

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

**LANNER ELECTRONICS INC.
AND ITS SUBSIDIARIES**

Consolidated Financial Statements

**December 31, 2017 and 2016
(With Independent Auditors' Report Thereon)**

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The independent 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 independent auditors' report and consolidated financial statements, the Chinese version shall prevail.

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Representation Letter

The entities that are required to be included in the combined financial statements of LANNER ELECTRONICS INC. as of and for the year ended December 31, 2017, 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 endorsed by the Financial Supervisory Commission, "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. do not prepare a separate set of combined financial statements.

Company name: LANNER ELECTRONICS INC.

Chairman: Chou I Wen

Date: March 21, 2018



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Independent Auditors' Report

To the Board of Directors of LANNER ELECTRONICS INC.:

Opinion

We have audited the consolidated financial statements of LANNER ELECTRONICS INC. and its subsidiaries ("Group"), which comprise the consolidated statement of financial position as of December 31, 2017 and 2016, 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, 2017 and 2016, 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 Group as of December 31, 2017 and 2016, and its consolidated financial performance and its consolidated cash flows for the years ended December 31, 2017 and 2016 in accordance with the Regulations Governing the Preparation of Financial Reports by Securities Issuers and with the International Financial Reporting Standards ("IFRSs"), International Accounting Standards ("IASs"), Interpretations developed by the International Financial Reporting Interpretations Committee ("IFRIC") or the former Standing Interpretations Committee ("SIC") endorsed and issued into effect 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 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. Based on our audits and report of another auditor, 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. of the Group. Those statements were audited by another auditor, 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 another auditor. The financial statements of LANNER ELECTRONICS USA INC. reflect total assets constituting 12% and 11% of consolidated total assets at December 31, 2017 and 2016, respectively, and total revenues constituting 28% and 23% of consolidated total revenues for the years ended December 31, 2017 and 2016, respectively.

LANNER ELECTRONICS INC. has prepared its parent company only financial statements as of and for the years ended December 31, 2017 and 2016, on which we have issued an unmodified opinion 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 of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. We have determined the matters described below to be the key audit matters to be communicated in our report.

1. Revenue recognition

Please refer to notes 4(m) and 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 amount of revenue recognized has significant impact on the financial statements. Therefore, we consider it as a key audit matter.

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

Description of key audit matter:

The trade receivable is constituting of 23% of consolidated total assets of the Group as of December 31, 2017, therefore, management is required to establish 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, selecting confirmation samples and examining relevant documents to verify the accuracy aging period; inspecting the reasonableness of the overdue receivables and whether the Group has taken the appropriate procedures on the litigation or negotiation of the Group 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 notes 4(h), 5, and 6(d) for disclosures related to inventory measurement.

Description of key audit matter:

The electronic industry faces rapidly evolving technology. Therefore, the characteristic of fierce competition results in large fluctuations in demand and prices. In addition, the increasing performance of product with in-time basis which may result in a declination on the price of raw material, 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 performed is to understand management's accounting policy of inventory measurement and determine whether if it is reasonable and is being implement. The procedures includes reviewing the inventory aging documents and analyzing its changes; obtaining the documents of inventory measurement and evaluating whether if the bases 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, IFRC, SIC endorsed and issued into effect 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 Group or to cease operations, or has no realistic alternative but to do so.

Those charged with governance (including the supervisors) are responsible for overseeing 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 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 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 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 Po-Shu Huang and Yung-Sheng Wang.

KPMG

Taipei, Taiwan (Republic of China)

March 21, 2018

Notes to Readers

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

The independent 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 independent 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 ITS SUBSIDIARIES

Consolidated Statements of Comprehensive Income

For the years ended December 31, 2017 and 2016

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

		2017		2016	
		Amount	%	Amount	%
4000	Operating revenue (notes 6(q) and 7)	\$ 6,434,499	100	6,120,048	100
5000	Operating cost (notes 6(d), 6(g), 6(k), 6(l), 6(o), 6(r) and 7)	<u>4,634,471</u>	<u>72</u>	<u>4,397,865</u>	<u>72</u>
	Gross profit, net	<u>1,800,028</u>	<u>28</u>	<u>1,722,183</u>	<u>28</u>
	Operating expenses (notes 6(c), 6(g), 6(h), 6(l), 6(o), 6(r) and 7):				
6100	Selling expenses	532,721	8	539,001	9
6200	Administrative expenses	291,909	5	317,129	5
6300	Research and development expenses	<u>477,443</u>	<u>7</u>	<u>442,200</u>	<u>7</u>
	Total operating expenses	<u>1,302,073</u>	<u>20</u>	<u>1,298,330</u>	<u>21</u>
	Operating profit	<u>497,955</u>	<u>8</u>	<u>423,853</u>	<u>7</u>
	Non-operating income and expenses (notes 6(j) and 6(s)):				
7010	Other income	38,835	1	87,971	1
7020	Other gains and losses	(41,181)	(1)	(9,971)	-
7050	Financial costs	<u>(3,657)</u>	<u>-</u>	<u>(6,956)</u>	<u>-</u>
	Total non-operating income and expenses	<u>(6,003)</u>	<u>-</u>	<u>71,044</u>	<u>1</u>
	Net income before tax	491,952	8	494,897	8
7951	Less: income tax expense (note 6(m))	<u>98,025</u>	<u>2</u>	<u>84,750</u>	<u>1</u>
	Net income	<u>393,927</u>	<u>6</u>	<u>410,147</u>	<u>7</u>
8300	Other comprehensive income (loss) (note 6(n)):				
8310	Components of other comprehensive income that will not be reclassified to profit or loss				
8311	Gains (losses) on remeasurements of defined benefit plans	850	-	(4,307)	-
8349	Income tax related to components of other comprehensive income that will not be reclassified to profit or loss	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
	Components of other comprehensive income that will not be reclassified to profit or loss	<u>850</u>	<u>-</u>	<u>(4,307)</u>	<u>-</u>
8360	Items that may be reclassified subsequently to profit or loss				
8361	Exchange differences on translation of foreign financial statements	(18,553)	-	(55,342)	(1)
8399	Income tax related to components of other comprehensive income that will be reclassified to profit or loss	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
	Total Items that may be reclassified subsequently to profit or loss	<u>(18,553)</u>	<u>-</u>	<u>(55,342)</u>	<u>(1)</u>
8300	Other comprehensive income (loss), net	<u>(17,703)</u>	<u>-</u>	<u>(59,649)</u>	<u>(1)</u>
	Total comprehensive income	<u>\$ 376,224</u>	<u>6</u>	<u>350,498</u>	<u>6</u>
	Net income attributable to:				
8610	Shareholders of the parent company	\$ 348,628	5	380,927	7
8620	Non-controlling interests	<u>45,299</u>	<u>1</u>	<u>29,220</u>	<u>-</u>
		<u>\$ 393,927</u>	<u>6</u>	<u>410,147</u>	<u>7</u>
	Total comprehensive income attributable to:				
8710	Shareholders of the parent company	\$ 332,446	5	329,142	6
8720	Non-controlling interests	<u>43,778</u>	<u>1</u>	<u>21,356</u>	<u>-</u>
		<u>\$ 376,224</u>	<u>6</u>	<u>350,498</u>	<u>6</u>
9750	Basic earnings per share (in New Taiwan dollars) (note 6(p))	<u>\$ 3.33</u>		<u>3.83</u>	
9850	Diluted earnings per share (in New Taiwan dollars) (note 6(p))	<u>\$ 3.26</u>		<u>3.60</u>	

See accompanying notes to consolidated financial statements.

(English Translation of Consolidated Financial Statements and Report Originally Issued in Chinese)
LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES

Consolidated Statements of Changes in Equity

For the years ended December 31, 2017 and 2016
(Expressed in Thousands of New Taiwan Dollars)

	Equity attributable to owners of parent						Financial statements translation differences for foreign operations	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				
Balance at January 1, 2016	\$ 975,008	462,135	163,059	2,225	628,724	794,008	19,995	2,251,146	52,353	2,303,499
Appropriation and distribution:										
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 at 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
Appropriation and distribution:										
Legal reserve	-	-	38,092	-	(38,092)	-	-	-	-	-
Special reserve	-	-	-	27,483	(27,483)	-	-	-	-	-
Cash dividends	-	-	-	-	(313,950)	(313,950)	-	(313,950)	-	(313,950)
Net income	-	-	-	-	348,628	348,628	-	348,628	45,299	393,927
Other comprehensive income (loss)	-	-	-	-	850	850	(17,032)	(16,182)	(1,521)	(17,703)
Total comprehensive income (loss)	-	-	-	-	349,478	349,478	(17,032)	332,446	43,778	376,224
Changes in ownership interests in subsidiaries	-	846	-	-	-	-	-	846	98,538	99,384
Remuneration cost of employee stock options	-	7,187	-	-	-	-	-	7,187	-	7,187
Stock options exercised by employees	10,048	8,441	-	-	-	-	-	-	-	18,489
Balance at December 31, 2017	\$ 1,046,494	656,348	232,991	29,708	748,447	1,011,146	(44,515)	2,669,473	247,439	2,916,912

See accompanying notes to consolidated financial statements.

