TSE: 2412
NYSE: CHT

中華電信
Chunghwa Telecom

Annual Report 2006

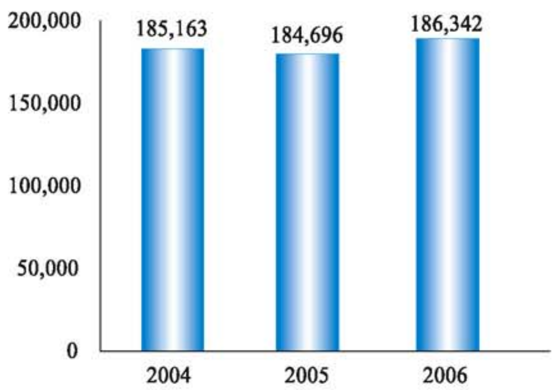
CHT annual report is available at http://www.cht.com.tw/ir
Taiwan Stock Exchange Market Observation Post System http://mops.tse.com.tw

Printed on March 31, 2007

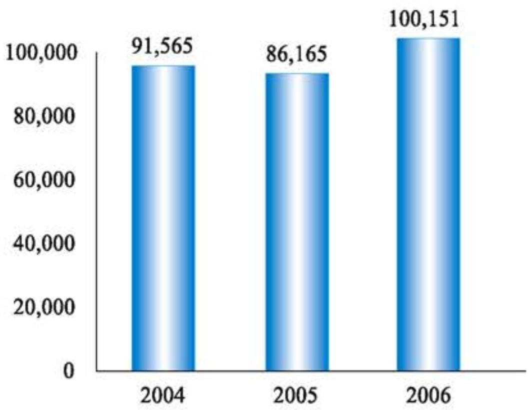
The harvest is ready for sharing…

OPERATING AND FINANCIAL SUMMARY

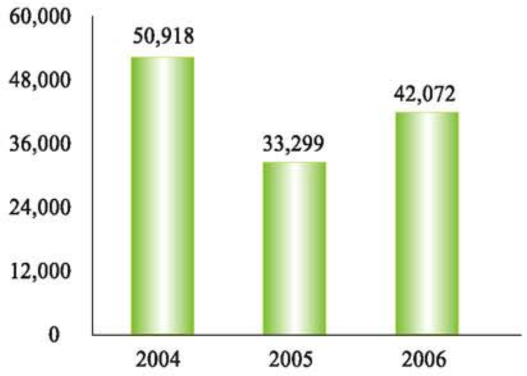
Revenues (in millions NT$)



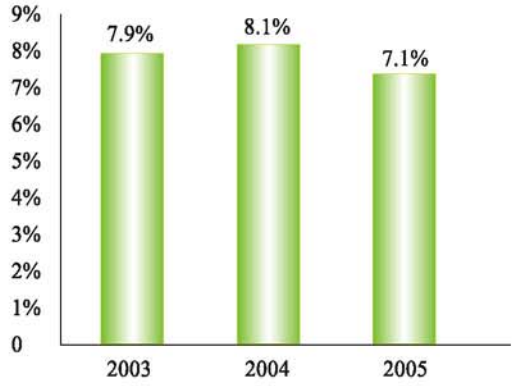
Operating Cash Flow (in millions NT$)



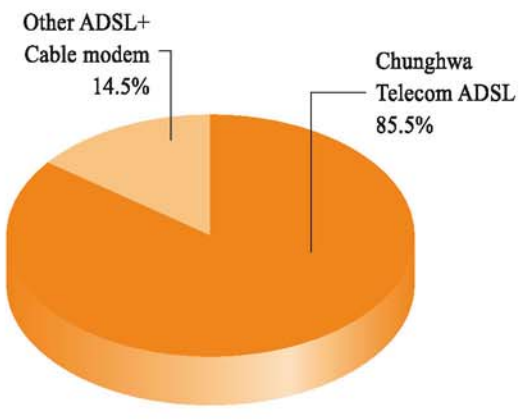
Net Income (in millions NT$)



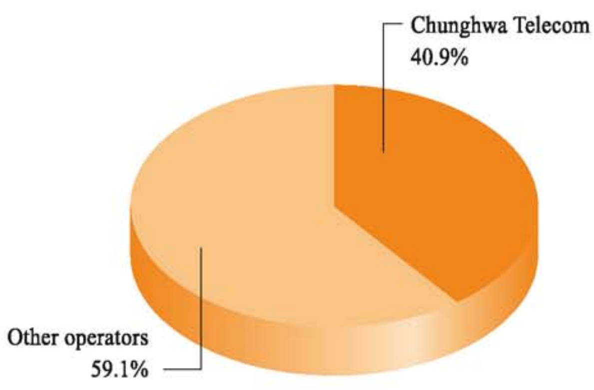
Dividend Yield



Broadband Market Share



Mobile Subscriber Market Share



Source : Ministry of Transportation and Communications
Note : Figures shown as of Dec. 2006

LETTER TO SHAREHOLDERS

To All Our Shareholders:

Thank you for your continued support of Chunghwa Telecom. 2006 marked the first full year in which Chunghwa Telecom Co., Ltd. operated as a private company. As a result of our privatization, we have not only repositioned our business to become more specialized and flexible, but have also executed a series of integration initiatives designed to streamline our operations. As a result, we have allocated our human resources more efficiently while expanding our business through strategic alliances and investments, leading to a new era of sustained growth built upon our core business.

At the same time, we have continued our commitment to our shareholders. In addition to our high dividend distribution policy, we have augmented our capital structure and shareholder returns through a share repurchase. In February 2006, we repurchased 192 million common shares, representing 1.99% of outstanding shares, all of which were cancelled in June. Our performance was recognized by *Finance Asia* (a leading Asian Finance magazine), which awarded Chunghwa Telecom the "Best Managed Company" and "Best Commitment to Strong Dividends" distinctions, in each case ranking Chunghwa Telecom first among all Taiwan telecommunications operators. Furthermore, at the end of September 2006, with the participation of leading domestic and international capital markets players, Chunghwa Telecom assisted its largest shareholder in successfully completing the third concurrent offering of its Chunghwa Telecom shares at home and abroad. This action enabled a broader group of global investors to benefit from the value that we are generating for our shareholders and furthered our efforts to make Chunghwa Telecom a truly global brand name.

Superior Financial Performance

Despite increasingly intense market competition, our employees' concerted efforts drove Chunghwa Telecom's 2006 fiscal year operating results to remarkable levels. Under US GAAP, we generated a total consolidated annual revenue of NT$186.34 billion, net income of NT$42.07 billion and earnings per share (EPS) of NT$4.34. In March 2006, we were ranked Number 471 on the "Forbes Global 2000", *Forbes* magazine's comprehensive list of the world's largest and most powerful companies; we were Number 5 among all Taiwan companies and Number 29 among all telecommunications operators worldwide.

Our significant revenue growth during the year was coupled with an intense focus on cost control. In March 2006, we conducted an early retirement program expected to reduce personnel cost for the following years. We have prudently designed investment strategies to pursue growth opportunities and controlled capital expenditure to reduce the depreciation and amortization expense year by year.

Sound Business Structure

2006 was a year full of challenges for the Taiwan telecommunications industry; and for the wireless business in particular. With the debut of the 3G (third generation cellular network) market and "Mobile Number Portability" services, operators launched new services and price plans concurrently, creating a more competitive environment and tightening relative growth opportunities. Despite this severe competitive environment, our mobile operations outperformed our competitors in Taiwan mobile market. Fortunately, our Internet and data business has continued to generate outstanding operational results. The launch of faster and more stable broadband access services has enabled us to adopt various bundling options for value-added services, making the Internet and data business a key growth driver for Chunghwa Telecom. The proportion of total revenue attributable to the wireless and Internet and data businesses increased to 64.8% in 2006 from 62.8% in 2005. At the same time, we are committed to developing fixed-line value-added services and have launched a wide variety of bundled and promotional packages to help extract more value out of this segment of our business.

Chunghwa Telecom continues to play a leading role in the telecommunications services market based on its superior network and high-quality service. At the end of fiscal 2006, our market share for local calls, wireless, ADSL and HiNet was 97.4%, 36.5%, 85.5% and 61.2%, respectively. In 2006, we were able to grow our wireless and broadband customer bases by 4.0% and 9.9%, respectively, demonstrating the power of the Chunghwa Telecom brand among new and existing customers alike. Our brand equity was endorsed further with the receipt of the *Reader's Digest* "Trusted Brand" Platinum Award for the telecommunications services category for the fourth year in a row.

Dual-Core Strategy

Chunghwa Telecom constantly strives to achieve "total customer satisfaction." We have created a dual-core strategy focusing on both digital entertainment services for individuals and families as well as information and communication integration upgrade services for corporate customers. By making full use of our position as an integrated telecommunications operator with specializations in three telecommunications areas (i.e., fixed-line, wireless and Internet and data), and by leveraging our advanced technology platform, integrated resources and valuable strategic alliances, Chunghwa Telecom provides exceptional service to the general public and has become a business partner for a large number of enterprises.

■ Individuals and Families

As the overall voice market becomes more saturated, the 3G service has opened another channel for revenue growth for telecommunications operators. Through our exclusive emome cellular value-added platform integrating various multimedia content services, and the provision of 384Kbps to 3.6Mbps high speed wireless Internet access utilizing the characteristics of the high 3G bandwidth, we have made it possible for individuals and families to experience the high-speed fun of "wireless life." With our customer base exceeding 943,000 at the end of 2006, Chunghwa ranks No. 1 among the 3G services operators over the same period.

We have also introduced diversified fixed-line and broadband value-added services based on our existing infrastructure. Customers are enjoying a more diversified and interactive suite of telecommunications services such as our personal ring back tones, local attractions directory assistance services (dial 1288), Xuite individual integrated Internet services and MOD service.

Since Chunghwa Telecom joined the Global Business Dialogue on e-Business (GBDe) in 2004, we have been committed to promoting information society policy and developing digital transaction security. In 2006, we were pleased to be appointed the overall Chair of the GBDe. The Company also has chaired the interest group in developing and establishing an International Micropayment Service System, which provides a more convenient, safe and secure global e-Commerce environment by integrating customer identification and authentication with a bill generating system.

■ Corporate Customers

With expectations of a growing corporate customer market, Chunghwa Telecom has been actively expanding the application integration of its telecommunications network and information technology, providing information and communication technologies (ICT) services with its leading telecommunications expertise and extensive information system development capacity. In addition to the provision of mobilized custom integration solutions and the setup of a seamless and exclusive communication network, we cooperated with a handset manufacturer to launch customized cellular phones: the CHT9000 and CHT9100 were launched in July and December of 2006. Each model was supplied with our unique mPro value-added service, featuring mobile office functionalities such as push mail, calendar, to-do list, remote sync and RSS real-time information subscription services.

As for the opening of emerging telecommunications markets, Asian countries, including mainland China, India, Thailand, Indonesia and Vietnam, have experienced sustained and rapid economic growth year after year, as well as significant increases in bandwidth demand. To maximize this business opportunity, we have expanded our APCN2 capacity investment and private submarine cable procurement in order to establish a robust backbone network. This network will serve as an interconnection platform among telecommunications operators in key Asia Pacific countries, such as Taiwan, Japan, Korea, China, Hong Kong, Malaysia, Singapore and the Philippines. Chunghwa Telecom has also invested in submarine cable networks (such as TPE, JP-US and TGNP) aimed at establishing a transit center between Southeast Asian countries and the United States to facilitate further development of communications in the region.

In order to meet the needs of Taiwanese enterprises tapping overseas markets, Chunghwa Telecom established a footprint in Shanghai and a representative office in Ho Chi Minh City, Vietnam in 2006, assisting in offering total solutions for our overseas enterprise customers. Additionally, Chunghwa Telecom continues to build its global network, with the establishment of more than 20 new POPs in 2006, enabling corporate customers to operate global businesses from Taiwan.

Solid Organization and Allied Partnership

■ Organizational Reform

In order to strengthen its core operations, Chunghwa Telecom successfully integrated its internal engineering and business resources in 2006 and actively aligned its organizational structure to allow for a greater focus on our customers.

