statements that are audited and attested by R.O.C. parent company's CPA.
C. Others.

Note 3: The numbers in this table are expressed in New Taiwan Dollars.

Note 4: The Company was incorporated in Cayman Islands and investment amount of \$14,906 was transferred from the Company's U.S. bank account to mainland China on June 23, 2017. In addition, the company acquired the additional 2% shareholding of Xiamen Global Advanced Semiconductor Co., Ltd. in the amount of US\$ 80 thousands (NT\$ 2,442 thousands) in September 2018.