

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

**LANNER ELECTRONICS INC.
AND SUBSIDIARIES**

CONSOLIDATED FINANCIAL STATEMENTS

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

**Address: 7rd Floor, No. 173, Sec. 2, Datong Rd., Xizhi Dist., New Taipei City,
Taiwan, R.O.C.**

Tel: (02)8692-6060

REPRESENTATION LETTER

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

Company name: LANNER ELECTRONICS INC.

Chairman: Chou I Wen

Date: March 2, 2017



安侯建業聯合會計師事務所
KPMG

台北市11049信義路5段7號68樓(台北101大樓)
68F., TAIPEI 101 TOWER, No. 7, Sec. 5,
Xinyi Road, Taipei City 11049, Taiwan (R.O.C.)

Telephone 電話 + 886 (2) 8101 6666
Fax 傳真 + 886 (2) 8101 6667
Internet 網址 kpmg.com/tw

Independent Auditor's Report

To the Board of Directors of LANNER ELECTRONICS INC.:

Opinion

We have audited the consolidated financial statements of LANNER ELECTRONICS INC. and subsidiaries ("the Group"), which comprise the consolidated statement of financial position as of December 31, 2016 and 2015, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the years ended December 31, 2016 and 2015, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, based on our audits and the report of another auditor (please refer to Other Matter paragraph), the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the the Group as of December 31, 2016 and 2015, and its consolidated financial performance and its consolidated cash flows for the years ended December 31, 2016 and 2015 in accordance with the Regulations Governing the Preparation of Financial Reports by Securities Issuers and with the International Financial Reporting Standards ("IFRSs"), International Accounting Standards ("IASs"), interpretation as well as related guidance endorsed by the Financial Supervisory Commission of the Republic of China.

Basis for Opinion

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

Other Matter

We did not audit the financial statements of LANNER ELECTRONICS USA INC. whose statements were audited by another auditors and whose report has been furnished to us; and our opinion, insofar as it relates to the amounts included for LANNER ELECTRONICS USA INC., is based solely on the report of other auditors. The financial statements of LANNER ELECTRONICS USA INC. reflect the total assets constituting 11% and 14% of the total consolidated assets as of December 31, 2016 and 2015, respectively, and total revenues constituting 23% of consolidated total revenues for the years ended December 31, 2016 and 2015.

LANNER ELECTRONICS INC. and subsidiaries has additionally prepared its parent company only financial statements as of and for the years ended December 31, 2016 and 2015, on which we have issued an unmodified mopinion with other matter.



Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements for the year end December 31, 2016. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

1. Revenue recognition

Please refer to note 4(n) and note 6(q) for disclosures related to revenue recognition.

Description of key audit matter:

Revenue is the key indicator used by investors and management while evaluating the Group's finance or operating performance. Therefore, the accuracy of the timing and the amount of revenue recognized have significant impact on the financial statements. Therefore, we consider them as key audit matters.

How the matter was addressed in our audit:

Testing the effectiveness of design and implementing the internal control (both manual and system control) of sales and collecting cycle; reviewing significant sales contracts to determine whether the accounting treatment is reasonable; analyzing the changes in significant sales customers from the most recent period and last year, and the changes in the price and quantity of each category of product line to determine whether if there are any significant misstatements; selecting sales transactions from a period of time before and after the balance sheet date, and verifying with the vouchers to determine the accuracy of the timing and amounts of revenue recognition; understanding whether if there is a significant subsequent sales return or discount; and reviewing whether the disclosure of revenue made by the management is appropriate.

2. Impairment of trades receivable

Please refer to note 4(g), note 5, and note 6(c) for disclosures related to trade receivable of the financial statements.

Description of key audit matter:

The trade receivable constituted 24% of the total consolidated assets of the Group as of December 31, 2016; therefore, the management is required to set up a policy on its allowance for impairment in order to evaluate its customers' financial status, as well as the political and economic environment. Therefore, we consider it as a key audit matter.

How the matter was addressed in our audit:

The key audit procedures for the assessment of the Group's aging analysis of accounts receivable included confirmation by sampling and examining relevant documents to verify the accuracy aging period; inspecting the reasonableness of the overdue receivables whether the Group has taken the appropriate procedures on its litigation or negotiation subsequent to the financial year end, and verifying the adequacy of impairment assessment of accounts receivable; verifying the reasonableness of the management's assessment on the Group's disclosure on the impairment of trade receivable.

3. Inventory measurement

Please refer to note 4(h), note 5, and note 6(d) for disclosures related to inventory measurement.

Description of key audit matter:

The electronic industry is vulnerable to the rapid advancement of technology. Therefore, the characteristic of fierce competition may result in large fluctuations in market demand, and prices may result in a decline on the price of raw material, wherein the carrying value of inventories may exceed its net realizable value. The measurement of inventory depends on the evaluation of the management based on evidence from internal and external, both subjective and objective. Therefore, we consider it as a key audit matter.



How the matter was addressed in our audit:

The key audit procedures included understanding the management's accounting policy on inventory measurement to determine its reasonableness whether or not it is being implemented; reviewing the inventory aging documents and analyzing the changes; obtaining the documents of inventory measurement and evaluating whether if the basis used for net realizable value is reasonable; selecting samples and verifying them with the vouchers to test the accuracy of the amount; and reviewing whether the disclosure of inventory measurement made by the management is appropriate.

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

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

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

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

Auditors' Responsibilities for the Audit of the Consolidated Financial Statements

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

As part of an audit in accordance with auditing standards generally accepted in the Republic of China, we exercise professional judgment and maintain professional skepticism throughout the audit. 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 control.
2. Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
3. Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.



4. 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 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 auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the the Group to cease to continue as a going concern.
5. Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
6. Obtain sufficient and appropriate audit evidence regarding the financial information of the entities or business activities within the 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 control that we identify during our audit.

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

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

The engagement partners on the audit resulting in this independent auditor's report are Yung-Sheng Wang and Lin Wu.

KPMG

Taipei, Taiwan (Republic of China)
March 2, 2017

Note to Readers

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

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

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

LANNER ELECTRONICS INC. and subsidiaries

Consolidated Balance Sheets

December 31, 2016 and 2015

(Expressed in thousands of New Taiwan dollars)

Assets	December 31, 2016		December 31, 2015		Liabilities and Stockholders' Equity		December 31, 2016		December 31, 2015	
	Amount	%	Amount	%			Amount	%	Amount	%
Current assets:					Current liabilities:					
Cash and cash equivalents (note 6(a))	\$ 761,323	16	412,427	10	Short-term debts (notes 6(i) and 8)		\$ 55,659	1	42,604	1
Financial assets at fair value through profit or loss—current (note 6(b))	50,009	1	-	-	Long-term debts, current portion (notes 6(i) and 8)		1,932	-	1,966	-
Notes receivable, net (note 6(c))	6,461	-	12,506	-	Financial liabilities at fair value through profit or loss—current (note 6(b))		1,009	-	-	-
Accounts receivable, net (note 6(c))	1,105,343	23	1,061,641	25	Notes payable		7,060	-	-	-
Other receivables (notes 6(c) and 6(q))	69,031	1	646	-	Accounts payable		1,022,436	21	829,130	19
Inventories (note 6(d))	1,385,524	29	1,415,992	33	Accounts payable due to related parties (note 7)		-	-	6,480	-
Other financial assets—current(note 8)	75,921	2	37,139	1	Current tax liabilities		47,268	1	51,221	1
Prepayments	65,723	1	68,155	2	Other payables (notes 6(l), 6(q), and 6(r))		589,902	12	496,313	12
Other current assets	50,563	1	39,699	1	Provisions—current (notes 6(k) and 9)		41,354	1	32,630	1
Total current assets	3,569,898	74	3,048,205	72	Bonds payable, current portion (note 6(j))		-	-	223,505	5
Non-current assets:					Other current liabilities (note 6(q))		123,205	3	126,926	3
Financial assets carried at cost—non-current (note 6(e))	500	-	1,000	-	Total current liabilities		1,889,825	39	1,810,775	42
Property, plant and equipment (notes 6(g) and 8)	1,114,550	23	1,157,649	27	Non-current liabilities:					
Prepayments for equipment	54,822	1	18,343	-	Financial liabilities at fair value through profit or loss—non-current (notes 6(b) and 10)		-	-	23	-
Intangible assets (note 6(h))	7,975	-	-	-	Long-term debts (notes 6(i) and 8)		39,773	1	42,440	1
Deferred income tax assets (note 6(m))	60,794	2	54,708	1	Long-term deferred revenue (note 6(q))		36,734	1	32,881	1
Other non-current assets (note 7)	11,442	-	7,674	-	Deferred income tax liabilities (note 6(m))		89,373	2	68,241	1
Total non-current assets	1,250,083	26	1,239,374	28	Accrued pension liabilities (note 6(l))		34,496	-	29,168	1
					Other non-current liabilities		202	-	552	-
					Total non-current liabilities		200,578	4	173,305	4
					Total liabilities		2,090,403	43	1,984,080	46
					Equity attributable to shareholders of the Company (notes 6(j), 6(l), 6(m), 6(n) and 6(o)):					
					Common stock		1,036,446	22	975,008	23
					Capital surplus		639,874	13	462,135	11
					Retained earnings:					
					Legal reserve		194,899	4	163,059	4
					Special reserve		2,225	-	2,225	-
					Unappropriated retained earnings		778,494	16	628,724	15
							975,618	20	794,008	19
					Other equity:					
					Financial statements translation differences for foreign operations		(27,483)	-	19,995	-
					Total equity attributable to shareholders of the Company		2,624,455	55	2,251,146	53
					Non-controlling interests		105,123	2	52,353	1
					Total equity		2,729,578	57	2,303,499	54
Total assets	\$ 4,819,981	100	4,287,579	100	Total liabilities and stockholders' equity		\$ 4,819,981	100	4,287,579	100

See accompanying notes to the consolidated financial statements.

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

LANNER ELECTRONICS INC. AND SUBSIDIARIES

Consolidated Statements of Comprehensive Income

For the years ended December 31, 2016 and 2015

(Expressed in thousands of New Taiwan dollars)

	2016		2015	
	Amount	%	Amount	%
Operating revenue (notes 6(q) and 7)	\$ 6,120,048	100	5,439,499	100
Operating costs (notes 6(d), 6(k), 6(l), 6(o), 6(r) and 7)	<u>4,397,865</u>	<u>72</u>	<u>3,877,383</u>	<u>71</u>
Gross profit, net	<u>1,722,183</u>	<u>28</u>	<u>1,562,116</u>	<u>29</u>
Operating expenses (notes 6(c), 6(l), 6(o), 6(r) and 7):				
Selling expenses	539,001	9	446,070	8
Administrative expenses	317,129	5	348,103	7
Research and development expenses	<u>442,200</u>	<u>7</u>	<u>426,525</u>	<u>8</u>
Total operating expenses	<u>1,298,330</u>	<u>21</u>	<u>1,220,698</u>	<u>23</u>
Operating profit	<u>423,853</u>	<u>7</u>	<u>341,418</u>	<u>6</u>
Non-operating income and expenses (notes 6(j), 6(s) and 7):				
Other income	87,971	1	100,479	2
Other gains and losses	(9,971)	-	(5,834)	-
Financial costs	<u>(6,956)</u>	<u>-</u>	<u>(8,116)</u>	<u>-</u>
Total non-operating income and expenses	<u>71,044</u>	<u>1</u>	<u>86,529</u>	<u>2</u>
Net income before tax	494,897	8	427,947	8
Less: income tax expenses (note 6(m))	<u>84,750</u>	<u>1</u>	<u>98,831</u>	<u>2</u>
Net income	<u>410,147</u>	<u>7</u>	<u>329,116</u>	<u>6</u>
Other comprehensive income (loss):				
Items that will not be reclassified subsequently to profit or loss:				
Remeasurements of the defined benefit plans	(4,307)	-	(1,662)	-
Income tax benefit (expense) related to items that will not be reclassified subsequently	-	-	-	-
Total Items that will not be reclassified subsequently to profit or loss	<u>(4,307)</u>	<u>-</u>	<u>(1,662)</u>	<u>-</u>
Items that may be reclassified subsequently to profit or loss:				
Financial statements translation differences for foreign operations	(55,342)	(1)	(12,352)	-
Income tax expense relating to components of other comprehensive income (loss)	-	-	-	-
Total Items that may be reclassified subsequently to profit or loss	<u>(55,342)</u>	<u>(1)</u>	<u>(12,352)</u>	<u>-</u>
Other comprehensive income (loss), net of tax	<u>(59,649)</u>	<u>(1)</u>	<u>(14,014)</u>	<u>-</u>
Total comprehensive income	<u>\$ 350,498</u>	<u>6</u>	<u>315,102</u>	<u>6</u>
Net income attributable to:				
Shareholders of the parent company	\$ 380,927	7	318,404	6
Non-controlling interests	<u>29,220</u>	<u>-</u>	<u>10,712</u>	<u>-</u>
	<u>\$ 410,147</u>	<u>7</u>	<u>329,116</u>	<u>6</u>
Total comprehensive income attributable to:				
Shareholders of the parent company	\$ 329,142	6	305,531	6
Non-controlling interests	<u>21,356</u>	<u>-</u>	<u>9,571</u>	<u>-</u>
	<u>\$ 350,498</u>	<u>6</u>	<u>315,102</u>	<u>6</u>
Basic earnings per share (in New Taiwan dollars) (note 6(p))	<u>\$ 3.83</u>		<u>3.29</u>	
Diluted earnings per share (in New Taiwan dollars) (note 6(p))	<u>\$ 3.60</u>		<u>3.04</u>	

See accompanying notes to the consolidated financial statements.