In January 2007, Chunghwa Telecom established its Enterprise Business Group; this group's team is focused on providing the best service to corporate customers, with customized solutions and professional consulting. We also established a Customer Service Department, which aims to convert our customer service system into a comprehensive, interactive and multimedia call center.

In line with our corporate goal of divesting non-core businesses, in January 2007, Chunghwa Telecom spun off the Telephone Directory Department from its Data Communications Business Group, establishing Chunghwa International Yellow Pages Corporation. This company aims to convert the conventional yellow page business into a cross-platform search service by strengthening functionalities of the online yellow page (hiPage) and telephone directory services. The new subsidiary will also expand its scope of business by exploring the growth opportunities offered by professional advertisements.

■ Investment and Strategic Alliances

To address the liberalization of the telecommunications market and both downstream and upstream industrial integration while maintaining our focus on our core telecommunications business, Chunghwa Telecom has been actively cooperating with its alliances to seek new business opportunities with growth potential. Furthermore, in August 2006, the Company set up an Investment Department to strengthen its investment interests and property development.

In order to expand our Internet data center (IDC) business and enhance our cooperation with international telecommunications operators, Chunghwa Telecom acquired a 70% equity interest in Chief Telecom, a neutral aggregator in the telecommunications and information industries, which provides telehousing and bandwidth exchange services. This acquisition will complement Chunghwa's business offerings in overseas markets. Moreover, we invested in Spring House Entertainment Inc., a long term partner of content providers, to introduce its shared technology to our Xuite service, as well as redesign our emome platform and incorporate the spirit of Web 2.0 into the creation of value-added content. Further, after evaluation of potential channel distribution partners, an important part of our expansion plan, we became a controlling shareholder of Senao International Co., by way of participating in a public tender offer. By using Senao's expertise and experience in handset distribution, channel development and logistics management, Chunghwa expects to enhance its comprehensive operational efficiency, promotion of the value-added services, and expansion of demographics of the youngsters.

Chunghwa Telecom also launched land revitalization initiatives in order to effectively increase the value of its property management activities. In the first phase, we selected six lots across Taiwan and worked with real estate developers to develop plans for high-tech residences, business offices and resort hotels for sale or lease. Next, we plan to establish a new subsidiary specializing in property development and management. With its professional expertise and focused operations, we expect to open a new avenue for our revenue streams.

Regulatory Environment

There were substantial Taiwan telecommunications regulatory reforms in 2006. Established in February 2006 as the regulator for both the telecommunications and media industries, with the aim of facilitating effective competition in the convergence of telecommunications and media, the National Communications Commission (NCC) has enacted and adjusted a number of operation rulings and measures. These operation rulings and measures of course would have certain impact on our business; however, we have been adjusting our business strategies and expect to minimize its impact.

Corporate Governance

Chunghwa Telecom has always been committed to implementing strong corporate governance and controls, and has consistently been recognized for its efforts. In August 2006, the Securities and Futures Institute published the third information transparency and disclosure ranking results. Among 1,032 companies that were assessed, Chunghwa was awarded the highest honor, A+, with 11 other companies. In March 2007, we were granted our second consecutive CG6002 Certificate by the Corporate Governance Association in Taiwan. These accolades are the result of our continuous dedication to best practice corporate governance. Meanwhile, given the more complicated market and technology environments in which we operate, we formulated a risk management policy to establish a concrete roadmap for the most appropriate and effective risk control management procedures.

Corporate Social Responsibility

It has been ten years since Chunghwa Telecom was divested from the Directorate General of Telecommunications. Since then, the most important thing for Chunghwa has been to maximize value for its shareholders, customers and employees. In addition to our business operations, we also place great importance on corporate social responsibility.

In February 2006, following our privatization, we set up the Chunghwa Telecom Foundation, an organization focused on bridging the digital divide, assisting local cultural assets and cultivating community life. In June 2006, we established the Chunghwa Telecom Corporate Social Responsibility Committee, the aim of which is to extend the areas of corporate social responsibility to our customers, employees, shareholders, partners and suppliers; we aim to leverage the strength of our human resources and technology to implement our mission and commitment as a leader in corporate social responsibility. Our performance in this area recently earned us a spot on the 2007 *CommonWealth* magazine annual survey of the Top 50 companies with Excellence in Corporate Social Responsibility.

Prospects for the Future – Converged Services

While technology evolution and market competition present sector-wide challenges, we expect to derive further growth opportunities from digital convergence and the increasing bandwidth demand resulting from comprehensive multimedia applications. We will not only continue to enhance 3G services and promotions, accelerate the progress of broadband upgrade, improve ICT service offerings, and create the MOD open platform, but also enter into strategic alliances to integrate upstream and downstream resources, establish a global arrangement to explore business opportunities, and encourage innovative research and development. We commence the migration to the Next Generation Network (NGN) in 2007, meeting our customers' needs for integrated fixed-line and mobile services, and aiming to become the leading provider of digital converged services in Taiwan.

Our NGN plan includes FTTB deployment, PSTN to IP network migration and optical transport and IP backbone network integration. By utilizing the high bandwidth capacity of the fiber network to enable voice, video and data to fully integrate with real-time, interactive and on-demand functionalities, we believe this transition will not only improve overall operational efficiency while reducing operating costs, but also produce further opportunities for broadband applications such as MOD, HDTV, home surveillance, corporate high speed network connections and VPN services, resulting in our continued market leadership position and a blueprint for a new era in network integration.

Converged services and network integration are the newest telecommunications industry trends. With our dominant local and cellular market positions, quality fixed-line and cellular networks, and advanced telecommunications technologies, Chunghwa Telecom is in the best position to drive Fixed Mobile Convergence (FMC) services. After obtaining permissions from regulatory authorities, we will gradually integrate our fixed and cellular network resources, creating synergies by launching various new services, such as the integration of terminal devices (dual-mode handsets), service accounts, and other value-added services. Ultimately, we will fully integrate the core network in accordance with the migration of the NGN network, making it both convenient and economical for customers to enjoy fixed and mobile services with one single mobile terminal device.

As we look forward to the 2007 fiscal year, we are focused on growing our businesses with professional and focused operations, best-in-class customer service and corporate governance, and efficient capital management and cost controlling measures. With the continued support of all our shareholders, employees, customers and partners, we believe that Chunghwa Telecom will further its leading position in the industry and continue to create value for our shareholders.

Tan Ho Chen
Chairman & CEO

Shyue-Ching Lu
President

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

We have made forward-looking statements in this annual report. These forward-looking statements contain information regarding, among other things, our financial condition, future expansion plans and business strategy. The words “believe” ”expect” “estimate” “intend” “plan” “seek” “will” “shall” and other similar words identify forward-looking statements. We have based these forward-looking statements on our current expectations and projections about future events. Although we believe that these expectations and projections are reasonable, such forward-looking statements are inherently subject to risks, uncertainties and assumptions.

MEMO

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 20-F

(Mark One)

☐ **Registration statement pursuant to Section 12(b) or 12(g) of the Securities Exchange Act of 1934**

or

☒ **Annual report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the fiscal year ended *December 31, 2006*

or

☐ **Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the transition period from to

or

☐ **Shell company report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
Date of event requiring this shell company report

Commission file number 001-31731

Chunghwa Telecom Co., Ltd.
(Exact Name of Registrant as Specified in Its Charter)

Taiwan, Republic of China
(Jurisdiction of Incorporation or Organization)

**21-3 Hsinyi Road, Section 1, Taipei,
Taiwan, Republic of China**
(Address of Principal Executive Offices)

Securities registered or to be registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Common Shares, par value NT$10 per share	New York Stock Exchange*
American Depositary Shares, as evidenced by American Depositary Receipts, each representing 10 Common Shares	New York Stock Exchange

Securities registered or to be registered pursuant to Section 12(g) of the Act:
None

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act:
None

Indicate the number of outstanding shares of each of the Issuer's classes of capital or common stock as of the close of the period covered by the annual report.

9,667,845,093 Common Shares
307,398,771 American Depositary Shares

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☒ No ☐

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934. Yes ☐ No ☒

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ☒ Accelerated filer ☐ Non-accelerated filer ☐

Indicate by check mark which financial statement item the registrant has elected to follow. Item 17 ☐ Item 18 ☒

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Securities Exchange Act of 1934). Yes ☐ No ☒

* Not for trading, but only in connection with the listing on the New York Stock Exchange of the American Depositary Shares

CHUNGHWA TELECOM CO., LTD.

FORM 20-F ANNUAL REPORT

FISCAL YEAR ENDED DECEMBER 31, 2006

TABLE OF CONTENTS

SUPPLEMENTAL INFORMATION

All references to "we," "us," "our" and "our company" in this annual report are to Chunghwa Telecom Co., Ltd. All references to "shares" and "common shares" are to our common shares, par value NT$10 per share, and to "ADSs" are to our American depositary shares, each of which represents ten of our common shares. The ADSs are issued under the deposit agreement, as amended, supplemented or modified from time to time, dated as of July 17, 2003, among Chunghwa Telecom Co., Ltd., The Bank of New York, as depository, and the holders and beneficial owners from time to time of American Depositary Receipts issued thereunder. All references to "Taiwan" are to the island of Taiwan and other areas under the effective control of the Republic of China. All references to "the government" or "the Republic of China government" are to the government of the Republic of China. All references to the "Ministry of Transportation and Communications" are to the Ministry of Transportation and Communications of the Republic of China. All references to the "Securities and Futures Bureau" are to the Securities and Futures Bureau of the Republic of China or its predecessors, as applicable. "ROC GAAP" means the generally accepted accounting principles of the Republic of China, and "US GAAP" means the generally accepted accounting principles of the United States. Any discrepancies in any table between totals and sums of the amounts listed are due to rounding. Unless otherwise indicated, or the context otherwise requires, references in this annual report to financial and operational data of the Company for a particular year refer to the fiscal year of the Company ending December 31 of that year.

When we refer to our "privatization" or our being "privatized" in this annual report, we mean our status as a non-state-owned entity after the government reduced its ownership of our outstanding common shares, including our common shares owned by entities majority-owned by the government, to less than 50%. We were privatized in August 2005.

We publish our consolidated financial statements in New Taiwan dollars, the lawful currency of the Republic of China. In this annual report, "NT$" and "NT dollars" mean New Taiwan dollars, "$," "US$" and "U.S. dollars" mean United States dollars.

FORWARD-LOOKING STATEMENTS IN THIS ANNUAL REPORT MAY NOT BE REALIZED

This annual report contains forward-looking statements, including statements regarding:

- our business and operating strategy;
- our network expansion plans;
- our business, operations and prospects;
- our financial condition and results of operations;
- our dividend policy;
- the telecommunications industry regulatory environment in Taiwan; and
- future developments in the telecommunications industry in Taiwan.

These forward-looking statements are generally indicated by the use of forward-looking terminology such as "believe," "expect," "anticipate," "estimate," "plan," "project," "may," "will" or other similar words that express an indication of actions or results of actions that may or are expected to occur in the future. These statements are subject to risks, uncertainties and assumptions, many of which are beyond our control. You should not place undue reliance on these statements, which apply only as of the date of this annual report. These forward-looking statements are based on our own information and on information from other sources we believe to be reliable. Actual results may differ materially from those expressed or implied by these forward-looking statements. Factors that could cause differences include, but are not limited to, those discussed under "Item 3. Key Information—D. Risk Factors." In light of these risks, uncertainties and assumptions, the forward-looking events discussed in this annual report might not occur and our actual results could differ materially from those anticipated in these forward-looking statements. We undertake no obligation to update or revise any forward-looking statements whether as a result of new information, future events or otherwise.

PART I

ITEM 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS

Not applicable.

ITEM 2. OFFER STATISTICS AND EXPECTED TIMETABLE

Not applicable.

ITEM 3. KEY INFORMATION

The Company was privatized as a result of a secondary ADR offering and concurrent domestic auction of our common shares on August 12, 2005. The privatization has enabled us to develop our business and respond to changing market conditions more rapidly and efficiently.