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

LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES**Consolidated Statements of Cash Flows****For the years ended December 31, 2017 and 2016****(Expressed in Thousands of New Taiwan Dollars)**

	2017	2016
Cash flows from operating activities:		
Consolidated net income before tax	\$ 491,952	494,897
Adjustments:		
Adjustments to reconcile profit and loss:		
Depreciation expense	101,613	100,132
Amortization expense	1,502	1,277
Provision for bad debt	7,354	5,566
Net gain on financial assets or liabilities at fair value through profit or loss	(619)	(23)
Interest expense	3,657	6,956
Interest income	(4,936)	(4,648)
Remuneration cost of employee stock options	7,187	9,296
Loss on disposal of property, plant and equipment, net	898	1,197
Total adjustments to reconcile profit and loss	<u>116,656</u>	<u>119,753</u>
Changes in operating assets and liabilities:		
Changes in operating assets:		
Financial assets at fair value through profit or loss	(54,156)	(50,009)
Notes receivable	3,722	6,045
Accounts receivable (including related parties)	(2,484)	58,980
Other receivable	47,587	(67,106)
Inventories	(368,976)	302,094
Prepayments	(3,647)	13,362
Other current assets	(444)	(10,864)
Other financial assets	82,606	34,302
Total changes in operating assets, net	<u>(295,792)</u>	<u>286,804</u>
Changes in operating liabilities:		
Financial liabilities at fair value through profit or loss	(1,009)	1,009
Notes payable	(7,060)	7,060
Accounts payable (including related parties)	153,747	(176,491)
Other payables	(72,628)	88,046
Provisions	7,015	8,724
Other current liabilities	51,488	(1,824)
Net defined benefit liability	(453)	1,021
Deferred revenue	670	1,956
Total changes in operating liabilities, net	<u>131,770</u>	<u>(70,499)</u>
Total changes in operating assets and liabilities, net	<u>(164,022)</u>	<u>216,305</u>
Total adjustments	<u>(47,366)</u>	<u>336,058</u>
Cash provided by operating activities	444,586	830,955
Interest income received	4,967	4,653
Interest paid	(3,629)	(3,035)
Income taxes paid	<u>(95,132)</u>	<u>(88,703)</u>
Net cash provided by operating activities	<u>350,792</u>	<u>743,870</u>
Cash flows from investing activities:		
Proceeds from capital reduction of financial assets at cost	-	500
Net cash flow from acquisition of subsidiaries	-	8,781
Acquisition of property, plant and equipment	(74,337)	(52,163)
Proceeds from disposal of property, plant and equipment	1,012	6,257
Decrease (increase) in other financial assets	(9,067)	(73,089)
Increase in other non-current assets	(6,713)	(3,768)
Decrease (increase) in prepayments for equipment	2,902	(52,463)
Net cash used in investing activities	<u>(86,203)</u>	<u>(165,945)</u>
Cash flows from financing activities:		
Increase in short-term loans	113,514	104,618
Decrease in short-term loans	(42,220)	(90,000)
Repayments of bonds	-	(24,300)
Repayments of long-term debt	(18,874)	(1,940)
Increase (decrease) in other non-current liabilities	915	(350)
Cash dividends paid	(313,950)	(195,010)
Exercise of employee share options	18,489	15,967
Change in non-controlling interests	20,087	-
Net cash used in financing activities	<u>(222,039)</u>	<u>(191,015)</u>
Effects of changes in exchange rates	<u>(15,717)</u>	<u>(38,014)</u>
Net increase in cash and cash equivalents	26,833	348,896
Cash and cash equivalents at beginning of period	761,323	412,427
Cash and cash equivalents at end of period	<u>\$ 788,156</u>	<u>761,323</u>

See accompanying notes to consolidated financial statements.

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

LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES

Notes to the Consolidated Financial Statements

For the years ended December 31, 2017 and 2016

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

(1) Company history

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 17.

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

The consolidated financial statements were approved by the Board of Directors and published on March 21, 2018.

(3) New standards, amendments and interpretations adopted:

- (a) The impact of the International Financial Reporting Standards ("IFRSs") endorsed by the Financial Supervisory Commission, R.O.C. ("FSC") which have already been adopted.

The following new standards, interpretations and amendments have been endorsed by the FSC and are effective for annual periods beginning on or after January 1, 2017:

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 "Presentation of Financial Statements-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 "Impairment of Non-Financial assets- Recoverable Amount Disclosures for Non Financial Assets"	January 1, 2014
Amendments to IAS 39 "Financial Instruments-Novation of Derivatives and Continuation of Hedge Accounting"	January 1, 2014
Annual Improvements to IFRSs 2010-2012 Cycle and 2011-2013 Cycle	July 1, 2014

(Continued)

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

<u>New, Revised or Amended Standards and Interpretations</u>	<u>Effective date per IASB</u>
Annual Improvements to IFRSs 2012-2014 Cycle	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.

(b) The impact of IFRS endorsed by FSC but not yet effective

The following new standards, interpretations and amendments have been endorsed by the FSC and are effective for annual periods beginning on or after January 1, 2018 in accordance with Ruling No. 1060025773 issued by the FSC on July 14, 2017.

<u>New, Revised or Amended Standards and Interpretations</u>	<u>Effective date per IASB</u>
Amendment to IFRS 2 "Clarifications of Classification and Measurement of Share-based Payment Transactions"	January 1, 2018
Amendments to IFRS 4 "Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts"	January 1, 2018
IFRS 9 "Financial Instruments"	January 1, 2018
IFRS 15 "Revenue from Contracts with Customers"	January 1, 2018
Amendment to IAS 7 "Statement of Cash Flows -Disclosure Initiative"	January 1, 2017
Amendment to IAS 12 "Income Taxes- Recognition of Deferred Tax Assets for Unrealized Losses"	January 1, 2017
Amendments to IAS 40 "Transfers of Investment Property"	January 1, 2018
Annual Improvements to IFRS Standards 2014–2016 Cycle:	
Amendments to IFRS 12	January 1, 2017
Amendments to IFRS 1 and Amendments to IAS 28	January 1, 2018
IFRIC 22 "Foreign Currency Transactions and Advance Consideration"	January 1, 2018

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LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES

Notes to the Consolidated Financial Statements

Except for the following items, the Group believes that the adoption of the above IFRSs would not have any material impact on its consolidated financial statements. The extent and impact of signification changes are as follows:

(i) IFRS 9 "Financial Instruments"

IFRS 9 replaces IAS 39 "Financial Instruments: Recognition and Measurement" which contains classification and measurement of financial instruments, impairment and hedge accounting.

1) Classification- Financial assets

IFRS 9 contains a new classification and measurement approach for financial assets that reflects the business model in which assets are managed and their cash flow characteristics. IFRS 9 contains three principal classification categories for financial assets: measured at amortized cost, fair value through other comprehensive income (FVOCI) and fair value through profit or loss (FVTPL). The standard eliminates the existing IAS 39 categories of held to maturity, loans and receivables and available for sale. Under IFRS 9, derivatives embedded in contracts where the host is a financial assets in the scope of the standard are never bifurcated. Instead, the hybrid financial instrument as a whole is assessed for classification.

Based on its assessment, the Group does not believe that the new classification requirements will have a material impact on its accounting for trade receivables, investments in debt securities and investments in equity securities that are managed on a fair value basis. At December 31, 2017, the Group had equity investments classified as financial assets measured at cost of 500 thousand that are held for long-term strategic purposes. At initial application of IFRS 9, the Group has designated these investments as measured at FVOCI. Consequently, all fair value gains and losses will be reported in other comprehensive income, no impairment losses would be recognized in profit or loss and no gains or losses will be reclassified to profit or loss on disposal. The Group estimated the application of IFRS 9's classification requirements on January 1, 2018 would not generate a material impact on non-controlling interest and retained earnings.

2) Impairment-Financial assets and contract assets

IFRS 9 replaces the 'incurred loss' model in IAS 39 with a forward-looking 'expected credit loss' (ECL) model. This will require considerable judgment as to how changes in economic factors affect ECLs, which will be determined on a probability-weighted basis.

The new impairment model will apply to financial assets measured at amortized cost or FVOCI, except for investments in equity instruments, and to contract assets.

Under IFRS 9, loss allowances will be measured on either of the following bases:

- 12-month ECLs. These are ECLs that result from possible default events within the 12 months after the reporting date; and
- Lifetime ECLs. These are ECLs that result from all possible default events over the expected life of a financial instrument.

