

**Phihong Technology Co., Ltd. and  
Subsidiaries**

**Consolidated Financial Statements for the  
Nine Months Ended September 30, 2012 and 2011 and  
Independent Accountants' Review Report**

## **INDEPENDENT ACCOUNTANTS' REVIEW REPORT**

The Board of Directors and Stockholders  
Phihong Technology Co., Ltd.

We have reviewed the accompanying consolidated balance sheets of Phihong Technology Co., Ltd. and subsidiaries (collectively, the "Company") as of September 30, 2012 and 2011, and the related consolidated statements of income, changes in stockholders' equity and cash flows for the nine months then ended (all expressed in thousands of New Taiwan dollars). These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to issue a report based on our reviews.

Except as discussed in the following paragraph, we conducted our reviews in accordance with Statement of Auditing Standards No. 36, "Review of Financial Statements," of the Republic of China. A review consists principally of applying analytical procedures to financial data and of making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the consolidated financial statements taken as a whole. Accordingly, we do not express an opinion on these consolidated financial statements.

As mentioned in Note 9 to the consolidated financial statements, long-term equity investments accounted for under the equity method for the nine months ended September 30, 2012 and 2011 were based on unreviewed financial statements. As of September 30, 2012 and 2011, the aggregate balances of the Company's investments in its investees whose financial statements have not been reviewed by independent accountants amounted to \$327,602 thousand and \$354,728 thousand, respectively. For the nine months ended September 30, 2012 and 2011, the Company's investment income from such investments amounted to \$2,003 thousand and \$16,659 thousand, respectively. Additionally, as mentioned in Note 1 to the consolidated financial statements, certain subsidiaries' assets amounted to \$103,490 thousand and \$115,730 thousand, which represented 1.08% and 1.09% of the consolidated total assets as of September 30, 2012 and 2011 were based on unreviewed financial statements of the subsidiary.

Based on our reviews, except for the effects of such adjustments, if any, as might have been determined to be necessary had the long-term equity investments and investment income (loss) of investees mentioned above been recognized based on reviewed financial statements, we are not aware of any material modifications that should be made to the accompanying consolidated financial statements for them to be in conformity with the Guidelines Governing the Preparation of Financial Reports by Securities Issuers, the interpretation No. 0960064020 issued by Financial Supervisory Commission, Executive Yuan on November 15, 2007, and accounting principles generally accepted in the Republic of China.

October 26, 2012

Notice to Readers

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

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

**PHIHONG TECHNOLOGY CO., LTD. AND SUBSIDIARIES**

**CONSOLIDATED BALANCE SHEETS**

**SEPTEMBER 30, 2012 AND 2011**

**(In Thousands of New Taiwan Dollars, Except Par Value)**

**(Reviewed, Not Audited)**

ASSETS	2012		2011		LIABILITIES AND STOCKHOLDERS' EQUITY	2012		2011	
	Amount	%	Amount	%		Amount	%	Amount	%
<b>CURRENT ASSETS</b>					<b>CURRENT LIABILITIES</b>				
Cash and cash equivalents (Note 4)	\$ 1,598,649	17	\$ 1,811,114	17	Accounts payable	\$ 2,013,839	21	\$ 1,999,642	19
Accounts receivable (Note 5)	1,868,592	20	2,123,611	20	Accounts payable to related parties (Note 19)	40,568	-	28,938	-
Other financial assets, current	30,497	-	44,958	-	Income tax payable (Note 16)	136,473	2	66,520	1
Inventories (Note 6)	1,624,495	17	2,157,311	20	Other payables (Note 11)	1,101,889	12	1,560,386	15
Deferred income tax asset, current (Note 16)	38,990	-	59,565	1	Other current liabilities	35,739	-	52,363	-
Other current assets	317,538	3	164,483	2					
Total current assets	5,478,761	57	6,361,042	60	Total current liabilities	3,328,508	35	3,707,849	35
<b>FUNDS AND LONG-TERM INVESTMENTS</b>					<b>LONG-TERM LIABILITIES</b>				
Available-for-sale financial assets, noncurrent (Note 7)	31,458	-	31,579	-	Long-term debts (Note 12)	200,000	2	200,000	2
Financial assets carried at cost, noncurrent (Note 8)	90,945	1	116,254	1	<b>OTHER LIABILITIES</b>				
Long-term equity investments at equity method (Note 9)	327,602	4	354,728	4	Accrued pension cost	65,064	1	64,216	1
Total funds and long-term investments	450,005	5	502,561	5	Advance deposits received	987	-	932	-
<b>PROPERTY, PLANT AND EQUIPMENT (Note 10)</b>					Deferred income tax liabilities, noncurrent (Note 16)	69,592	1	69,732	1
Cost	5,638,730	59	5,564,504	52	Others	50,485	-	49,052	-
Less accumulated depreciation	(2,373,526)	(25)	(2,128,941)	(20)	Total other liabilities	186,128	2	183,932	2
Prepayments for purchase of equipment	170,226	2	69,211	1	Total liabilities	3,714,636	39	4,091,781	39
Property, plant and equipment, net	3,435,430	36	3,504,774	33	<b>STOCKHOLDERS' EQUITY OF PARENT COMPANY</b>				
<b>INTANGIBLE ASSETS</b>					Capital stock, \$10 par value (Note 13)				
Computer software	32,596	1	17,789	-	Authorized - 600,000 thousand shares at September 30, 2012 and 2011				
Goodwill	-	-	1,398	-	Issued - 277,044 thousand shares and 274,933 thousand shares at September 30, 2012 and 2011	2,770,439	29	2,749,329	26
Land use rights	111,636	1	118,055	1	Capital surplus				
Total intangible assets	144,232	2	137,242	1	Additional paid-in capital - common stock	225,572	2	203,406	2
<b>OTHER ASSETS</b>					Additional paid-in capital - bond conversion	661,582	7	661,582	6
Deferred charges	-	-	2,657	-	Treasury stock transactions	48,234	1	48,234	1
Refundable deposits	29,357	-	29,701	-	From long-term equity investments	11,305	-	11,132	-
Others	134	-	46,542	1	Interest payable from bond conversion	13,243	-	13,243	-
Total other assets	29,491	-	78,900	1	Retained earnings (Note 15)				
<b>TOTAL</b>	<b>\$ 9,537,919</b>	<b>100</b>	<b>\$ 10,584,519</b>	<b>100</b>	Legal reserve	1,052,192	11	909,627	9
					Unappropriated earnings	927,278	10	1,641,119	15
					Other equity				
					Cumulative translation adjustments	124,027	1	250,163	2
					Unrealized loss on financial instruments	(17,772)	-	(21,783)	-
					Unrealized revaluation increment	10,968	-	10,968	-
					Total stockholders' equity of parent company	5,827,068	61	6,477,020	61
					Total stockholders' equity	5,827,068	61	6,477,020	61
					<b>MINORITY INTEREST</b>	(3,785)	-	15,718	-
					<b>TOTAL</b>	<b>\$ 9,537,919</b>	<b>100</b>	<b>\$ 10,584,519</b>	<b>100</b>

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

(With Deloitte & Touche review report dated October 26, 2012)

# PHIHONG TECHNOLOGY CO., LTD. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF INCOME

NINE MONTHS ENDED SEPTEMBER 30, 2012 AND 2011

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

(Reviewed, Not Audited)