A. Selected Financial Data

The selected income statement data and cash flow data for the years ended December 31, 2004, 2005 and 2006, and the selected balance sheet data as of December 31, 2005 and 2006, set forth below have been prepared in accordance with US GAAP and are derived from our audited consolidated financial statements included elsewhere in this annual report and should be read in conjunction with, and are qualified in their entirety by reference to our consolidated financial statements and the related notes. The selected income statement and cash flow data for the years ended December 31, 2002 and 2003, and the selected balance sheet data as of December 31, 2002, 2003 and 2004 set forth below are derived from our audited consolidated financial statements not included in this annual report.

	As of or for the year ended December 31,					
	2002(1)	2003(1)	2004(1)	2005(1)	2006	
		(in billions, except per share and per pro forma ADS information)				
	NT$	NT$	NT$	NT$	NT$	US$
Income Statement Data:						
Revenues	179.4	182.5	185.2	184.7	186.3	5.7
Operating costs and expenses:						
Costs of revenues(2)	56.6	58.3	58.7	68.1	62.6	1.9
Marketing(2)	20.2	20.0	19.3	23.7	20.6	0.6
General and administrative(2)	2.6	2.7	2.5	3.5	3.3	0.1
Research and development(2)	2.4	2.6	2.5	3.1	2.8	0.1
Depreciation and amortization—costs of revenues	37.9	39.2	38.4	38.8	38.4	1.2
Depreciation and amortization—operating expenses	2.4	2.4	2.3	2.4	2.3	0.1
Total operating costs and expenses	122.1	125.2	123.7	139.6	130.0	4.0
Operating income	57.3	57.3	61.5	45.1	56.3	1.7
Other income(3)	0.7	0.8	1.1	2.0	1.6	0.1
Other expenses(4)	1.1	0.5	0.4	1.1	0.5	0.0
Income before income tax and minority interest	56.9	57.6	62.2	46.0	57.4	1.8
Income tax	12.8	10.3	11.3	12.7	15.3	0.5
Income before minority interest	44.1	47.3	50.9	33.3	42.1	1.3
Minority interest	—	—	—	—	0.013	—
Net income	44.1	47.3	50.9	33.3	42.1	1.3
Net income per share(5)	4.48	4.81	5.18	3.39	4.34	0.13
Net income per pro forma equivalent ADS(6)	44.82	48.10	51.76	33.85	43.43	1.33

	As of or for the year ended December 31,					
	2002[1]	2003[1]	2004[1]	2005[1]	2006	
	(in billions, except per share and per pro forma ADS information)					
	NT$	NT$	NT$	NT$	NT$	US$
Balance Sheet Data:						
Cash and cash equivalents	7.7	13.6	29.3	41.9	70.7	2.2
Property, plant and equipment—net	338.4	329.7	311.6	293.5	277.4	8.5
Total assets[7]	428.6	429.7	438.4	395.2	398.8	12.2
Total debt	17.7	0.7	0.7	0.5	0.4	0.0
Total liabilities[7]	128.6	118.9	119.7	67.4	78.6	2.4
Minority interest	—	—	—	—	0.1	0.0
Capital stock	96.5	96.5	96.5	96.5	96.7	3.0
Total stockholders' equity[7]	300.0	310.8	318.7	327.8	320.1	9.8
Cash Flow Data:						
Net cash provided by operating activities	91.3	93.6	91.6	86.2	100.1	3.1
Net cash used in investing activities	(55.3)	(32.2)	(32.4)	(28.0)	(19.1)	(0.6)
Net cash used in financing activities	(33.0)	(55.5)	(43.4)	(45.6)	(52.2)	(1.6)

	As of or for the year ended December 31,					
	2002	2003	2004	2005	2006	
	(in billions, except per share and per pro forma ADS information)					
	NT$	NT$	NT$	NT$	NT$	US$
Capital expenditures	43.3	32.2	22.9	22.9	27.7	0.8
Dividends:						
Cash dividends declared per share	4.00	4.50	4.70	4.30	—[8]	—[8]
Stock dividends declared per share	—	—	—	0.20	—[8]	—[8]

(1) Certain items have been reclassified in 2005 and prior years to conform to the presentation in 2006.
(2) Excludes related depreciation and amortization which is presented separately.
(3) Includes interest income of NT$187 million, NT$100 million, NT$224 million, NT$452 million and NT$804 million (US$25 million) for the years ended December 31, 2002, 2003, 2004, 2005 and 2006, respectively.
(4) Includes interest expense of NT$171 million, NT$43 million, NT$5 million, NT$2 million and NT$6 million (US$0.2 million) for the years ended December 31, 2002, 2003, 2004, 2005 and 2006, respectively.
(5) Net income per share is the same on both a basic and a diluted basis.
(6) Each equivalent ADS represents ten of our common shares.
(7) As of December 31, 2006, we adopted SFAS 158 "Employers' Accounting for Defined Benefit Pensions and Other Postretirement Benefits" and recorded the under-funded status of our defined benefit pension plan as a liability of NT$3.34 billion (US$0.1 billion) with a corresponding offset, net of taxes, to deferred income tax assets of NT$1.08 billion (US$0.03 billion) and accumulated other comprehensive income within stockholders' equity of NT$2.26 billion (US$0.07 billion).
(8) Dividends for 2006 are expected to be declared at our 2007 annual general shareholders' meeting scheduled for June 2007.

Currency Translations and Exchange Rates

In portions of this annual report, we have translated New Taiwan dollar amounts into U.S. dollars for the convenience of readers. The rate we used for the translations was NT$32.59 = US$1.00, which was the noon buying rate in the City of New York for cable transfers of New Taiwan dollars as certified for customs purposes by the Federal Reserve Bank of New York on December 29, 2006. This translation does not mean that New

Taiwan dollars could actually be converted into U.S. dollars at that or any other rate or at all. The following table shows the noon buying rates for New Taiwan dollars expressed in New Taiwan dollar per US$1.00.

Year Ended December 31,	Average(1)	High	Low	At Period End
2001	33.91	35.13	32.23	35.00
2002	34.53	35.16	32.85	34.70
2003	34.40	34.98	33.72	33.99
2004	33.37	34.16	31.74	31.74
2005	32.13	33.77	30.65	32.80
2006	32.51	33.31	31.28	32.59
October	33.19	33.31	33.05	33.26
November	32.81	33.16	32.49	32.35
December	32.51	32.74	32.27	32.59
2007				
January	32.77	32.99	32.38	32.95
February	32.97	33.08	32.90	32.98
March	33.06	33.13	32.84	33.01
April (through April 20)	33.11	33.16	33.05	33.15

Source: Federal Reserve Statistical Release, Board of Governors of the Federal Reserve System.

(1) Annual averages are calculated using the average of the exchange rates on the last day of each month during the period. Monthly averages are calculated using the average of the daily rates during the relevant period.

B. Capitalization and Indebtedness

Not applicable.

C. Reasons for the Offer and Use of Proceeds

Not applicable.

D. Risk Factors

Our business and operations are subject to various risks, many of which are beyond our control. If any of the risks described below actually occurs, our business, financial condition or results of operations could be seriously harmed.

Risks Relating to Our Company and the Taiwan Telecommunications Industry

We were privatized in August 2005, so we have a limited history of operations as a non-state-owned enterprise. We may not enjoy the benefits of privatization as quickly as we anticipate or at the level that we expect.

Before we were privatized in August 2005, our business and operations were subject to extensive regulation under Republic of China laws, rules and regulations applicable to state-owned enterprises. As a result, we only have a very limited history of operations as a non-state-owned enterprise. We cannot assure you that we will be successful in achieving the benefits we expect from our privatization, such as increased management flexibility in implementing measures to improve our cost structure, efficient operations of our business and expansion into new businesses in a timely manner or at all. Factors that may cause the actual benefits we may enjoy from privatization to deviate from our expectations include:

- adverse developments in our relations with our labor union that affect our costs, including with respect to compensation and other benefits, and efficient management of our workforce;
- increased costs with respect to our plans to incentivize employees through contributions to employee child education funds, performance-based cash bonuses and company subsidized purchases by employees of our common shares;

- changes in regulations affecting us following our privatization; and
- the speed with which we are able to implement more efficient procurement and other management systems, and the resulting levels of cost savings.

Extensive regulation of our industry may limit our flexibility to respond to market conditions and competition, and our business may suffer.

As a telecommunications service provider in Taiwan, we are subject to extensive regulation. Any changes in the regulatory environment applicable to us may adversely affect our business, financial condition and results of operations.

Prior to March 1, 2006, we were under the supervision of the Ministry of Transportation and Communications and the Directorate General of Telecommunications. On March 1, 2006, the National Communications Commission was formed in accordance with the National Communications Commission Organization Law, or Organization Law, which was intended to transfer regulatory authority over the Taiwan telecommunications industry from the Ministry of Transportation and Communications and the Directorate General of Telecommunications to the National Communications Commission.

The National Communications Commission is currently comprised of nine commissioners who have been recommended by the government and opposition political parties in the Legislative Yuan, as well as recommended by the Executive Yuan and approved by the Legislative Yuan. However, the Executive Yuan considered the composition of the National Communications Commission unconstitutional and petitioned the Grand Justices of the Republic of China, or the Grand Justices, to interpret the constitutionality of the formation of the National Communications Commission and the procedure for nominating commissioners to serve on the National Communications Commission. On July 21, 2006, the Grand Justices rendered an interpretation and held that the relevant provisions under the Organization Law as to the nomination procedures for the commissioners of the National Communications Commission were unconstitutional. However, the Grand Justices granted a grace period allowing such provisions of the Organization Law to remain in effect until December 31, 2008. Consequently, the National Communications Commission will have the authority at least until the end of 2008. As of the date of this annual report, the Ministry of Transportation and Communications is responsible for determining the policies for the telecommunications industry while the National Communications Commission is responsible for supervising the telecommunications industry and maintaining fair competition. Any changes in the regulatory environment applicable to us may adversely affect our business, financial condition and results of operations.

We have been designated by the government as a dominant provider of fixed line and cellular services within the meaning of applicable telecommunications regulations, and as a result, we are subject to special additional requirements imposed by the National Communications Commission. For example, the regulation governing setting and changing of tariffs allows non-dominant telecommunications service providers greater freedom to set and change tariffs within the range set by the government. If we are unable to respond effectively to tariff changes by our competitors, then our competitiveness, market position and profitability will be materially and adversely affected. We were subject to the Statute of Chunghwa Telecom Co., Ltd. prior to our privatization. Although we have been privatized, the Legislative Yuan has not yet abolished the Statute of Chunghwa Telecom Co., Ltd., and at this time, the Statute of Chunghwa Telecom Co., Ltd. is still applicable to us. Under the Statute of Chunghwa Telecom Co., Ltd., the Ministry of Transportation and Communications has the authority to regulate aspects of our business. Any such regulation could be burdensome or conflict with regulations of the National Communications Commission or may otherwise adversely affect our business, financial condition and results of operations.

The regulatory framework within which we operate may limit our flexibility to respond to market conditions, competition or changes in our cost structure. In particular, future decreases in tariff policies and rates could immediately and substantially decrease our revenues. In particular, as a Type I service provider under the

Telecommunications Act, we are constrained in our ability to raise tariffs. Furthermore, the National Communications Commission adopted a price reduction plan on December 12, 2006 and is considering a number of changes to the tariff structures relating to our local telephone, cellular and leased line services. See "Item 5 Operating and Financial Review and Prospects—Overview—Tariff Adjustments".

In addition, we operate our businesses with approvals and licenses granted by the government. If these approvals or licenses are revoked or suspended or are not renewed, or if we are unable to obtain any additional licenses that we may need to operate or expand our business in the manner we desire, then our financial condition and results of operations, as well as our prospects, will suffer. For example, in April 2007, the National Communications Commission began to accept license applications according to the Regulation Governing the Worldwide Interoperability for Microwave Access, or WiMAX, and announced that it planned to issue six WiMAX licenses. WiMAX is a standards-based technology providing high-speed mobile data and telecommunications services and enabling wireless delivery of last mile broadband access as an alternative to cable and digital subscriber line. We may be unable to obtain a WiMAX license that we may need to provide the next generation telecommunication services.