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LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES

Notes to the Consolidated Financial Statements

Lifetime ECL measurement applies if the credit risk of a financial asset at the reporting date has increased significantly since initial recognition and 12-month ECL measurement applies if it has not. An entity may determine that a financial asset's credit risk has not increased significantly if the asset has low credit risk at the reporting date. However, lifetime ECL measurement always applies for trade receivables and contract assets without a significant financing component; an entity may choose to apply this policy also for trade receivables and contract assets with a significant financing component.

The Group believes that impairment losses are likely to increase and become more volatile for assets in the scope of the IFRS 9 impairment model. The Group estimated the application of IFRS 9's impairment requirements on January 1, 2018 would not generate a material impact on assets, liabilities and equity.

3) Disclosures

IFRS 9 will require extensive new disclosures, in particular about hedge accounting, credit risk and expected credit losses. The Group's assessment included an analysis to identify data gaps against current processes and the Group plans to implement the system and controls changes that it believes will be necessary to capture the required data.

4) Transition

Changes in accounting policies resulting from the adoption of IFRS 9 will generally be applied retrospectively, except as described below.

- The Group will take advantage of the exemption allowing it not to restate comparative information for prior periods with respect to classification and measurement (including impairment) changes. Differences in the carrying amounts of financial assets and financial liabilities resulting from the adoption of IFRS 9 generally will be recognized in retained earnings and reserves as at January 1, 2018.
- The new hedge accounting requirements should generally be applied prospectively. However, the Group has decided to apply the accounting for the forward element of forward contracts retrospectively.
- The following assessments have to be made on the basis of the facts and circumstances that exist at the date of initial application.
 - The determination of the business model within which a financial asset is held.
 - The designation and revocation of previous designations of certain financial assets and financial liabilities as measured at FVTPL.
 - The designation of certain investments in equity instruments not held for trading as at FVOCI.

(ii) IFRS 15 Revenue from Contracts with Customers

IFRS 15 establishes a comprehensive framework for determining whether, how much and when revenue is recognized. It replaces existing revenue recognition guidance, including IAS 18 "Revenue" and IAS 11 "Construction Contracts".

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LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES
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The Group has completed an initial assessment of the potential impact of the adoption of IFRS 15 on its consolidated financial statements.

1) Sales of goods

For the sale of products, revenue is currently recognized when the customer accepts the goods and the related risks and rewards of ownership transfer. Revenue is recognized at this point provided that the revenue and costs can be measured reliably, the recovery of the consideration is probable and there is no continuing management involvement with the goods. Under IFRS 15, revenue will be recognized when a customer obtains control of the goods.

2) Transition

The Group plans to adopt IFRS 15 using the cumulative effect method. Therefore, the comparative information will not be restated. The cumulative effect of initially applying IFRS 15 will be recognized as an adjustment to the opening balance of retained earnings at 1 January 2018. The Group plans to use the practical expedient in paragraph C5(a) of IFRS 15, under which, for contracts that are completed at the date of the initial application (i.e. 1 January 2018) will not be restated.

The Group preliminary assessment indicated that the application of IFRS 15 Revenue from Contracts with Customers would not have material on consolidated financial statements.

(iii) Amendments to IAS 7 "Disclosure Initiative"

The amendments require disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flow and non-cash changes.

To satisfy the new disclosure requirements, the Group intends to present a reconciliation between the opening and closing balances for liabilities with changes arising from financing activities.

The actual impacts of adopting the standards may change depending on the economic conditions and events which may occur in the future.

(c) The impact of IFRS issued by IASB but not yet endorsed by the FSC

As of the date the following IFRSs that have been issued by the IASB, but not yet endorsed by the FSC:

New, Revised or Amended Standards and Interpretations	Effective date per IASB
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 16 "Leases"	January 1, 2019

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LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES
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New, Revised or Amended Standards and Interpretations	Effective date per IASB
IFRS 17 "Insurance Contracts"	January 1, 2021
IFRIC 23 "Uncertainty over Income Tax Treatments"	January 1, 2019
Amendments to IFRS 9 "Prepayment features with negative compensation"	January 1, 2019
Amendments to IAS 28 "Long-term interests in associates and joint ventures"	January 1, 2019
Annual Improvements to IFRS Standards 2015–2017 Cycle	January 1, 2019
Amendments to IAS 19 "Plan Amendment, Curtailment or Settlement"	January 1, 2019

Those which may be relevant to the Group are set out below:

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.

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

Issuance / Release Dates	Standards or Interpretations	Content of amendment
June 7, 2017	IFRIC 23 "Uncertainty over Income Tax Treatments"	<ul style="list-style-type: none"> · In assessing whether and how an uncertain tax treatment affects the determination of taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates, an entity shall assume that a taxation authority will examine the amounts it has the right to examine and have a full knowledge on all related information when making those examinations. · If an entity concludes that it is probable that the taxation authority will accept an uncertain tax treatment, the entity shall determine the taxable profit (tax loss), tax bases, unused tax losses, unused tax credits or tax rates consistently with the tax treatment used or planned to be used in its income tax filings. Otherwise, an entity shall reflect the effect of uncertainty for each uncertain tax treatment by using either the most likely amount or the expected value, depending on which method the entity expects to better predict the resolution of the uncertainty.
February 7, 2018	Amendments to IAS 19 "Plan Amendment, Curtailment or Settlement"	<p>The amendments clarify that:</p> <ul style="list-style-type: none"> · on amendment, curtailment or settlement of a defined benefit plan, a company now uses updated actuarial assumptions to determine its current service cost and net interest for the remainder of the reporting period after the change to the plan; and · the effect of the asset ceiling is disregarded when calculating past service cost and the gain or loss on settlement. Any change in that effect is recognised in other comprehensive income.

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

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

(4) Summary of significant accounting policies

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

(a) Statement of compliance

These consolidated financial statements have been prepared in accordance with the Regulations Governing the Preparation of Financial Reports by Securities Issuers (hereinafter referred to as “the Regulations”) and the International Financial Reporting Standards, International Accounting Standards, IFRIC Interpretations, and SIC Interpretations endorsed by the Financial Supervisory Commission, R.O.C..

(b) Basis of preparation

(i) Basis of measurement

The consolidated financial statements have been prepared on a historical cost basis except for those otherwise explained in the accounting policies in the notes.

(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.

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

(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, 2017	December 31, 2016	
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	80.00 %	90.91 %	Note 1
LANCOM	Lanner Technology (Dongguan) Co., Ltd. (Lanner Technology)	Trading of computer peripheral products	100.00 %	-	% Note 2
L&S	Beijing LSZC Investment Co., Ltd. (LSZC)	Investing	100.00 %	100.00 %	
Beijing LSZC Investment Co., Ltd.	Dongguan Lihua Haiwell Tech. Co., Ltd. (Haiwell)	Manufacture and trading of computer peripheral products	100.00 %	100.00 %	
Beijing LSZC Investment Co., Ltd.	Beijing HDZX Technology Co., Ltd. (HDZX)	Trading of computer peripheral products	39.90 %	42.99 %	Note 3 and 4

Note 1: In June 2017, Beijing L&S Lancom Platform Tech. Co., Ltd. approved a resolution for a capital increase in cash amounting to CNY 3,000 thousand, wherein the Group did not proportionally acquire these new common shares, resulting in its shares decrease.

Note 2: In March 2017, the Board of Directors passed a resolution to acquire 100% ownership of Lanner Technology (Dongguan) Co., Ltd. The process was completed in with the acquisition price of USD250 thousand.

Note 3: In June 2017, Beijing HDZX Technology Co., Ltd. approved a resolution for a capital increase in cash amounting to CNY 1,438 thousand, wherein the Group did not proportionally acquire these new common shares, resulting in its shares decrease.

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.

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

(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.

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.

- 1) It expects to realize the asset, or intends to sell or consume it, in its normal operating cycle;
- 2) It holds the asset primarily for the purpose of trading;
- 3) It expects to realize the asset within twelve months after the reporting period; or
- 4) 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.

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LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES

Notes to the Consolidated Financial Statements

(ii) A liability is classified as current under one of the following criteria, and all other liabilities are classified as non current.

- 1) It expects to settle the liability in its normal operating cycle;
- 2) It holds the liability primarily for the purpose of trading;
- 3) 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
- 4) 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.

1) 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.

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LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES

Notes to the Consolidated Financial Statements

2) 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.

3) 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.

4) Impairment of financial assets

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

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.

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LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES

Notes to the Consolidated Financial Statements

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.

5) Derecognition of financial assets

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

(ii) Financial liabilities

1) 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.

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.

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

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.

2) 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.

3) 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.

4) 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.

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

5) 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.

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LANNER ELECTRONICS INC. AND ITS 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.

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LANNER ELECTRONICS INC. AND ITS 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) 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.

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.