	2012		2011	
	Amount	%	Amount	%
GROSS SALES AND REVENUES	\$ 8,880,780	100	\$ 11,063,804	100
LESS SALES RETURNS AND ALLOWANCES	<u>-</u>	<u>-</u>	<u>(41,201)</u>	<u>-</u>
NET SALES AND REVENUES	8,880,780	100	11,022,603	100
COST OF GOODS SOLD	<u>7,108,104</u>	<u>80</u>	<u>8,176,134</u>	<u>74</u>
GROSS PROFIT	<u>1,772,676</u>	<u>20</u>	<u>2,846,469</u>	<u>26</u>
OPERATING EXPENSES				
Sales and marketing	607,515	7	731,820	7
General and administration	406,272	5	437,425	4
Research and development	<u>377,646</u>	<u>4</u>	<u>470,525</u>	<u>4</u>
Total operating expenses	<u>1,391,433</u>	<u>16</u>	<u>1,639,770</u>	<u>15</u>
INCOME FROM OPERATIONS	<u>381,243</u>	<u>4</u>	<u>1,206,699</u>	<u>11</u>
NONOPERATING INCOME AND GAINS				
Interest income	12,638	-	10,197	-
Investment income recognized under equity method, net (Note 9)	2,003	-	16,659	-
Dividend income	4,927	-	4,776	-
Gain on disposal of investment (Note 7)	-	-	213,370	2
Foreign exchange gain, net	-	-	76,619	1
Gain on reversal of bad debts	20,519	1	-	-
Others	<u>96,234</u>	<u>1</u>	<u>118,141</u>	<u>1</u>
Total nonoperating income and gains	<u>136,321</u>	<u>2</u>	<u>439,762</u>	<u>4</u>
NONOPERATING EXPENSES AND LOSSES				
Interest expense	3,069	-	3,023	-
Loss on disposal of property, plant and equipment	17,474	-	10,443	-
Foreign exchange loss, net	63,558	1	-	-
Impairment loss (Note 8)	-	-	31,969	1
Others	<u>13,867</u>	<u>-</u>	<u>31,670</u>	<u>-</u>
Total nonoperating expenses and losses	<u>97,968</u>	<u>1</u>	<u>77,105</u>	<u>1</u>

(Continued)

# PHIHONG TECHNOLOGY CO., LTD. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF INCOME

NINE MONTHS ENDED SEPTEMBER 30, 2012 AND 2011

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

(Reviewed, Not Audited)

	2012		2011	
	Amount	%	Amount	%
INCOME BEFORE INCOME TAX	\$ 419,596	5	\$ 1,569,356	14
PROVISION FOR INCOME TAX (Note 16)	<u>(195,516)</u>	<u>(2)</u>	<u>(345,655)</u>	<u>(3)</u>
CONSOLIDATED NET INCOME	<u>\$ 224,080</u>	<u>3</u>	<u>\$ 1,223,701</u>	<u>11</u>
ATTRIBUTED TO				
Parent company's shareholders	\$ 237,450	3	\$ 1,238,410	11
Minority interest	<u>(13,370)</u>	<u>-</u>	<u>(14,709)</u>	<u>-</u>
	<u>\$ 224,080</u>	<u>3</u>	<u>\$ 1,223,701</u>	<u>11</u>
	2012		2011	
	Before Income Tax	After Income Tax	Before Income Tax	After Income Tax
BASIC EARNINGS PER SHARE (Note 17)				
Included income for minority interest	<u>\$ 1.52</u>	<u>\$ 0.81</u>	<u>\$ 5.71</u>	<u>\$ 4.45</u>
Attributed to shareholders of the parent company		<u>\$ 0.86</u>		<u>\$ 4.51</u>
DILUTED EARNINGS PER SHARE (Note 17)				
Included income for minority interest	<u>\$ 1.49</u>	<u>\$ 0.80</u>	<u>\$ 5.52</u>	<u>\$ 4.30</u>
Attributed to shareholders of the parent company		<u>\$ 0.85</u>		<u>\$ 4.35</u>

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

(With Deloitte & Touche review report dated October 26, 2012)

(Concluded)

**PHIHONG TECHNOLOGY CO., LTD. AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY**  
**NINE MONTHS ENDED SEPTEMBER 30, 2012 AND 2011**  
(In Thousands of New Taiwan Dollars)  
(Reviewed, Not Audited)

	Capital Stock		Capital Surplus					Retained Earnings			Other Equity			Total	
	Capital Stock	Advanced Collections for Common Stocks	Additional Paid-in Capital - Common stock	Additional Paid-in Capital-Bond Conversion	Treasury Stock Transactions	From Long-term Equity Investments	Interest Payable from Bond Conversion	Legal Reserve	Unappropriated Earnings		Cumulative Translation Adjustments	Unrealized (Loss) Gain on Financial Instruments	Unrealized Revaluation Increment		Minority Interest
									Unappropriated Earnings	Unappropriated Earnings					
BALANCE, JANUARY 1, 2012	\$ 2,749,329	\$ 16,154	\$ 203,406	\$ 661,582	\$ 48,234	\$ 11,305	\$ 13,243	\$ 909,627	\$ 1,828,362	\$ 250,296	\$ (22,304)	\$ 10,968	\$ 9,643	\$ 6,689,845	
Appropriation of 2011 net income (Note 15)															
Legal reserve	-	-	-	-	-	-	-	142,565	(142,565)	-	-	-	-	-	
Cash dividends	-	-	-	-	-	-	-	-	(995,969)	-	-	-	-	(995,969)	
Advanced collections for common stock transferred to capital stock (Note 13)	7,880	(16,154)	8,274	-	-	-	-	-	-	-	-	-	-	-	
Employee stock option (Note 14)	13,230	-	13,892	-	-	-	-	-	-	-	-	-	-	27,122	
Recognition of unrealized loss on investee's financial instruments	-	-	-	-	-	-	-	-	-	-	(2,764)	-	-	(2,764)	
Unrealized gain on available-for-sale financial assets	-	-	-	-	-	-	-	-	-	-	7,296	-	-	7,296	
Translation adjustments on long-term equity investments	-	-	-	-	-	-	-	-	-	(126,269)	-	-	-	(126,269)	
Changes of minority interest	-	-	-	-	-	-	-	-	-	-	-	-	(58)	(58)	
Net income for the nine months ended September 30, 2012	-	-	-	-	-	-	-	-	237,450	-	-	-	(13,370)	224,080	
BALANCE, SEPTEMBER 30, 2012	<u>\$ 2,770,439</u>	<u>\$ -</u>	<u>\$ 225,572</u>	<u>\$ 661,582</u>	<u>\$ 48,234</u>	<u>\$ 11,305</u>	<u>\$ 13,243</u>	<u>\$ 1,052,192</u>	<u>\$ 927,278</u>	<u>\$ 124,027</u>	<u>\$ (17,772)</u>	<u>\$ 10,968</u>	<u>\$ (3,785)</u>	<u>\$ 5,823,283</u>	
BALANCE, JANUARY 1, 2011	\$ 2,725,939	\$ 17,520	\$ 175,659	\$ 661,582	\$ 48,234	\$ 11,132	\$ 13,243	\$ 748,423	\$ 1,621,692	\$ (27,030)	\$ 185,552	\$ 10,968	\$ 29,898	\$ 6,222,812	
Appropriation of 2010 net income (Note 15)															
Legal reserve	-	-	-	-	-	-	-	161,204	(161,204)	-	-	-	-	-	
Cash dividends	-	-	-	-	-	-	-	-	(1,057,779)	-	-	-	-	(1,057,779)	
Advanced collections for common stock transferred to capital stock (Note 13)	8,000	(17,520)	9,520	-	-	-	-	-	-	-	-	-	-	-	
Employee stock option (Note 14)	15,390	-	18,227	-	-	-	-	-	-	-	-	-	-	33,617	
Recognized of unrealized loss on investee's financial instruments	-	-	-	-	-	-	-	-	-	-	(180,010)	-	-	(180,010)	
Unrealized loss on available-for-sale financial instrument	-	-	-	-	-	-	-	-	-	-	(27,325)	-	-	(27,325)	
Translation adjustments on long-term equity investments	-	-	-	-	-	-	-	-	-	277,193	-	-	-	277,193	
Changes of minority interest	-	-	-	-	-	-	-	-	-	-	-	-	529	529	
Net income for the nine months ended September 30, 2011	-	-	-	-	-	-	-	-	1,238,410	-	-	-	(14,709)	1,223,701	
BALANCE, SEPTEMBER 30, 2011	<u>\$ 2,749,329</u>	<u>\$ -</u>	<u>\$ 203,406</u>	<u>\$ 661,582</u>	<u>\$ 48,234</u>	<u>\$ 11,132</u>	<u>\$ 13,243</u>	<u>\$ 909,627</u>	<u>\$ 1,641,119</u>	<u>\$ 250,163</u>	<u>\$ (21,783)</u>	<u>\$ 10,968</u>	<u>\$ 15,718</u>	<u>\$ 6,492,738</u>	