Increasing competition resulting from the ongoing liberalization of the Taiwan telecommunications industry or from alternative means of communication may materially and adversely affect our growth and profitability by causing us to lose customers, charge lower tariffs or spend more on marketing.

We have faced increasing competition from new entrants in the Taiwan telecommunications market in recent years. In particular, multiple licenses to operate fixed line, cellular, paging and other services have been issued by the Republic of China government since 1996. Furthermore, three additional operators began providing fixed line services in June 2001, and licenses were granted to four undersea cable operators to engage in the undersea cable leased-circuit business in August 2001. In addition, the government awarded third generation, or 3G, cellular services concessions to five companies in February 2002, including two new cellular operators. Since early 2004, the government has also issued four mobile virtual network operator licenses that allow operators without a spectrum allocation to provide cellular services by leasing the network capacity and facilities from a licensed cellular service provider.

We also face increased competition from local loop unbundling. We first entered into agreements regarding local loop unbundling of voice with New Century InfoComm Tech. Co., Ltd., or Sparq, in March 2004, and with Taiwan Fixed Network and Asia Pacific Broadband Telecom in May 2004. We subsequently entered into an agreement for full local loop unbundling of both voice and data with Sparq in July 2005. In January 2007, the National Communications Commission requested each dominant integrated services operator, including us, to reserve fifteen percent of its local loop for leasing to other service operators unless the then remaining available local loop of the operator not leased out is less than fifteen percent, in which case the operator should reserve such remaining loop. In addition, the National Communications Commission had defined the local loop as facilities "at the bottleneck of telecommunications networks" in accordance with the Regulations Governing Fixed Network Telecommunications Businesses The National Communications Commission further amended the Administrative Rules for Network Interconnection Between Telecommunication Service Providers in April 2007 which provides that we can only charge other local telephone service providers at cost for local loop services instead of on the basis of commercial negotiations.

Many of our competitors are in alliances with leading international telecommunications service providers and have access to financial and other resources or technologies that may not be available to us. Moreover, as the government continues to liberalize the telecommunications market, such as through the issuance of new licenses or establishment of additional networks, our market position and competitiveness could be materially and adversely affected.

In addition, the focus of competition among cellular service providers in Taiwan has been shifting, as companies that traditionally offered second generation services, such as us, began offering 3G services, and as new 3G service providers started to enter the market. As a result, we expect competition in 3G services to continue to intensify. We may also be subject to competition from providers of new telecommunications services as a result of technological development and the convergence of various telecommunications services. In particular, as a result of technological innovations and other factors, we have been facing competition from alternative means of communication, including voice over internet protocol, or VoIP, high-speed cable internet service, cable telephony, e-mail and wireless services. Providers of these products and services include cable television companies, direct broadcast satellite companies and digital subscriber line, or DSL, resellers.

Increasing competition may also cause the rate of our customer growth to reverse or decline, bring about further decreases in tariff rates and necessitate increases in our selling and promotional expenses. Any of these developments could materially and adversely affect our business growth and profitability, as well as our financial condition and results of operations.

If we fail to maintain a good relationship with our labor union, work stoppages or labor unrest could occur and the quality of our services as well as our reputation could suffer.

As of the date of this annual report, almost all of our employees were members of our principal labor union. Since our incorporation in 1996, we have experienced disputes with our labor union on such issues as employee benefits and retirement benefits in connection with our privatization as well as the right to protest. In particular, our labor union initiated a demonstration in August 2000 to express concerns over job security after our privatization. Furthermore, following our failure to sign the collective agreement proposed by the labor union, the union resolved on December 5, 2004 to hold strikes anytime before our privatization. In response to our proposed privatization, the labor union held a strike on May 17, 2005. The labor union also strongly opposed our privatization and has threatened to launch a nationwide strike or take other forms of action to hinder our privatization. In addition, one of our directors has been designated by the Republic of China government as a labor union representative on our board. Any deterioration of our relationship with our labor union could result in work stoppages, strikes or threats to take such an action, which could disrupt our business and operations, and materially and adversely affect the quality of our services and harm our reputation. The latest collective bargaining agreement, which was entered into between us and our labor union on January 6, 2006 and commenced in effect from March 3, 2006, will result in us having to incur higher costs in connection with the implementation of certain incentive programs, including employee skill development programs, as well as employee child education funds, company subsidized share purchases by employees, and discretionary, performance-based cash bonuses. We cannot accurately quantify the increase in costs at this time, but we expect that it may be material.

Changes in technology may render our current technologies obsolete or require us to obtain licenses for introducing new services or make substantial capital investments, financing for which may not be available to us on favorable commercial terms.

The Taiwan telecommunications industry has been characterized by rapid increases in the diversity and sophistication of the technologies and services offered. As a result, we expect that we will need to constantly upgrade our telecommunications technologies and services in order to respond to competitive industry conditions and customer requirements. Developments of new technologies have rendered some less advanced technologies unpopular or obsolete. For example, demand for our paging services has declined significantly since the introduction of GSM services, improvements in other technologies and changes in the market. As a result, we recognized an impairment charge of NT$343 million (US$10.5 million) relating to our paging business in 2005. If we fail to develop, or to obtain timely access to, new technologies and equipment, or if we fail to obtain the necessary licenses to provide services using these new technologies, we may lose our customers and market share and become less profitable. For example, we began offering multimedia on demand, or MOD, services in March 2004. Although we were not, and are not, in compliance with some applicable ownership restrictions under the Cable Radio and Television Law of the Republic of China, or the Cable Radio and Television Law, we were nevertheless granted a permit as a fixed line operator to offer cable television services by the Government Information Office, the regulatory authority previously governing the cable television industry. In January 2007, the National Communications Commission, after reviewing our improvement in opening of platform of the MOD service, held that we had complied with the request in its order and therefore we would not be considered a cable, radio or television system operator under the Cable Radio and Television Law with respect to this business. Consequently, we are not currently subject to such ownership restrictions. However, the National Communications Commission did announce that it would further amend the Regulation Governing Fixed Line Services in order to regulate the MOD service provided by fixed line operators and would then ask us to submit our operation rules, tariff and service agreement for MOD services for its review. We cannot predict the outcome of this review and cannot assure you that further amendments would not subject us to ownership restrictions or other limitations on our MOD business. Moreover, our plans to introduce VoIP telephone services have also been delayed because we have not received requisite approvals from the applicable regulatory authority.

In addition, the cost of implementing new technologies, upgrading our networks or expanding capacity could be significant. In particular, we have made and will continue to make substantial capital expenditures in the near future in order for us to effectively respond to technological changes, such as the continued expansion of our 3G cellular mobile network. We will also need to make additional capital expenditures relating to the launch of new businesses, including MOD, ADSL services, fiber-to-the-building services WiMAX and VoIP services, and the implementation of a network modernization program, including the planned migration of our fixed line networks to internet protocol next generation networks. To the extent these expenditures exceed our cash resources, we will be required to seek additional debt or equity financing. Our ability to obtain additional financing on favorable commercial terms will depend on a number of factors. These factors include our financial condition, results of operations, cash flows and the prevailing market conditions in the Taiwan and international telecommunications industry, the cost of financing and conditions in the financial markets, and the issuance of relevant government and other regulatory approvals. The failure to obtain funding for our capital expenditures on commercially acceptable terms and on a timely basis, or at all, could jeopardize our expansion plans and materially and adversely affect our business, financial condition, results of operations and prospects.

We may not realize the benefits we expect from our investments, which may materially and adversely affect our business, financial condition, results of operations and prospects.

We have made significant capital investments in our network infrastructure and information technology systems to provide the services we offer. In 2006, we had capital expenditures in relation to our network infrastructure and information technology systems of NT$27.7 billion. Of this amount, we had capital expenditures of NT$5.4 billion in our fixed line services, NT$9.4 billion in our cellular services, NT$12.5 billion in our internet and data services and NT$0.4 billion in other areas. In order to continue to develop our business and offer new and more sophisticated services, we intend to continue to invest in these areas as well as new technologies. The launch of new and commercially viable products and services is important to the success of our business. We expect to incur substantial capital expenditures to further develop our range of services and products. Commercial acceptance by consumers of new and more sophisticated services we offer may not occur at the rate or level expected, and we may not be able to successfully adapt these services to effectively and economically meet our customers' demand, thus impairing our expected return from our investments.

We cannot assure you that services enabled by new technologies we implement, such as 3G cellular technology, will be accepted by the public to the extent required to generate an acceptable rate of return. In addition, we face the risk of unforeseen complications in the deployment of these new services and technologies, and we cannot assure you that our estimate of the necessary capital expenditure to offer such services will not be exceeded. New services and technologies may not be developed and/or deployed according to expected schedules or may not achieve commercial acceptance or be cost effective. The failure of any of our services to achieve commercial acceptance could result in additional capital expenditures or a reduction in profitability to the extent that we are required under the applicable accounting standards to recognize a charge for the impairment of assets. Any such charge could materially and adversely affect our financial condition and results of operations.

We may also from time to time make equity investments in companies, but we cannot assure you of their profitability. For example, Chunghwa Investment Co., Ltd, a company in which we hold a 49% interest and which we account for using the equity method, suffered losses in 2004. As a result, the carrying value of

Chunghwa Investment in our consolidated financial statements was reduced from NT$987 million in 2003 to NT$930 million in 2004. These losses were partially attributable to the write-off of certain short-term investments in the amount of NT$80 million that were not authorized by Chunghwa Investment, but were made by the then chairman of Chunghwa Investment, Mr. Jing-Biao Hu, who was removed from office on December 31, 2004. In addition, another of our investments, the Taipei Financial Center Corporation, in which we hold a 12% interest and which we account for using the cost method, commenced commercial operations after completing construction of Taipei 101, which it owns and which is the tallest building in Taiwan. In 2005, we recognized a loss of NT$740 million in relation to this investment due to lower than expected leasing rates for office and retail space in Taipei 101. We cannot assure you that any unprofitable equity investments will not have a material adverse effect on our financial condition or results of operations.

Our ability to deliver services may be disrupted due to a systems failure, shutdown in our networks, earthquakes or other natural disasters.

Our services are currently carried through our fixed line and cellular telecommunications networks, as well as through our transmission networks comprised of optical fiber cable, microwave, submarine cable and satellite transmission links. Our networks may be vulnerable to damage or interruptions in operations due to adverse weather conditions, earthquakes, fires, power loss, telecommunications failures, software flaws, transmission cable cuts or similar events. For example, on December 26, 2006, a 6.9 magnitude earthquake in the southern seas of Taiwan caused significant damage to the undersea cable networks that connect Taiwan to the United States, Japan, Hong Kong, China and other countries in South East Asia. The earthquake resulted in major outages in telephone and internet services throughout the region. It took one week to restore 90% of the capacity and repairs were not completed until February 2, 2007, when all four affected undersea cables finally returned to normal operations. As a result of the December 2006 earthquake, we suffered repair costs of approximately NT$10 million. Taiwan is susceptible to earthquakes and typhoons, however, we do not carry any insurance to cover damages caused by earthquakes, typhoons or other natural disasters, or to cover any resulting business interruption. Any failure of our networks, servers, or any link in the delivery chain that results in an interruption in our operations or an interruption in the provision of any of our services, whether from operational disruption, natural disaster, military or terrorist activity, or otherwise, could damage our ability to attract and retain subscribers and materially and adversely affect our business, financial condition, results of operations and prospects.

If new technologies adopted by us do not perform as expected, or if we are unable to effectively deliver new services based on these technologies in a commercially viable manner, our revenue growth and profitability will decline.