(n) Employee benefits

(i) Defined contribution plans

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

(Continued)

LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES

Notes to the Consolidated Financial Statements

(ii) Defined benefit plans

A defined benefit plan is a post-employment benefit plan other than a defined contribution plan. The Group's net obligation in respect of defined benefit pension plans is calculated separately for each plan by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods; that benefit is discounted to determine its present value. 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.

(o) 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.

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LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES

Notes to the Consolidated Financial Statements

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.

(p) **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
- (ii) The taxing of deferred income tax assets and liabilities fulfill one of the below scenarios:
 - 1) levied by the same taxing authority; or
 - 2) levied by different taxing authorities, but where each such authority 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.

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LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES

Notes to the Consolidated Financial Statements

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.

(q) **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.

(r) **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.

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LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES

Notes to the Consolidated Financial Statements

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.

(s) 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 assumptions and judgments, and major sources of estimation 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 account receivable

Assessing impairment loss of account receivables takes company arrears record, receivable aging analysis and receiving to the customers in to consideration, and measured by the difference between the carrying amount of the assets and the present value of the recoverable amount. Please refer to note 6(c) for the recognition of impairment loss.

(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 6(d) for inventory measurement.

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

(6) Explanation of significant accounts

(a) Cash and cash equivalents

	December 31, 2017	December 31, 2016
Cash	\$ 9,244	1,275
Working capital	80	80
Cash in banks	360,208	419,498
Checking deposits	5,385	16,053
Time deposits	-	8,051
Foreign currency deposits	<u>413,239</u>	<u>316,366</u>
Cash and cash equivalents per consolidated statements of cash flow	<u><u>\$ 788,156</u></u>	<u><u>761,323</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, 2017	December 31, 2016
Financial assets held for trading:		
Non-derivative financial assets	\$ 104,534	50,009
Derivative instruments not used for hedging	250	-
Total	<u><u>\$ 104,784</u></u>	<u><u>50,009</u></u>
	December 31, 2017	December 31, 2016
Financial liabilities held for trading:		
Derivative instruments not used for hedging	-	1,009
Total	<u><u>\$ -</u></u>	<u><u>1,009</u></u>

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

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LANNER ELECTRONICS INC. AND ITS 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:

<u>Fluctuation in market price at reporting date</u>	<u>2017</u>		<u>2016</u>	
	<u>Other comprehensive income (after tax)</u>	<u>Net income</u>	<u>Other comprehensive income (after tax)</u>	<u>Net income</u>
Increase 1%	\$ -	-	-	<u>500</u>
Decrease 1%	\$ -	-	-	<u>(500)</u>

The Company had not provided any financial assets mentioned above as collateral as of December 31, 2017 and 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, 2017 and 2016, the Group reported the following derivative financial instruments as held-for-trading financial assets (liabilities) without the application of hedge accounting:

	<u>Fair value</u>	<u>Currency</u>	<u>Contract amount</u>
December 31, 2017			
Forward Contracts	\$ 250	USD/TWD	2,800
December 31, 2016			
Forward Contracts	\$ (1,009)	USD/TWD	1,550

As of December 31, 2017 and 2016, the maturity dates of the derivative financial assets and liabilities were between February 2, 2018 to March 5, 2018 and January 25, 2017 to March 6, 2017.

(c) Notes and accounts receivable and other receivables

	<u>December 31, 2017</u>	<u>December 31, 2016</u>
Notes receivable	\$ 2,739	6,461
Accounts receivable	1,118,150	1,116,096
Other receivables	97,214	69,031
Less: allowance for impairment	<u>17,685</u>	<u>10,753</u>
	<u>\$ 1,200,418</u>	<u>1,180,835</u>

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

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

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

	December 31, 2017	December 31, 2016
Past due 1~30 days	\$ 133,357	49,661
Past due 31~90 days	74,551	26,228
Past due over 90 days	14,334	7,708
	\$ 222,242	83,597

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 during the period were as follows:

	Individually assessed impairment	Collectively assessed impairment	Total
Balance at January 1, 2017	\$ 10,753	-	10,753
Impairment loss recognized	-	7,354	7,354
Written-off in current period	(424)	-	(424)
Effect of changes in exchange rates	(64)	66	2
Balance at December 31, 2017	\$ 10,265	7,420	17,685

	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	(123)	-	(123)
Balance at December 31, 2016	\$ 10,753	-	10,753

(d) Inventories

	December 31, 2017	December 31, 2016
Merchandise	\$ 1,092	1,360
Finished goods	846,761	689,966
Work in process	234,957	265,186
Raw material	671,690	429,012
Total	\$ 1,754,500	1,385,524

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LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES

Notes to the Consolidated Financial Statements

Inventories are measured at the lower of cost and net realizable value. Hence, the Group makes judgments and estimates in the net realizable value of inventory for financial statement. The rapid development on technology may significantly affect the market demand on electronic products, which can lead to product obsolescence, resulting in the cost of inventory to exceed its 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, 2017 and 2016, the Group's inventories had not pledged as collateral.

Aside from charging operating costs through the ordinary sale of inventories, other gains and losses directly recorded under operating costs for the years ended December 31, 2017 and 2016 were as follows:

	<u>2017</u>	<u>2016</u>
Loss on market value of inventory	\$ 15,045	35,370
Loss on physical count	14,966	37,443
Loss (gain) from scrapped inventory	<u>(25)</u>	<u>21</u>
Total	<u>\$ 29,986</u>	<u>72,834</u>

(e) Financial assets carried at cost—noncurrent

	<u>Stockholding rate %</u>	<u>Investment cost</u>	<u>Amount</u>
December 31, 2017			
Alliance III venture Capital Corp	1.00	\$ <u>500</u>	<u>500</u>
	<u>Stockholding rate %</u>	<u>Investment cost</u>	<u>Amount</u>
December 31, 2016			
Alliance III venture Capital Corp	1.00	\$ <u>500</u>	<u>500</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 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.

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LANNER ELECTRONICS INC. AND ITS 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 (CNY\$3,700 thousand) and \$15,550 thousand (CNY\$3,137 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:

- 1) The transfer consideration of \$18,339 thousand was paid in cash.
- 2) 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.

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LANNER ELECTRONICS INC. AND ITS 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:

- 1) The transfer consideration of \$15,550 thousand transferred was paid in cash.
- 2) 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 \$53,577 thousand. The amount is expected to be collectible on the acquisition date.

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LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES

Notes to the Consolidated Financial Statements

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.

3) 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.

4) 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:

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

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LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES
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(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, 2017	\$ 500,964	462,606	134,665	408,244	-	1,506,479
Additions	-	-	4,783	69,554	-	74,337
Disposals	-	-	(463)	(20,845)	-	(21,308)
Reclassification	-	(8,637)	-	7,784	-	(853)
Effect of changes in exchange rates	(2,293)	(3,580)	(683)	(1,609)	-	(8,165)
Balance at December 31, 2017	<u>\$ 498,671</u>	<u>450,389</u>	<u>138,302</u>	<u>463,128</u>	<u>-</u>	<u>1,550,490</u>
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>
Depreciation and impairment loss:						
Balance at January 1, 2017	\$ -	78,523	101,501	211,905	-	391,929
Depreciation	-	11,396	15,865	74,352	-	101,613
Disposal	-	-	(331)	(19,067)	-	(19,398)
Reclassification	-	(1,076)	-	164	-	(912)
Effect of changes in exchange rates	-	(535)	(376)	(818)	-	(1,729)
Balance at December 31, 2017	<u>\$ -</u>	<u>88,308</u>	<u>116,659</u>	<u>266,536</u>	<u>-</u>	<u>471,503</u>
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>
Carrying value:						
December 31, 2017	<u>\$ 498,671</u>	<u>362,081</u>	<u>21,643</u>	<u>196,592</u>	<u>-</u>	<u>1,078,987</u>
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>
January 1, 2016	<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>

Please refer to note 8 for the information of the pledged property, plant and equipment, as of December 31, 2017 and 2016.

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LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES
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(h) Intangible assets

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

	<u>Goodwill</u>	<u>Customer relation</u>	<u>Total</u>
Costs:			
Balance at January 1, 2017	\$ 4,654	4,598	9,252
Effect of changes in exchange rates	(53)	(53)	(106)
Balance at December 31, 2017	<u>\$ 4,601</u>	<u>4,545</u>	<u>9,146</u>
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 and impairment loss:			
Balance at January 1, 2017	\$ -	1,277	1,277
Amortization	-	1,502	1,502
Effect of changes in exchange rates	-	(2)	(2)
Balance at December 31, 2017	<u>\$ -</u>	<u>2,777</u>	<u>2,777</u>
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, 2017	<u>\$ 4,601</u>	<u>1,768</u>	<u>6,369</u>
December 31, 2016	<u>\$ 4,654</u>	<u>3,321</u>	<u>7,975</u>
January 1, 2016	<u>\$ -</u>	<u>-</u>	<u>-</u>

(i) Amortization

Goodwill and customer relations were obtained by acquiring subsidiaries in March 2016. For amortization expense, please refer to note 12.