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

(With Deloitte & Touche review report dated October 26, 2012)

# PHIHONG TECHNOLOGY CO., LTD. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF CASH FLOWS NINE MONTHS ENDED SEPTEMBER 30, 2012 AND 2011 (In Thousands of New Taiwan Dollars) (Reviewed, Not Audited)

	2012	2011
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Consolidated net income	\$ 224,080	\$ 1,223,701
Adjustments to reconcile consolidated net income to net cash provided by operating activities		
Depreciation and amortization	355,348	301,126
(Recovery from) provision for loss on doubtful accounts	(19,651)	4,297
Investment income recognized under the equity method	(2,003)	(16,659)
Cash dividend received from equity-method investees	16,261	23,254
Impairment loss	-	31,969
Net loss on disposal of property, plant and equipment	17,474	10,443
Net gain on disposal of investments	-	(213,370)
Net changes in operating assets and liabilities		
Accounts receivable	87,167	(316,240)
Other financial assets, current	55,783	165,953
Inventories	455,505	331,837
Deferred income tax asset, current	16,870	56,585
Other current assets	(98,420)	(49,820)
Other assets	18,172	(45,838)
Notes payable	-	(23)
Accounts payable	(14,858)	(392,191)
Accounts payable to related parties	4,629	28,934
Income tax payable	(68,159)	(306,376)
Other payables	(122,790)	175,343
Other current liabilities	(30,586)	10,571
Reserve for retirement plan	416	1,331
Deferred income tax liability, noncurrent	(70)	(210)
Other liabilities	<u>1,433</u>	<u>15,000</u>
Net cash provided by operating activities	<u>896,601</u>	<u>1,039,617</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Increase in available-for-sale financial assets	-	(33,042)
Proceeds from disposal of available-for-sale financial assets	-	517,466
Acquisition of investments accounted for by equity method	-	(150,000)
Decrease and return the capital from investees	22,483	41,128
Acquisition of property, plant and equipment	(441,749)	(522,268)
Proceeds from disposal of property, plant and equipment	2,534	12,230
Decrease (increase) in refundable deposits	3,081	(845)
Increase in deferred charges	-	(13,079)
Increase in intangible asset - computer software	<u>(16,909)</u>	<u>(7,267)</u>
Net cash used in investing activities	<u>(430,560)</u>	<u>(155,677)</u>

(Continued)



# PHIHONG TECHNOLOGY CO., LTD. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF CASH FLOWS NINE MONTHS ENDED SEPTEMBER 30, 2012 AND 2011 (In Thousands of New Taiwan Dollars) (Reviewed, Not Audited)

	2012	2011
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Employee stock options	\$ 27,122	\$ 33,617
Cash dividends	(995,969)	(1,057,779)
Decrease in advanced deposits received	(141)	(515)
Changes of minority interest	<u>(58)</u>	<u>529</u>
Net cash used in financing activities	<u>(969,046)</u>	<u>(1,024,148)</u>
<b>EFFECT OF EXCHANGE RATE CHANGES</b>	<u>(17,732)</u>	<u>61,078</u>
<b>NET DECREASE IN CASH AND CASH EQUIVALENTS</b>	(520,737)	(79,130)
<b>CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD</b>	<u>2,119,386</u>	<u>1,890,244</u>
<b>CASH AND CASH EQUIVALENTS, END OF PERIOD</b>	<u>\$ 1,598,649</u>	<u>\$ 1,811,114</u>
<b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION</b>		
Cash paid during the period		
Interest (excluding interest capitalized)	<u>\$ 2,589</u>	<u>\$ 2,224</u>
Income tax	<u>\$ 219,966</u>	<u>\$ 595,655</u>
<b>NONCASH INVESTING AND FINANCING ACTIVITIES</b>		
Translation adjustments on long-term equity investments	<u>\$ (126,269)</u>	<u>\$ 277,193</u>
Recognized unrealized loss on financial instruments of investees	<u>\$ 2,764</u>	<u>\$ 180,010</u>
Change in unrealized loss on available-for-sale financial instruments	<u>\$ (7,296)</u>	<u>\$ 27,325</u>
<b>ACQUISITION OF PROPERTY, PLANT AND EQUIPMENT</b>		
Increase in property, plant and equipment acquired	\$ 441,683	\$ 522,568
Add payables for acquisition of property, plant and equipment, beginning of period	256	1,352
Less payables for acquisition of property, plant and equipment, end of period	<u>(190)</u>	<u>(1,652)</u>
Cash paid for acquisition of property, plant and equipment	<u>\$ 441,749</u>	<u>\$ 522,268</u>

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

(With Deloitte & Touche review report dated October 26, 2012)

(Concluded)

# PHIHONG TECHNOLOGY CO., LTD. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NINE MONTHS ENDED SEPTEMBER 30, 2012 AND 2011

(In Thousands of New Taiwan Dollars (Except Per Share Data), Unless Stated Otherwise)  
(Reviewed, Not Audited)

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### 1. ORGANIZATION AND OPERATIONS

Phihong Technology Co., Ltd. (“Phihong”), which was formerly known as Phihong Enterprise Co., Ltd. was incorporated on December 12, 1972 under the laws of the Republic of China (“ROC”). Under a resolution approved in the stockholders’ meeting in June 2003, Phihong changed its name to Phihong Technology Co., Ltd. Phihong primarily manufactures and sells AC/DC power adapters, charger bases, power supply modules, UPS (uninterruptible power supply) for computers, ballasts, etc.

In February 2000, Phihong was authorized to have its stocks traded on the over-the-counter (OTC) securities exchange in Taiwan. In September 2001, Phihong’s stocks ceased to be OTC traded and Phihong later obtained authorization to have its stocks listed on the Taiwan Stock Exchange.

In addition to Phihong, the consolidated financial statements included the following companies:

Name	Place of Incorporation	Phihong and Its Subsidiaries’ Ownership Percentage
Phihong International Corp.	British Virgin Islands	100.00
Phitek International Co., Ltd.	British Virgin Islands	100.00
Ascent Alliance Ltd.	British Virgin Islands	100.00
Phihong USA Corp.	USA	100.00
American Ballast Corp.	USA	100.00
Guang-Lai Investment Co., Ltd.	Republic of China	100.00
Phihong Technology Japan Co., Ltd.	Japan	100.00

Phihong International Corp. (PHI), a 100% subsidiary of Phihong incorporated in the British Virgin Islands in 1996, sells power supplies as well as invests in its subsidiaries in China to manufacture various power supplies.

PHI’s subsidiaries were as follows:

Name	Place of Incorporation	Direct Ownership Percentage	Primary Operations
Phihong (Dongguan) Electronics Co., Ltd.	Mainland China	100.00	Manufactures various power supplies
Phitek (Tianjin) Electronics Co., Ltd.	Mainland China	100.00	Manufactures various power supplies
Phihong Electronics (Suzhou) Co., Ltd.	Mainland China	100.00	Manufactures various power supplies and ballasts
Value Dynamic Investment Ltd.	British Virgin Islands	100.00	Makes investments
N-Lighten Technologies, Inc.	USA	58.45	Makes investments

Phihong owned 78.23% ownership of N-Lighten Technologies, Inc. through the PHI and Guang-Lai Investment Co., Ltd. as of September 30, 2012.