We are pursuing a number of new growth opportunities in the broader telecommunications industry, including wireless data services, MOD services and VoIP, WiMAX. These opportunities involve new services for which there are no proven markets. Our ability to deploy and deliver these services will depend, in many instances, on new and unproven technologies. These new technologies, such as 3G cellular telecommunications technologies, may not perform as expected or generate an acceptable rate of return. In addition, we may not be able to successfully develop new technologies to effectively and economically deliver these services, or be able to compete successfully in the delivery of telecommunications services based on new technologies. Furthermore, the success of our wireless data services is substantially dependent on the availability of wireless data applications and devices that are being developed by third-party developers. These applications or devices may not be sufficiently developed to support the deployment of our wireless data services. If we are unable to deliver commercially viable services based on the new technologies that we adopt, then our revenue growth and profitability, as well as our financial condition and results of operations, will be materially and adversely affected.

We depend on select personnel and could be affected by the loss of their services.

We depend on the continued service of our executive officers and skilled technical and other personnel. Our business could suffer if we lose the services of any of these personnel and cannot adequately replace them. In particular, we are not insured against the loss of any of our personnel. Moreover, we may be required to increase substantially the number of these employees in connection with any expansion, and there is intense competition for experienced personnel in the Taiwan telecommunications industry. We may not be able to either retain our present personnel or attract additional qualified personnel as and when needed. In addition, we may need to increase employee compensation levels in order to attract and retain personnel. We cannot assure you that the loss of the services of any of these personnel would not disrupt our business and operations, and materially and adversely affect the quality of our services and harm our reputation.

Our largest shareholder may take actions that conflict with our public shareholders' best interests.

As of April 17, 2007, the Republic of China government, through the Ministry of Transportation and Communications, owned approximately 35.41% of our outstanding common shares. Accordingly, the government, through its control over our board, may continue to have the ability to control our business, including matters relating to:

- any sale of all or substantially all of our assets;
- the approval of our annual operation and projects budget;
- the composition of our senior management;
- the timing and distribution of dividends;
- the election of a majority of our directors and supervisors; and
- our business activities and direction.

In addition, pursuant to the Republic of China Telecommunications Act, or the Telecommunications Act, and our articles of incorporation, our board of directors approved the issuance of two preferred shares on March 28, 2006 to the Ministry of Transportation and Communications. As the holder of these preferred shares, the Ministry & Transportation and Communications has the right to veto any change in our name or our business and any transfer of the whole or the main part of our business or property and to act as a director and supervisor on the basis of its preferred shareholding. Under our articles of incorporation, these preferred shares are non-transferable and will be redeemed by us three years after the record date of their issuance at their par value.

The value of your investment may be reduced by future sales of our ADSs or common shares by us, by the Republic of China government or by other shareholders.

The government may continue to sell our common shares. Sales of substantial amounts of ADSs or common shares by the government or any other shareholder in the public market, or the perception that future sales may occur, could depress the prevailing market price of our ADSs and common shares.

We may be sanctioned or lose our licenses for violations of limits on foreign ownership of our common shares, and these limits may materially and adversely affect our ability to obtain financing.

The laws of the Republic of China limit foreign ownership of our common shares. Prior to March 1, 2006, the Ministry of Transportation and Communications, as the competent authority under the Telecommunications Act, had the power to prescribe the limits on foreign ownership of our common shares. After the formation of the National Communications Commission, on March 1, 2006, the National Communications Commission replaced the Ministry of Transportation and Communications as the competent authority under the Telecommunications Act pursuant to the Organization Law. However, it is unclear whether the National Communications Commission (instead of the Ministry of Transportation and Communications) has the authority to prescribe the limits of foreign ownership of our common shares. On July 19, 2006, the Ministry of Transportation and Communications increased our foreign ownership limitation from 40% to 49% pursuant to the Telecommunications Act. Since our foreign ownership is now above 40%, we could be deemed in violation of the foreign ownership limitations if it is determined that the Ministry of Transportation and Communications did not have authority to increase our foreign ownership limit to 49% as it purported to do on July 19, 2006. If we fail to comply with the applicable foreign ownership limitations, our licenses to operate some of our businesses could be revoked. Moreover, we cannot predict the manner in which the National Communications Commission will exercise its authority over us, and the National Communications Commission could decline to raise, or determine to reduce, this foreign ownership limitation.

In addition, the Cable Radio and Television Law, under which we operate our MOD business, provides that direct foreign ownership in a cable operator may not exceed 20%, and that the combined direct and indirect foreign ownership in a cable operator may not exceed 60%. We were granted a license under this law, even though we were not, and are not, in compliance with this and other ownership restrictions. However, the National Communications Commission, which has been responsible for administering regulations in this area since March 1, 2006, issued an order on August 23, 2006 requesting us to open our MOD services platform to non-Chunghwa Telecom HiNet subscribers and other service operators and content providers by December 31, 2006. In January 2007, the National Communications Commission, after reviewing the opening in our platform for MOD service, held that we had complied with the request in its order and therefore we would not be considered a cable, radio or television system operator under the Cable Radio and Television Law with respect to this business. Consequently, we are not subject to such ownership restrictions. However, the National Communications Commission did announce that it would further amend the Regulation Governing Fixed Line Services in order to regulate the MOD service provided by fixed line operators and would then ask us to submit our operation rules, tariff and service agreement for MOD services for its review. We cannot predict the outcome of such review and we cannot assure you that further amendment would not subject us to ownership restrictions or other limitations on our MOD business.

Since it is unclear whether the National Communications Commission or the Ministry of Transportation and Communications has the authority to exercise power with respect to raising our foreign ownership limitations, we cannot assure you that we are not in violation of the limits on our foreign ownership under the Telecommunications Act. If we are deemed to be in violation of our foreign ownership limitations, any consequences arising from such violation may materially and adversely affect us. Moreover, since we are unable to control ownership of our common shares or ADSs representing our common shares, and because we have no ability to stop transfers among shareholders, or force particular shareholders to sell their shares, we may be subject to monetary fine or lose our licenses through no fault of our own. In that event, our business could be disrupted, our reputation could be damaged and the market price of our ADSs and common shares could decline. These limitations may also materially and adversely affect our ability to obtain adequate financing to fund our future capital requirements or to obtain strategic partners, and alternate forms of financing may not be available on terms favorable to us or at all.

Actual or perceived health risks related to cellular handsets and base stations could lead to decreased cellular telephone usage and difficulties in increasing network coverage and could expose us to potential liability.

According to some published reports, the electromagnetic signals from cellular handsets and cellular base stations may pose health risks or interfere with the operation of electronic equipment. Although the findings of those reports are disputed, actual or perceived risks of using cellular telecommunications devices or of base stations could have a material adverse effect on cellular service providers, including us. For example, our customer base could be reduced, our customers may reduce their usage of our cellular services, we could encounter difficulties in obtaining sites for additional cellular base stations required to expand our network coverage or we may be requested to reduce the number of existing cellular base stations. As a result, our cellular business may generate less revenue and our financial condition and results of operations may be materially and adversely affected. In addition, we could be exposed to potential liability for any health problems caused by cellular handsets and base stations.

The market value of your investment may fluctuate due to financial results released in the Republic of China that are prepared on a basis that is different from generally accepted accounting principles in the United States.

Our ongoing financial reporting with the SEC is currently under US GAAP. Beginning in 2008, we plan to prepare our financial reporting with the SEC under generally accepted accounting principles in the Republic of

China, or ROC GAAP, with reconciliation to US GAAP in accordance with the requirements of the SEC. Our reported financial condition and results of operations under US GAAP may differ significantly from ROC GAAP. The price of our common shares trading on the Taiwan Stock Exchange may be based on, among other things, our consolidated financial statements prepared for ongoing reporting purposes in the Republic of China, and this in turn may affect the market price of our ADSs.

We are subject to litigation that could expose us to substantial liabilities.

We are from time to time involved in litigation, arbitration or administrative proceedings in the ordinary course of our business. See "Item 4. Information on the Company—B. Business Overview—Legal Proceedings." We cannot predict the outcome of these proceedings, and we cannot assure you that if a judgment is rendered against us in any or all of these proceedings, our financial condition and results of operations would not be materially and adversely affected.

Investor confidence in us may be adversely impacted if we or our independent registered public accountants are unable to attest to the effectiveness of our internal control over financial reporting.

We are subject to the reporting requirements of the SEC. The SEC, as directed by Section 404 of the U.S. Sarbanes-Oxley Act of 2002, adopted rules requiring U.S. public companies to include a report of management on our internal control over financial reporting in their annual reports that contain an assessment by management of the effectiveness of the company's internal control over financial reporting. In addition, each company's independent registered public accountants must attest to and report on the design and operating effectiveness of and management's assessment of the effectiveness of the company's internal control over financial reporting. These requirements first applied to us in connection with our annual report on Form 20-F for the fiscal year ending on December 31, 2006.

While the management report included in this annual report concluded that our internal control over financial reporting was effective, we cannot assure you that our management will be able to conclude that our internal control over financial reporting is effective in future years. Moreover, even if our management concludes that our internal control over financial reporting is effective, our independent registered public accounting firm may still conclude that our internal control is not effective due to any inability to fully remedy the material weaknesses already reported to our audit committee by our independent registered public accounting firm or additional material weaknesses that may be identified during the Section 404 audit process or other reasons. If in future years we fail to achieve and maintain effective internal control over financial reporting in accordance with the Sarbanes-Oxley Act, we could suffer a loss of investor confidence in the reliability of our consolidated financial statements, which in turn could negatively impact the trading price of our ADSs, result in lawsuits being filed against us by our shareholders or otherwise harm our reputation. Furthermore, we have incurred and anticipate that we will continue to incur considerable costs and use significant management time and other resources in our efforts to comply with Section 404 and other requirements of the Sarbanes-Oxley Act.

Our investments in real estate projects may not be profitable and will subject us to additional risks not related to our core businesses.

We have recently begun investing in real estate revitalization projects as part of our efforts to make more productive use of certain undeveloped or underdeveloped properties that we own. Our revitalization projects include the development of high-tech residences, commercial offices and resorts. As of the date of this annual report, we have six such projects underway relating to properties in and around Taipei and other parts of Taiwan. We have no prior experience operating real estate development projects and cannot assure you that our investments will achieve their expected results. Operating or investing in real estate projects involves numerous risks for which we may not be adequately protected. Many of these risks are also beyond our control. For example, our projects may be delayed or never completed due to the failure of other parties with which we have contracted to fulfill their contractual obligations or because of unexpected problems that arise during the planning or construction phases of the projects. Any significant delay or any failure to complete our projects might result in our projects not achieving their expected return and could subject us to a loss on our investment. In addition, changes in the regulatory or economic environment relating to real estate, such as changes in interest rates affecting the financing of our projects, increases in the applicable property tax rates relating to our properties and decreases in demand for residential, commercial or resort properties, could adversely affect the value of our properties and/or reduce or eliminate the profitability of our projects. If our revitalization projects do not achieve their expected results or subject us to a significant financial loss, this could have a adverse effect on our financial condition and results of operations.

Any further economic downturn or decline in the growth of the population in Taiwan may materially and adversely affect our financial condition, results of operations and prospects.

We conduct most of our operations and generate most of our revenues in Taiwan. As a result, any decline in the Taiwan economy or a decline in the growth of the population in Taiwan may materially and adversely affect our financial condition, results of operations and prospects. In recent years, the banking and financial sectors in Taiwan have been seriously harmed by the general economic downturn in Taiwan and the rest of Asia, which has resulted in a depressed property market and an increase in the number of companies filing for corporate reorganization and bankruptcy protection. Although economic conditions in Taiwan improved since 2003, the global slowdown in technology expenditures has also from time to time adversely affected the Taiwan economy, which is highly dependent on the technology industry. We cannot assure you that economic conditions in Taiwan will continue to improve in the future or that our business and operations will not be materially and adversely affected by a deterioration in the Taiwan economy.

We face substantial political risks associated with doing business in Taiwan, particularly due to domestic political events and the tense relationship between the Republic of China and the People's Republic of China, that could negatively affect the value of your investment.