(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, 2017 and 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.

- 1) The cash flow projections were estimated on the basis of previous experience, actual operating results, and the financial budget.

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LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES
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- 2) 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.
- 3) For the years 2017 and 2016, the discount rates for the present value of recoverable amounts were 9%.

(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, 2017				
	Currency	Interest rate	Maturity year	Amount
Secured loans	TWD	1.05	2018	\$ 50,000
Unsecured loans	TWD	1.08	2018	50,000
Unsecured loans	RMB	5.65	2018	13,635
Unsecured loans	USD	3.6183	2018	11,672
Total				<u>\$ 125,307</u>

December 31, 2016				
	Currency	Interest rate	Maturity year	Amount
Unsecured loans	RMB	5.22	2017	\$ 41,866
Unsecured loans	USD	3.0095	2017	13,793
Total				<u>\$ 55,659</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, 2017 and 2016, the unused credit facilities of the Group's short-term borrowings amounted to \$829,815 thousand and \$877,195 thousand, respectively.

(ii) Long-term borrowings

December 31, 2017				
	Currency	Interest rate	Maturity year	Amount
Secured loans	USD	3.4606	2020	\$ 20,071
Current				\$ 1,784
Non-current				18,287
Total				<u>\$ 20,071</u>

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LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES
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	December 31, 2016		
	Currency	Interest rate	Maturity year
Secured loans	USD	2.9889	2020
Current			\$ <u>41,705</u>
Non-current			\$ 1,932
Total			<u>39,773</u> \$ <u>41,705</u>

Please refer to note 6(u) 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
Total amount of convertible Bonds	\$ 400,000
Accumulated converted balance	(375,700)
Redemption	<u>(24,300)</u>
Bonds payable of ending balance	\$ -
Equity component—conversion options (Capital surpluses — Share options)	<u>\$ -</u>
	2016
Embedded Derivatives—put option and call option measured at fair value through profit or loss (reported in other gains and losses)	<u>\$ 23</u>
Interest expenses (financial costs)	<u>\$ 3,895</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

- 1) Bondholders are eligible to exercise the conversion right between one month after the bond issuance and ten days before the expiration date.

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LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES

Notes to the Consolidated Financial Statements

- 2) 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):

- 1) 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.

(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, 2017	\$ 34,984	6,370	41,354
Provisions made during the year	33,676	-	33,676
Provisions used during the year	(26,338)	-	(26,338)
Effect of changes in exchange rates	(323)	-	(323)
Balance at December 31, 2017	<u>\$ 41,999</u>	<u>6,370</u>	<u>48,369</u>

(Continued)

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

	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>

(i) Warranties

For the years ended December 31, 2017 and 2016, 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 \$3,884 thousand 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. 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, 2017 and 2016, the Group estimated the debt provision to be \$6,370 thousand due to the aforementioned lawsuit.

(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, 2017	December 31, 2016
The present value of the defined benefit obligations	\$ 56,167	56,401
Fair value of plan assets	(22,974)	(21,905)
The net defined benefit liability	<u>\$ 33,193</u>	<u>34,496</u>

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LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES

Notes to the Consolidated Financial Statements

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.

1) 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 \$22,974 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.

2) 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, 2017 and 2016, were as follows:

	<u>2017</u>	<u>2016</u>
Defined benefit obligation at 1 January	\$ 56,401	52,659
Current service costs and interest	976	1,469
Remeasurements of the net defined benefit liability (asset)		
— Return on plan assets (excluding amounts included in net interest expense)	637	(463)
— Due to changes in financial assumption of actuarial (losses) gains	(1,494)	4,516
Past service cost	-	1,190
Benefits paid by the plan	<u>(353)</u>	<u>(2,970)</u>
Defined benefit obligation at 31 December	\$ <u>56,167</u>	<u>56,401</u>

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

3) Movement of defined benefit plan assets

The movements in the fair value of the defined benefit plan assets for the years ended December 31, 2017 and 2016, were as follows:

	<u>2017</u>	<u>2016</u>
Fair value of plan assets, January 1	\$ 21,905	23,491
Remeasurements of the net defined benefit liability (asset)		
—Return on plan assets (excluding amounts included in net interest expense)	220	160
Contributions made	1,202	1,224
Benefits paid by the plan	(353)	(2,970)
Fair value of plan assets, December 31	<u>\$ 22,974</u>	<u>21,905</u>

4) Expenses recognized in profit or loss

The expenses recognized on profit or loss for the years ended December 31, 2017 and 2016, were as follows:

	<u>2017</u>	<u>2016</u>
Current service cost	\$ 368	520
Net interest on the defined benefit liability (asset)	381	535
Past service cost and gains (losses) due to settlement	-	1,190
	<u>\$ 749</u>	<u>2,245</u>

	<u>2017</u>	<u>2016</u>
Operating costs	\$ 447	469
Selling expenses	31	171
Administration expenses	-	1,328
Research and development expenses	271	277
	<u>\$ 749</u>	<u>2,245</u>

5) 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, 2017 and 2016, were as follows:

	<u>2017</u>	<u>2016</u>
Cumulative amount, January 1	\$ 13,988	9,681
Recognized during the period	(850)	4,307
Cumulative amount, December 31	<u>\$ 13,138</u>	<u>13,988</u>

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

6) Actuarial assumptions

The principal actuarial assumption used to determine the present value of the defined benefit obligation on December 31, 2017 and 2016 is as follows:

	<u>2017.12.31</u>	<u>2016.12.31</u>
Discount rate	1.375 %	1.125 %
Future salary increases rate	3.300 %	3.300 %

The Group expects to make contributions of \$1,216 thousand to the defined benefit plans in the next year starting from the reporting date of 2017.

The weighted average duration of the defined benefit obligation is 13.98 years.

7) 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.

As of December 31, 2017 and 2016, the present value of defined benefit obligation impact was as follow:

	The impact of defined benefit obligation	
	<u>Increase 0.25%</u>	<u>Decrease 0.25%</u>
December 31, 2017		
Discount rate	\$ (1,440)	1,494
Future salary increase rate	1,439	(1,393)
December 31, 2016		
Discount rate	(1,569)	1,621
Future salary increase rate	1,555	(1,515)

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.

The method and assumptions used on current sensitivity analysis is the same as those of the prior year.

(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.

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LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES

Notes to the Consolidated Financial Statements

The Group's pension costs under the defined contribution method were \$34,155 thousand and \$32,831 thousand for the years ended December 31, 2017 and 2016, 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, 2017	December 31, 2016
Annual leave benefit	\$ <u>25,610</u>	<u>20,782</u>

(m) Income tax

(i) Income tax expenses (benefit)

The amount of income tax for the years ended December 31, 2017 and 2016 were as follows:

	2017	2016
Current tax expense		
Current period	\$ 73,105	72,214
Adjustment for prior periods	<u>5,191</u>	<u>(2,368)</u>
	<u>78,296</u>	<u>69,846</u>
Deferred income tax expense		
Origination and reversal of temporary differences	<u>19,729</u>	<u>14,904</u>
Income tax expense from continuing operations	\$ <u>98,025</u>	<u>84,750</u>

Reconciliation of the Company's income tax expense (benefit) and the profit before tax for the years ended December 31, 2017 and 2016 were as follows:

	2017	2016
Net income before tax	\$ <u>491,952</u>	<u>494,897</u>
Income tax using the Company's domestic tax rate	\$ 83,632	84,132
Effect of tax rates in foreign jurisdiction	25,488	21,155
Previously underestimate (overestimate) income tax	5,191	(2,368)
Non-deductible expenses	2,391	(56)
Tax-free revenue	-	(3,635)
Unrecognized changes in temporary differences	(3,809)	(6,570)
10% surtax on unappropriated earnings	-	8,993
R&D tax credits utilized	(13,611)	(14,377)
Others	<u>(1,257)</u>	<u>(2,524)</u>
Total	\$ <u>98,025</u>	<u>84,750</u>

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LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES
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(ii) Deferred income tax assets and liabilities

1) Unrecognized deferred income tax assets

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

	December 31, 2017	December 31, 2016
Deductible temporary differences	\$ 2,097	4,143
Tax losses	11,721	6,500
	<u>\$ 13,818</u>	<u>10,643</u>

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, 2017, the deferred income tax assets of Tax losses which have not been recognized were as follows:

Canada

Year	Amount	Year of expiration
2012	\$ 8,129	2032
2013	2,576	2033
2014	1,016	2034
	<u>\$ 11,721</u>	

2) Recognized deferred income tax assets and liabilities

Changes in the amount of deferred income tax assets and liabilities for the years ended December 31, 2017 and 2016 were as follows:

Deferred income tax assets:

	Unrealized profit from sales	Tax differences from sales	Others	Total
Balance at January 1, 2017	\$ 23,598	12,988	24,208	60,794
Recognized in profit or loss	(6,336)	(2,251)	2,356	(6,231)
Balance at December 31, 2017	<u>\$ 17,262</u>	<u>10,737</u>	<u>26,564</u>	<u>54,563</u>
Balance at January 1, 2016	\$ 17,329	11,863	25,516	54,708
Recognized in profit or loss	6,269	1,125	(1,308)	6,086
Balance at December 31, 2016	<u>\$ 23,598</u>	<u>12,988</u>	<u>24,208</u>	<u>60,794</u>

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LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES
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Deferred income tax liabilities:

	Foreign investment income accounted for using equity method	Others	Total
Balance at January 1, 2017	\$ (89,373)	-	(89,373)
Recognized in profit or loss	(9,782)	(942)	(10,724)
Balance at December 31, 2017	<u>\$ (99,155)</u>	<u>(942)</u>	<u>(100,097)</u>
Balance at January 1, 2016	\$ (68,008)	-	(68,008)
Recognized in profit or loss	(21,365)	-	(21,365)
Balance at December 31, 2016	<u>\$ (89,373)</u>	<u>-</u>	<u>(89,373)</u>

(iii) Examination and Approval

The tax returns of the Company were examined and approved by the tax authorities through 2015.