Value Dynamic's subsidiary was as follows:

<b>Name</b>	<b>Place of Incorporation</b>	<b>Direct Ownership Percentage</b>	<b>Primary Operations</b>
Yanghong Lighting Trade Co., Ltd.	Mainland China	100.00	Sells various lighting supplies

Phitek International Co., Ltd. (PHK), a 100% subsidiary of Phihong incorporated in the British Virgin Islands in 1999, is an agent of selling power supplies as well as an investors in its subsidiary in China which manufacture various power supplies.

PHK's subsidiary was as follows:

<b>Name</b>	<b>Place of Incorporation</b>	<b>Direct Ownership Percentage</b>	<b>Primary Operations</b>
Dongguan Phitek Electronics Co., Ltd.	Mainland China	100.00	Manufactures various power supplies
Suzhou Xin Phihong Electronics Co., Ltd.	Mainland China	10.12	Manufactures and sells lighting supplies

Suzhou Xin Phihong Electronics Co., Ltd., a subsidiary of PHK and Phihong Electronics (Suzhou) Co., Ltd. in China, manufactures and sells lighting supplies. PHK and Phihong Electronics (Suzhou) Co., Ltd. acquired 10.12% and 89.88% ownership of Suzhou Xin Phihong Electronics Co., Ltd., respectively.

Ascent Alliance Ltd. (PHQ), a 100% subsidiary of Phihong incorporated in the British Virgin Islands in 2004, is an agent of selling electronic materials as well as an investors in its subsidiary in China which manufacture various electronic materials.

PHQ's subsidiaries were as follows:

<b>Name</b>	<b>Place of Incorporation</b>	<b>Direct Ownership Percentage</b>	<b>Primary Operations</b>
Dongguan Shuang-Ying Electronics Co., Ltd.	Mainland China	100.00	Manufactures and sells electronic materials
Jin-Sheng-Hong (Jiangxi) Electronics Co., Ltd.	Mainland China	100.00	Manufactures and sells the electronic materials and transformers

Phihong USA Corp. (PHA), a 100% subsidiary of Phihong incorporated in the USA in 1997, sells various power supplies.

American Ballast Corp. (PHAB), a 100% subsidiary of Phihong incorporated in the USA in 2004, sells various ballasts.

Guang-Lai Investment Co., Ltd. ("Guang-Lai"), was incorporated in Taiwan in October 2001, primarily engages in investments.

Before December 30, 2011, Guang-Lai held 25.33% ownership interest of Ai-Hon Investment Co., Ltd. (“Ai-Hon”). Spring City Resort Co., Ltd. (“Spring City Resort”) merged with Ai-Hon on December 31, 2011 and Spring City Resort is the surviving company. Therefore, Guang-Lai gets Spring City Resort’s shares.

N-Lighten Technologies’ Inc., a subsidiary of PHI and Guang-Lai incorporated in the USA, invests in its subsidiary in China.

N-Lighten Technologies’ subsidiary was as follows:

<b>Name</b>	<b>Place of Incorporation</b>	<b>Direct Ownership Percentage</b>	<b>Primary Operations</b>
N-Lighten (Shanghai) Trading Inc.	Mainland China	100.00	Develop, manufacture and sale various equipment and monitors

Phihong Technology Japan Co., Ltd. (“PHJ”) was incorporated in Japan in April 2010. It primarily engages in sales of power components.

Except PHJ’s financial statements were based on its unreviewed financial statements as of and for the nine months ended September 30, 2012 and 2011, the other financial statements were reviewed as of and for the nine months ended September 30, 2012 and 2011.

Phihong and its subsidiaries (collectively, the “Company”) had 9,066 and 9,412 employees as of September 30, 2012 and 2011, respectively.

## **2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

### **Basis of Presentation**

The accompanying consolidated financial statements have been prepared in conformity with the Guidelines Governing the Preparation of Financial Reports by Securities Issuers, the Interpretation No. 0960064020 issued by Financial Supervisory Commission, Executive Yuan on November 15, 2007, and accounting principles generally accepted in the ROC. Except for the Note 3 to the consolidated financial statements, the adoption of the accounting policies by the consolidated financial statements for the nine months ended September 30, 2012 and 2011 were same as the consolidated financial statements for the six months ended June 30, 2012 and 2011.

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

Certain accounts in the consolidated financial statement as of and for the nine months ended September 30, 2011 have been reclassified to conform to the presentation of the consolidated financial statement as of and for the nine months ended September 30, 2012.

### 3. ACCOUNTING CHANGES

#### Accounting Treatment for the Financial Instruments

On January 1, 2011, the Company adopted the newly revised Statement of Financial Accounting Standards (SFAS) No. 34, "Financial Instruments: Recognition and Measurement." The main revisions include loans and receivables originated by the Company are now covered by SFAS No. 34. This accounting change did not have a significant effect on the Company's consolidated financial statements as of and for the nine months ended September 30, 2011.

#### Operating Segments

On January 1, 2011, the Company adopted the newly issued SFAS No. 41, "Operating Segments." The statement requires identification and disclosure of operating segments on the basis of how the Company's chief operating decision maker regularly reviews information in order to allocate resources and assess performance. This statement supersedes SFAS No. 20, "Segment Reporting" and it only changes the disclosure of segment reporting due to the adoption.

### 4. CASH AND CASH EQUIVALENTS

Cash and cash equivalents as of September 30, 2012 and 2011 were as follows:

	<b>2012</b>	<b>2011</b>
Cash on hand	\$ 2,519	\$ 2,298
Checking accounts	638	3,560
Savings accounts	212,875	97,979
Foreign-currency deposits	1,325,617	1,314,220
Time deposits	57,000	103,500
Short-term notes	<u>-</u>	<u>289,557</u>
	<u>\$ 1,598,649</u>	<u>\$ 1,811,114</u>

### 5. ACCOUNTS RECEIVABLE

Accounts receivable as of September 30, 2012 and 2011 were as follows:

	<b>2012</b>	<b>2011</b>
Accounts receivable	\$ 1,898,260	\$ 2,174,643
Less allowance for doubtful accounts	<u>(29,668)</u>	<u>(51,032)</u>
	<u>\$ 1,868,592</u>	<u>\$ 2,123,611</u>

As of September 30, 2012 and 2011, accounts receivable of PHA amounted to \$531,653 thousand and \$753,013 thousand, respectively, had been pledged to secure short-term debts (the amount was not used as of September 30, 2012 and 2011, respectively). See Note 20 to the consolidated financial statements.

## 6. INVENTORIES

Inventories as of September 30, 2012 and 2011 were as follows:

	<b>2012</b>	<b>2011</b>
Raw materials	\$ 524,099	\$ 659,236
Work-in-process	221,254	261,514
Finished goods	247,281	257,022
Merchandise	<u>631,861</u>	<u>979,539</u>
	<u>\$ 1,624,495</u>	<u>\$ 2,157,311</u>

As of September 30, 2012 and 2011, the allowance for inventory devaluation was \$280,287 thousand and \$217,675 thousand, respectively.

The cost of inventories recognized as cost of goods sold for the nine months ended September 30, 2012 and 2011 was \$7,108,104 thousand and \$8,176,134 thousand, respectively. In which included \$21,628 thousand and \$88,366 thousand of inventory devaluation for the nine months ended September 30, 2012 and 2011, respectively.

As of September 30, 2011, inventories of PHA amounted \$703,262 thousand had been pledged to secure short-term debts (the amount was not used as of September 30, 2011). See Note 20 to the consolidated financial statements.