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

LANNER ELECTRONICS INC. AND SUBSIDIARIES

Consolidated Statements of Changes in Equity

For the years ended December 31, 2016 and 2015

(All amounts expressed in thousands of New Taiwan dollars)

Equity attributable to shareholders of the parent											
	Retained earnings					Financial statements translation differences for foreign operations	Treasury stock	Total equity attributable to shareholders of the parent company	Non-controlling interests	Total Equity	
	Common stock	Capital surplus	Legal reserve	Special reserve	Unappropriated earnings						Total
\$	908,114	384,347	132,687	2,225	539,231	674,143	31,206	-	1,997,810	42,782	2,040,592
Balance on January 1, 2015											
Appropriations and distributions:											
Legal reserve	-	-	30,372	-	(30,372)	-	-	-	-	-	-
Cash dividends	-	-	-	-	(136,218)	(136,218)	-	-	(136,218)	-	(136,218)
Stock dividends	45,406	-	-	-	(45,406)	(45,406)	-	-	-	-	-
Net income	-	-	-	-	318,404	318,404	-	-	318,404	10,712	329,116
Other comprehensive income (loss)	-	-	-	-	(1,662)	(1,662)	(11,211)	-	(12,873)	(1,141)	(14,014)
Total comprehensive income (loss)	-	-	-	-	316,742	316,742	(11,211)	-	305,531	9,571	315,102
Conversion of convertible bonds	-	8,779	28,173	-	-	-	-	-	36,952	-	36,952
Acquisition of treasury stock	-	-	-	-	-	-	-	(25,678)	(25,678)	-	(25,678)
Retirement of treasury stock	(7,200)	(3,225)	-	-	(15,253)	(15,253)	-	25,678	-	-	-
Remuneration cost of employee stock options	-	3,612	-	-	-	-	-	-	3,612	-	3,612
Stock options exercised by employees	7,687	8,148	-	-	-	-	-	-	15,835	-	15,835
Increase in capital from employee bonus	12,222	41,080	-	-	-	-	-	-	53,302	-	53,302
Balance on December 31, 2015	975,008	462,135	163,059	2,225	628,724	794,008	19,995	-	2,251,146	52,353	2,303,499
Appropriations and distributions:											
Legal reserve	-	-	31,840	-	(31,840)	-	-	-	-	-	-
Cash dividends	-	-	-	-	(195,010)	(195,010)	-	-	(195,010)	-	(195,010)
Net income	-	-	-	-	380,927	380,927	-	-	380,927	29,220	410,147
Other comprehensive income (loss)	-	-	-	-	(4,307)	(4,307)	(47,478)	-	(51,785)	(7,864)	(59,649)
Total comprehensive income (loss)	-	-	-	-	376,620	376,620	(47,478)	-	329,142	21,356	350,498
Conversion of convertible bonds	53,122	149,978	-	-	-	-	-	-	203,100	-	203,100
Remuneration cost of employee stock options	-	9,296	-	-	-	-	-	-	9,296	-	9,296
Stock options exercised by employees	8,316	7,651	-	-	-	-	-	-	15,967	-	15,967
Changes in non-controlling interests from acquisition of subsidiaries	-	-	-	-	-	-	-	-	-	30,333	30,333
Due to donated assets received	-	10,814	-	-	-	-	-	-	10,814	1,081	11,895
Balance on December 31, 2016	\$ 1,036,446	639,874	194,899	2,225	778,494	975,618	(27,483)	-	2,624,455	105,123	2,729,578

See accompanying notes to the consolidated financial statements.

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

LANNER ELECTRONICS INC. AND SUBSIDIARIES

Consolidated Statements of Cash Flows

For the years ended December 31, 2016 and 2015

(All amounts expressed in thousands of New Taiwan dollars)

	2016	2015
Cash flows from operating activities:		
Consolidated net income before tax	\$ 494,897	427,947
Adjustments:		
Adjustments to reconcile profit and loss		
Depreciation	100,132	74,994
Amortization	1,277	-
Bad debt provision	5,566	572
Net loss (gain) on financial assets and liabilities at fair value through profit or loss	(23)	42
Interest expenses	6,956	8,116
Interest income	(4,648)	(1,783)
Remuneration cost of employee stock options	9,296	3,612
Loss on disposal of property, plant and equipment, net	1,197	375
Total adjustments to reconcile profit and loss	<u>119,753</u>	<u>85,928</u>
Changes in assets / liabilities relating to operating activities:		
Net changes in operating assets:		
Financial assets at fair value through profit or loss	(50,009)	-
Notes receivable	6,045	6,534
Accounts receivable (including related parties)	58,980	(110,725)
Other receivables	(67,106)	1,799
Inventories	302,094	(387,254)
Prepayments	13,362	4,141
Other current assets	(10,864)	(9,130)
Other financial assets	<u>34,302</u>	<u>(28)</u>
Total changes in operating assets, net	<u>286,804</u>	<u>(494,663)</u>
Net changes in operating liabilities:		
Financial liabilities at fair value through profit or loss	1,009	-
Notes payable	7,060	-
Accounts payable (including related parties)	(170,011)	205,545
Accounts payable—related parties	(6,480)	6,270
Other payables	88,046	113,612
Provisions	8,724	14,790
Other current liabilities	(1,824)	20,361
Accrued pension liabilities	1,021	(65)
deferred revenue	<u>1,956</u>	<u>7,526</u>
Total changes in operating liabilities, net	<u>(70,499)</u>	<u>368,039</u>
Total changes in operating assets / liabilities, net	<u>216,305</u>	<u>(126,624)</u>
Total adjustments	<u>336,058</u>	<u>(40,696)</u>
Cash provided by operating activities	830,955	387,251
Interest income received	4,653	1,782
Interest paid	(3,035)	(2,910)
Income taxes paid	<u>(88,703)</u>	<u>(66,208)</u>
Net cash provided by operating activities	<u>743,870</u>	<u>319,915</u>
Cash flows from investing activities:		
Proceeds from capital reduction of financial assets at cost	500	-
Acquisition of subsidiaries (after deduction of cash obtained)	8,781	-
Acquisition of property, plant and equipment	(52,163)	(116,976)
Proceeds from disposal of property, plant and equipment	6,257	2,533
Increase in other financial assets	(73,089)	(34,804)
Increase in other non-current assets	(3,768)	(2,240)
Increase in prepayments for equipment	<u>(52,463)</u>	<u>(18,343)</u>
Net cash used in investing activities	<u>(165,945)</u>	<u>(169,830)</u>
Cash flows from financing activities:		
Increase in short-term debts	104,618	-
Decrease in short-term debts	(90,000)	(50,000)
Repayment of corporate bonds	(24,300)	-
Repayment of long-term debts	(1,940)	(1,914)
Decrease in other non-current liabilities	(350)	(216)
Cash dividends paid	(195,010)	(136,218)
Exercise of employee share options	15,967	15,835
Purchase of treasury stock	-	(25,678)
Net cash used in financing activities	<u>(191,015)</u>	<u>(198,191)</u>
Effects of changes in exchange rates	<u>(38,014)</u>	<u>(21,187)</u>
Increase (decrease) in cash and cash equivalents	348,896	(69,293)
Cash and cash equivalents at beginning of period	<u>412,427</u>	<u>481,720</u>
Cash and cash equivalents at end of period	<u>\$ 761,323</u>	<u>412,427</u>

See accompanying notes to the consolidated financial statements.

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

LANNER ELECTRONICS INC. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

December 31, 2016 and 2015

(expressed in thousands of New Taiwan dollars unless otherwise stated)

(1) Organization and Business Scope

LANNER ELECTRONICS INC. (the Company) was incorporated on October 30, 1986, under the laws of the Republic of China (ROC). The Company and its subsidiaries (the Group) are mainly engaged in the manufacturing and trading of computer peripheral equipment, computer software design and development services, and related information processing trade business. Please refer to note 14.

(2) Financial Statements Authorization Date and Authorization Process

These consolidated financial statements were approved by the Board of Directors on March 2, 2017.

(3) New Standards and Interpretations Not Yet Adopted

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

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

New, Revised or Amended Standards and Interpretations	Effective date per IASB
Amendments to IFRS 10, IFRS 12 and IAS 28 "Investment Entities: Applying the Consolidation Exception"	January 1, 2016
Amendments to IFRS 11 "Accounting for Acquisitions of Interests in Joint Operations"	January 1, 2016
IFRS 14 "Regulatory Deferral Accounts"	January 1, 2016
Amendment to IAS 1 "Disclosure Initiative"	January 1, 2016
Amendments to IAS 16 and IAS 38 "Clarification of Acceptable Methods of Depreciation and Amortization"	January 1, 2016
Amendments to IAS 16 and IAS 41 "Agriculture: Bearer Plants"	January 1, 2016
Amendments to IAS 19 "Defined Benefit Plans: Employee Contributions"	July 1, 2014
Amendment to IAS 27 "Equity Method in Separate Financial Statements"	January 1, 2016
Amendments to IAS 36 "Recoverable Amount Disclosures for Non-Financial Assets"	January 1, 2014
Amendments to IAS 39 "Novation of Derivatives and Continuation of Hedge Accounting"	January 1, 2014
Annual improvements cycles 2010-2012 and 2011-2013	July 1, 2014
Annual improvements cycle 2012-2014	January 1, 2016
IFRIC 21 "Levies"	January 1, 2014

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

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES
Notes to the Consolidated Financial Statements

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

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

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

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES
Notes to the Consolidated Financial Statements

The Group is still currently determining the potential impact of the standards listed below:

Issuance / Release Dates	Standards or Interpretations	Content of amendment
May 28, 2014 April 12, 2016	IFRS 15 "Revenue from Contracts with Customers"	<p>IFRS 15 establishes a five-step model for recognizing revenue that applies to all contracts with customers, and will supersede IAS 18 "Revenue," IAS 11 "Construction Contracts," and a number of revenue-related interpretations.</p> <p>Final amendments issued on April 12, 2016, clarify how to (i) identify performance obligations in a contract; (ii) determine whether a company is a principal or an agent; (iii) account for a license for intellectual property (IP); and (iv) apply transition requirements.</p>
November 19, 2013 July 24, 2014	IFRS 9 "Financial Instruments"	<p>The standard will replace IAS 39 "Financial Instruments: Recognition and Measurement", and the main amendments are as follows:</p> <ul style="list-style-type: none"> • Classification and measurement: Financial assets are measured at amortized cost, fair value through profit or loss, or fair value through other comprehensive income, based on both the entity's business model for managing the financial assets and the financial assets' contractual cash flow characteristics. Financial liabilities are measured at amortized cost or fair value through profit or loss. Furthermore, there is a requirement that "own credit risk" adjustments be measured at fair value through other comprehensive income. • Impairment: The expected credit loss model is used to evaluate impairment. • Hedge accounting: Hedge accounting is more closely aligned with risk management activities, and hedge effectiveness is measured based on the hedge ratio.

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES
Notes to the Consolidated Financial Statements

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

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

(4) Significant Accounting Policies

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

The significant accounting policies presented in the financial statements are summarized as follows. Except for those described otherwise, the accounting policies have been applied consistently to all periods presented in these financial statements, and have been applied consistently to the balance sheet as of reporting date.

(a) Statement of compliance

The consolidated financial statements have been prepared in accordance with the Regulations Governing the Preparation of Financial Reports by Securities Issuers (the Regulations) and the IFRSs endorsed by the FSC.

(b) Basis of preparation

i) Basis of measurement

The consolidated financial statements have been prepared on a historical cost basis except for the following accounts:

- i. Financial instruments measured at fair value through profit or loss are measured at fair value (Included derivative financial instrument)

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

- ii. Pension liabilities (and assets) are measured at the fair value of the pension deducted by the present value of the defined benefit obligations and the effect of the maximum rate which is mentioned in note 4(l).

ii) Functional and presentation currency

The functional currency of each individual consolidated entity is determined based on the primary economic environment in which the entity operates. The Group's consolidated financial statements are presented in New Taiwan dollars, which is Company's functional currency. The assets and liabilities of foreign operations are translated to the Group's functional currency at the exchange rates at the reporting date. The income and expenses of foreign operations are translated to the Group's functional currency at the average rate. Foreign currency differences are recognized in other comprehensive income. All financial information presented in New Taiwan dollars has been rounded to the nearest thousand.

(c) Basis of consolidation

i) Principles of preparation of consolidated financial statements

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

Intra-group balances and transactions, and any unrealized income and expenses arising from intra-group transactions are eliminated in preparing the consolidated financial statements.

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

ii) List of subsidiaries included in the consolidated financial statements

Name of investor	Name of subsidiary	Scope of business	Percentage of ownership		Note
			December 31, 2016	December 31, 2015	
The Company	LANNER ELECTRONICS USA, INC. (LANNER (USA))	Trading of computer peripheral products	100.00 %	100.00 %	
The Company	LANNER ELECTRONICS (MAURITIUS) INC. (LANNER (MAURITIUS))	Investing	100.00 %	100.00 %	
The Company	LEI TECHNOLOGY CANADA INC. (LEI)	Trading of computer peripheral products	100.00 %	100.00 %	
LANNER (MAURITIUS)	LANCOM HOLDING CO., LTD. (LANCOM)	Investing	100.00 %	100.00 %	
LANCOM	Beijing L&S Lancom Platform Tech. Co., Ltd. (L&S)	Trading of computer peripheral products	90.91 %	90.91 %	

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

Name of investor	Name of subsidiary	Scope of business	Percentage of ownership		Note
			December 31, 2016	December 31, 2015	
L&S	Beijing LSZC Investment Co., Ltd. (LSZC)	Investing	100.00 %	-	% Note 1
Beijing LSZC Investment Co., Ltd.	Dongguan Lihua Haiwell Tech. Co., Ltd. (Haiwell)	Manufacture and trading of computer peripheral products	100.00 %	-	% Note 2
Beijing LSZC Investment Co., Ltd.	Beijing HDZX Technology Co., Ltd. (HDZX)	Trading of computer peripheral products	42.99 %	-	% Note 3 and 4

Note 1: In January 2016, the Board of Directors decided to establish Beijing LSZC Investment Co., Ltd.; and the registration process had already been completed. The amount of investment was CNY10,000 thousand (TWD49,566 thousand). In addition, the Group increased its investment of CNY3,300 thousand (TWD15,171 thousand) in December 2016.

Note 2: In February 2016, the Board of Directors passed a resolution to acquire 100% ownership of Dongguan Lihua Haiwell Tech. Co., Ltd. The process was completed in March 2016 with the acquisition price of CNY3,700 thousand (TWD18,339 thousand). In addition, the Group increased its investment of CNY3,080 thousand (TWD15,266 thousand) and CNY3,300 thousand (TWD15,172 thousand) in March 2016 and December 2016, respectively.

Note 3: In February 2016, the Board of Directors passed a resolution to acquire 42.99% ownership of Beijing HDZX Technology Co., Ltd. The process had been completed in March 2016, with the acquisition price of CNY3,137 thousand (TWD15,550 thousand).

Note 4: Lanner holds less than 50% of the ownership of Beijing LSZC Investment Co., Ltd. However, considering the proportion of the remaining shares held by the management of the Group, the Group still holds control over Beijing LSZC Investment Co., Ltd. and its operation. As such, Beijing HDZX Technology Co., Ltd. is considered to be a subsidiary of the Group.

(d) Foreign currency

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

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

Foreign currency differences arising on translation are recognized in profit or loss, except for the available-for-sale financial assets which are recognized in other comprehensive income.

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES
Notes to the Consolidated Financial Statements

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

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

- i) An asset is classified as current under one of the following criteria, and all other assets are classified as non current.
 - i. It expects to realize the asset, or intends to sell or consume it, in its normal operating cycle;
 - ii. It holds the asset primarily for the purpose of trading;
 - iii. It expects to realize the asset within twelve months after the reporting period; or
 - iv. The asset is cash or a cash equivalent unless the asset is restricted from being exchanged or used to settle a liability for at least twelve months after the reporting period.
- ii) A liability is classified as current under one of the following criteria, and all other liabilities are classified as non current.
 - i. It expects to settle the liability in its normal operating cycle;
 - ii. It holds the liability primarily for the purpose of trading;
 - iii. The liability is due to be settled within twelve months after the reporting period even if refinancing or a revised repayment plan is arranged between the reporting date and the issuance date of the financial statements; or
 - iv. It does not have an unconditional right to defer settlement of the liability for at least twelve months after the reporting period. Terms of a liability that could, at the option of the counterparty, result in its settlement by the issue of equity instruments do not affect its classification.

(f) Cash and cash equivalents

Cash and cash equivalents comprised cash, cash in banks and short term investments with high liquidity that are subject to an insignificant risk of changes in their fair value.