(iv) Integrated income tax information

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

	December 31, 2017	December 31, 2016
Unappropriated earnings of 1997 and before	(Note)	\$ -
Unappropriated earnings of 1998 and after	(Note)	778,494
		<u>\$ 778,494</u>
	December 31, 2017	December 31, 2016
Balance of the imputation credit account	(Note)	<u>\$ 92,240</u>
	2017 (estimated)	2016 (distributed)
Creditable ratio for earnings distribution to R.O.C. residents	(Note)	<u>16.72 %</u>

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.

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LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES
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Note: According to the amendments to the "Income Tax Act" enacted by the office of the President of the Republic of China (Taiwan) on February 7, 2018, effective January 1, 2018, companies will no longer be required to establish, record, calculate, and distribute their ICA due to the abolishment of the imputation tax system.

(n) Capital and other equity

As of December 31, 2017 and 2016, the ordinary shares, with par value of \$10 per share, amounted to \$1,500,000 thousand; also, 104,649 thousand and 103,645 thousand common stocks, respectively, were issued from the shares mentioned above. All issued shares were paid up upon issuance.

A reconciliation of the Company's outstanding shares for the years ended December 31, 2017 and 2016 were as follows:

	Unit: thousands shares	
	2017	2016
Balance at January 1	103,645	97,501
Exercise of employee share options	1,004	832
Conversion of convertible bonds	-	5,312
Balance at December 31	<u>104,649</u>	<u>103,645</u>

(i) Issue of common stock

Due to the exercise of the employee stock options for the years ended December 31, 2017 and 2016, the Company issued 1,004 thousand and 832 thousand shares of stocks, respectively. Exercise prices were \$18.4 and \$19.2 per share for the years ended December 31, 2017 and 2016, respectively.

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

(ii) Capital surplus

The composition of the Company's capital surplus are as follows:

	December 31, 2017	December 31, 2016
Share premium from issuance	\$ 610,987	600,483
Changes in equity of associates and joint ventures accounted for using equity method	17,539	16,693
Employee share options	19,016	14,269
Employee share options expired	<u>8,806</u>	<u>8,429</u>
	<u>\$ 656,348</u>	<u>639,874</u>

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LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES
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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

1) 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.

2) 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.

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.

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LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES

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3) 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 Ruling No. 1010012865 issued by the FSC on April 6, 2012, a portion of current-period earnings and undistributed prior-period earnings shall be reclassified as special earnings reserve during earnings distribution. The amount to be reclassified should equal the current-period total net reduction of other shareholders' equity. Similarly, a portion of undistributed prior-period earnings shall be reclassified as special earnings reserve (which does not qualify for earnings distribution) to account for cumulative changes to other shareholders' equity pertaining to prior periods. The amounts of subsequent reversals pertaining to the net reduction of other shareholders' equity shall qualify for additional distributions. As of December 31, 2017 and 2016 the special earnings reserve amounted to \$29,708 thousand and \$2,225 thousands, respectively.

Earnings distribution for 2016 and 2015 was decided via the general meeting of shareholders held on June 15, 2017 and June 16, 2016, respectively. The relevant dividend distributions to shareholders were as follows:

	2016		2015	
	Amount per share (NT dollars)	Total Amount	Amount per share (NT dollars)	Total Amount
Dividends distributed to common stockholders:				
· Cash	\$ 3.0000	<u>313,950</u>	1.9713	<u>195,010</u>

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(iv) Other equities (net of tax)

	Foreign exchange differences arising from foreign operation	Non-controlling interests	Total
Balance at January 1, 2017	\$ (27,483)	(2,833)	(30,316)
Foreign exchange differences arising from net assets of foreign operation	(17,032)	(1,521)	(18,553)
Balance at December 31, 2017	<u>\$ (44,515)</u>	<u>(4,354)</u>	<u>(48,869)</u>
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>

(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 had been completed amortized from 2012 to 2015.

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LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES
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The outstanding stock option rights as follows:

Employee stock options in 2012	2017	
	Units	Exercise price (dollars)
Outstanding balance as of January 1	795	\$ 18.4
Options granted	-	-
Options exercised	725	18.4
Options cancelled	70	18.4
Options expired	-	-
Outstanding balance as of December 31	-	-
Exercisable as of December 31	-	-
Exercisable shares per unit as of December 31 — adjusted	-	-
Fair market value	\$ 3.7	

Employee stock options in 2012	2016	
	Units	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	795	18.4
Exercisable as of December 31	795	18.4
Exercisable shares per unit as of December 31 — adjusted	1,386	
Fair market value	\$ 3.7	

The expected duration of the employee stock option issued in 2012 was expired on June 7, 2017.

(Continued)

LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES
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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 \$7,187 thousand and \$9,296 thousand for the years ended December 31, 2017 and 2016. The additional paid-in capital also increased due to the stock option plan.

The outstanding stock option rights as follows:

	2017	
	Units	Exercise price (dollars)
Employee stock options in 2015		
Outstanding balance as of January 1	2,810	\$ 34.1
Options granted	-	-
Options exercised	-	-
Options cancelled	30	31.7
Options expired	-	-
Outstanding balance as of December 31	<u>2,780</u>	31.7
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>	

(Continued)

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

	2016	
	Units	Exercise price (dollars)
Employee stock options in 2015		
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>	

As of December 31, 2017, the expected duration of the employee stock option issued in 2015 was 2.71 years.

(p) Earnings per share

The calculation of the Group's basic earnings per share and diluted earnings per share for the years ended December 31, 2017 and 2016 were as follows:

(i) Basic earnings per share

	2017	2016
Net income attributable to ordinary shareholders of the Company	<u>\$ 348,628</u>	<u>380,927</u>
Weighted-average number of ordinary shares	<u>104,561</u>	<u>99,580</u>
Basic earnings per share (in NT dollars)	<u>\$ 3.33</u>	<u>3.83</u>

(ii) Diluted earnings per share

	2017	2016
Net income of the company	<u>\$ 348,628</u>	<u>380,927</u>
Effect of after tax interest expense of conversion bonds	-	3,233
Net income attributable to ordinary shareholders of the Company	<u>\$ 348,628</u>	<u>384,160</u>
Weighted-average number of ordinary shares (basic)	104,561	99,580
Impact of potential common shares		
Effect of employee stock bonus	1,421	1,825
Effect of employee stock option	797	1,136
Effect of conversion bonds	-	4,248
Weighted-average number of ordinary shares (diluted)	<u>106,779</u>	<u>106,789</u>
Diluted earnings per share (in NT dollars)	<u>\$ 3.26</u>	<u>3.60</u>

(Continued)

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

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, 2017 and 2016 were as follows:

	<u>2017</u>	<u>2016</u>
Sale of goods	\$ 6,354,394	6,062,703
Service income	<u>80,105</u>	<u>57,345</u>
	<u>6,434,499</u>	<u>6,120,048</u>

Unearned revenue, net for consolidated Company amounted to \$(4,557) thousand and \$5,172 thousand for the years ended December 31, 2017 and 2016, respectively. As of December 31, 2017 and 2016, accumulated unearned revenue amounted to \$54,362 thousand and \$58,978 thousand, respectively. Unearned revenue was booked due to identifiable services to be rendered.

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 transaction were recognized as other receivables and other payable amounting to \$67,293 thousand and \$71,605 thousand, respectively. There were no such conditions in 2017.

(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.