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

Available-for-sales financial asset, noncurrent as of September 30, 2012 and 2011 were as follows:

	<b>2012</b>	<b>2011</b>
Marketable equity securities		
Hua Jung Component Co., Ltd.	<u>\$ 31,458</u>	<u>\$ 31,579</u>

Hua Jung Component Co., Ltd. decreased its paid-in capital by cash at the ratio 18% in September 2012. Pihong has received amount \$9,195 thousand.

PHI sold all of its own shares of JK Yaming International Holdings Ltd. in May 2011. As a result, the gain on such disposal of investment amounted to \$189,319 thousand was recorded as gain on disposal of investment for the nine months ended September 30, 2011.

## 8. FINANCIAL ASSETS CARRIED AT COST, NONCURRENT

Financial assets carried at cost, noncurrent as of September 30, 2012 and 2011 were as follows:

	2012	2011
Bao-Dian Venture Capital Co., Ltd.	\$ 30,000	\$ 30,000
Yuan-Jing Venture Capital Co., Ltd.	33,500	33,500
Asiatech Taiwan Venture Fund	12,748	15,057
NeoPac Lighting Limited	32,224	32,224
Yong-Li Investment Ltd.	50,000	50,000
TC-1 Culture Fund	30,000	30,000
Hui-Cheng Electronic Co., Ltd.	15,248	15,248
Less: Accumulated impairment	<u>(112,775)</u>	<u>(89,775)</u>
	<u>\$ 90,945</u>	<u>\$ 116,254</u>

The stocks and other investments mentioned above do not have open pricing and reliable fair values, thus they are carried at cost. Pihong performed impairment testing on them periodically.

Bao-Dian Venture Capital Co., Ltd., Yong-Li Investment Ltd., TC-1 Culture Fund, and NeoPac Lighting Limited have experienced continuous operating loss; thus, the Company recognized \$31,969 thousand impairment loss for the nine months ended September 30, 2011.

Bao-Dian Venture Capital Co., Ltd. decreased its paid-in capital to write-off its accumulated deficits for nine months ended September 30, 2012, at a rate of 55%. As a result, its paid-in capital was \$128,700 thousand as of September 30, 2012.

Yuan-Jing Venture Capital Co., Ltd. had paid-in capital of \$925,000 thousand as of January 1, 2011. It decreased its paid-in capital by cash in the amount of \$305,250 thousand at a rate of 33% for nine months ended September 30, 2011 and the Company received \$16,500 thousand as capital return. As a result, its paid-in capital was \$619,750 thousand as of September 30, 2012.

## 9. LONG-TERM EQUITY INVESTMENTS AT EQUITY METHOD

Long-term equity investments at equity method as of September 30, 2012 and 2011 were as follows:

	2012			2011	
	Original Cost	Carrying Value	Ownership Percentage	Carrying Value	Ownership Percentage
Hao-Xuan Venture Capital Co., Ltd.	\$ 59,851	\$ 60,941	24.67	\$ 69,554	24.67
H&P Venture Capital Investment Corp.	150,000	144,921	32.26	148,748	32.26
Pihong PWM Brasil Ltda.	8,258	-	60.00	-	60.00
First International Computer Do Brasil Ltda.	67,618	-	33.85	-	33.85
Han-Yu Venture Capital Co., Ltd.	100,000	91,808	22.22	108,020	22.22
Spring City Resort Co., Ltd. (Formerly name Ai-Hon Investment Co., Ltd.)	<u>190,000</u>	<u>29,932</u>	25.33	<u>28,406</u>	25.33
	<u>\$ 575,727</u>	<u>\$ 327,602</u>		<u>\$ 354,728</u>	

Long-term equity investment income (loss) for the nine months ended September 30, 2012 and 2011 is summarized as follows:

	<b>2012</b>	<b>2011</b>
Hao-Xuan Venture Capital Co., Ltd.	\$ 5,781	\$ 3,894
H&P Venture Capital Investment Corp.	(2,040)	(1,252)
Han-Yu Venture Capital Co., Ltd.	(963)	17,505
Spring City Resort Co., Ltd.	<u>(775)</u>	<u>(3,488)</u>
	<u>\$ 2,003</u>	<u>\$ 16,659</u>

Long-term equity investments accounted for under the equity method for the nine months ended September 30, 2012 and 2011 were based on unreviewed financial statements.

Hao-Xuan Venture Capital Co., Ltd. (“Hao-Xuan”) was incorporated in May 2004 to engage in investing activities. The Company had paid-in capital of \$387,000 thousand as of January 1, 2011. It decreased its paid-in capital by cash amounted to \$44,509 thousand and \$99,846 thousand for the nine months ended September 30, 2012 and 2011, respectively. The Company had received the amount of \$10,979 thousand and \$24,628 thousand, respectively. As a result, its paid-in capital was \$242,645 thousand as of September 30, 2012.

Han-Yu Venture Capital Co., Ltd. (“Han-Yu”) was incorporated in June 2004 to engage in investments. Its paid-in capital was \$450,000 thousand as of September 30, 2012.

Ai-Hon, which was invested by Phihong, was primarily engaged in investment business. Spring City Resort, which was a wholly-owned subsidiary of Ai-Hon, was founded in 1975 and is primarily engaged in hotel, restaurant and bathroom services. Spring City Resort merged with Ai-Hon on December 31, 2011; Spring City Resort is the surviving company. Its paid-in capital was \$112,000 thousand as of September 30, 2012.

Phihong’s investments in Brazil include 60% ownership interest of Phihong PWM Brasil Ltda. and 33.85% ownership interest of First International Computer Do Brasil Ltda. Additionally, Phihong PWM Brasil Ltda. also holds 21.15% ownership interest of First International Computer Do Brasil Ltda. The other 40% ownership interest of Phihong PWM Brasil Ltda. is held by the local management team. According to cooperation mode between the Company and the local management team and Brazilian local laws, the Company has no controlling power over Phihong PWM Brasil Ltda. Because the recoverability of the investments in Phihong PWM Brasil Ltda. and First International Computer Do Brasil Ltda. is considered remote, the Company reduced the carrying value of both investments to zero.

H&P Venture capital Investment Corp. was incorporated in May 2011. It primarily engages in investing activities. Its paid-in capital was \$465,000 thousand as of September 30, 2012.



## 10. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment as of September 30, 2012 and 2011 were as follows:

	2012			2011
	Cost	Accumulated Depreciation	Carrying Value	Carrying Value
Land	\$ 254,867	\$ -	\$ 254,867	\$ 256,571
Buildings and improvements	2,451,593	812,533	1,639,060	1,839,572
Machinery and equipment	2,341,063	1,134,683	1,206,380	1,148,211
Transportation equipment	36,133	28,291	7,842	14,598
Furniture, fixtures and office equipment	275,159	230,578	44,581	76,816
Other equipment	279,915	167,441	112,474	99,795
Construction in progress and prepayments for purchase of equipment	170,226	-	170,226	69,211
	\$ 5,808,956	\$ 2,373,526	\$ 3,435,430	\$ 3,504,774

In March 2011, Pihong purchased a parcel of land amounted to \$85,136 thousand in Yongkang Dist, Tainan City for factory.

Under the long-term loan agreement, the Company has mortgaged the following property, plant and equipment as collaterals.

	September 30	
	2012	2011
Land	\$ 112,450	\$ 112,450
Buildings and improvements	162,154	171,985
	\$ 274,604	\$ 284,435

## 11. OTHER PAYABLES

	September 30	
	2012	2011
Accrued expenses	\$ 676,371	\$ 859,690
Bonus payable	160,488	405,955
Salaries payable	239,928	240,968
Others	25,102	53,773
	\$ 1,101,889	\$ 1,560,386

## 12. LONG-TERM DEBTS

Long-term debts as of September 30, 2012 and 2011 were as follows:

	<u>September 30</u>	
	<u>2012</u>	<u>2011</u>
Hua Nan Bank		
Medium-term secured loan. The loan term was from September 27, 2012 to September 27, 2014. Interest rate was 1.37% on September 30, 2012. Interest is paid monthly. The principal of \$200,000 thousand will be paid on September 27, 2014	\$ 200,000	\$ -
Medium-term secured loan. The loan term was from September 30, 2010 to September 30, 2017; interest rate was 1.37% on September 30, 2011. Interest is paid monthly. The principal is due in monthly installments commencing from September 30, 2012. The full principle was early repaid in December 2011.	<u>-</u>	<u>200,000</u>
	<u>\$ 200,000</u>	<u>\$ 200,000</u>

The pledged properties and endorsements/guarantees as collaterals for bank loans, please see Notes 10, 19 and 20 to the consolidated financial statements.