The time deposits with maturity of one year or less from the acquisition date are listed in cash and cash equivalents because they are held for the purpose of meeting short-term cash commitments instead of investment or other purposes. They are also readily convertible to fixed amount of cash, and are subject to an insignificant risk of changes in value.

(g) Financial instruments

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

i) Financial assets

The Group classifies financial assets as financial assets at fair value through profit or loss, available-for-sale financial assets, and loans to other parties and receivables.

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES**Notes to the Consolidated Financial Statements****i. Financial assets at fair value through profit or loss**

A financial asset is classified in this category if it is acquired principally for the purpose of selling or repurchasing in the short term. This type of financial asset is measured at fair value at initial recognition. Attributable transaction costs are recognized in profit or loss as incurred. Financial assets at fair value through profit or loss are measured at fair value, and changes therein, which take into account any dividend and interest income, are recognized in profit or loss, and are included in non-operating income and expense. Based on previous experiences, the Group uses trade-date accounting upon acquiring or disposing financial assets.

ii. Available-for sale financial assets

Available-for-sale financial assets are recognized initially at fair value, plus, any directly attributable transaction cost. Subsequent to initial recognition, they are measured at fair value, and changes therein, other than impairment losses, interest income calculated using the effective interest method, dividend income, and foreign currency differences on available-for-sale debt instruments, are recognized in other comprehensive income and presented in the fair value reserve in equity. When an investment is derecognized, the gain or loss accumulated in equity is reclassified to profit or loss, and is included in non-operating income and expense.

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

iii. Receivables

Receivables are financial assets with fixed or determinable payments that are not quoted in an active market. Receivables comprise trade receivables, other receivables, and other financial assets-noncurrent. Such assets are recognized initially at fair value, plus, any directly attributable transaction costs. Subsequent to initial recognition, receivables are measured at amortized cost using the effective interest method, less, any impairment losses other than insignificant interest on short-term receivables.

iv. Impairment of financial assets

A financial asset is impaired if, and only if, there is objective evidence of impairment as a result of one or more events 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 that can be estimated reliably.

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

LANNER ELECTRONICS INC. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

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

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

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

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

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

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

Impairment losses and recoveries are recognized in profit or loss. Recovery and loss on doubtful debts of account receivables is included in operating expense, others are included in non-operating income and expense.

v. Derecognition of financial assets

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

ii) Financial liabilities

i. Classification of debt or equity

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

Equity instruments refer to surplus equities of the assets after the deduction of all the debts for any contracts. Equity instruments issued are recognized as the amount of consideration received, less, the direct cost of issuing.

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES**Notes to the Consolidated Financial Statements**

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

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

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

Interest, gains or losses related to financial liabilities are recognized in profit or loss, and recorded under non-operating income and expenses.

Upon conversion, the financial liability shall be reclassified as equity, and no gain or loss will be recognized.

ii. Financial liability at fair value through profit or loss

Available-for-sale financial liabilities are recognized initially at fair value, plus, any directly attributable transaction cost. Subsequent to initial recognition, they are measured at fair value, and changes therein, other than impairment losses, interest income calculated using the effective interest method, dividend expense, and foreign currency differences on available-for-sale debt instruments, are recognized in other comprehensive expense and presented in the fair value reserve in equity. When an investment is derecognized, the gain or loss accumulated in equity is reclassified to profit or loss, and is included in non-operating income and expense.

iii. Other financial liabilities

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

iv. Derecognition of financial liabilities

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

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES**Notes to the Consolidated Financial Statements**

v. Offsetting of financial assets and liabilities

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

(h) Inventories

The cost of inventories consists of all costs of purchase, costs of conversion, and other costs incurred in bringing the inventories to their present location and condition. The cost of inventories includes an appropriate share of fixed production overhead based on normal capacity and allocated variable production overhead based on actual output. However, unallocated fixed production overhead arising from lower or idle capacity is recognized in cost of goods sold during the period. If actual capacity is higher than normal capacity, fixed production overhead should be allocated based on actual capacity. The method of valuing inventories is the weighted-average method.

Inventories are measured at the lower of cost or net realizable value. Net realizable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses at the end of the period. When the cost of inventories is higher than the net realizable value, inventories are written down to net realizable value, and the write-down amount is charged to current year's cost of goods sold. If net realizable value increases in the future, the cost of inventories is reversed within the original write-down amount, and such reversal is treated as a reduction of cost of goods sold.

(i) Property, plant and equipment

i) Recognition and measurement

Property, plant and equipment are measured at cost, less, accumulated depreciation and accumulated impairment losses. Cost includes expenditure that is directly attributed to the acquisition of the asset, and any borrowing cost that is eligible for capitalization.

Each part of an item of property, plant and equipment with a cost that is significant in relation to the total cost of the item shall be depreciated separately, unless the useful life and the depreciation method of a significant part of an item of property, plant and equipment are the same as the useful life and depreciation method of another significant part of that same item.

The gain or loss arising from the derecognition of an item of property, plant and equipment shall be determined as the difference between the net disposal proceeds, if any, and the carrying amount of the item, and it shall be recognized as non-operating income and expense.

ii) Subsequent cost

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

LANNER ELECTRONICS INC. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

iii) Depreciation

The depreciable amount of an asset is determined after deducting its residual amount, and it shall be allocated on a systematic basis over its useful life. Items of property, plant and equipment with the same useful life may be grouped in determining the depreciation charge. The remainder of the items may be depreciated separately. The depreciation charge for each period shall be recognized in profit or loss.

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

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

Buildings	20~50 years
Machinery equipment	3~10 years
Other equipment	2.5~24 years

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

(j) Intangible assets

i) Goodwill

Goodwill arises from business combinations in which the acquisition method is adopted, and is recorded at cost, less, accumulated impairment losses.

ii) Customer relations

The customer relations due from acquisition is assessed to amortize using a direct method of 3-year basis. The face value of the customer relations is measured by deducting the accumulated amortization or impairment from the cost.

(k) Impairment—non-financial assets

With regard to non-financial assets (other than inventories and deferred tax assets), the Group assesses at the end of each reporting period whether there is any indication that an impairment loss has occurred, and estimates the recoverable amount for assets with an indication of impairment. If it is not possible to determine the recoverable amount for the individual asset, then the Group will have to determine the recoverable amount for the asset's cash-generating unit.

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

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

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES
Notes to the Consolidated Financial Statements

The Group assesses at the end of each reporting period whether there is any indication that an impairment loss recognized in prior periods for an asset other than goodwill may no longer exist or may have decreased. If any such indication exists, the entity shall estimate the recoverable amount of that asset. Impairment loss is reversed if, and only if, there has been a change in the estimates used to determine the asset's recoverable amount, increasing the individual asset's or cash-generating unit's carrying amount to its estimated recoverable amount. The reversal of an impairment loss of an individual asset or cash-generating unit cannot exceed the carrying amount of the individual asset or cash-generating unit, less any depreciation or amortization, had it not recognized an impairment loss.

(l) Provisions

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

A provision for warranties is recognized when the underlying products or services are sold. The provision is based on historical warranty data and a weighting of all possible outcomes against their associated probabilities.

(m) Treasury stock

Under the cost method, the treasury stock account is debited for the cost of the Group's shares purchased. When the disposal price of treasury stock is greater than the cost, the difference is credited to capital surplus—treasury stock; otherwise, the excess of the cost over the price is debited to capital surplus generated from similar treasury stock transactions. If the capital surplus—treasury stock account is insufficient to cover the excess of the cost over the price, retained earnings should be debited for the remaining amount. The book value of each share of treasury stock is equal to its weighted-average cost and is calculated by each group according to the reason for purchase.

When treasury stock is retired, capital surplus and common stock are debited according to the ratio of retiring treasury stock to total issued stock. When the book value of the retiring treasury stock is higher than the sum of its par value and capital surplus, the difference is debited to capital surplus generated from similar treasury stock transactions. If the capital surplus—treasury stock account is insufficient to cover the difference, retained earnings should be debited for the remaining amount. When the book value of the retiring treasury stock is lower than the sum of its par value and capital surplus, the difference is credited to capital surplus generated from similar treasury stock transactions.

(n) Revenue

Revenue from the sale of goods in the course of ordinary activities is measured at the fair value of the consideration received or receivable, net of returns, trade discounts, and volume rebates. Revenue is recognized when persuasive evidence exists, usually in the form of an executed sales agreement, that the significant risks and rewards of ownership have been transferred to the customer, recovery of the consideration is probable, the associated costs and possible return of goods can be estimated reliably, there is no continuing management involvement with the goods, and the amount of revenue can be measured reliably. If it is probable that discounts will be granted and the amount can be measured reliably, then the discount is recognized as a reduction of revenue as the sales are recognized. Revenue is deferred and realized at execution if it can be distinguished by after-sale services; relative cost is recognized at execution as well.

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES
Notes to the Consolidated Financial Statements

The timing of the transfers of risks and rewards varies depending on the individual terms of the sales agreement. For export transactions, transfer occurs upon loading the goods onto the relevant carrier at the port; however, for sales in the domestic market, transfer usually occurs when the product is received at the customer's warehouse.

(o) Employee benefits

i) Defined contribution plans

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

ii) Defined benefit plans

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

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

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

Remeasurements of the net defined benefit liability (asset), which comprise (1) actuarial gains and losses, (2) the return on plan assets (excluding interest) and (3) the effect of the asset ceiling (if any, excluding interest), are recognized immediately in other comprehensive income. The Group can reclassify the amounts recognized in other comprehensive income to retained earnings.

iii) Short-term employee benefits

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

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

LANNER ELECTRONICS INC. AND SUBSIDIARIES**Notes to the Consolidated Financial Statements****(p) Share-based payment**

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

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

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

(q) Income tax

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

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

Deferred income taxes arise due to temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and their respective tax bases. Deferred income taxes shall not be recognized for the below exceptions:

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

Deferred income tax assets and liabilities shall be measured at the tax rates that are expected to apply to the period when the asset is realized or the liability is settled based on tax rates that have been enacted or substantively enacted by the end of the reporting period.

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

- i) The entity has the legal right to settle tax assets and liabilities on a net basis; and

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES**Notes to the Consolidated Financial Statements**

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

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

(r) **Business combination**

The Group uses the acquisition method for its business combination. Goodwill is measured as an aggregation of the consideration transferred (which generally is measured at fair value at the acquisition date) and the amount of any non-controlling interest in the acquiree, including non-controlling interests that belong to the acquiree, net of the acquisition-date amounts of the identifiable assets acquired and liabilities assumed. If the residual balance is negative, the Group shall re-assess whether it has correctly identified all of the assets acquired and liabilities assumed, and recognize a gain on the bargain purchase thereafter.

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

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

Non-controlling interests that are present ownership interests which entitle their holders to a proportionate share of the entity's net assets in the event of liquidation are measured by the Group using either the fair value on acquisition date or the non-controlling interests' proportionate share of the recognized amounts of the acquire's identifiable net assets. The choice of measurement is based on every transaction. Other types of non-controlling interests are measured (1) at fair value on the acquisition date or (2) by using other basis in accordance with the IFRSs endorsed by FSC.

LANNER ELECTRONICS INC. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(s) Earnings per share

The Group discloses the Company's basic and diluted earnings per share attributable to ordinary equity holders of the Company. The calculation of basic earnings per share is based on the profit attributable to the ordinary shareholders of the Company divided by the weighted-average number of ordinary shares outstanding. The calculation of diluted earnings per share is based on the profit attributable to ordinary shareholders of the Company, divided by the weighted-average number of ordinary shares outstanding after adjustment for the effects of all dilutive potential ordinary shares. The weighted-average number of common shares outstanding is adjusted retroactively for the increase in common shares outstanding from stock issuance arising from the capitalization of retained earnings, or additional paid-in capital.

When computing diluted earnings per share with regards to employee bonuses in the form of stock, the closing price at the balance sheet date is used as the basis of computation in the number of shares to be issued. When computing diluted earnings per share prior to the following year's Board of Directors the effect of dilution from these potential stocks is taken into consideration.

(t) Operating segments

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

(5) Significant Accounting Judgments and Sources of Estimation and Uncertainty

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

The Management will continually review the estimates and basic assumptions. Changes in accounting estimates will be recognized in the period of change and the future period of their impact.

There are no critical judgments in applying the accounting policies that have significant effect on the amounts recognized in the consolidated financial statements.

Information about assumptions and estimation uncertainties that have a significant risk of resulting in a material adjustment within the next financial year is as follows:

(a) Impairment assessment of trades receivable

When there is objective evidence of impairment loss, the Group takes into consideration the estimation of future cash flows. 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 (excluding the possible future credit losses) discounted at the financial asset's original effective interest rate. When the actual future cash flows are less than expected, a material impairment loss may arise. Please refer to note 6(c) for further description of the impairment of trade receivable.

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(b) Inventory measurement

Since inventories are measured at the lower of cost or net realizable value, the Group evaluated the net realizable value of inventories for obsolescence and unmarketable items at the end of the reporting period, and then writes down the cost of inventories to net realizable value. Please refer to note (d) for inventory measurement.

(6) Description of Significant Accounts

(a) Cash and cash equivalents

	December 31, 2016	December 31, 2015
Cash	\$ 1,275	1,780
Working capital	80	80
Cash in banks	419,498	141,828
Checking deposits	16,053	2,192
Time deposits	8,051	8,193
Foreign currency deposits	<u>316,366</u>	<u>258,354</u>
Cash and cash equivalents per consolidated statements of cash flow	<u><u>\$ 761,323</u></u>	<u><u>412,427</u></u>

Please refer to note 6(t) for the interest rate risk and the fair value sensitivity analysis of the financial assets and liabilities of the Group.

(b) Financial assets and liabilities at fair value through profit or loss

	December 31, 2016	December 31, 2015
Financial assets held for trading:		
Non-derivative financial assets	<u><u>\$ 50,009</u></u>	<u><u>-</u></u>
	December 31, 2016	December 31, 2015
Financial liabilities at fair value through profit or loss:		
Convertible bonds	\$ -	23
Financial liabilities held for trading:		
Derivative instruments not used for hedging	<u>1,009</u>	<u>-</u>
Total	<u><u>\$ 1,009</u></u>	<u><u>23</u></u>

Please refer to note 6(s) for net gains or losses on disposal of financial assets and liabilities remeasured at fair value through profit or loss.

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

If the market price of the available-for-sale financial assets fluctuates (assuming that all other variables remain the same, and the two-year analysis is conducted on the same basis), the impact on other comprehensive income will be as follows:

Fluctuation in market price at reporting date	2016		2015	
	Other comprehensive income (after tax)	Net income	Other comprehensive income (after tax)	Net income
Increase 1%	\$ -	500	-	-
Decrease 1%	\$ -	(500)	-	-

The Company had not provided any financial assets mentioned above as collateral as of December 31, 2016.

The Group uses derivative financial instruments to manage exposures due to fluctuations of foreign exchange risk derived from its operating activities. As of December 31, 2016, the Group reported the following derivative financial instruments as available-for-sale financial assets and liabilities without the application of hedge accounting:

	Fair value	Currency	Contract amount
December 31, 2016			
Forward Contracts	\$ (1,009)	USD/TWD	1,550

As of December 31, 2016, the maturity dates of the derivative financial liabilities were between January 25, 2017 to March 6, 2017.