For the years ended December 31, 2017 and 2016, the Company recognized its employee remuneration of \$56,482 thousand and \$63,934 thousand, respectively, and directors' and supervisors' remuneration of \$5,648 thousand and \$6,393 thousand, respectively. These amounts are calculated by using the Company's pre-tax net profit for the period before deducting the amount of the remuneration to employees and directors under the Company's articles of association, and expensed under operating cost or expense. Related information would be available at the Market Observation Post System website.

The Company accrued its remuneration to employees, and directors and supervisors amounting to \$63,934 and \$6,393, respectively. However, the amounts approved by the board on March 2, 2017 were \$59,972 thousand and \$6,920 thousand, respectively. The differences between the actual amounts and the accrued amounts will be treated as the changes in accounting estimates and recognized as profit or loss in 2017.

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

(s) Non-operating income and expenses

(i) Other income

The details of the Group's other income for the years ended December 31, 2017 and 2016 were as follows:

	<u>2017</u>	<u>2016</u>
Rent income	\$ 3,556	793
Interest income	4,936	4,648
Other	<u>30,343</u>	<u>82,530</u>
	<u>\$ 38,835</u>	<u>87,971</u>

(ii) Other gains and losses

The details of the Group's other gains and losses for the years ended December 31, 2017 and 2016 were as follows:

	<u>2017</u>	<u>2016</u>
Gian (loss) on foreign exchange	\$ (39,974)	(7,087)
Loss on disposal of property, plant and equipment	(898)	(1,197)
Valuation gain (loss) on financial assets	619	(870)
Other gain (loss)	<u>(928)</u>	<u>(817)</u>
	<u>\$ (41,181)</u>	<u>(9,971)</u>

(iii) Finance costs

The details of the Group's finance costs for the years ended December 31, 2017 and 2016 were as follows:

	<u>2017</u>	<u>2016</u>
Interest expenses — convertible bonds	\$ -	3,895
Interest expenses — short-term loans	<u>3,657</u>	<u>3,061</u>
	<u>\$ 3,657</u>	<u>6,956</u>

(t) Financial instruments

(i) Credit risk

1) Exposure to credit risk

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

(Continued)

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

2) Concentration of credit risk

Approximately, 17% and 25% of the Group's total sales were derived from a single client for the years ended December 31, 2017 and 2016, respectively. Region wise, approximately 89% and 93% of the sales were significantly concentrated in Asia and America for the years ended December 31, 2017 and 2016, 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, 2017						
Non-derivative financial liabilities						
Short-term debts	\$ 125,307	126,311	126,311	-	-	-
Accounts payable	1,176,183	1,176,183	1,176,183	-	-	-
Other payables	139,573	139,573	139,573	-	-	-
Long-term debts (including due within a year)	20,071	21,809	1,939	1,939	17,931	-
Guarantee deposits received	1,028	1,028	-	-	-	1,028
	<u>\$ 1,462,162</u>	<u>1,464,904</u>	<u>1,444,006</u>	<u>1,939</u>	<u>17,931</u>	<u>1,028</u>
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	-	-	-
Notes payable	7,060	7,060	7,060	-	-	-
Accounts payable (including related parties)	1,022,436	1,022,436	1,022,436	-	-	-
Other payables	289,054	289,054	289,054	-	-	-
Long-term debts (including due within a year)	41,705	46,061	2,134	2,134	41,793	-
Guarantee deposits received	39	39	-	-	-	39
	<u>\$ 1,416,962</u>	<u>1,422,453</u>	<u>1,378,487</u>	<u>2,134</u>	<u>41,793</u>	<u>39</u>

(iii) Currency risk

1) Exposure to foreign currency risk

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

	Foreign currency	Exchange rate	NTD
December 31, 2017			
Financial assets:			
Monetary items:			
USD (note)	\$ 56,921	29.7350	1,692,556
Financial liabilities:			
Monetary items:			
USD (note)	\$ 37,726	29.7350	1,121,780

(Continued)

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

	<u>Foreign currency</u>	<u>Exchange rate</u>	<u>NTD</u>
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

Note: Amounts are designated before consolidation.

2) 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 receivables and trade and other payables that are denominated in foreign currency. A 1 dollar appreciation (depreciation) of the NTD against the USD as of December 31, 2017 and 2016 would have increased or decreased the net income by \$15,932 thousand and \$12,224 thousand, respectively. The analysis is performed on the same basis for both periods.

3) 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 years ended December 31, 2017 and 2016, foreign exchange loss (including realized and unrealized abortions) amounted to \$39,974 thousand and \$7,087 thousand, respectively.

(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 or decrease by \$1,207 thousand and \$808 thousand, respectively, for the years ended December 31, 2017 and 2016, with all other variable factors remain constant. This is mainly due to the Group's borrowing in variable rates.

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LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES

Notes to the Consolidated Financial Statements

(v) Information of fair value

1) Categories and fair value of financial instruments

Except for the following, 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, 2017					
	Carrying amount	Fair value			
		Level 1	Level 2	Level 3	Total
Financial assets at fair value through profit or loss					
Derivative financial assets	\$ 250	-	250	-	250
Non-derivative financial assets for trading	104,534	-	104,534	-	104,534
Total	\$ 104,784	-	104,784	-	104,784
December 31, 2016					
	Carrying amount	Fair value			
		Level 1	Level 2	Level 3	Total
Financial assets at fair value through profit or loss					
Non-derivative financial assets for trading	\$ 50,009	50,009	-	-	50,009
Derivative financial liabilities	\$ 1,009	-	1,009	-	1,009

2) 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. The financial instrument in China is evaluated based on the market value.

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

(u) Financial risk management

(i) Overview

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

- 1) Credit risk
- 2) Liquidity risk
- 3) 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.

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LANNER ELECTRONICS INC. AND ITS 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.

1) 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 89% and 96% of the total amount of the receivables as of December 31, 2017, and 2016, 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.

2) 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.

3) 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, 2017 and 2016, the Group did not provide any endorsement and guarantees.

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LANNER ELECTRONICS INC. AND ITS 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.

1) 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.

2) 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.

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LANNER ELECTRONICS INC. AND ITS 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, 2017	December 31, 2016
Total liabilities	\$ 2,264,168	2,090,403
Less: cash and cash equivalents	788,156	761,323
Net debt	<u>\$ 1,476,012</u>	<u>1,329,080</u>
Total equity	<u>\$ 2,916,912</u>	<u>2,729,578</u>
Debt-to-adjusted-capital ratio	<u>51 %</u>	<u>49 %</u>

The reduction of the debt to capital equity ratio as of December 31, 2017 was due to the increase in equity from additional profits and additional paid in capital.

As of December 31, 2017, no changes have been made on the capital management.

(7) Related-party transactions

(a) Parent Company and ultimate controlling party

The Company is the ultimate controlling party of the Group.

(b) Related-party and relationship between the Company

The Group has transactions with its related parties as follows:

<u>Related-parties</u>	<u>Relationship between the Company</u>
Beijing HDZX Technology Co., Ltd. (HDZX)	Since the acquisition date on March 1, 2016, the Group has obtained control over its related party, which therefrom, became its subsidiary
Jie Wei Investment Development Co., Ltd. (Jie Wei)	One of the board of directors of the Company also serves as a director of the related-party
Lanner Foundation	Related party
Mr. Zhang Jun Hai	Key management of Consolidated Company

(c) Significant related party transactions

(i) Operating revenue

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

	2017	2016
Other related parties	<u>\$ -</u>	<u>17,694</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.

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

(ii) Purchases

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

	<u>2017</u>	<u>2016</u>
Other related parties	\$ <u>-</u>	<u>498</u>

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

(iii) Property translation

In March 2016, 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.

(iv) 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 the years ended December 31, 2017 and 2016 were both amounted to \$1,322 thousand. There were no outstanding balance as of December 31, 2017 and 2016.

(v) Contribution

With the approval from the broad of directors, the Group agreed to contribute \$6,200 thousand to Lanner Foundation for the years ended December 31, 2017. The Group recognized the contribution under the other current assets.

(vi) Other

The key management personnel of the Group participated in the cash increase of Beijing Lihua Haiwell Technology Co., Ltd. with the amount of \$75,770 thousand, recognized under other accounts receivable, as of December 31, 2017.

(d) Key management personnel compensations

Key management personnel compensation comprised:

	<u>2017</u>	<u>2016</u>
Short-term employee benefits	\$ 93,945	116,160
Post-employment benefits	<u>810</u>	<u>924</u>
	<u>\$ 94,755</u>	<u>117,084</u>

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LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES
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(8) Pledged assets

The carrying values of pledged assets were as follows:

<u>Pledged assets</u>	<u>Object</u>	<u>December 31, 2017</u>	<u>December 31, 2016</u>
Certificate of deposits (recorded under other financial assets—current)	Guarantee for customs	\$ 2,327	2,302
Land	Guarantee for long and short- term debts	413,582	415,873
Building	Guarantee for long and short- term debts	257,676	268,313
		<u>\$ 673,585</u>	<u>686,488</u>

(9) Commitments and contingencies

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

	<u>December 31, 2017</u>	<u>December 31, 2016</u>
Acquisition of property, plant and equipment	<u>\$ 115,101</u>	<u>116,437</u>

(b) Operating lease commitments

As of December 31, 2017 and 2016, 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:

	<u>December 31, 2017</u>	<u>December 31, 2016</u>
Under a year	\$ 37,112	38,180
Over 1 year but under 5 years	78,655	91,283
Over 5 years	46,664	64,560
	<u>\$ 162,431</u>	<u>194,023</u>

(c) Contingencies

Please refer to note 6(k) for related legal information.