## 13. CAPITAL STOCK

### Phihong

	<u>September 30</u>	
	<u>2012</u>	<u>2011</u>
Authorized capital		
Shares (in thousands)	<u>600,000</u>	<u>600,000</u>
Par value (in dollars)	<u>\$ 10</u>	<u>\$ 10</u>
Capital	<u>\$ 6,000,000</u>	<u>\$ 6,000,000</u>
Issued capital		
Shares (in thousands)	<u>277,044</u>	<u>274,933</u>
Par value (in dollars)	<u>\$ 10</u>	<u>\$ 10</u>
Capital	<u>\$ 2,770,439</u>	<u>\$ 2,749,329</u>

Phihong's outstanding capital amounted to \$2,725,939 thousand on January 1, 2011. The employee stock warrant holders exercised 1,477 thousand shares and 62 thousand shares at an exercise price of \$21.90 and \$20.50, respectively, and exercised 800 thousand common shares for advanced collections for capital stock transferred to capital stock between January 1, 2011 to September 30, 2011. As of September 30, 2011, Phihong's outstanding capital amounted to \$2,749,329 thousand, divided into 274,933 thousand common shares with a par value of NT\$10.

As of January 1, 2012, Phihong's outstanding capital amounted to \$2,749,329 thousand. The employee stock warrant holders exercised 1,323 thousand common shares at an exercise price of \$20.50, and exercised 788 thousand common shares for advanced collections for capital stock transferred to capital stock between January 1, 2012 to September 30, 2012. As of September 30, 2012, Phihong's outstanding capital amounted to \$2,770,439 thousand, divided into 277,044 thousand common shares with a par value of NT\$10.

#### 14. EMPLOYEE STOCK OPTION PLANS

At the November 23, 2007 meeting, the Board of Directors of Pihong resolved to issue employee stock warrants in accordance with Securities and Exchange Law Article 28-3 within the quantity of 15,000 units. Each individual employee stock warrant is granted the right to purchase 1,000 new issued common shares. The exercise price is the closing price of Pihong's common shares at the employee stock warrants' issuance date. The warrant holders can exercise the right up to half of the granted warrant units no earlier than two years from the granted date. After three years from the granted date, the warrants holders are eligible to exercise the right up to three-fourth of the granted warrant units. After four years from the granted date, the warrants holders are eligible to exercise all the warrants owned. The options granted are valid for six years and the warrant holders can not exercise the right after six years from the granted date. As of December 28, 2007, Pihong issued stock warrants of 15,000 units at an exercise price of \$21.30 per share. The exercise price will be adjusted according to calculating formula when there are stock and cash dividends and issuance of capital stock. As a result, the exercise price was \$18.20 per share as of September 30, 2012.

Information about employee stock option plans for the nine months ended September 30, 2012 and 2011 was as follows:

	2012		2011	
	Number of Options (In Thousand Shares)	Weighted- average Exercise Price (NT\$)	Number of Options (In Thousand Shares)	Weighted- average Exercise Price (NT\$)
Balance, beginning of period	6,867	\$ 20.50	9,194	\$ 21.90
Options exercised	<u>(1,323)</u>	20.50	<u>(1,539)</u>	21.84
Balance, end of period	<u>5,544</u>	18.20	<u>7,655</u>	20.50
Options exercisable, end of period	<u>5,544</u>		<u>3,905</u>	

Information about outstanding and exercisable options as of September 30, 2012 and 2011 were as follows:

Range of Exercise Price (NT\$)	Options Outstanding			Options Exercisable	
	Number of Options (In Thousand Shares)	Weighted- average Remaining Life (Years)	Weighted- average Exercise Price (NT\$)	Number of Options (In Thousand Shares)	Weighted- average Exercise Price (NT\$)
<u>September 30, 2012</u>					
\$ 18.20	<u>5,544</u>	<u>1.25</u>	<u>\$ 18.20</u>	<u>5,544</u>	<u>\$ 18.20</u>
<u>September 30, 2011</u>					
\$ 20.50	<u>7,655</u>	<u>2.25</u>	<u>\$ 20.50</u>	<u>3,905</u>	<u>\$ 20.50</u>

Had the Company recognized the compensation cost under the fair value method using the Black-Scholes pricing model, the assumptions and pro forma results of the Company for the nine months ended September 30, 2011 would have been as follows:

	<b>2011</b>
<b>Assumptions</b>	
Risk-free interest rate	2.41%
Expected life	6 years
Expected volatility	48.59%
Expected dividend yield	-
<b>Net income</b>	
As reported (attributed to shareholders of the parent company)	\$ 1,238,410
Pro forma (attributed to shareholders of the parent company)	\$ 1,231,629
<b>Basic earnings per share after income tax (NT\$)</b>	
As reported (attributed to shareholders of the parent company)	\$4.51
Pro forma (attributed to shareholders of the parent company)	\$4.48

No more employee stock option information needs to be disclosed for the nine months ended September 30, 2012, because the service years of the employees was expired on December 28, 2011.

## **15. RETAINED EARNINGS**

Under the Company Law of the ROC and Pihong's Articles of Incorporation, 10% of Pihong's annual earnings, net of tax and any deficit, should first be appropriated as legal reserve until such reserve equals to the amount of Pihong's capital, and then a special reserve should be appropriated as required by laws or domestic authorities.

Any remaining earnings plus unappropriated earnings accumulated by prior years, unless to be retained partially by the Company or resolved otherwise by the stockholders, and plan to assign proposal, draw shareholders to recognize and should be appropriated as follows:

- a. Not greater than 2% as remuneration to directors and supervisors;
- b. Not less than 10% as bonuses to employees; and
- c. The remaining as dividends, of which at least 10% should be cash dividends.

Under the Company Law, capital surplus can only be used to offset a deficit. However, the capital surplus from shares issued in excess of par may be capitalized, which however is limited to a certain percentage of the Company's paid-in capital. Under the revised Company Law issued on January 4, 2012, the aforementioned capital surplus also may be distributed in cash. Legal reserve shall be appropriated until it has reached the Company's paid-in capital. This reserve may be used to offset a deficit. Under the aforesaid revised Company Law, when the legal reserve has exceeded 25% of the Company's paid-in capital, the excess may be transferred to capital or distributed in cash.

For the nine months ended September 30, 2012 and 2011, the bonus to employees was \$38,467 thousand and \$200,622 thousand, respectively, and the remuneration to directors and supervisors was \$4,274 thousand and \$22,292 thousand, respectively. The bonus to employees and remuneration to directors and supervisors represented 20%, of net income (net of the bonus and remuneration). Material differences between such estimated amounts and the amounts proposed by the Board of Directors in the following year are adjusted for in the current year. If the actual amounts subsequently resolved by the shareholders differ from the proposed amounts, the differences are recorded in the year of shareholders' resolution as a change in accounting estimate. If a share bonus is resolved to be distributed to employees, the number of shares is determined by dividing the amount of the share bonus by the closing price (after considering the effect of cash and stock dividends) of the shares of the day immediately preceding the shareholders' meeting.