Our principal executive offices and substantially all of our assets are located in Taiwan, and substantially all of our revenues are derived from our operations in Taiwan. Accordingly, our business, financial condition and results of operations and the market price of our common shares and the ADSs may be affected by changes in Republic of China governmental policies, taxation, inflation or interest rates and by social instability and diplomatic and social developments in or affecting Taiwan which are outside of our control. For example, in 2006 a mass movement formed calling for the resignation of the president of Taiwan over a series of alleged corruption scandals and staged dramatic protests. In addition, Taiwan has a unique international political status. Since 1949, Taiwan and the Chinese mainland have been separately governed. The People's Republic of China, or PRC, claims that it is the sole government in China and that Taiwan is part of China. Although significant economic and cultural relations have been established during recent years between the Republic of China and the PRC, relations have often been strained. The PRC government has refused to renounce the use of military force to gain control over Taiwan. Furthermore, the PRC government passed an Anti-Secession Law in March 2005, which authorizes non-peaceful means and other necessary measures should Taiwan move to gain independence from the PRC. In February 2006, the president of Taiwan ceased activities of the country's National Unification Council, a committee established to assist Taiwan in its efforts to reunite with the PRC. Such cessation is commonly viewed as having a detrimental effect on relations between the two countries. Past developments in relations between the Republic of China and the PRC have on occasion depressed the market prices of the securities of companies in the Republic of China. Relations between the Republic of China and the PRC and other factors affecting military, political or economic conditions in Taiwan could materially and adversely affect our financial condition and results of operations, as well as the market price and the liquidity of our securities.

Any future outbreak of contagious diseases may materially and adversely affect our business and operations, as well as our financial condition and results of operations.

Any future outbreak of contagious diseases, such as severe acute respiratory syndrome or avian influenza, may disrupt our ability to adequately staff our business and may generally disrupt our operations. If any of our employees is suspected of having contracted any contagious disease, we may under certain circumstances be required to quarantine such employees and the affected areas of our premises. As a result, we may have to temporarily suspend part or all of our operations. Furthermore, any future outbreak may restrict the level of economic activity in affected regions, including Taiwan, which may adversely affect our business and prospects. As a result, we cannot assure you that any future outbreak of contagious diseases would not have a material adverse effect on our financial condition and results of operations.

Shareholders may have more difficulty protecting their interests under the laws of the Republic of China than they would under the laws of the United States.

Our corporate affairs are governed by our articles of incorporation, the Telecommunications Act, and by the laws governing corporations incorporated in the Republic of China. In addition, our corporate affairs may remain governed by the Statute of Chunghwa Telecom Co., Ltd. See "—Extensive regulation of our industry may limit our flexibility to respond to market conditions and competition, and our business may suffer." The rights of shareholders and the responsibilities of management and the members of the board of directors of Taiwan companies are different from those applicable to a corporation incorporated in the United States. For example, controlling or major shareholders of Taiwan companies do not owe fiduciary duties to minority shareholders. As a result, holders of our common shares and ADSs may have more difficulty in protecting their interests in connection with actions taken by our management or members of our board of directors than they would as public shareholders of a United States corporation.

The market value of your investment may fluctuate due to the volatility of, and government intervention in, the Taiwan securities market.

Our common shares are traded on the Taiwan Stock Exchange, which has a smaller market capitalization and is more volatile than the securities markets in the United States and many European countries. The market value of our ADSs may fluctuate in response to the fluctuation of the trading price of our common shares on the Taiwan Stock Exchange. The Taiwan Stock Exchange has experienced substantial fluctuations in the prices and trading volumes of listed securities and there are currently limits on the range of daily price movements. In recent years, the Taiwan Stock Exchange Index reached a peak of 10,202.20 in February 2000 and subsequently fell to a low of 3,446.26 in October 2001. During 2006, the Taiwan Stock Exchange Index peaked at 7,823.72 on December 29, 2006, and reached a low of 6,257.80 on July 17, 2006. On April 20, 2007, the Taiwan Stock Exchange Index closed at 7,942.67. The Taiwan Stock Exchange has experienced certain problems, including market manipulation, insider trading and payment defaults. The recurrence of these or similar problems could have a material adverse effect on the market price and liquidity of the securities of Taiwan companies, including our ADSs and common shares, in both the domestic and the international markets.

In response to declines and volatility in the securities markets in Taiwan, the Republic of China government formed the National Financial Stabilization Fund to support these markets through open market purchases of shares in Taiwan companies from time to time. The details of the transactions of the National Financial Stabilization Fund have not been made public. In addition, the government's Labor Insurance Fund and other funds associated with the government have in the past purchased, and may from time to time purchase, shares of Taiwan companies listed on the Taiwan Stock Exchange or other markets. As a result of these activities, the market price of common shares of Taiwan companies may have been and may currently be higher than the prices that would otherwise prevail in the open market. Market intervention by government entities, or the perception that such activity is taking place, may take place or has ceased, may cause sudden movements in the market prices of the securities of Taiwan companies, which may affect the market price and liquidity of our common shares and ADSs.

Risks Relating to Ownership of Our ADSs

Restrictions on the ability to deposit our common shares into our ADS program may adversely affect the liquidity and price of the ADSs.

The ability to deposit shares into our ADS program is restricted by Republic of China law, under which no person or entity, including you and us, may deposit our common shares into our ADS program unless the

Securities and Futures Bureau has not objected within a prescribed period following the filing with it of an application to do so, except for the deposit of the common shares into our ADS program and for the issuance of additional ADSs in connection with:

- distribution of share dividends or free distribution of our common shares;
- exercise of preemptive rights of ADS holders applicable to the common shares evidenced by our ADSs in the event of capital increases for cash; or
- purchases of our common shares in the domestic market in Taiwan by the investor directly or through the depositary and delivery of such shares or delivery of our common shares held by such investors to the custodian for deposit into our ADS program, subject to the following conditions: (a) the depositary may accept deposit of those shares and issue the corresponding number of ADSs with regard to such deposits only if the total number of ADSs outstanding after the deposit does not exceed the number of ADSs previously approved by the Securities and Futures Bureau, plus any ADSs issued pursuant to the events described above; and (b) this deposit may only be made to the extent previously issued ADSs have been cancelled.

As a result of the limited ability to deposit common shares into our ADS program, the prevailing market price of our ADSs on the New York Stock Exchange may differ from the prevailing market price of the equivalent number of our common shares on the Taiwan Stock Exchange.

You will be more restricted in your ability to exercise voting rights than the holders of our common shares, which may diminish your influence over our corporate affairs and may reduce the value of your ADSs.

Holders of American depositary receipts evidencing our ADSs may exercise voting rights with respect to the common shares represented by these ADSs only in accordance with the provisions of our deposit agreement. The deposit agreement provides that, upon receipt of notice of any meeting of holders of our common shares, the depositary bank will, as soon as practicable thereafter if requested by us in writing, mail to ADS holders the notice of the meeting sent by us, voting instruction forms and a statement as to the manner in which instructions may be given by the holders.

ADS holders will not generally be able to exercise voting rights attaching to the deposited securities on an individual basis. Under the deposit agreement, the voting rights attaching to the deposited securities must be exercised as to all matters subject to a vote of shareholders collectively in the same manner, except in the case of an election of directors and supervisors. The election of our directors and supervisors is by means of cumulative voting. In the event the depositary does not receive voting instructions from ADS holders in accordance with the deposit agreement, our chairman or his or her designee will be entitled to vote the common shares represented by the ADSs in the manner he or she deems appropriate at his or her discretion, which may not be in your interest.

Your right to participate in any future rights offerings may be limited, which may cause dilution to your holdings.

We may from time to time distribute rights to our shareholders, including rights to acquire our securities. Under the deposit agreement, the depositary will not offer you those rights unless the distribution to ADS holders of both the rights and any related securities are either registered under the U.S. Securities Act of 1933, as amended, or the Securities Act, or exempt from registration under the Securities Act. We are under no obligation to file a registration statement with respect to any such rights or securities or to endeavor to cause such a registration statement to be declared effective. Moreover, we may not be able to establish an exemption from registration under the Securities Act. Accordingly, you may be unable to participate in our rights offerings and may experience dilution in your holdings.

If the depositary is unable to sell rights that are not exercised or not distributed or if the sale is not lawful or reasonably practicable, it will allow the rights to lapse, in which case you will receive no value for these rights.

Changes in exchange controls that restrict your ability to convert proceeds received from your ownership of ADSs may have an adverse effect on the value of your investment.

Your ability to convert proceeds received from your ownership of ADSs depends on existing and future exchange control regulations of the Republic of China. Under the current laws of the Republic of China, an ADS holder or the depositary, without obtaining further approvals from the Central Bank of the Republic of China (Taiwan) or any other governmental authority or agency of the Republic of China, may convert NT dollars into other currencies, including U.S. dollars, in respect of:

- the proceeds of the sale of common shares represented by ADSs or received as share dividends with respect to the common shares and deposited into the depositary receipt facility; and
- any cash dividends or distributions received from the common shares represented by ADSs.

In addition, the depositary may also convert into NT dollars incoming payments for purchases of common shares for deposit in the depositary receipt facility against the creation of additional ADSs. If you withdraw the common shares underlying your ADSs and become a holder of our common shares, you may convert into NT dollars subscription payments for rights offerings. The depositary may be required to obtain foreign exchange approval from the Central Bank of the Republic of China (Taiwan) on a payment-by-payment basis for conversion from NT dollars into foreign currencies of the proceeds from the sale of subscription rights of new common shares. Although it is expected that the Central Bank of the Republic of China (Taiwan) will grant approval as a routine matter, required approvals may not be obtained in a timely manner, or at all.

Under the Republic of China Foreign Exchange Control Law, the Executive Yuan of the Republic of China may, without prior notice but subject to subsequent legislative approval rendered within ten days from such imposition, impose foreign exchange controls or other restrictions in the event of, among other things, a material change in domestic or international economic conditions which might threaten the stability of the domestic economy in Taiwan.

You are required to register with the Taiwan Stock Exchange and appoint several local agents in Taiwan if you withdraw common shares from our ADS facility and become our shareholder, which may make your ownership burdensome.

If you are a non-Republic of China person and wish to withdraw common shares represented by your ADSs from our ADS facility and hold those common shares, you are required under the current laws and regulations of the Republic of China to appoint an agent, also referred to as a tax guarantor, in the Republic of China for filing tax returns and making tax payment. A tax guarantor must meet certain qualifications set by the Ministry of Finance of the Republic of China and, upon appointment, becomes a guarantor of your Republic of China tax obligations. If you wish to repatriate profits derived from the sale of withdrawn common shares or cash dividends or interest on funds derived from the withdrawn common shares, you will be required to submit evidence of your appointment of a tax guarantor and the approval of the appointment by the Republic of China tax authorities. You may not be able to appoint and obtain approval for a tax guarantor in a timely manner.

In addition, under the current laws of the Republic of China, you will be required to be registered as a foreign investor with the Taiwan Stock Exchange for making investments in the Republic of China securities market prior to your withdrawal and holding of common shares represented by the ADSs. You will be required to appoint a local agent in Taiwan to, among other things, open a securities trading account with a local securities brokerage firm and a bank account to remit funds, exercise shareholders' rights and perform other functions as holders of ADSs may designate. You must also appoint a local bank to act as custodian for handling confirmation and settlement of trades, safekeeping of securities and cash proceeds and reporting and declaration of information. Without the relevant registration and appointment of the local agent and custodian and the opening of a securities trading account and bank account, you will not be able to hold, subsequently sell or otherwise transfer our common shares withdrawn from the ADSs facilities on the Taiwan Stock Exchange.

Always dynamic, always on the move.

Our actual financial results may differ materially from our announced full year guidance.

Each year, we announce guidance for the current fiscal year prepared in accordance with ROC GAAP and the requirements of the Taiwan Stock Exchange. These projections are based on a number of estimates and assumptions and are inherently subject to significant uncertainties and contingencies, including the risks factors described in this annual report. These projections are not prepared with a view towards compliance with published guidelines of the SEC, the U.S. Public Company Accounting Oversight Board or generally accepted accounting principles and, accordingly, you should not rely on this information. In particular, projections are forward-looking statements that are necessarily speculative in nature, and it can be expected that one or more of the estimates on which the projections were based will not materialize or will vary significantly from actual results, and such variances will likely increase over time.