(10) Losses Due to Major Disasters: None.

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LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES

Notes to the Consolidated Financial Statements

(11) Subsequent Events

According to the amendments to the "Income Tax Act" enacted by the office of the President of the Republic of China (Taiwan) on February 7, 2018, an increase in the corporate income tax rate from 17% to 20% is applicable upon filing the corporate income tax return commencing FY 2018. This increase does not affect the amounts of the current or deferred income taxes recognized on December 31, 2017. However, it will increase the Group's current tax charge accordingly in the future. On the other hand, if the new tax rate is applied in calculating the taxable temporary differences and tax losses recognized on December 31, 2017, the deferred tax assets and deferred tax liabilities would increase by \$8,200 and \$17,498, respectively.

(12) Other

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

By item	By function	Years ended December 31, 2017			Years ended December 31, 2016		
		Operating costs	Operating expenses	Total	Operating costs	Operating expenses	Total
Employee benefits							
Salary		188,053	697,910	885,963	179,121	691,534	870,655
Labor and health insurance		15,414	48,040	63,454	14,712	41,856	56,568
Pension		7,502	27,402	34,904	7,613	27,463	35,076
Others		12,505	35,534	48,039	10,692	30,128	40,820
Depreciation		40,049	61,564	101,613	43,333	56,799	100,132
Amortization		-	1,502	1,502	-	1,277	1,277

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LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES
Notes to 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 to other parties: None.
- (ii) Guarantees and endorsements for other parties: None.
- (iii) Information regarding securities held at the reporting date (subsidiaries, associates and joint ventures not included):

Unit: thousand dollars/thousand shares

Name of holder	Nature and name of security	Relationship with the security issuer	Account name	December 31, 2017				Maximum investment in 2017	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	5,000	-
L&S	China Merchants Bank Financial Products	—	Financial assets at fair value through profit or loss—current	-	104,534	- %	104,534	104,534	

- (iv) Information regarding purchase or sale of securities for the period exceeding 300 million or 20% of the Company's paid-in capital: None.
- (v) Information on acquisition of real estate with purchase amount exceeding 300 million or 20% of the Company's paid-in capital: None.
- (vi) Information regarding receivables from disposal of real estate exceeding 300 million or 20% of the Company's paid-in capital: None.
- (vii) Information regarding related-parties purchases and/or sales exceeding 100 million or 20% of the Company's 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 (USA)	Subsidiary	Sales	(1,623,059)	(32)	%90 days	-	-	427,371	37 %	(Note 1)
The Company	Haiwell	Subsidiary	Sales	(562,859)	(11)	%60 days	-	-	148,420	13 %	(Note 1)
The Company	LEI	Subsidiary	Sales	(274,771)	(5)	%120 days	-	-	101,391	9 %	(Note 1)
The Company	LANNER (USA)	Subsidiary	Purchase	138,028	3	%90 days	-	-	-	- %	(Note 1)
Haiwell	L&S	Subsidiary	Sales	(1,086,895)	(84)	%60 days	-	-	-	- %	(Note 1)
Haiwell	HIDZX	Associated company	Sales	(201,637)	(15)	%60 days	-	-	55,119	99 %	(Note 1)

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

- (viii) Information regarding receivables from related-parties exceeding 100 million or 20% of the Company's 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 (USA)	Subsidiary	427,371 (Note)	4.14	-		357,622 (Until March 21, 2018)	-
The Company	LEI	Subsidiary	101,391 (Note)	2.50	-		69,826 (Until March 21, 2018)	-
The Company	Haiwell	Subsidiary	148,420 (Note)	3.98	-		146,781 (Until March 21, 2018)	-

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

- (ix) Information regarding trading in derivative financial instruments: Please refer to Notes 6(b).

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LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES

Notes to Consolidated Financial Statements

(x) Significant transactions and business relationship between the parent company and its subsidiaries in December 31, 2017:

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 (USA)	1	Sales	1,623,059	No significant differences	25.22%
0	The Company	LEI	1	Sales	274,771	120 days	4.27 %
0	The Company	Haiwell	1	Sales	562,859	No significant differences	8.75 %
0	The Company	LANNER (USA)	1	Accounts receivable	427,371	No significant differences	8.24 %
0	The Company	LEI	1	Accounts receivable	101,391	120 days	1.95 %
0	The Company	Haiwell	1	Accounts receivable	148,420	No significant differences	2.86 %
1	Haiwell	L&S	3	Sales	1,086,895	No significant differences	16.89%
1	Haiwell	L&S	3	Advance sales receipts	68,578	No significant differences	1.32 %
1	Haiwell	HDZX	3	Sales	201,633	No significant differences	3.13 %
1	Haiwell	HDZX	3	Accounts receivable	55,119	No significant differences	1.06 %
2	LANNER (USA)	The Company	2	Sales	138,028	No significant differences	2.15 %

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 are the information on investees for the years ended December 31, 2017 (excluding information on investees in Mainland China):

Unit: thousand dollars/thousand shares

Name of investor	Investor investee	Address	Scope of business	Original cost		Ending balance		Book value	Maximum investment in 2017	Net income of investee (Note 2)	Investment income (losses)	Remarks
				December 31, 2017	December 31, 2016	Shares	Ratio of shares					
The Company	LANNER (USA)	USA	Trading of computer peripheral equipment	140,935	80,633	2,500	100 %	103,640	140,935	15,358	15,358	(Note 1)
The Company	LANNER (MAURITIUS)	Mauritius	Investing	84,990	84,990	2,653	100 %	643,892	84,990	91,094	91,094	(Note 1)
The Company	LEI	Canada	Trading of computer peripheral equipment	56,936	56,936	2,000	100 %	28,239	56,936	6,651	6,651	(Note 1)
LANNER (MAURITIUS)	LANCOM	Samoa	Investing	78,251	78,251	2,623	100 %	679,757	78,251	91,166	91,166	(Note 1)

Note 1: Aforementioned amounts have been eliminated upon consolidation

(c) Information on investment in Mainland China:

(i) The names of investees in Mainland China, the scope of businesses and products, and other information:

Unit: thousand dollars

Name of investee in Mainland China	Scope of business	Issued capital	Method of investment (Note 1)	Cumulative investment (amount) from January 1, 2017	Investment flow during current period		Cumulative investment (amount) from January 1, 2017	Net income on investee	Direct / Indirect investment holding percentage	Maximum investment in 2017	Investment income (loss) (Note 2)	Book value (Note 2)	Accumulated remittance of earnings in current period
					Remittance amount	Repayment amount							
L&S	Trading of computer peripheral equipment	118,388	(3)	75,982	-	-	75,982	110,087	80.90 %	75,982	91,199	678,674	-
LSZC	Investing	64,737	(4)a	-	-	-	-	47,366	80.00 %	64,737	37,893	127,891	-
Haiwell	Manufacture and trading of computer peripheral products	48,777	(4)b	-	-	-	-	29,815	80.00 %	48,777	23,852	58,408	-
HDZX	Trading of computer peripheral equipment	70,358	(4)b	-	-	-	-	45,467	31.92 %	70,358	14,643	43,639	-
Lanner Technology	Trading of computer peripheral equipment	7,434	(1)	-	-	-	-	-	100.00 %	7,434	-	7,037	-

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 consolidated financial statements.

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LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES

Notes to the Consolidated Financial Statements

(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.

(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	2017	2016
Revenue from external customers:		
United States	\$ 2,662,472	2,253,928
China	1,643,253	1,522,047
Israel	700,640	1,041,486
Canada	423,604	408,733
Korea	2,524	264,400
Other countries	1,002,006	629,454
Total	<u>\$ 6,434,499</u>	<u>6,120,048</u>

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LANNER ELECTRONICS INC. AND ITS SUBSIDIARIES

Notes to the Consolidated Financial Statements

Geographical information	December 31, 2017	December 31, 2016
Non-current assets:		
Taiwan	\$ 981,280	1,001,510
United States	71,296	82,399
China	81,624	90,082
Canada	<u>3,076</u>	<u>3,356</u>
Total	<u><u>\$ 1,137,276</u></u>	<u><u>1,177,347</u></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

	2017	2016
Customer A	<u><u>\$ 1,100,706</u></u>	<u><u>1,513,290</u></u>