The appropriations of earnings for 2011 and 2010 had been approved in the shareholders' meetings on June 19, 2012 and June 15, 2011, respectively. The appropriations and dividends per share were as follows:

	<b>Appropriation of Earnings</b>		<b>Dividends Per Share (NT\$)</b>	
	<b>For Year 2011</b>	<b>For Year 2010</b>	<b>For Year 2011</b>	<b>For Year 2010</b>
Legal reserve	\$ 142,565	\$ 161,204	\$ -	\$ -
Cash dividends	<u>995,969</u>	<u>1,057,779</u>	3.59	3.85
	<u>\$ 1,138,534</u>	<u>\$ 1,218,983</u>		

The stockholders' meeting approved the following appropriation of the 2011 and 2010 earnings: \$236,998 thousand and \$267,167 thousand as employees' bonuses and \$19,620 thousand and \$23,000 thousand as remuneration to directors and supervisors. The approved amounts of the bonus to employees and the remuneration to directors and supervisors have no difference from the accrual amounts.

Information about the bonus to employees, directors and supervisors is available on the Market Observation Post System website of the Taiwan Stock Exchange.

## 16. INCOME TAX

The income tax for the nine months ended September 30, 2012 and 2011 was as follows:

	<b>2012</b>	<b>2011</b>
Income tax expense, current period	\$ 166,402	\$ 303,172
Additional tax at 10% of unappropriated earnings	28,712	-
Adjustments to prior year's income tax expense	<u>402</u>	<u>42,483</u>
Income tax expense, net	<u>\$ 195,516</u>	<u>\$ 345,655</u>

The components of deferred tax asset (liability) as of September 30, 2012 and 2011 were as follows:

	<b>2012</b>	<b>2011</b>
Deferred tax asset assets (liabilities)		
Unrealized exchange losses (gains)	\$ 980	\$ (11,790)
Unrealized inventory devaluation losses	9,070	9,070
Unrealized bad-debt losses	10,450	8,700
Unrealized gross profit	10,150	45,245
Unrealized export trading losses	8,340	8,340
Unrealized pension expense	10,240	10,100
Long-term equity investments income	<u>(79,832)</u>	<u>(79,832)</u>
Deferred tax liability, net	(30,602)	(10,167)
Deferred tax asset - current	<u>(38,990)</u>	<u>(59,565)</u>
Deferred tax liability - noncurrent	<u>\$ (69,592)</u>	<u>\$ (69,732)</u>

Current income tax expense and income tax payable as of September 30, 2012 and 2011 were reconciled as follows:

	<b>2012</b>	<b>2011</b>
Income tax expense at statutory rate	\$ 154,580	\$ 319,857
Loss (income) on long-term equity investments accounted for by the equity method	12,635	(10,270)
Gain on disposal of investment	-	(4,050)
Impairment loss of financial assets carried at cost	-	5,430
Exempt dividends	(610)	(770)
Others	<u>(203)</u>	<u>(7,025)</u>
Current income tax expense	166,402	303,172
Provision for (reversal of) deferred income tax assets (liabilities)		
Unrealized exchange gains	(400)	(26,040)
Unrealized export trading losses	-	2,550
Unrealized bad-debt expense	390	(2,630)
Unrealized gross profit	(16,870)	(30,450)
Unrealized pension expense	70	230
Others	<u>262</u>	<u>(20)</u>
	149,854	246,812
Less current year's tax payments and withholding income tax	(75,495)	(212,864)
Add prior year's income tax payable	33,402	32,572
Additional 10% income tax on unappropriated earnings	<u>28,712</u>	<u>-</u>
Income tax payable as of September 30, 2012 and 2011	<u>\$ 136,473</u>	<u>\$ 66,520</u>

The income tax returns examined and approved by the tax authorities are summarized as follows:

	<b>Year</b>
Phihong	2009
Guang-Lai	2010

Information on the integrated income tax system of Phihong as of September 30, 2012 is as follows:

Balance of imputation credit account	<u>\$ 193,131</u>
Undistributed earnings generated until 1997	<u>\$ -</u>
Undistributed earnings (accumulated deficits) generated since 1998	<u>\$ 927,278</u>
Actual IC ratio for earnings distribution in 2012	<u>23.28%</u>
Actual IC ratio for earnings distribution in 2011	<u>20.48%</u>

## 17. EARNINGS PER SHARE

Earnings per share (“EPS”) before and after income tax for the nine months ended September 30, 2012 and 2011 were as follows:

	2012				EPS(NT\$)		
	Income Before Tax	Income After Tax	Income After Tax (Attributed to Parent's Shareholders)	Weighted Average Number of Common Shares (Outstanding in Thousands)	Income Before Tax	Income After Tax	Income After Tax (Attributed to Parent's Shareholders)
Basic earnings per share							
Net income	\$ 419,596	\$ 224,080	\$ 237,450	276,877	\$ 1.52	\$ 0.81	\$ 0.86
Effect of dilutive potential common shares							
Employee stock option				2,548			
Employee bonuses				1,482			
Diluted earnings per share							
Net income attributed to shareholders of common shares plus the effect of dilutive potential common shares	\$ 419,596	\$ 224,080	\$ 237,450	280,907	\$ 1.49	\$ 0.80	\$ 0.85
	2011				EPS(NT\$)		
	Income Before Tax	Income After Tax	Income After Tax (Attributed to Parent's Shareholders)	Weighted Average Number of Common Shares (Outstanding in Thousands)	Income Before Tax	Income After Tax	Income After Tax (Attributed to Parent's Shareholders)
Basic earnings per share							
Net income	\$1,569,356	\$1,223,701	\$1,238,410	274,719	\$ 5.71	\$ 4.45	\$ 4.51
Effect of dilutive potential common shares							
Employee stock option				4,583			
Employee bonuses				5,156			
Diluted earnings per share							
Net income attributed to shareholders of common shares plus the effect of dilutive potential common shares	\$1,569,356	\$1,223,701	\$1,238,410	284,458	\$ 5.52	\$ 4.30	\$ 4.35

The Company should presume that the entire amount of the employees bonus will be settled in shares and the resulting potential shares should be included in the weighted average number of shares outstanding in calculation of diluted EPS, if the shares have a dilutive effect. The number of shares is estimated by dividing the amount of bonus to employees by the closing price of the common shares on the balance sheet date. The dilutive effect of the potential shares needs to be considered until the shares of employee bonus are resolved in the shareholders' meeting in the following year.

## 18. OTHERS

### Fair Value of Financial Instruments

The fair values of nonderivative financial instruments as of September 30, 2012 and 2011 are summarized as follows:

	2012		2011	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Assets				
Cash and cash equivalents	\$ 1,598,649	\$ 1,598,649	\$ 1,811,114	\$ 1,811,114
Accounts receivable	1,868,592	1,868,592	2,123,611	2,123,611
Other financial assets, current	30,497	30,497	44,958	44,958
Available-for-sale financial assets, noncurrent	31,458	31,458	31,579	31,579
Financial assets carried at cost, noncurrent	90,945	-	116,254	-
Long-term equity investments at equity method	327,602	327,602	354,728	354,728
Refundable deposits	29,357	29,357	29,701	29,701
Liabilities				
Accounts payable	2,013,839	2,013,839	1,999,642	1,999,642
Accounts payable to related parties	40,568	40,568	28,938	28,938
Others payable	1,101,889	1,101,889	1,560,386	1,560,386
Long-term debts	200,000	200,000	200,000	200,000
Advanced deposits received	987	987	932	932

### Reporting of Derivative Instruments in the Financial Statements

Approaches and assumptions used to assess the fair value of financial instruments are summarized as follows:

- Fair values of current assets and liabilities, cash and cash equivalents, notes receivable, accounts receivable, other financial assets - current, refundable deposits, notes payable, accounts payable, accounts payable to related parties, other payable, advanced deposits received, etc. are based on carrying values because of their short maturities.
- Fair values of financial instruments measured at fair value through profit or loss and available-for-sale financial assets are determined using the market value in the open market or estimated by evaluation method according to the open information in the market.
- Fair values of long-term equity investments at equity method are estimated based on the unreviewed net value of investees as of September 30, 2012 and 2011.
- Financial assets carried at cost are investments in unquoted shares, which have no quoted price in an active market and entail an unreasonably high cost to obtain verifiable fair value. Therefore, no fair value is presented.
- Fair values of long-term borrowings are determined using the present value of the forecasted cash flows discounted at interest rates of similar long-term debts.