ITEM 4. INFORMATION ON THE COMPANY

A. History and Development of the Company

Our legal and commercial name is Chunghwa Telecom Co., Ltd. Our common shares have been listed on the Taiwan Stock Exchange under the number "2412" since October 27, 2000 and our ADSs have been listed on the New York Stock Exchange under the symbol "CHT" since July 17, 2003. Our principal executive offices are located at 21-3 Hsinyi Road, Section 1, Taipei, Taiwan, Republic of China, and our telephone number is (886) 2-2344-5488. Our website address is *http://www.cht.com.tw*. The information on our website does not form a part of this annual report.

We were established as a company on July 1, 1996 as a result of the separation of the business and regulatory functions of the Directorate General of Telecommunications. We were privatized in August 2005.

We are the largest telecommunications service provider in Taiwan and one of the largest in Asia in terms of revenues. As an integrated telecommunications service provider, our principal services include:

- fixed line services, including local, domestic long distance and international long distance telephone services;
- cellular services; and
- Internet and data services, including HiNet, our internet service provider, FTTB services, ADSL services and leased line services.

As our traditional fixed line business has matured and new technologies have become available, we have pursued new growth opportunities in the cellular and internet and data services markets. We are focusing on enhancing our leading position in each of our principal lines of business, and expanding into new lines of business such as third generation, or 3G, cellular services. We enjoy leading positions across a number of areas:

- we are Taiwan's largest provider of fixed line services in terms of both revenues and subscribers;
- we are Taiwan's largest cellular service provider in terms of both revenues and subscribers;
- we are Taiwan's largest broadband internet access provider as well as Taiwan's largest internet service provider in terms of both revenues and subscribers; and
- we are also a leading player in the data communications market in Taiwan.

In 2006, our revenues were NT$186.3 billion (US$5.7 billion), our net income was NT$42.1 billion (US$1.3 billion) and our net income per share was NT$4.34 (US$0.13).

In 2006, we incurred capital expenditures totaling NT$27.7 billion (US$0.8 billion), of which 64.7% was related to wireline equipment, 34.0% was related to cellular equipment and 1.3% was related to other items. See "Item 5. Operating and Financial Review and Prospects—B. Liquidity and Capital Resources—Capital Expenditures" for a discussion of our capital expenditures.

Competitive Strengths

We believe that we are well positioned to take advantage of growth opportunities in the telecommunications market in Taiwan as new technologies evolve. In particular, we have maintained our leading market share in cellular and internet and data services since the opening of the Taiwan telecommunications market to competition in June 2001. Furthermore, we have enjoyed greater flexibility in making purchasing and other business decisions after we were privatized in August 2005. In addition, our responsiveness to market conditions has been enhanced by the shortening in May 2002 of the approval period for primary tariff adjustments and promotional packages from 40 to 14 days.

We believe that further deregulation and market liberalization will continue to drive the growth of the overall market for telecommunications services in Taiwan, as well as the development of new products and services. We expect to benefit from additional opportunities as the telecommunications market in Taiwan continues to grow.

We believe that our primary competitive strengths are:

- our position as the only integrated, full-service telecommunications provider in Taiwan, and
- our capital resources and technology, which we believe we can build on to expand our leading position in the growing cellular and internet and data services markets, including through our continued construction of a 3G cellular network, fiber in the loop broadband access services, our IP-based MOD services and our rollout of VoIP services.

We are the only integrated full-service telecommunications provider in Taiwan.

We are the largest telecommunications service provider in Taiwan with a leading position in local, domestic long distance and international long distance telephone services, wireless services and internet and data services.

Broad range of communications products and services. We believe that our ability to provide an attractive and comprehensive range of telecommunications services uniquely positions us to provide bundled and value-added services to our business and residential customers. In addition, we are able to offer innovative bundled services and tariff packages to meet the specific needs of our customers.

Broad network coverage. The breadth of our network and our ownership of the so called "last mile" infrastructure in Taiwan, which comprises the connection between the local telephone service provider's switching centers to the end-users' buildings or homes, provide us with access to existing and potential customers and creates a platform for expanding our services. As of December 31, 2006, substantially all of our installed telephone lines are capable of delivering ADSL services. In addition, our cellular services network provides nationwide coverage. Our large cellular spectrum allocation together with our network of 8,597 base stations position us well for the continued expansion of our cellular services in Taiwan.

Brand awareness, distribution channels and customer service. Our principal brands "Chunghwa Telecom" and "HiNet" have a reputation for quality, reliability and technology. In particular, we are the leading internet service provider in Taiwan through HiNet. We serve our large and well-established customer base through our extensive customer service network in Taiwan, including 24 operations offices, 322 service centers, 121 exclusive services stores and six integrated call centers. We also offer comprehensive and high-quality point of sale and after sale services, and we provide web-based customer services. Moreover, our extensive sales and distribution channels help us attract additional customers and develop new business opportunities. In the Reader's Digest Super Brands Award 2005, we stood out and won Platinum Award of Telecom Company in Taiwan. We were also awarded "Best Managed Company" and "Best Commitment to Strong Dividends" in Taiwan by Finance Asia in 2006. In January 2007, the Standard & Poor's Ratings Services raised our long-term foreign currency credit rating to AA from AA- and removed us from CreditWatch, where it was placed with positive implications.

Operational expertise. Our management and employees have extensive operating experience and technical knowledge, which we believe cannot be easily replicated by competitors. We also believe we will continue to attract and retain high quality employees.

Comprehensive customer billing infrastructure. As Taiwan's leading telecommunications services provider, we have extensive resources and infrastructure relating to billing services. In particular, we issue, in the aggregate, approximately 16 million invoices, including integrated bills, every month. We intend to continue taking advantage of this unique attribute by offering bill collection services to internet content providers and other entities that lack the necessary resources and infrastructure for effective customer billing.

We have the capital resources and technology to enhance our leading position in the growing cellular and internet services markets.

Established position in growing markets. Revenues from our cellular and internet and data services have increased from 55.8% of revenues in 2003 to 64.1% in 2006. We expect our cellular and internet and data services to continue to be the key drivers of our future growth. With our leading market share, we enjoy substantial economies of scale in equipment procurement as well as the marketing of our products and services.

Strong capital structure. We believe we have greater financial resources than other telecommunications operators in Taiwan. In particular, our relatively low debt-to-equity capital structure, together with our high levels of cash and operating cash flows, provides us with the flexibility and resources to invest in capital intensive and growing businesses. In particular, we continue to invest in broadband internet protocol networks, fiber-optic networks, and 3G cellular communications networks and services. We also have begun making investments in or acquiring other companies which provide complementary telecommunications and internet-related services to further expand our business and offer new products and services.

Advanced network technology. Since 2003, we have developed and upgraded our existing infrastructure for both mobile and fixed line networks. We developed a high-speed internet protocol backbone network and expanded the coverage of our ADSL network. In 2007, we launched a long-term next generation network construction project that will upgrade the local fixed line networks to high-speed packet-based digital networks with fiber in the loop. Our investment in network infrastructure places us in a position to capture a significant share of the internet and high-speed data transmission market.

Research and development expertise. We employ over 1,187 research professionals and engineers whose principal focus is to develop advanced network services and operations support systems and to build selected core technologies. In 2006, our research and development expenses, excluding depreciation and amortization, accounted for 1.5% of our revenues. We believe our focus on research and development will allow us to efficiently develop and deploy new technologies and services ahead of our competitors.

Business Strategy

Taiwan has one of the highest fixed line penetration rates in Asia and has also experienced rapid adoption of wireless communications and internet services, including broadband access services. We believe that telecommunications services will evolve over the coming years, driven by a number of technological innovations. We also believe that the convergence of communications technologies will provide a significant competitive advantage to integrated telecommunications service providers that are able to design and construct sophisticated and scalable networks capable of serving as a common platform for a broad range of services.

Our key strategic objectives are to maintain our position as a leading integrated telecommunications services provider in Taiwan and to enhance our leadership position in growing markets, such as cellular and internet and data markets, including broadband access services and value-added services.

Consistent with our strategic objectives, we have developed the following business strategies:

Focus on our core strengths while expanding our scope of services to capture new growth opportunities

Our core strengths are the management of telecommunication networks and the provision of services over these networks. We currently operate several networks linked by a core backbone infrastructure consisting of public switched telephone, cellular, ADSL and internet protocol networks. Our strategy for each network differs depending on the market dynamics and future growth prospects of services delivered over these networks. In general, we endeavor to maintain our strong market position in each of our business lines and seek to expand the scope of our business beyond network services by offering value-added services to generate growth and new opportunities.

Fixed line: Our strategy is to maintain our position as the market leader in fixed line communications. In December 2006, we launched value-added services for the local telephone market, such as personal ring back tone. We also seek to enhance customer loyalty by promoting virtual private network and information communication systems integration services targeted at our corporate customers. In January 2007, we launched a long-term project to create our next generation network that will upgrade the local fixed line networks to high-speed packed-based digital networks with fiber in the loop. We expect our entire fixed line network to be eventually based on a fully integrated IP telephony system. We also plan to launch phone-to-phone voice VoIP after the National Communications Commission authorizes the 070 prefix for our phone-to-phone VoIP service.

Cellular: Our strategy for our existing 2G cellular services, which uses the GSM standard, is to continue to expand service offerings that take advantage of our strong customer base and extensive network coverage. In particular, we will focus on increasing our average revenue per subscriber by expanding our post-paid subscriber base and promoting increased use of wireless value-added services, such as our "emome" mobile internet service, Java games, ring back tone services and video streaming. Furthermore, we launched our 3G cellular service based on a wideband code division multiple access, or WCDMA, technology on July 26, 2005 and launched 3.5G services on September 12, 2006. Our strategy with respect to our 3G cellular service includes the following initiatives:

- taking advantage of our ability to provide services using either the GSM or WCDMA standards and offer seamless service to customers with dual mode handsets, which enable our customers to enjoy the benefits of network coverage while retaining their GSM cellular phone number. In order to meet the demand from our customers for high-speed wireless data access, we adopted high-speed downlink packet access technology and continued developing third-generation cellular technology;
- encouraging our high-end customers, who are more likely to demand wireless internet services with higher data speed access capabilities, to use our 3G and 3.5G services by offering attractive service packages;
- converging fixed line and cellular services to provide customers with access to personalized information through personal computers, personal digital assistants or cellular handsets; and
- taking advantage of our superior brand and network quality to attract our competitors' subscribers.
- expanding our High-Speed Downlink Packet Access, or HSDPA, coverage to attract more 3.5G mobile internet users.

Internet and data: Our strategy for internet and data services is to continue to build on the success of our HiNet internet services and ADSL access services. We seek to complement the government's plan to grow Taiwan's broadband subscriber base to 6 million subscribers by the end of 2007. We are the leading provider of broadband internet access in Taiwan, with a significant market share as of December 31, 2006. We have successfully migrated many of our customers from low-speed to higher-speed internet access services. Approximately 62.5% of our broadband customers subscribe for downlink speeds of over 2 megabits per second, and the average downlink speed of our internet subscribers, defined as the total downlink speed subscribed divided by the total number of subscribers, increased from 0.6 Mbps as of December 31, 2002 to 2.56 Mbps as of December 31, 2006. We are developing new media to provide both higher-speed access as well as attractive content to our customers. We are continuing our build-out of fiber-to-the-building infrastructure, and continually enhancing our internet value-added services, such as online gaming, internet music, internet banking and internet protocol video services, including multimedia on demand, or MOD, and hiChannel. We will launch VoIP services, after the National Communications Commission authorizes the 070 prefix for our phone-to-phone VoIP service.

Bundled services: We believe bundled services are effective in encouraging usage and enhancing customer loyalty. We intend to increase our offerings for bundled services. In particular, we believe we are uniquely positioned to provide our customers with fully integrated solutions across fixed line, cellular and internet platforms. Our "Friends and Family" service, which offers customers preferential rates, has attracted over 1.86 million mobile phone subscribers. In addition, we provide a wide range of bundled services customized to meet the needs of our corporate customers, such as integrated network management services, secure internet services and 3G mobile office.