(c) Notes and accounts receivable and other receivables

	December 31, 2016	December 31, 2015
Notes receivable	\$ 6,461	12,506
Accounts receivable	1,116,096	1,067,195
Other receivables	69,031	646
Less: allowance for impairment	10,753	5,554
	<u>\$ 1,180,835</u>	<u>1,074,793</u>

The Group has not provided the notes and accounts receivable and other receivables as collateral or factored them for cash.

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES
Notes to the Consolidated Financial Statements

The aging analyses that were past due but not impaired were as follows:

	December 31, 2016	December 31, 2015
Past due 1~30 days	\$ 49,661	75,355
Past due 31~90 days	26,228	38,288
Past due over 90 days	<u>7,708</u>	<u>13,353</u>
	<u>\$ 83,597</u>	<u>126,996</u>

Since the payment of trading receivables that have past due date are still ongoing, The Group did not recognize related impairment loss.

The movement in the allowance for impairment with respect to notes and accounts receivable and other receivables were as follows:

	Individually assessed impairment	Collectively assessed impairment	Total
Balance at January 1, 2016	\$ 5,554	-	5,554
Impairment loss recognized	5,566	-	5,566
Written-off in current period	(244)	-	(244)
Effect of changes in exchange rates	<u>(123)</u>	<u>-</u>	<u>(123)</u>
Balance at December 31, 2016	<u>\$ 10,753</u>	<u>-</u>	<u>10,753</u>

	Individually assessed impairment	Collectively assessed impairment	Total
Balance at January 1, 2015	\$ 4,998	-	4,998
Impairment loss recognized	572	-	572
Effect of changes in exchange rates	<u>(16)</u>	<u>-</u>	<u>(16)</u>
Balance at December 31, 2015	<u>\$ 5,554</u>	<u>-</u>	<u>5,554</u>

(d) Inventories

The components of the Group's inventories were as follows:

	December 31, 2016	December 31, 2015
Merchandise	\$ 1,360	3,139
Finished goods	689,966	695,068
Work in process	265,186	270,031
Raw material	<u>429,012</u>	<u>447,754</u>
Total	<u>\$ 1,385,524</u>	<u>1,415,992</u>

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

Inventories are measured at the lower of cost and net realizable value. Hence, the Group makes judgment and estimates which shortens the life cycles of electronic products, the net realizable value of inventory for financial statement. Due to the rapid technology change, which shortens the life cycles of electronic products, the Group assessed the financial statement decrease to net realizable value of inventory at cost which is caused by normal wear and tear, obsolescence or no market value of the amount and cost of inventory write-downs to net realizable value. Valuation of the inventory is based according to the estimated future demand for its products. Hence, there is a possibility for the valuation to have a significant fluctuation.

As of December 31, 2016 and 2015, the Group's inventories are not pledged as collateral.

Aside from charging operating costs through the ordinary sale of inventories, other gains and losses directly recorded under operating costs in the years 2016 and 2015 are as follows:

	2016	2015
Loss on market value of inventory	\$ 35,370	28,612
Loss from scrapped inventory	37,443	12,617
Loss on physical count	<u>21</u>	<u>1,888</u>
Total	<u>\$ 72,834</u>	<u>43,117</u>

(e) Financial assets carried at cost—noncurrent

	Stockholding rate %	Investment cost	Amount
December 31, 2016			
Alliance III venture Capital Corp.	1.00	\$ <u>500</u>	<u>500</u>
	Stockholding rate %	Investment cost	Amount
December 31, 2015			
Alliance III venture Capital Corp	1.00	\$ <u>1,000</u>	<u>1,000</u>

In August 2016, Alliance III venture Capital Corp, one of the Group investments carried at cost, executed a capital reduction by canceling 5,000 thousand of its shares amounting to \$50,000 thousand, which had already been distributed to its shareholders. Therefore, the Group had received \$500 thousand, which resulted in a reduction of 50 thousand shares from Alliance III venture Capital Corp.

The Group has assessed the recoverable amount of the investment on Hua Dian (Beijing) Technology Ltd. is less than the book value. Therefore, the Group has recognized the entire investment as impairment loss. Further, the Group disposed the entire investment in August 2015.

The aforementioned investments held by the Group are measured at amortized cost at year-end given the range of reasonable fair value estimates is large and the probability for each estimate cannot be reasonably determined; therefore, the Group management had determined that the fair value cannot be measured reliably.

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES
Notes to the Consolidated Financial Statements

(f) Business combination

In February 2016, the Board of Directors has decided to obtained 100% shares of Dongguan Lihua Haiwell Technology Co., Ltd. and 42.99% shares of Beijing HDZX Technology Co., Ltd. for 18,339 thousand (CNY3,700 thousand) and \$15,550 thousand (CNY3,137 thousand), respectively.

i) Dongguan Lihua Haiwell Technology Co., Ltd.

The Group has obtained control over Dongguan Lihua Haiwell Technology Co., Ltd. on March 1, 2016 (acquisition date) and the payment for the acquisition has been made.

The acquisition of Dongguan Lihua Haiwell Technology Co., Ltd. allows the Group to expand its product capacity in China to meet future demands.

For the period from the acquisition date to December 31, 2016, the net income after tax attributed to the Group amounted to \$(2,812) thousand. If the acquisition occurred on January 1, 2016, the management estimates that the net income after tax for the period from January 1, 2016 to December 31, 2016 will increase to \$408,721 thousand. The aforementioned amounts were based on the management's assumptions that the acquisition took place on January 1, 2016 and that the adjustments of the temporarily determined fair value on the acquisition date remain unchanged.

The major categories and fair values of acquired assets and liabilities are as follows:

- i. The transfer consideration of \$18,339 thousand was paid in cash.
- ii. Identifiable assets and liabilities obtained

The fair values of identifiable assets acquired and liabilities assumed on the date of acquisition are as follows:

Property, plant and equipment	\$ 135
Inventories	232,108
Accounts receivable	54,582
Cash and cash equivalent	10,538
Other current and non-current assets	11,028
Accounts payable	(287,932)
Other current liabilities	(2,120)
	<u>\$ 18,339</u>

The gross contractual amounts of accounts receivable totaled \$54,582 thousand. The amount is expected to be collectible on the acquisition date.

If there is any information indicating that facts and circumstances exist on the acquisition date which leads to an adjustment to the above provisional amounts, or any additional provisions as of the acquisition date, within one year from the acquisition date, then the acquisition accounting will be revised.

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES
Notes to the Consolidated Financial Statements

ii) Beijing HDZX Technology Co., Ltd.

The Group has obtained the control over HDZX on March 1, 2016 (acquisition date) and the payment for the acquisition had already been made.

The acquisition of HDZX allows the Group to increase its product types, which is mainly power-saving products.

For the period from the acquisition date to December 31, 2016, the operating revenue and net income after tax attributed to the Group amounted to \$253,812 thousand and \$12,705 thousand, respectively. If the acquisition occurred on January 1, 2016, the management estimates that the operating revenue and net income after tax for the period from January 1, 2016 to December 31, 2016 will increase to \$6,135,202 thousand and \$380,491 thousand, respectively. The aforementioned amounts were based on the management's assumptions that the acquisition took place on January 1, 2016 and that the adjustments of the temporarily determined fair value on the acquisition date remain unchanged.

The major categories and fair values of acquired assets and liabilities are as follows:

i. The transfer consideration of \$15,550 thousand transferred was paid in cash.

ii. Identifiable assets and liabilities obtained

The fair values of identifiable assets acquired and liabilities assumed on the date of acquisition are as follows:

Property, plant and equipment	\$ 180
Identifiable intangible assets—customer relations	4,957
Inventories	39,518
Accounts receivable	53,577
Cash and cash equivalent	32,129
Other current and non-current assets	1,183
Accounts payable	(75,385)
Other current liabilities	(3,397)
	<u>\$ 52,762</u>

The following fair values of the assets and liabilities have been determined on a temporary basis:

The fair value of the identifiable intangible asset acquired was temporarily determined to be \$4,957 thousand. The valuation of the said intangible asset has not yet been completed. Customer relations were mainly from HDZX's market share. Synergy is expected to arise from the business combination of the Company and the Group.

The gross contractual amounts of accounts receivable totaled \$52,762 thousand. The amount is expected to be collectible on the acquisition date.

If there is any information indicating facts and circumstances exist on the acquisition date which leads to an adjustment to the above provisional amounts, or any additional provisions as of the acquisition date, within one year from the acquisition date, then the acquisition accounting will be revised.

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES
Notes to the Consolidated Financial Statements

iii. Goodwill

Goodwill arising from the acquisition is as follows:

Consideration transfer	\$ 15,550
Plus: Fair value of acquiree's original interests	11,896
Plus: Non-controlling interests	30,333
Less: Fair value of identifiable net assets acquired	<u>52,762</u>
Goodwill arising on acquisition	<u><u>\$ 5,017</u></u>

The recognition of goodwill do not expect to have any impact on tax.

iv. Non-controlling interest

Fair value of the non-controlling interest of HDZX amounted to \$30,333 thousand. The fair value is determined based on a market approach and an income approach. The measurement of fair value was estimated using unobservable parameters, indicating that the measurement belongs to the third hierarchy of the fair value. The key model inputs used for determining the fair value are as follows:

- 1) An assumed discount rate of 21% to 25%;
- 2) Final values are based on 2.5% to 4% long-term growth rate;
- 3) Assumed that financial multiplier of a company is similar to that of Beijing HDZX Technology Co., Ltd.; and
- 4) Market participants take into consideration the controlling power and liquidity of HDZX when measuring the fair value of its non-controlling interest.

(g) Property, plant and equipment

The cost, depreciation, and impairment of the property, plant and equipment of the Group were as follows:

	Land	Buildings	Machinery	Other equipment	Construction in progress	Total
Cost or deemed cost:						
Balance at January 1, 2016	\$ 501,490	462,377	132,914	366,445	2,041	1,465,267
Additions	-	-	9,740	42,423	-	52,163
Disposals	-	-	(8,437)	(10,227)	-	(18,664)
Reclassification	-	1,082	931	14,392	(2,013)	14,392
Effect of consolidation	-	-	-	698	-	698
Effect of changes in exchange rates	(526)	(853)	(483)	(5,487)	(28)	(7,377)
Balance at December 31, 2016	<u>\$ 500,964</u>	<u>462,606</u>	<u>134,665</u>	<u>408,244</u>	<u>-</u>	<u>1,506,479</u>
Balance at January 1, 2015	\$ 500,420	458,089	127,689	257,935	2,199	1,346,332
Additions	-	2,353	5,253	109,370	-	116,976
Disposals	-	-	(113)	(12,716)	-	(12,829)
Reclassification	-	231	-	13,440	(231)	13,440
Effect of changes in exchange rates	1,070	1,704	85	(1,584)	73	1,348
Balance at December 31, 2015	<u>\$ 501,490</u>	<u>462,377</u>	<u>132,914</u>	<u>366,445</u>	<u>2,041</u>	<u>1,465,267</u>

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES
Notes to the Consolidated Financial Statements

	Land	Buildings	Machinery	Other equipment	Construction in progress	Total
Depreciation and impairment loss:						
Balance at January 1, 2016	\$ -	66,187	88,754	152,677	-	307,618
Depreciation	-	12,435	17,460	70,237	-	100,132
Disposal	-	-	(4,518)	(6,692)	-	(11,210)
Reclassification	-	-	-	(1,592)	-	(1,592)
Effect of consolidation	-	-	-	383	-	383
Effect of changes in exchange rates	-	(99)	(195)	(3,108)	-	(3,402)
Balance at December 31, 2016	<u>\$ -</u>	<u>78,523</u>	<u>101,501</u>	<u>211,905</u>	<u>-</u>	<u>391,929</u>
Balance at January 1, 2015	\$ -	53,676	70,090	119,181	-	242,947
Depreciation	-	12,348	18,617	44,029	-	74,994
Disposal	-	-	(13)	(9,908)	-	(9,921)
Effect of changes in exchange rates	-	163	60	(625)	-	(402)
Balance at December 31, 2015	<u>\$ -</u>	<u>66,187</u>	<u>88,754</u>	<u>152,677</u>	<u>-</u>	<u>307,618</u>
Carrying value:						
December 31, 2016	<u>\$ 500,964</u>	<u>384,083</u>	<u>33,164</u>	<u>196,339</u>	<u>-</u>	<u>1,114,550</u>
December 31, 2015	<u>\$ 501,490</u>	<u>396,190</u>	<u>44,160</u>	<u>213,768</u>	<u>2,041</u>	<u>1,157,649</u>
January 1, 2015	<u>\$ 500,420</u>	<u>404,413</u>	<u>57,599</u>	<u>138,754</u>	<u>2,199</u>	<u>1,103,385</u>

Please refer to note 8 for the information of the pledged property, plant and equipment, as of December 31, 2016 and 2015.

(h) Intangible assets

The cost and amortization of the intangible assets of the Group were as follows:

	Goodwill	Customer relation	Total
Costs:			
Balance at January 1, 2016	\$ -	-	-
Acquisition of consolidation	5,017	4,957	9,974
Effect of changes in exchange rates	(363)	(359)	(722)
Balance at December 31, 2016	<u>\$ 4,654</u>	<u>4,598</u>	<u>9,252</u>
Amortization:			
Balance at January 1, 2016	\$ -	-	-
Amortization	-	1,277	1,277
Balance at December 31, 2016	<u>\$ -</u>	<u>1,277</u>	<u>1,277</u>
Carrying value:			
December 31, 2016	<u>\$ 4,654</u>	<u>3,321</u>	<u>7,975</u>

i) Amortization

Goodwill and customer relations were obtained by acquiring subsidiaries in March 2015. For amortization expense, please refer to note 12.

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

ii) Impairment Loss

In accordance with IAS 36 “impairment of assets,” the Group assesses the impairment loss of intangible assets—goodwill, at the end of each reporting period. The recoverable amount of the cash generating unit is the expected discount present value of future cash in flows. As of December 31, 2016, based on the result of the assessment of the Group, the recoverable amount of the cash-generating unit was higher than the book value. Therefore, there was no impairment loss.

- i. The cash flow projections were estimated on the basis of previous experience, actual operating results, and the financial budget.
- ii. Forecast of operating revenue, operating cost, and operating expenses are based on the future operational plan, with consideration on the changes and competition in the market industry.
- iii. For the year 2016, the discount rates for the present value of recoverable amounts was 12%.

iii) The Group did not pledge any collateral on intangible assets.

(i) Short-term and long-term borrowings

The details, terms and clauses of the Group's short-term and long-term borrowings were as follows:

i) Short-term borrowings

December 31, 2016				
	Currency	Interest rate	Maturity year	Amount
Unsecured loans	RMB	5.22	2017	\$ 41,866
Unsecured loans	USD	3.0095	2017	<u>13,793</u>
Total				<u><u>\$ 55,659</u></u>

December 31, 2015				
	Currency	Interest rate	Maturity year	Amount
Unsecured loans	USD	2.5762	2016	<u><u>\$ 42,604</u></u>

Please refer to note 6(u) for the disclosures on the Group's risk exposure to interest rates and liquidity risks.