The amounts of financial assets determined by market value in the open market or estimated by evaluation method as of September 30, 2012 and 2011 are summarized as follows:

	<b>Market Value in the Open Market</b>		<b>By Evaluation Method</b>	
	<b>2012</b>	<b>2011</b>	<b>2012</b>	<b>2011</b>
Available for sale financial assets, noncurrent	\$ 31,458	\$ 31,579	\$ -	\$ -

For the nine months ended September 30, 2011, the net foreign exchange gains on forwards was \$2,435 thousand, which was recorded as nonoperating income and gains.

The information of financial risk was summarized as follows:

### **Market Risk**

The Company is exposed to investing risk because it invests in the listed companies; therefore, the fair value of the stock are fluctuated due to changes in market price. One percent decline in market rate will cause the fair value of financial instruments to decline by \$315 thousand.

### **Credit Risk**

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

### **Liquidity Risk**

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

### **Cash Flow Interest Rate Risk**

The Company's long-term borrowings had floating interest rate. Therefore, cash flows are expected to fluctuate due to changes in market interest rates. One percentage increase in market rate will cause the Company to increase its cash-out by \$2,000 thousand.

Hedge of fair value, hedge of cash flow, and hedge of a net investment in a foreign operation: None.

## **19. RELATED-PARTY TRANSACTIONS**

The Company's related parties were as follows:

<b>Related Party</b>	<b>Relationship with the Company</b>
Xu Sheng Technology Co., Ltd. ("Xu Sheng") Shine Tech Ltd. ("Shine Tech")	The chairman of Xu Sheng is a director of Phihong The chairman of Shine Tech is the spouse of Phihong's director
Peter Lin	Phihong's chairman

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

### Cost of Sales - Purchases

Purchases from related parties for the nine months ended September 30, 2012 and 2011 are summarized as follows:

	2012		2011	
	Amount	Percentage to Total Purchases	Amount	Percentage to Total Purchases
Shine Tech Ltd.	<u>\$ 85,020</u>	<u>1</u>	<u>\$ 81,726</u>	<u>1</u>

There is no significant difference between related parties and unrelated parties for purchase price.

### Accounts Payable

Accounts payable due to related parties as of September 30, 2012 and 2011 are summarized as follows:

	2012		2011	
	Amount	%	Amount	%
Shine Tech Ltd.	\$ 40,560	2	\$ 28,889	1
Other	<u>8</u>	<u>-</u>	<u>49</u>	<u>-</u>
	<u>\$ 40,568</u>	<u>2</u>	<u>\$ 28,938</u>	<u>1</u>

### Credit Guarantees

See Note 21 to the consolidated financial statements.

Related parties have guaranteed the payments of loans of Phihong as of September 30, 2012 and 2011 were as follows:

Related Parties	Nature	2012	2011
Peter Lin	Long-term debts	<u>\$ 200,000</u>	<u>\$ 200,000</u>

## 20. PLEDGED PROPERTIES

As of September 30, 2012 and 2011, Phihong offered the property, plant and equipment amounted to \$274,604 thousand and \$284,435 thousand as collateral for long term loan.

As of September 30, 2012 and 2011, the following assets of PHA had been pledged to secure PHA's bank loans:

	2012	2011
Accounts receivable	\$ 531,653	\$ 753,013
Inventory	<u>-</u>	<u>703,262</u>
	<u>\$ 531,653</u>	<u>\$ 1,456,275</u>

## 21. COMMITMENTS AND CONTINGENCIES

### Loan Guarantees

As of September 30, 2012, Phihong had guaranteed the US\$6,000 thousand loan of Phihong USA Corp.

## 22. OTHERS

As of September 30, 2012 and 2011, significant foreign currency financial assets and liabilities are as follows:

	2012			2011		
	Foreign Currencies (In Thousands)	Exchange Rate (Note)	New Taiwan Dollars (In Thousands)	Foreign Currencies (In Thousands)	Exchange Rate (Note)	New Taiwan Dollars (In Thousands)
<u>Financial assets</u>						
Monetary items						
USD	\$ 103,315	29.3600	\$ 3,033,328	\$ 91,712	30.4150	\$ 2,789,420
JPY	350,078	0.3777	132,224	324,070	0.3978	128,915
RMB	45,179	4.6266	209,025	45,220	4.7774	216,034
HKD	1,294	3.7865	4,900	24,400	3.9013	95,192
SGD	-	-	-	6,873	23.5600	161,928
<u>Financial liabilities</u>						
Monetary items						
USD	74,210	29.3600	2,178,806	55,617	30.4150	1,691,591
JPY	17,508	0.3777	6,613	12,802	0.3978	5,093
RMB	99,838	4.6266	461,910	127,272	4.7774	608,029
HKD	3,599	3.7865	13,627	17,016	3.9013	66,385

Note: Exchange rate represents the number of N.T. dollars for which one foreign currency could be exchanged.

## 23. OPERATING SEGMENTS

The Company's power supply segment is the only one reportable segment. The power supply segment mainly engages in the manufacturing and selling AC/DC power adapters, charger bases, and power supply modules for computers. The Company also had other operating segments that did not exceed the quantitative threshold so that they are not the reportable segments. These segments mainly engage in manufacturing and selling lighting supply and developing, manufacturing and selling monitors.

The Company took the operating profits as the measurement. There was no material inconsistency between the accounting policies of the operating segment and the accounting policies described in Note 2.

The Company's operating segments information was as follows:

a.

	<u>Segment Revenues</u>		<u>Segment Profit</u>	
	<u>Nine Months Ended</u>		<u>Nine Months Ended</u>	
	<u>September 30</u>		<u>September 30</u>	
	<b>2012</b>	<b>2011</b>	<b>2012</b>	<b>2011</b>
Power supply	\$ 8,315,453	\$ 10,473,942	\$ 556,275	\$ 1,648,357
Others	<u>565,327</u>	<u>548,661</u>	<u>(175,032)</u>	<u>(441,658)</u>
Income from continuing operations	<u>\$ 8,880,780</u>	<u>\$ 11,022,603</u>	381,243	1,206,699
Interest income			12,638	10,197
Investment income recognized under equity method			2,003	16,659
Dividend income			4,927	4,776
Gain on disposal of investment			-	213,370
Gain on reversal of bad debts			20,519	-
Loss on disposal of property, plant and equipment			(17,474)	(10,443)
Foreign exchange gains (losses), net			(63,558)	76,619
Interest expense			(3,069)	(3,023)
Impairment loss			-	(31,969)
Others income			96,234	118,141
Others expenses			<u>(13,867)</u>	<u>(31,670)</u>
Income before income tax			<u>\$ 419,596</u>	<u>\$ 1,569,356</u>

b. Segment assets and liabilities

	<u>September 30</u>	
	<b>2012</b>	<b>2011</b>
Power supply segment assets	\$ 1,787,336	\$ 2,033,789
Other assets	<u>7,750,583</u>	<u>8,550,730</u>
	<u>\$ 9,537,919</u>	<u>\$ 10,584,519</u>
	<b>2012</b>	<b>2011</b>
Power supply segment liabilities	\$ 1,965,071	\$ 1,942,777
Other liabilities	<u>1,749,565</u>	<u>2,149,004</u>
	<u>\$ 3,714,636</u>	<u>\$ 4,091,781</u>