As of December 31, 2016, and 2015, the unused credit facilities of the Group's short-term borrowings amounted to \$877,195 and \$870,000 thousand, respectively.

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES
Notes to the Consolidated Financial Statements

ii) Long-term borrowings

December 31, 2016				
	Currency	Interest rate	Maturity year	Amount
Secured loans	USD	2.9829	2020	\$ <u>41,705</u>
Current				\$ 1,932
Non-current				<u>39,773</u>
Total				\$ <u>41,705</u>

December 31, 2015				
	Currency	Interest rate	Maturity year	Amount
Secured loans	USD	2.4490	2020	\$ <u>44,406</u>
Current				\$ 1,966
Non-current				<u>42,440</u>
Total				\$ <u>44,406</u>

Please refer to note 6(t) for the disclosures on the Group's risk exposure to interest rates and liquidity risks.

iii) Collateral of loans

The Group has mortgaged their assets as collateral of loans. Please refer to note 8.

(j) Bonds payable

The Company issued unsecured convertible bonds as follows:

	December 31, 2016	December 31, 2015
Total amount of convertible Bonds	\$ 400,000	400,000
Discount on bonds payable unamortized balance	-	(4,195)
Accumulated converted balance	(375,700)	(172,300)
Redemption	<u>(24,300)</u>	<u>-</u>
Bonds payable of ending balance	<u>\$ -</u>	<u>223,505</u>
Embedded Derivatives — put option and call option (financial liability at fair value through profit or loss — non-current)	<u>\$ -</u>	<u>(23)</u>
Equity component — conversion options (Capital surpluses — Share options)	<u>\$ -</u>	<u>11,483</u>

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

	2016	2015
Embedded Derivatives — put option and call option measured at fair value through profit or loss (reported in other gains and losses)	\$ <u>23</u>	<u>(42)</u>
Interest expenses (financial costs)	\$ <u>3,895</u>	<u>5,196</u>

i) Denomination and coupon rate

On October 21, 2013, the Company issued 4,000 shares of unsecured convertible bonds with 0% coupon rate and three years maturity amounted to \$400,000 thousand.

ii) Conversion provision

- i. Bondholders are eligible to exercise the conversion right between one month after the bond issuance and ten days before the expiration date.
- ii. Conversion price: The conversion price at the issuance date was NTD\$48 per share. If there is any increase in the Company's common stock (such as cash injection, capital increase from related earnings or capital surplus, issuance of new shares for consolidation purposes or as the consideration payable by the Company for its acquisition of another company's shares, stock split or cash injection by participating in the issuance of overseas depository receipts, etc), the Company shall calculate and adjust the conversion price based on the formula stated in the second conversion arrangement before publishing an announcement through GTSM. The Company set August 16, 2014, August 19, 2015, September 3, 2015 and August 2, 2016 as the date of ex-dividend and ex-right. The conversion price amounted to \$43.51, \$39.81, \$39.80 and \$38.10 per share after the dividends and rights distribution have been adjusted.

iii) Redemption method

The Company's call option (right of redemption):

- i. If, between one month after the bond issuance and forty days before the expiration date, the closing price of the stocks is higher than 1.3 times the conversion price for 30 consecutive working days, the Company is entitled to send a "bond redemption notification" to the bondholders and post an announcement to notify GTSM that the Company is to repurchase all bonds at their face value by cash within 5 workings days after the benchmark date of bond redemption. The benchmark date of the bond redemption is the 30 days after the notification has been sent.
- ii. If, between one month after bond issuance and forty days before the expiration date, the outstanding balance of the bonds is lower than 10% of the total issued amount, the Company is entitled to, with notification in advance, repurchase all outstanding bonds at their face value.

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES
Notes to the Consolidated Financial Statements

iv) Bondholders' put option

Bondholders are entitled to exercise the put option beginning from the put day, which is two or three years after the issue date. The Company should send "bond put table notification" to bondholders and publish an announcement through GTSM, and bondholders then can exercise their put option by written notice to the Company to redeem the bonds at face value within 30 days.

(k) Provisions

	Warranty provision	Legal matter	Total
Balance at January 1, 2016	\$ 26,260	6,370	32,630
Provisions made during the year	30,690	-	30,690
Provisions used during the year	(21,369)	-	(21,369)
Effect of changes in exchange rates	(597)	-	(597)
Balance at December 31, 2016	<u>\$ 34,984</u>	<u>6,370</u>	<u>41,354</u>
Balance at January 1, 2015	\$ 11,470	6,370	17,840
Provisions made during the year	45,091	-	45,091
Provisions used during the year	(30,174)	-	(30,174)
Effect of changes in exchange rates	(127)	-	(127)
Balance at December 31, 2015	<u>\$ 26,260</u>	<u>6,370</u>	<u>32,630</u>

i) Warranties

In 2016 and 2015, provisions are estimated based on the historical data of trading of interment communications equipment, which are mainly associated with the Company's business products. The Group anticipates the warranties to occur in the following year of the sales.

ii) Legal

The Group assumed a contingent liability in respect of a legal claim brought against the Group by a former employee. The plaintiff made claims in the amount of \$10,963 thousand. The Group also assumed other contingent liability of \$5,290 as the result determined by Taiwan High Court. Interest is calculated using the 5% per annum rate from October 14, 2007 until the repayment date. The Group and another accused both appealed to the Supreme Court concerning the aforementioned matter. The Supreme Court handed the case back over to the High Court for re-assessment. The High Court then overruled the lawsuit against the plaintiff in November 2014. However, since the plaintiffs disagreed with the verdict, they filed another appeal to the Supreme Court, and the case is still in progress. As of December 31, 2016 and 2015, the Group estimated the debt provision to be \$6,370 thousand due to the aforementioned lawsuit.

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES
Notes to the Consolidated Financial Statements

(l) Employee benefits

i) Defined benefit plans

The following table shows a reconciliation between the present value of the defined benefit obligation and the fair value of plan assets:

	December 31, 2016	December 31, 2015
The present value of the defined benefit obligations	\$ 56,401	52,659
Fair value of plan assets	<u>(21,905)</u>	<u>(23,491)</u>
The net defined benefit liability	<u>\$ 34,496</u>	<u>29,168</u>

The Group makes defined benefit plan contributions to the pension fund account at Bank of Taiwan that provides pensions for employees upon retirement. The plans (covered by the Labor Standards Law) entitle a retired employee to receive an annual payment based on years of service and average salary for the six months prior to retirement.

i. Composition of plan assets

The Group allocates pension funds in accordance with the Regulations for Revenues, Expenditures, Safeguard and Utilization of the Labor Retirement Fund, and such funds are managed by the Bureau of Labor Funds, Ministry of Labor. With regard to the utilization of the funds, minimum earnings in the annual distributions on the final financial statements shall be no less than the earnings attainable from the amounts accrued from two-year time deposits with interest rates offered by local banks.

The Group's Bank of Taiwan labor pension reserve account balance amounted to \$21,905 thousand at the end of the reporting period. For information on the utilization of the labor pension fund assets including the asset allocation and yield of the fund, please refer to the website of the Bureau of Labor Funds, Ministry of Labor.

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

ii. Movements in present value of the defined benefit obligations

The movements in present value of the Group's defined benefit plan obligation for the years ended December 31, 2016 and 2015, were as follows:

	2016	2015
Defined benefit obligation at 1 January	\$ 52,659	49,291
Current service costs and interest	1,469	1,536
Remeasurements of the net defined benefit liability (asset)		
— Return on plan assets (excluding amounts included in net interest expense)	(463)	1,089
— Due to changes in financial assumption of actuarial (losses) gains	4,516	743
Past service cost	1,190	-
Benefits paid by the plan	(2,970)	-
Defined benefit obligation at 31 December	<u>\$ 56,401</u>	<u>52,659</u>

iii. Movement of defined benefit plan assets

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

	2016	2015
Fair value of plan assets, January 1	\$ 23,491	21,720
Remeasurements of the net defined benefit liability (asset)		
— Return on plan assets (excluding amounts included in net interest expense)	160	577
Contributions made	1,224	1,194
Benefits paid by the plan	(2,970)	-
Fair value of plan assets, December 31	<u>\$ 21,905</u>	<u>23,491</u>

iv. Expenses recognized in profit or loss

The expenses recognized on profit or loss for the years ended December 31, 2016 and 2015, were as follows:

	2016	2015
Current service cost	\$ 520	589
Net interest on the defined benefit liability (asset)	535	540
Past service cost and gains (losses) due to settlement	1,190	-
	<u>\$ 2,245</u>	<u>1,129</u>

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

	2016	2015
Operating costs	\$ 469	478
Selling expenses	171	140
Administration expenses	1,328	259
Research and development expenses	<u>277</u>	<u>252</u>
	<u>\$ 2,245</u>	<u>1,129</u>

- v. Remeasurement in the net defined benefit liability (asset) recognized in other comprehensive income

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

	2016	2015
Cumulative amount, January 1	\$ 9,681	8,019
Recognized during the period	<u>4,307</u>	<u>1,662</u>
Cumulative amount, December 31	<u>\$ 13,988</u>	<u>9,681</u>

- vi. Actuarial assumptions

The principal actuarial assumption used to determine the present value of the defined benefit obligation on December 31, 2016 and 2015 is as follows:

	2016.12.31	2015.12.31
Discount rate	1.125 %	1.875 %
Future salary increases rate	3.300 %	3.300 %

The Group expects to make contributions of \$1,195 thousand to the defined benefit plans in the next year starting from the reporting date of 2016.

The weighted average duration of the defined benefit obligation is 14.93 years.

- vii. Sensitivity analysis

When calculating the present value of the defined benefit obligations, the Group uses judgments and estimations to determine the actuarial assumptions, and future salary changes, as of the financial statement date. Any changes in the actuarial assumptions may significantly impact the amount of the defined benefit obligations.

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES
Notes to the Consolidated Financial Statements

As of December 31, 2016 and 2015, the present value of defined benefit obligation impact was as follow:

	The impact of defined benefit obligation	
	Increase 0.25%	Decrease 0.25%
December 31, 2016		
Discount rate (0.25%)	\$ (1,569)	1,621
Future salary increase rate (0.25%)	1,555	(1,515)
December 31, 2015		
Discount rate (0.25%)	(1,475)	1,529
Future salary increase rate (0.25%)	1,482	(1,427)

Reasonably possible changes at the reporting date to one of the relevant actuarial assumptions, holding other assumptions constant, would have affected the defined benefit obligation by the amounts shown above. The method used in the sensitivity analysis is consistent with the calculation of pension liabilities in the balance sheets.

There is no change in the method and assumptions used in the preparation of sensitivity analysis for 2016 and 2015.

ii) **Defined contribution plans**

The Group allocates 6% of each employee's monthly wages to the labor pension personal account at the Bureau of the Labor Insurance in accordance with the provisions of the Labor Pension Act. Under this defined contribution plan, the Group allocates a fixed amount to the Bureau of the Labor Insurance without additional legal or constructive obligations.

The Group's pension costs under the defined contribution method were \$32,831 thousand and \$29,768 thousand for 2016 and 2015, respectively. Payment was made to the Bureau of the Labor Insurance and the local authorities of the consolidated overseas subsidiaries.

iii) **Short-term employee benefit**

	December 31, 2016	December 31, 2015
Annual leave benefit	\$ <u>20,782</u>	<u>17,656</u>

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES
Notes to the Consolidated Financial Statements

(m) Income tax

i) Income tax expenses (benefit)

The amount of income tax for 2016 and 2015 were as follows:

	2016	2015
Current tax expense		
Current period	\$ 72,214	99,780
Adjustment for prior periods	<u>(2,368)</u>	<u>1,042</u>
	<u>69,846</u>	<u>100,822</u>
Deferred income tax expense		
Origination and reversal of temporary differences	<u>14,904</u>	<u>(1,991)</u>
Income tax expense from continuing operations	<u><u>\$ 84,750</u></u>	<u><u>98,831</u></u>

Reconciliation of the Company's income tax expense (benefit) and the profit before tax for 2016 and 2015 were as follows:

	2016	2015
Net income before tax	\$ <u>494,897</u>	<u>427,947</u>
Income tax using the Company's domestic tax rate	\$ 84,132	72,751
Effect of tax rates in foreign jurisdiction	21,155	32,775
Previously underestimate (overestimate) income tax	(2,368)	1,042
Non-deductible expenses	(56)	3,230
Tax-free revenue	(3,635)	(5,246)
Unrecognized tax loss of deferred tax assets	-	165
Unrecognized changes in temporary differences	(6,570)	(2,000)
10% surtax on unappropriated earnings	8,993	9,372
R&D tax credits utilized	(14,377)	(10,309)
Others	<u>(2,524)</u>	<u>(2,949)</u>
Total	<u><u>\$ 84,750</u></u>	<u><u>98,831</u></u>

ii) Deferred income tax assets and liabilities

i. Unrecognized deferred income tax assets

Deferred income tax assets have not been recognized in respect of the following items:

	December 31, 2016	December 31, 2015
Deductible temporary differences	\$ 4,143	7,000
Tax losses	<u>6,500</u>	<u>10,039</u>
	<u><u>\$ 10,643</u></u>	<u><u>17,039</u></u>

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

Tax losses are applied to Income Tax Act in Canada that can be carried forward for twenty years, after assessed by tax authority, to offset taxable income before apply to tax rate. Deferred income tax assets have not been recognized in respect of these items because it is not probable that the future taxable profit will be available, against which, the Group can utilize the benefits there from.

As of December 31, 2016, the deferred income tax assets of Tax losses which have not been recognized were as follows:

1) Canada — federal

Year	Amount	Year of expiration
2012	\$ 3,166	2032
2013	10,213	2033
2014	2,595	2034
2015	<u>1,024</u>	2035
	<u><u>\$ 16,998</u></u>	

2) Canada — state

Year	Amount	Year of expiration
2012	\$ 3,166	2032
2013	10,213	2033
2014	2,595	2034
2015	<u>1,024</u>	2035
	<u><u>\$ 16,998</u></u>	

ii. Recognized deferred income tax assets and liabilities

Changes in the amount of deferred income tax assets and liabilities for 2016 and 2015 were as follows:

Deferred income tax assets:

	Unrealized profit from sales	Tax differences from sales	Others	Total
Balance at January 1, 2016	\$ 17,329	11,863	25,516	54,708
Recognized in profit or loss	<u>6,269</u>	<u>1,125</u>	<u>(1,308)</u>	<u>6,086</u>
Balance at December 31, 2016	<u><u>\$ 23,598</u></u>	<u><u>12,988</u></u>	<u><u>24,208</u></u>	<u><u>60,794</u></u>
Balance at January 1, 2015	\$ 11,652	8,985	13,945	34,582
Recognized in profit or loss	<u>5,677</u>	<u>2,878</u>	<u>11,571</u>	<u>20,126</u>
Balance at December 31, 2015	<u><u>\$ 17,329</u></u>	<u><u>11,863</u></u>	<u><u>25,516</u></u>	<u><u>54,708</u></u>

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES
Notes to the Consolidated Financial Statements

Deferred income tax liabilities:

	Foreign investment income accounted for using equity method
Balance at January 1, 2016	\$ (68,008)
Recognized in profit or loss	<u>(21,365)</u>
Balance at December 31, 2016	\$ <u>(89,373)</u>
Balance at January 1, 2015	\$ (49,452)
Recognized in profit or loss	<u>(18,556)</u>
Balance at December 31, 2015	\$ <u>(68,008)</u>

iii) Examination and Approval

The tax authorities have assessed the Company's income tax return for 2014. However, as the tax authorities ruled that extra taxes of \$22,149 thousand be paid, the company is intended to appeal to the court for re-assessment.

iv) Integrated income tax information

Information related to the unappropriated earnings and tax deduction ratio is summarized as below:

	December 31, 2016	December 31, 2015
Unappropriated earnings of 1997 and before	\$ -	-
Unappropriated earnings of 1998 and after	<u>778,494</u>	<u>628,724</u>
	\$ <u>778,494</u>	<u>628,724</u>
	December 31, 2016	December 31, 2015
Balance of imputation credit account	\$ <u>92,240</u>	<u>64,802</u>

After the Group's income tax returns were examined and assessed by the tax authorities, the imputation tax credit ratio of earnings to be distributed in 2017 and 2016 is estimated at 16.92%. The actual imputation tax credit ratio of earnings distributed in 2016 and 2015 was 15.87%.

From January 1, 2015, as the resident of the Republic of China received the distributions of dividends or earnings, the imputation tax credit is revised to 50% of the original tax credit. The shareholder received the net distribution of dividends or earnings and the imputation tax credit which was levied 10% surplus tax that the 50% of the surplus tax can be used to deduct the withholding tax.

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES
Notes to the Consolidated Financial Statements

(n) Capital and other equity

With 150,000 thousand shares and 100,000 thousand shares and each share amounting to \$10, the total value of the nominal ordinary shares both amounted to \$1,500,000 and \$1,000,000 as of December 31, 2016 and 2015. 103,645 and 97,501 thousand shares of common stocks were issued as of December 31, 2016 and 2015, respectively. All issued shares were paid up upon issuance.

A reconciliation of the Company's outstanding shares the years 2016 and 2015 is as follows:

	Unit: thousands shares	
	2016	2015
Balance at January 1	97,501	90,811
Exercise of employee share options	832	769
Capitalization of retained earnings	-	4,541
Capitalization of employee bonus	-	1,222
Conversion of convertible bonds	5,312	878
Cancellation of Treasury Stock	-	(720)
Balance at December 31	<u>103,645</u>	<u>97,501</u>

i) Issue of common stock

On June 18, 2015, the stockholders approved a resolution to transfer the stockholders' bonus of \$45,406 thousand and the employee bonus of \$53,302 thousand for the issuance of 5,763 thousand shares of common stocks, with a face value of 10 dollars per share. The Company has received the approval from the Financial Supervisory Commission for this capital increase on July 7, 2015, with August 19, 2015 recognized as the date of capital increase. The Company has registered the change with the relevant authorities. Among the total bonus transferred, the employee bonus of \$53,302 was transferred for the issuance of 1,222 thousand shares of common stocks. The Employee bonus was calculated based on the closing price one day prior to the stockholders' resolution and the impacts from ex-right and ex-dividend. The face value will be recognized as "share capital" on the date of issuance, and the remaining amount that exceeds the face value will be recognized as "additional paid-in capital".

Due to the exercise of the employee stock options in 2016 and 2015, the Company issued 832 and 769 thousand shares of stocks, respectively. Exercise prices were \$19.2 and \$20.6 per share in 2016 and 2015, respectively.

In 2016 and 2015, the Company issued puttable convertible bonds of \$203,400 thousand and \$38,200 thousand, which were converted to 5,312 thousand and 878 thousand shares of common stocks in 2016 and 2015, respectively, at \$39.80, \$38.10 and \$43.51 per share.

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

ii) Capital surplus

The composition of the Company's capital surplus as of December 31, 2016 and 2015, are as follows:

	December 31, 2016	December 31, 2015
Share premium from issuance	\$ 600,483	430,911
Changes in equity of associates and joint ventures accounted for using equity method	16,693	5,879
Employee share options	14,269	6,659
Share options	-	11,483
Employee share options expired	<u>8,429</u>	<u>7,203</u>
	<u><u>\$ 639,874</u></u>	<u><u>462,135</u></u>

In accordance with the ROC Company Act, realized capital reserves can only be reclassified as share capital or distributed as cash dividends after offsetting losses. The aforementioned capital reserves include share premiums and donation gains. In accordance with the Securities Offering and Issuance Guidelines, the amount of capital reserves to be reclassified under share capital shall not exceed 10% of the actual share capital amount.

iii) Retained earnings

i. Legal reserve

In accordance with the Company Act, 10% of net income after tax should be set aside as legal reserve, until it is equal to authorized capital. If the Company experienced profit for the year, the distribution of the statutory earnings reserve, either by new shares or by cash, shall be decided at the shareholders meeting, and the distribution amount is limited to the portion of legal reserve which exceeds 25% of the paid-in capital.

ii. Special earnings reserve

By choosing to apply exemptions granted under IFRS 1 First-time Adoption of International Financial Reporting Standards during the Company's first-time adoption of the IFRSs endorsed by the FSC, cumulative translation adjustments (gains) recognized under shareholders' equity were reclassified to retained earnings at the adoption date. In accordance with Ruling No. 1010012865 issued by the FSC on April 6, 2012, an increase in retained earnings due to the first-time adoption of the IFRSs endorsed by the FSC shall be reclassified as a special earnings reserve during earnings distribution. However, when adjusted retained earnings due to the first-time adoption of the IFRSs endorsed by the FSC are insufficient for the appropriation of a special earnings reserve at the transition date, the Company may appropriate a special earnings reserve up to the amount of increase in retained earnings. Upon the use, disposal, or reclassification of related assets, the Company may reverse the special earnings reserve proportionately. As a result of elections made according to IFRS 1, the Company has reclassified \$(13,624) thousand to retained earnings and is not required to appropriate a special earnings reserve.

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

In accordance with the above Ruling, a portion of current-period earnings and undistributed prior-period earnings shall be reclassified as a special earnings reserve during earnings distribution. The amount to be reclassified should be equal to the difference between the total net current-period reduction of special earnings reserve resulting from the first-time adoption of IFRSs and the carrying amount of other shareholders' equity as stated above. Similarly, a portion of undistributed prior-period earnings shall be reclassified as a special earnings reserve (which does not qualify for earnings distribution) to account for cumulative changes to other shareholders' equity pertaining to prior periods due to the first-time adoption of IFRSs. Amounts of subsequent reversals pertaining to the net reduction of other shareholders' equity shall qualify for additional distributions.

iii. Earnings distribution

The Company's articles of incorporation require that after-tax earnings from the current year shall first be used to offset any prior year's deficit and pay income tax; and 10% of the remaining balance shall be set aside as legal reserve. The appropriation for legal reserve is discontinued when the balance of the legal reserve equals the total authorized capital. Special reserve may be appropriated for operations or to meet regulations. After the distribution of dividends, the remaining earnings, if any, may be appropriated according to the proposal presented in the annual stockholders' meetings by the board of directors.

After the abovementioned appropriation, in order to operate proper investment and maintain Capital adequacy ratio simultaneously, the Company uses the Residual dividend policy to measure its monetary demand for the future according to its budget planned for the following years, then executes financial intermediation with retain earnings, after which, distributes cash dividends with the remaining earnings, which should not less than 30% of the total dividends amount.

In accordance with the revised ROC Company Act, the supervisor's emoluments and employee bonuses are not appropriated from distributable earnings. The Company will revise the Company's articles of incorporation before the official due date. Please refer to note 6(r).

Earnings distribution for 2014 and 2015 was decided via the general meeting of shareholders held on June 16, 2016 and June 18, 2015, respectively. The relevant dividend distributions to shareholders were as follows:

	2015		2014	
	Amount per share (NT dollars)	Total Amount	Amount per share (NT dollars)	Total Amount
Dividends distributed to common stockholders:				
Cash	\$ 1.9713	195,010	1.4732	136,218
Stock	-	-	0.4910	45,406
Total		<u>\$ 195,010</u>		<u>181,624</u>

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES
Notes to the Consolidated Financial Statements

iv) Treasury stock

According to Securities and Exchange Act regulations, the number of shares of treasury stock is not allowed to exceed 10% of the number of shares issued. Moreover, the total value of treasury stock is not allowed to exceed the sum of retained earnings, paid-in capital in excess of par value, and realized capital surplus. During the years ended December 31, 2016, no shares have been recovered by the Company, and the years ended December 31, 2015, the number of shares have been recovered by the Company were 720 thousand shares, with a total value of \$25,678 thousand, were in compliance with the Securities and Exchange Act.

In 2015, in order to retain the Company's credits and shareholder's rights and benefits, the Company has purchased 720 thousand shares of treasury stock in compliance with the Securities and Exchange Act regulations. On November 10, 2015, the Board has declared a write-off, and therefore, debited the capital surplus and the unappropriated retained earnings by \$3,225 thousand and \$15,253 thousand, respectively. The Board has announced the write-off date as November 10, 2015, and the registration was filed and completed on November 20, 2015.

According to Securities and Exchange Act regulations, treasury stock cannot be pledged. Until the treasury stock is transferred, it does not carry any shareholder rights.

v) Other equities (net of tax)

	Foreign exchange differences arising from foreign operation	Non-controlling interests	Total
Balance at January 1, 2016	\$ 19,995	5,031	25,026
Foreign exchange differences arising from net assets of foreign operation	(47,478)	(7,864)	(55,342)
Balance at December 31, 2016	<u>\$ (27,483)</u>	<u>(2,833)</u>	<u>(30,316)</u>
Balance at January 1, 2015	\$ 31,206	6,172	37,378
Foreign exchange differences arising from net assets of foreign operation	(11,211)	(1,141)	(12,352)
Balance at January 1, 2015	<u>\$ 19,995</u>	<u>5,031</u>	<u>25,026</u>

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(o) Share-based payment

On January 6, 2012, the Securities and Futures Bureau approved the Company's issuance of 3,000 units of Employee's Stock option; with each unit representing 1,000 shares of common stock, wherein a total of 3,000 thousand shares may be subscribed. The option holder is eligible, two years after issuance until the sixth year of issuance, to convert a certain percentage of options to common stocks at the price designated on the issuance date. Under such circumstances as changes in equity or distribution of cash dividends, the exercise price per share and the number of subscription per option are to be adjusted using a specific formula. However, the adjusted exercise price should not be lower than the par value. All options were granted on June 7, 2012 and their fair value on the grant date was priced using the Black Scholes option pricing model. The weighted-average data of each assumption were as follows:

Dividend rate	-	%
Expected volatility	13.41	%
Risk-free interest rate	0.93	%
Expected life	5	years

The Company estimates the compensation to be \$6,936 thousand based on the above assumptions. The compensation will be amortized over three years. Under the fair value method, the compensation of the option were estimated to be \$0 thousand and \$299 thousand in 2016 and 2015, respectively. The additional paid-in capital also increased due to the stock option plan.

The outstanding stock option rights as follows:

Employee stock options in 2012	Units	2016
		Exercise price (dollars)
Outstanding balance as of January 1	1,405	\$ 19.2
Options granted	-	-
Options exercised	600	19.2
Options cancelled	10	19.2
Options expired	-	-
Outstanding balance as of December 31	<u>795</u>	18.4
Exercisable as of December 31	<u>795</u>	18.4
Exercisable shares per unit as of December 31 — adjusted	<u>1,386</u>	
Fair market value	<u>\$ 3.7</u>	

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES
Notes to the Consolidated Financial Statements

Employee stock options in 2012	Units	2015 Exercise price (dollars)
Outstanding balance as of January 1	2,042	\$ 20.6
Options granted	-	-
Options exercised	589	20.6
Options cancelled	48	20.6
Options expired	-	-
Outstanding balance as of December 31	<u>1,405</u>	19.2
Exercisable as of December 31	<u>1,405</u>	19.2
Exercisable shares per unit as of December 31 — adjusted	<u>1,386</u>	
Fair market value	<u>\$ 3.7</u>	

As of December 31, 2016, the expected duration of the employee stock option issued in 2012 was 0.44 years.

On August 25, 2015, the Securities and Futures Bureau approved the Company's issuance of 3,000 units of Employee's Stock option; with each unit representing 1,000 shares of common stock, wherein a total of 3,000 thousand shares may be subscribed. The option holder is eligible, two years after issuance until the sixth year of issuance, to convert a certain percentage of options to common stocks at the price designated on the issuance date. Under such circumstances as changes in equity or distribution of cash dividends, the exercise price per share and the number of subscription per option are to be adjusted using a specific formula. However, the adjusted exercise price should not be lower than the par value. All options were granted on September 17, 2015 and their fair value on the grant date was priced using the Black Scholes option pricing model. The weighted-average data of each assumption were as follows:

Dividend rate	- %
Expected volatility	34.99 %
Risk-free interest rate	0.8779 %
Expected life	5 years

The Company estimates the compensation to be \$20,657 thousand based on the above assumptions. The compensation will be amortized over three years. Under the fair value method, the compensation of the option were estimated to be \$9,296 thousand and \$2,711 thousand in 2016 and 2015. The additional paid-in capital also increased due to the stock option plan.

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES
Notes to the Consolidated Financial Statements

The outstanding stock option rights as follows:

Employee stock options in 2015	2016	
	Units	Exercise price (dollars)
Outstanding balance as of January 1	2,970	\$ 35.6
Options granted	-	-
Options exercised	-	-
Options cancelled	160	35.6 / 34.1
Options expired	-	-
Outstanding balance as of December 31	<u>2,810</u>	34.1
Exercisable as of December 31	<u>-</u>	-
Exercisable shares per unit as of December 31 — adjusted	<u>1,000</u>	
Fair market value	<u>\$ 4.3</u>	

Employee stock options in 2012	2015	
	Units	Exercise price (dollars)
Outstanding balance as of January 1	-	\$ -
Options granted	3,000	35.6
Options exercised	-	-
Options cancelled	30	36
Options expired	-	-
Outstanding balance as of December 31	<u>2,970</u>	35.6
Exercisable as of December 31	<u>-</u>	35.6
Exercisable shares per unit as of December 31 — adjusted	<u>1,000</u>	
Fair market value	<u>\$ 11.3</u>	

As of December 31, 2016, the expected duration of the employee stock option issued in 2015 was 3.71 years.

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES
Notes to the Consolidated Financial Statements

(p) Earnings per share

The calculation of the Group's basic earnings per share and diluted earnings per share for years ended December 31, 2016 and 2015 were as follows:

i) Basic earnings per share

	2016	2015
Net income attributable to ordinary shareholders of the Company	\$ <u>380,927</u>	<u>318,404</u>
Weighted-average number of ordinary shares	<u>99,580</u>	<u>96,867</u>
Basic earnings per share (in NT dollars)	\$ <u>3.83</u>	<u>3.29</u>

ii) Diluted earnings per share

	2016	2015
Net income of the company	\$ 380,927	318,404
Effect of after tax interest expense of conversion bonds	<u>3,233</u>	<u>4,313</u>
Net income attributable to ordinary shareholders of the Company	\$ <u>384,160</u>	<u>322,717</u>
Weighted-average number of ordinary shares (basic)	99,580	96,867
Impact of potential common shares		
Effect of employee stock bonus	1,825	1,938
Effect of employee stock option	1,136	1,511
Effect of conversion bonds	<u>4,248</u>	<u>5,721</u>
Weighted-average number of ordinary shares (diluted)	<u>106,789</u>	<u>106,037</u>
Diluted earnings per share (in NT dollars)	\$ <u>3.60</u>	<u>3.04</u>

For calculation of the dilutive effect of the stock option, the average market value is assessed based on the quoted market price where the Company's option is outstanding.

(q) Revenue

The details of the Group's revenue for the years ended December 31, 2016 and 2015 were as follows:

	2016	2015
Sale of goods	\$ <u>6,120,048</u>	<u>5,439,499</u>

Unearned revenue for consolidated company amounted to \$5,172 thousand and \$7,528 thousand in 2016 and 2015, respectively. As of December 31, 2016 and 2015, accumulated unearned revenue amounted to \$58,978 thousand and \$54,138 thousand, respectively. Unearned revenue was booked due to identifiable services to be rendered.

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

In 2016, operating revenue and operating costs incurred from repurchase transactions are not recognized after the management's judgment. As of December 31, 2016, receivables and payables incurred from those transactions were recognized as other receivables and other payables amounting to \$67,293 thousand and \$71,605 thousand, respectively. There were no such conditions in 2015.

(r) Remuneration to employees, directors and supervisors

In accordance with the Company's article, the Company should contribute 10% to 20% of its profit as employee remuneration, and no greater than 2% as directors' and supervisors' remuneration, when there is profit for the year. However, if the Company has accumulated deficits, the profit should first be used to offset the deficit. The amounts of remuneration to each director and supervisor, as well as the remuneration to employees, are subject for approval during the board of directors' meeting.

The employee bonuses, and directors' and supervisors' remuneration were recognized as cost of sales or operating expenses on a specific percentage of the net income. These amounts are calculated by using the Company's profit before tax (without the employee bonuses, and directors' and supervisors' remuneration), multiplied by the percentage specified in the Company's article for each period. For the year ended December 31, 2016 and 2015, the Company recognized its employee bonuses of \$63,934 thousand and \$54,193 thousand, respectively, and directors' and supervisors' remuneration of \$6,393 thousand and \$5,558 thousand, respectively.

There are no differences between the amounts of employee bonuses, directors' and supervisors' remuneration approved in the shareholder's meeting and those estimated in 2015 financial statement. On the board meeting at March 2, 2017, the Company approved that the amount for remuneration to employees, directors and supervisors are \$59,972 thousand and \$6,920 thousand, respectively. The difference between these amounts and the prior estimated amounts are recognized as gains(losses) of 2017.

(s) Non-operating income and expenses

i) Other income

The details of the Group's other income for the years ended December 31, 2016 and 2015 were as follows:

	2016	2015
Rent income	\$ 793	818
Interest income	4,648	1,783
Other	<u>82,530</u>	<u>97,878</u>
	<u>\$ 87,971</u>	<u>100,479</u>

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES
Notes to the Consolidated Financial Statements

ii) Other gains and losses

	2016	2015
Gain (loss) on foreign exchange	\$ (7,087)	(3,757)
Loss on disposal of property, plant and equipment	(1,197)	(375)
Valuation gain (loss) on financial assets	(870)	(42)
Other	(817)	(1,660)
	<u>\$ (9,971)</u>	<u>(5,834)</u>

iii) Finance costs

The details of the Group's finance costs for the years ended December 31, 2016 and 2015 were as follows:

	2016	2015
Interest expenses — convertible bonds	\$ 3,895	5,196
Interest expenses — short-term loans	3,061	2,920
	<u>\$ 6,956</u>	<u>8,116</u>

(t) Financial instruments

i) Credit risk

i. Exposure to credit risk

The carrying amount of financial assets represents the maximum amount exposed to credit risk.

ii. Concentration of credit risk

Approximately, 25% and 23% of the Group's total sales were derived from a single client in 2016 and 2015, respectively. Region wise, approximately 93% of the sales were significantly concentrated in Asia and America in 2016 and 2015, respectively.

ii) Liquidity risk

The following table shows the contractual maturities of financial liabilities, including estimated interest payments and excluding the impact of netting agreements.

	Carrying amount	Contractual cash flows	Within a year	1-2 years	3-5 years	Over 5 years
December 31, 2016						
Non-derivative financial liabilities						
Current financial liabilities at fair value through profit or loss	\$ 1,009	1,009	1,009	-	-	-
Short-term debts	55,659	56,794	56,794	-	-	-
Accounts payable	1,022,436	1,022,436	1,022,436	-	-	-
Other payable	289,054	289,054	289,054	-	-	-
Long-term debts (including due within a year)	41,705	46,061	2,134	2,134	41,793	-
	<u>\$ 1,409,863</u>	<u>1,415,354</u>	<u>1,371,427</u>	<u>2,134</u>	<u>41,793</u>	<u>-</u>

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES
Notes to the Consolidated Financial Statements

	Carrying amount	Contractual cash flows	Within a year	1-2 years	3-5 years	Over 5 years
December 31, 2015						
Non-derivative financial liabilities						
Non-current financial liabilities at fair value through profit or loss	\$ 23	23	23	-	-	-
Short-term debts	42,604	43,154	43,154	-	-	-
Bonds payable	223,505	223,505	223,505	-	-	-
Accounts payable	835,610	835,610	835,610	-	-	-
Other payable	220,382	220,382	220,382	-	-	-
Long-term debts (including due within a year)	44,406	49,304	2,183	2,183	6,549	38,389
	<u>\$ 1,366,530</u>	<u>1,371,978</u>	<u>1,324,857</u>	<u>2,183</u>	<u>6,549</u>	<u>38,389</u>

iii) Currency risk

i. Exposure to foreign currency risk

The Group's significant exposure to foreign currency risk was as follows:

	Foreign currency	Exchange rate	NTD
December 31, 2016			
Financial assets:			
Monetary items:			
USD (note)	\$ 47,664	32.2050	1,535,035
Financial liabilities:			
Monetary items:			
USD (note)	\$ 32,936	32.2050	1,060,705
December 31, 2015			
Financial assets:			
Monetary items:			
USD (note)	\$ 40,113	32.7720	1,314,589
Financial liabilities:			
Monetary items:			
USD (note)	\$ 20,539	32.7720	673,109

Note: Amounts are designated before consolidation.

ii. Sensitivity analysis

The Group's exposure to foreign currency risk arises from the translation of foreign currency exchange gains and losses on cash and cash equivalents, trade and other receivables and trade payables that are denominated in foreign currency. A weakening (strengthening) 1% of appreciation (depreciation) of the NTD against the USD as of December 31, 2016 and 2015 would have increased or decreased the net profit by \$12,224 and \$16,246 thousand, respectively. The analysis is performed on the same basis for both periods.

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

iii. Foreign exchange gain and loss on monetary item

Since the Group has many kinds of functional currency, the information on foreign exchange gain (loss) on Monetary items is disclosed by total amount. For the year 2016 and 2015, foreign exchange gain (loss) (including realized and unrealized abortions) amounted to \$7,087 thousand and \$3,757 thousand.

iv) Interest rate analysis

Please refer to the note for liquidity risk management and the Group's interest rate exposure to its financial assets and liabilities.

The following sensitivity analysis is based on the risk exposure of the interest rate on derivative and non-derivative financial instruments on the reporting date. Regarding assets with variable interest rates, the analysis is on the basis of the assumption that the amount of assets outstanding at the reporting date was outstanding throughout the year. The rate of change is expressed as the interest rate increases or decreases by 1% when reporting to management internally, which also represents the management of the Group's assessment on the reasonably possible interval of interest rate change.

If the interest rate increases or decreases by 1%, the Group's net income will increase /decrease by \$808 and \$722 thousand, respectively, for the years ended December 31, 2016, and 2015, with all other variable factors remain constant. This is mainly due to the Group's borrowing in variable rates and investment in variable rate bills.

v) Information of fair value

i. Categories and fair value of financial instruments

Except for the followings, carrying amount of the Group's financial assets and liabilities are valued approximately to their fair value. No additional disclosure is required in accordance to the Regulations.

		December 31, 2016			
		Fair value			
	Carrying amount	Level 1	Level 2	Level 3	Total
Financial assets at fair value through profit or loss					
Non derivative financial assets for trading	\$ <u>50,009</u>	<u>50,009</u>	<u>-</u>	<u>-</u>	<u>50,009</u>
Financial liabilities at fair value through profit or loss					
Derivative financial liabilities	\$ <u>1,009</u>	<u>-</u>	<u>1,009</u>	<u>-</u>	<u>1,009</u>

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES
Notes to the Consolidated Financial Statements

	Carrying amount	December 31, 2015 Fair value			Total
		Level 1	Level 2	Level 3	
Financial liabilities at fair value through profit or loss					
Derivative financial liabilities	\$ <u>23</u>	<u>-</u>	<u>23</u>	<u>-</u>	<u>23</u>

ii. Valuation techniques and assumptions used in fair value determination

The financial instruments of the Group are evaluated by using the publicly-adopted valuation models. Forward contracts are referred to the evaluation outcomes from financial institutions. Convertible bonds are measured by using the binary tree valuation model with consideration of the parameters of stock shares fluctuations and risk-free interests.

(u) Financial risk management

i) Overview

The Group is exposed to the following risks arising from financial instruments:

- i. Credit risk
- ii. Liquidity risk
- iii. Market risk

This note expresses the information on risk exposure and objectives, policies and process of risk measurement and management. For detailed information, please refer to the related notes to each risk.

ii) Risk management framework

The Board of Directors has overall responsibility for the establishment and oversight of the risk management framework. The Board has established the Risk Management Committee, which is responsible for establishing and monitoring the Group's risk management policies. The committee reports its activities regularly to the Board of Directors.

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

The Board of Directors oversees how management monitors the risk which should be in compliance with the Group's risk management policies and procedures, and reviews the adequacy of the risk management framework in relation to the risks faced by the Group. Assisting the Board of Directors in oversight, the internal Audit undertakes both regular and ad hoc reviews of risk management controls and procedures, and reports the results to the Board of Directors.

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES**Notes to the Consolidated Financial Statements**

iii) Credit risk

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Group's receivables from customers and investment securities.

i. Trade and other receivables

The Group's exposure to credit risk is influenced mainly by each customer's condition. However, management also considers the demographics of the customers, including the default risk of the industry and country in which customers operate, as these factors may have an influence on credit risk, particularly during deteriorating economic circumstances. The Group's Accounts Receivable and Notes Receivable are mainly due from customers in Asia and America, accounting 96% and 93% of the total amount of the receivables as of December 31, 2016, and 2015, respectively.

The Group has established a credit policy wherein each new customer is assessed for credit rating before standard payment, delivery terms, and conditions are granted. The analysis includes external ratings, when available, and in some cases, bank references. Purchase limits are established for each customer and reviewed regularly. Any amount below the limits requires no approval from the Board of Directors. Customers that fail to meet the Company's rating benchmark are allowed to transact with the Company only on a prepayment basis.

The Group has established an allowance for bad debt account to reflect the estimated losses on trade receivables, other receivables, and investments. The allowance for bad debt account consists of specific losses related to individually significant exposure and unrecognized losses arose from similar assets groups. The allowance for bad debt account is based on the historical collection record of similar financial assets.

ii. Investments

The credit risk exposure in the bank deposits, fixed income investments and other financial instruments are measured and monitored by the Group's finance department. Since the Group's transactions are with the counterparties, and the contractually obligated counterparties are the banks, financial institutions, corporate organizations and government agencies with good credits, there are no compliance issues, and therefore, there is no significant credit risk.

iii. Guarantees

The consolidated company policy provides endorsements and assurances to be offered only to companies who it has business relationship with, as well as to those companies who hold more than 50% of the voting rights of the consolidated company, either directly or indirectly. As of December 31, 2016 and 2015, the Group did not provide any endorsement and guarantees.

LANNER ELECTRONICS INC. AND SUBSIDIARIES**Notes to the Consolidated Financial Statements****iv) Liquidity risk**

Liquidity risk is the risk that the Group will encounter difficulty in meeting the obligations associated with its financial liabilities that are settled by delivering cash or another financial asset. The Group's approach to managing liquidity is to ensure, as far as possible, that it always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation. The Group aims to maintain the level of its cash and cash equivalents and other highly marketable debt investments at an amount in excess of the expected cash flows on financial liabilities (other than trade payables) over the succeeding 60 days. The Group also monitors the level of expected cash outflows on trade and other payables. This excludes the potential impact of extreme circumstances that cannot reasonably be predicted, such as natural disasters.

v) Market Risk

Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rate, and equity prices which will affect the group's income or the value of its holding of financial instrument. The objective of market risk management is to manage and control market risk exposure within acceptable parameters while optimizing the return.

In order to manage market risk, the Group conducts derivative transactions and incurs financial liabilities. All such transactions are within the guidelines set by the Risk Management Committee. Generally, the Group seeks to apply hedge accounting in order to manage volatility in profit or loss.

i. Currency risk

The group reports its financial statements in TWD, while conducting such transaction as sales, purchase, and borrowing in USD, thereby exposing itself to currency risk.

The Group hedges most of its trade receivables and trade payables denominated in a foreign currency. The Group hedges its currency risk through forward exchange contracts with maturity less than one year from the reporting date.

ii. Interest rate risk

To avoid interest rate risk, the Group raises its working capital mainly through long-term and short-term loans. Should long term loans be needed, plans and conditions of early repayment shall be settled in advance.

(v) Capital management

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

LANNER ELECTRONICS INC. AND SUBSIDIARIES
Notes to the Consolidated Financial Statements

The Group's debt-to-adjusted-capital ratio at the end of the reporting period was as follows:

	December 31, 2016	December 31, 2015
Total liabilities	\$ 2,090,403	1,984,080
Less: cash and cash equivalents	<u>761,323</u>	<u>412,427</u>
Net debt	<u>\$ 1,329,080</u>	<u>1,571,653</u>
Total equity	<u>\$ 2,729,578</u>	<u>2,303,499</u>
Debt-to-adjusted-capital ratio	<u>49 %</u>	<u>68 %</u>

The reduction of the debt to capital equity ratio as of December 31, 2016 was due to the increase in equity from additional profits and additional paid in capital.

With the approval from the Board of Directors, treasury stock repurchase can be applied to the respective authorities. Treasury stock repurchase is determined by the board of directors based on the specific transaction and shares distribution procedure. The Group does not foresee any shares buy-back plans in the near future. As of December 31, 2016, no changes have been made on the capital management.

(w) Investment and financing activities of non-cash transactions

From January 1 to December 31, 2016 and 2015, the Group has investment and financing activities of non-cash transactions as of following:

- i) Earnings convert to capital increase, refer to note 6(n).
- ii) Employee convert to capital increase, refer to note 6(n).
- iii) Conversion of convertible bonds to ordinary share, refer to note 6(n).

(7) Related-party Transactions

(a) Parent Company and ultimate controlling party

The Company is the ultimate controlling party of the Group.

(b) Significant related party transactions

i) Operating revenue

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

	2016	2015
Other related parties	\$ <u>17,694</u>	<u>795</u>

There were no significant differences between the pricing of sale transactions and receipts condition with related parties and that with other customers. Receivable between related parties have not receive collateral, and no need to provision for bad debt expense after evaluation.

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES
Notes to the Consolidated Financial Statements

ii) Purchases

The amount of purchase transactions between the Group and related parties were as follows:

	2016	2015
Other related parties	\$ <u>498</u>	<u>512</u>

There were no significant differences in purchase prices and payment terms between related parties and non-related suppliers.

iii) Payables to related parties

The payables due to related parties were as follows:

Accounts	Type of related parties	December 31, 2016	December 31, 2015
Accounts payable	Other related parties	\$ <u>-</u>	<u>6,480</u>

iv) Property transaction

In March 2015, the Group paid \$18,339 thousand (CNY\$3,700 thousand) to acquire 100% shares of Dongguan Lihua Haiwell Technology Co., Ltd. from the key management.

v) Leases

A lease contract with the period from June 2015 to May 2020 was signed with other related party on April 25, 2015. In accordance with the contract, the group provided \$175 thousand as deposit and booked the same amount under non-current asset. Rent for 2016 and 2015 amounted to \$1,322 thousand and \$1,272 thousand, respectively. There were no outstanding balance as of December 31, 2016 and 2015.

(c) Key management personnel compensations

Key management personnel compensation comprised:

	2016	2015
Short-term employee benefits	\$ 116,160	93,823
Post-employment benefits	<u>924</u>	<u>667</u>
	<u>\$ 117,084</u>	<u>94,490</u>

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES
Notes to the Consolidated Financial Statements

(8) Pledged Assets

The carrying values of pledged assets were as follows:

Pledged assets	Object	December 31, 2016	December 31, 2015
Certificate of deposits (recorded under other financial assets—current)	Guarantee for customs	\$ 2,302	2,275
Land	Guarantee for long and short-term debts	415,873	416,399
Building and structures	Guarantee for long and short-term debts	268,313	277,615
		<u><u>\$ 686,488</u></u>	<u><u>696,289</u></u>

(9) Significant Commitments and Contingencies

(a) The Group's unrecognized construction contract commitments are as follows:

	December 31, 2016	December 31, 2015
Acquisition of property, plant and equipment	<u><u>\$ 116,437</u></u>	<u><u>-</u></u>

(b) Operating lease commitments

Of the year ended December 31, 2016 and 2015, the Group had Signed uncancellable contracts in form of operating lease. The least amount of the rent to be paid in the future are listed as following:

	December 31, 2016	December 31, 2015
Under an year	\$ 38,180	16,391
Over 1 year but under 5 years	91,283	44,718
Over 5 years	<u>64,560</u>	<u>1,247</u>
	<u><u>\$ 194,023</u></u>	<u><u>62,356</u></u>

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(c) Contingencies

The Group assumed a contingent liability of \$10,963 thousand due to the compensation claim from its former employee. The high court ruled the amount of \$5,290 thousand paid by the Group plus an excluding 5% of annual interests counting back from October 14, 2007 to the date of discharged. The Group and the defendant have appealed to the Supreme Court and the Supreme Court then ruled the lawsuit back to the high court for reassessment in November 2015. The plaintiff appealed to the Supreme Court again but turn to the high court, the lawsuit is still pending on the high court. As of December 31, 2016 and 2015, the Group has estimated the cost of the lawsuit amounting to \$6,370 thousand, including the compensation and legal expenses, which is recognized as provision.

(10) Losses due to major disasters: None.

(11) Subsequent events: None.

(12) Others

The following is a summary statement of employee benefits, depreciation and amortization expensed by function:

By item	By function	2016			2015		
		Operating costs	Operating expenses	Total	Operating costs	Operating expenses	Total
Employee benefits							
Salary		179,121	691,534	870,655	185,775	636,118	821,893
Labor and health insurance		14,712	41,856	56,568	15,177	41,510	56,687
Pension		7,613	27,463	35,076	8,703	22,194	30,897
Others		10,692	30,128	40,820	11,291	27,433	38,724
Depreciation		43,333	56,799	100,132	34,970	40,024	74,994
Amortization		-	1,277	1,277	-	-	-

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(13) Other Disclosures

(a) Information on significant transactions

The following is the information on significant transactions required by the "Regulations Governing the Preparation of Financial Reports by Securities Issuers" for the Group:

- i) Loans extended to other parties: None.
- ii) Guarantees and endorsements for other parties: None.
- iii) Information regarding securities held at balance sheet date (Investment in subsidiaries, associates and joint ventures were excluded):

Unit: thousand dollars/thousand shares

Name of holder	Nature and name of security	Relationship with the security issuer	Account name	December 31, 2016				Maximum investment in 2016	Remarks
				Number of shares	Book value	Holding percentage	Market value		
The Company	Stock: Alliance III Venture Capital Corp.	—	Financial assets carried at cost—non current	50	500	1.00 %	500	1,000	-
The Company	Mutual fund: Capital Money Market	—	Financial assets at fair value though profit or loss—current	3,129	50,009	- %	50,009	90,000	

- iv) Accumulated holding amount of a single security in excess of \$300 million or 20% of the paid-in capital: None.
- v) Acquisition of real estate in excess of \$300 million or 20% of the paid-in capital: None.
- vi) Disposal of real estate in excess of \$300 million or 20% of the paid-in capital: None.
- vii) Sales to and purchases from related parties in excess of \$100 million or 20% of the paid-in capital:

Unit: thousand dollars

Name of Company	Counter-party	Relationship	Transaction details				The status and reason for deviation from arm's-length transaction		Account / note receivable (payable)		Remarks
			Purchase / Sale	Amount	Percentage of total purchases / sales	Credit period	Unit price	Credit period	Balance	Percentage of total accounts / notes receivable (payable)	
The Company	LANNER ELECTRONICS USA, INC	Subsidiary	Sales	(1,132,201)	(23)	%90 days	-	-	356,457	31 %	(Note 1)
The Company	Dongguan Lihua Haiwell Tech. Co., Ltd.	Subsidiary	Sales	(476,642)	(10)	%60 days	-		134,241	12 %	(Note 1)
The Company	LEI Technology Canada Ltd	Subsidiary	Sales	(310,010)	(6)	%180 days	-		118,547	10 %	(Note 1)
Dongguan Lihua Haiwell Tech Co., Ltd	Beijing L&S Lancom Platform Tech Co., Ltd (L&S)	Subsidiary	Sales	(922,483)	(89)	%60 days	-		-	- %	(Note 1)

Note 1 The transactions within the Group were eliminated in the consolidated financial statements

- viii) Receivables from related parties in excess of \$100 million or 20% of the paid-in capital:

Unit: thousand dollars

Name of related party	Counter-party	Relationship	Balance of receivables from related party	Turnover rate	Overdue amount		Amounts received in subsequent period	Allowances for bad debts
					Amount	Action taken		
The Company	LANNER ELECTRONICS USA, INC.	Subsidiary	356,457 (Note)	3.12 %	-		234,820 (Until March 2, 2017)	-
The Company	LEI TECHNOLOGY CANADA INC.	Subsidiary	118,547 (Note)	2.96 %	-		43,307 (Until March 2, 2017)	-
The Company	Dongguan Lihua Haiwell Tech. Co., Ltd.	Subsidiary	134,241 (Note)	3.55 %	-		133,718 (Until March 2, 2017)	-

Note: The transactions within the Group were eliminated in the consolidated financial statements.

- ix) Financial derivative instruments transactions: Please refer to Note 6(b).

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES
Notes to the Consolidated Financial Statements

x) Business relationships and significant intercompany transactions:

Unit: thousand dollars

No.	Name of company	Name of counter-party	Existing relationship with the counter-party	Transaction details			
				Account name	Amount	Trading terms	Percentage of the total consolidated revenue or total assets
0	The Company	LANNER ELECTRONICS USA, INC.	1	Sales	1,132,201	No significant differences	18.50%
0	The Company	Beijing L & S Lancom Platform of Technology CO., Ltd.	1	Sales	51,717	No significant differences	0.85 %
0	The Company	LEI Technology Canada Ltd.	1	Sales	310,010	120 days	5.07 %
0	The Company	Dongguan Lihua Haiwell Technology Co., Ltd.	1	Sales	476,642	No significant differences	7.79 %
0	The Company	LANNER ELECTRONICS USA, INC.	1	Accounts receivable	356,457	No significant differences	7.40 %
0	The Company	LEI Technology Canada Ltd.	1	Accounts receivable	118,547	120 days	2.46 %
0	The Company	Dongguan Lihua Haiwell Technology Co., Ltd.	1	Accounts receivable	134,241	No significant differences	2.79 %
1	Dongguan Lihua Haiwell Technology Co., Ltd.	Beijing L & S Lancom Platform of Technology CO., Ltd.	3	Sales	922,483	No significant differences	15.07%
1	Dongguan Lihua Haiwell Technology Co., Ltd.	Beijing L & S Lancom Platform of Technology CO., Ltd.	3	Advance sales receipts	25,307	No significant differences	0.53 %
1	Dongguan Lihua Haiwell Technology Co., Ltd.	Beijing HDZX Technology CO., Ltd.	3	Sales	96,453	No significant differences	1.58 %
1	Dongguan Lihua Haiwell Technology Co., Ltd.	Beijing HDZX Technology CO., Ltd.	3	Accounts receivable	33,531	No significant differences	0.70 %
2	Beijing L & S Lancom Platform of Technology CO., Ltd.	Beijing HDZX Technology CO., Ltd.	3	Sales	92,580	No significant differences	1.51 %

Note 1: Company numbering is as follows:

- (1) Parent company is 0.
- (2) Subsidiary starts from 1.

Note 2: The number of the relationship with the transaction counterparty represents the following:

- (1) "1" represents downstream transactions.
- (2) "2" represents upstream transactions.
- (3) "3" represents sidestream transactions.

(b) Information on investees:

The following is the information on investees for the years period ended December 31, 2016:

Name of investor	investor investee	Address	Scope of business	Original cost		Ending balance			Maximum investment in 2016	Net income of investee	Investment income (losses)	Remarks
				December 31, 2016	December 31, 2015	Shares	Ratio of shares	Book value				
The Company	LANNER ELECTRONICS USA, INC. CO., LTD	USA	Trading of computer peripheral equipment	80,633	80,633	2,350	100 %	52,864	80,633	3,648	3,648	(Note 1)
The Company	Lanner Electronics (Mauritius) Inc	Mauritius	Investing	84,990	84,990	2,653	100 %	545,649	84,990	99,135	99,135	(Note 1)
The Company	LEI Technology Canada Ltd	Canada	Trading of computer peripheral equipment	56,936	56,936	2,000	100 %	15,349	56,936	13,679	13,679	(Note 1)
Lanner Electronics (Mauritius) Inc	Lancom Holding Co., Ltd	Samoa	Investing	78,251	78,251	2,623	100 %	597,034	78,251	99,193	99,193	(Note 1)

Note 1. Aforementioned amounts have been eliminated upon consolidation

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(c) Information on investment in Mainland China:

i) Information on investment in Mainland China:

Name of investee in Mainland China	Scope of business	Issued capital	Method of investment (Note 1)	Cumulative investment (amount) from Taiwan at of January 1, 2016	Investment flow during current period		Cumulative investment (amount) from Taiwan at of December 31, 2016	Net income on investee	Direct / indirect investment holding percentage	Maximum investment in 2016	Investment income (loss) (Note 2)	Book value (Note 2)	Accumulated remittance of earnings in current period
					Remittance amount	Repatriation amount							
Beijing L&S Lancom Platform Tech. Co., Ltd. (L&S)	Trading of computer peripheral equipment	105,283	(3)	75,982	-	-	75,982	109,074	90.91 %	75,982	99,159	595,775	-
Beijing LSZC Investment Co., Ltd. (LSZC)	Investing	64,737	(4)a	-	-	-	-	10,070	90.91 %	64,737	9,155	81,686	-
Dongguan Libao Huwell Tech. Co., Ltd.	Manufacture and trading of computer peripheral products	48,777	(4)a	-	-	-	-	(3,093)	90.91 %	48,777	(2,812)	43,427	-
Beijing HDZX Technology Co., Ltd.	Trading of computer peripheral equipment	63,841	(4)b	-	-	-	-	32,509	39.08 %	15,550	12,705	34,472	-

Note 1 The method of investment is divided into the following four categories.

- (1) Remittance from third-region companies to invest in Mainland China
- (2) Through the establishment of third-region companies then investing in Mainland China.
- (3) Through transferring the investment to third-region existing companies then investing in Mainland China
- (4) Other methods
 - a. Investing in Mainland China through Beijing L & S Lancom Platform of Technology CO., Ltd
 - b. Investing in Mainland China through Beijing LSZC Investment Co., Ltd

Note 2 The investment income (losses) were recognized under the equity method and based on the financial statements audited by the auditor of the Company.

Note 3: Aforementioned amounts have been eliminated upon consolidation

ii) Limitation on investment in Mainland China:

Company name	Accumulated investment amount remitted from Taiwan to Mainland China at the end of the period	Investment (amount) approved by Investment Commission, Ministry of Economic Affairs	Maximum investment amount set by Investment Commission, Ministry of Economic Affairs
The Company	75,982	161,928	- (Note 1)

Note 1: The Company was certified as an operations center by the Industrial Development Bureau, Ministry of Economic Affairs, in approval letter No. 10420418550, and the certification is valid from 2015 to 2018. The Company has no limitation on investment in Mainland China during the abovementioned period.

iii) Significant transactions with investees in Mainland China:

Please refer to "Information on significant transactions" and "Business relationships and significant intercompany transaction" for the indirect and direct business transactions in China. All transactions were eliminated upon consolidation.

(Continued)

LANNER ELECTRONICS INC. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

(14) Segment information

(a) General information

The Group is mainly engaged in the manufacturing and selling of internet and communication equipments. Management reviews the Company's overall performance regularly to evaluate the performance of each segment and allocate its resources accordingly. As the production procedure is highly similar, the Group is identified as a sole operating segment.

(b) Geographic information

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

Geographic information	2016	2015
Revenue from external customers:		
United States	\$ 2,253,928	1,872,362
China	1,522,047	1,465,639
Israel	1,041,486	839,380
Canada	408,733	345,821
Korea	264,400	258,494
Other countries	629,454	657,803
Total	<u>\$ 6,120,048</u>	<u>5,439,499</u>

Geographical information	December 31, 2016	December 31, 2015
Non-current assets:		
Taiwan	\$ 1,001,510	1,040,878
United States	82,399	81,682
China	90,082	50,074
Canada	3,356	3,358
Total	<u>\$ 1,177,347</u>	<u>1,175,992</u>

Non-current assets include property, plant and equipment, intangible assets, and other assets. They do not include financial instruments and deferred income tax assets.

(c) Information about major customers

	2016	2015
Customer A	<u>\$ 1,513,290</u>	<u>1,268,615</u>