Emphasize quality of service and customer satisfaction

Quality of service is critical in attracting and retaining customers and enhancing our long-term profitability. In order to continually enhance and improve the quality of our services, we have, in addition to the quality assurance function of our regular operating units, established a number of dedicated task forces to monitor our network performance. Our senior management sets our quality evaluation criteria and regularly reviews the quality of our performance.

In order to ensure that our quality of service will translate into strong customer loyalty, we plan to continue to focus on and invest in the provision of a full range of services that emphasize customer care from the point of sale onward. For example, we have extended the focus of our corporate customer services from major accounts to include small and medium enterprises and on January 2007 established our Enterprise Business Group. Our Enterprise Business Group is staffed by approximately 1,200 professionals and offers packaged and customized services, customer-oriented solutions and integrated information and communications services. We have completed the integration of our call centers, all of which can now be reached by calling a single number "123." We offer 24-hour customer service, including the handling of service and billing inquiries with the assistance of an Interactive Voice Response, or IVR, system. We also offer consolidated billing for our customers who use multiple services. We began to provide an e-bill service option to our customers in August 2005. Moreover, we have put in place processes to enhance bill collection and improve the quality of our billing services. To improve the quality of our customer services, we implemented a customer relationship management system, which encompass, among other things, a customer complaint system, a business information database for the use of our call centers, and a data mining system to enhance our sales and market analysis efforts.

Improve operational efficiency and cost structure

We have historically been focused, and will continue to focus, on cost control, particularly in the areas of network efficiencies and personnel costs. We expect to be able to further improve our operational efficiency and cost structure by migrating to more advanced networks and sophisticated operational support systems, and efficiently managing our workforce.

Capital expenditures. Our long-term goal is to optimize our capital expenditures by focusing on investing in innovative products and services with attractive return profiles. We have commenced a project for gradually upgrading our entire public switched telephone network to a next-generation network. Next-generation internet protocol switches will have substantially more capacity and greater upgrade flexibility, and should result in savings from a reduced number of switching centers, and related property, materials and personnel costs. We have also devoted resources toward the expansion of our 3G cellular network and the continuing build-out of our fiber in the loop infrastructure.

Personnel costs. We seek to improve our operational efficiency by reducing our personnel costs. For example, we offered a number of voluntary retirement programs between July 1, 2003 and April 30, 2006 which resulted in reductions of 3,712 employees. On the other hand, we also hired more than 593 new employees after privatization. In 2006, we further aligned our organizational structure by integrating various operating units and departments. We will also continue to reallocate our personnel from traditional fixed line services to our growing businesses and to our marketing and customer services departments, as well as exploring outsourcing opportunities where we deem appropriate. In 2007, we also plan to offer another preferential voluntary retirement plan for our employees.

Expand our business through alliances, acquisitions and investments

We plan to expand our business in high growth areas, such as interactive multimedia broadband services, content delivery services and value-added services, through alliances, acquisitions and investments. We believe that our experience, operational scale and large subscriber base make us an attractive ally for other service providers.

Alliances. We have formed and will continue to pursue alliances with information content providers, multimedia service platform providers and customer premises equipment providers to diversify our business operations and enhance our service offerings. As of the date of this annual report, we have collaborated with more than 500 information content providers, more than 60 customer premises equipment providers, more than 6 internet service providers. We have signed cooperation memorandums with Microsoft and Intel to develop digital home services.

Acquisitions. We have focused our acquisition strategy on making acquisitions of companies that we believe to be complementary to our long-term strategic goals. During 2006, we acquired a 70% equity interest in Chief Telecom, a Type II operator and wholesaler of VoIP international voice traffic. This acquisition will complement our current telecommunications offerings by expanding our capacity. In order to facilitate any future overseas acquisitions, we have established New Prospect Investments Holdings Ltd. and Prime Asia Investments Group Ltd. in March 2006, which are wholly owned holding companies incorporated in the British Virgin Islands that operate as investment companies.

Investments. After the privatization, we have focused our investment strategy on the development of new business and the increase of our operation efficiency. We formed Chunghwa International Yellow Pages Corporation and invested a 30% stake in a content provider, Spring House Entertainment Inc. to help develop the content industry in Taiwan. In January 2007, we became a 31.3% shareholder of a mobile distributor, Senao International, by way of a public tender offer. Senao International is our largest cellular phone distributor with a significant market share of the total market in Taiwan. We expect that our investment in Senao will increase our competitiveness in the cellular business, and we expect to take a larger share of the cellular phone distribution market.

Going forward, we may consider making other equity investments and acquisitions that we believe are complementary to our business and other strategic goals. Our future investment will be aimed at expanding our business scale, making better use of our research and development resources and increasing our revenues through investing in online value-added services and digital content provision, technology development, distribution channels and wireless communication. We expect to expand the scope of our international investments from regional to global and plan on focusing on emerging markets and other high-growth enterprises while carefully evaluating the risks involved.

Maintain focus on maximizing shareholder value

We are committed to maximizing shareholder value and intend to maintain our high dividend payout policy. We have historically maintained a conservative capital structure and we were in a net cash position as of March 31, 2007. Following our privatization, we have more flexibility to implement capital management initiatives, including possible repurchases of our outstanding common shares and increases in our leverage through debt financing. We bought back 192,000,000 shares between February 10, 2006 and April 9, 2006 and cancelled those shares on June 30, 2006.

B. Business Overview

Our Principal Lines of Business

The following table sets forth our revenues from our principal lines of business for the periods indicated.

	Year ended December 31,					
	2004		2005		2006	
	(in billions, except percentages)					
	NT$		NT$		NT$	
Fixed line:						
Local	44.9	24.3%	40.7	22.1%	39.0	20.9%
Domestic long distance	12.0	6.4	11.0	5.9	9.9	5.3
International long distance	15.2	8.2	14.6	7.9	14.0	7.6
Total fixed line	72.1	38.9	66.3	35.9	62.9	33.8
Cellular	70.3	38.0	73.0	39.5	73.0	39.2
Internet and data:						
Internet	29.5	15.9	32.1	17.3	35.5	19.1
Data	9.8	5.3	10.1	5.5	10.8	5.8
Total Internet and data	39.3	21.2	42.2	22.8	46.3	24.9
Other	3.5	1.9	3.2	1.8	4.1	2.1
Total revenues	185.2	100.0%	184.7	100.0%	186.3	100.0%

Fixed Line

The provision of fixed line services is one of our principal business activities. We are the largest provider of local, domestic long distance and international long distance telephone services in Taiwan. We also provide interconnection with our fixed line network to other cellular and fixed line operators. Since June 2001, three new operators have begun offering fixed line services. Our revenues from fixed line services were NT$72.1 billion, or approximately 38.9% of our revenues, in 2004, NT$66.3 billion, or approximately 35.9% of our revenues, in 2005, and NT$62.9 billion, or approximately 33.8% of our revenues, in 2006. Owing primarily to the expansion of our broadband and cellular services, we expect that revenues from our fixed line business will continue to decline as a percentage of our total revenues.

Local Telephone

The following table sets forth our revenues from local telephone services for the periods indicated.

	Year ended December 31,		
	2004	2005	2006
		(in billions)	
	NT$	NT$	NT$
Local telephone revenues:			
Usage	16.3	14.6	13.3
Subscription	18.0	18.2	18.2
Interconnection	3.1	3.0	2.9
Pay telephone	0.4	0.2	0.1
Other	7.1	4.7	4.5
Total	44.9	40.7	39.0

We provide local telephone services to over 13.2 million subscribers in Taiwan. Our fixed line network reaches virtually all homes and businesses in Taiwan. Revenues from local telephone services comprised approximately 24.3%, 22.1% and 20.9% of our revenues in 2004, 2005 and 2006, respectively. Approximately 75.2% of our local telephone subscribers as of December 31, 2006 were residential customers, accounting for approximately 60.5% of our local telephone revenues in 2006. We are currently the leader of the local telephone service market, with an average market share of approximately 97.9%, 97.4% and 97.4% in 2004, 2005 and 2006, respectively.

The following table sets forth information with respect to our local telephone subscribers and penetration rates as of the dates indicated.

	As of December 31,		
	2004	2005	2006
	(in thousands, except percentages and per household data)		
Taiwan population(1)	22,689	22,770	22,877
Fixed line subscribers:			
Residential	9,950	9,942	9,822
Business	3,292	3,319	3,300
Total	13,242	13,261	13,122
Growth rate (compared to the same period in the prior year)	0.8%	0.1%	(1.0)%
Penetration rate (as a percentage of the population)	58.4%	58.2%	57.4%
Lines in service per household	1.39	1.36	1.33

(1) Data from the Department of Population, Ministry of the Interior, Republic of China.

Demand for local subscriber lines has historically been driven by population growth. In each of 2004 and 2005, fixed line subscriber growth slowed compared to prior periods, primarily due to market saturation and competition. In 2006, the number of fixed line subscribers decreased by 1% compared to 2005, primarily due to an increase in the number of cancellations of fixed line service.

The following table sets forth information with respect to local telephone usage for the periods indicated.

	Year ended December 31,		
	2004	2005	2006
	(in millions, except percentages)		
Minutes from local calls(1)(2)	24,548	21,116	18,575
Growth rate (compared to the same period in the prior year)	(15.7)%	(14.0)%	(12.0)%

(1) Includes minutes from local calls made on pay telephones.
(2) Calls to our HiNet service, which are recorded as part of our internet and data services, are not included in our local call minutes or revenues.

Minutes from local calls have declined as non-HiNet narrowband subscribers migrate to broadband internet services, which do not require dial-up telephone access. This decline was also due to traffic migration to broadband and cellular services. As a result of our promotion in 2005 and 2006 of lower speed ADSL services, we have experienced that some non-HiNet dial-up customers migrated to ADSL service, which has also contributed to a continued decline of minutes from local calls. However, we believe the rate of migration of traffic from fixed line services to broadband and cellular services is slowing.

We charge our local telephone service subscribers a monthly fee and a usage fee. We also charge separate fees for some value-added services. The monthly fees for our primary tariff plans are NT$70 with a deductible on usage fees of NT$25 for residential customers and NT$295 for business customers. Our primary peak time usage fee is NT$1.6 for three minutes or NT$2.7 for ten minutes, depending on the tariff plan selected by the subscriber, and our off-peak usage fee is NT$1.0 for ten minutes. Our usage fees are the same for residential and business customers.

The following table sets forth information with respect to the average local usage charge per minute for the periods indicated.

	Year ended December 31,		
	2004	2005	2006
Average local telephone usage fee (per minute)	NT$0.68	NT$0.70	NT$0.72
Growth rate (compared to the same period in the prior year)	4.6%	2.9%	2.9%

Average per minute usage charges increased from NT$0.68 per minute in 2004 to NT$0.7 per minute in 2005 and NT$0.72 per minute in 2006. The increases were primarily due to a decline in demand for our discounted internet tariff packages as a result of a migration of non-HiNet dial-up subscribers to our ADSL services.

Part of our competitive strategy is to offer customers innovative products and services intended to both secure customer loyalty and enhance revenues. In particular, our value-added services are designed to increase our call revenues by increasing the number of calls our customers make and by receiving fees for usage of the value-added services. These services include call waiting, caller identification, call forwarding, three-party calls, ring back tone and voicemail.

Domestic Long Distance Telephone

We provide domestic long distance telephone services in Taiwan. Revenues from domestic long distance telephone services comprised approximately 6.4%, 5.9% and 5.3% of our revenues in 2004, 2005 and 2006, respectively. Our average market share in the domestic long distance market was 86.4%, 84.7% and 83.6% in 2004, 2005 and 2006, respectively. Residential customers accounted for approximately 61.3% of our domestic long distance revenues in 2006.

The following table sets forth information with respect to usage of our domestic long distance telephone services for the periods indicated.

	Year ended December 31,		
	2004	2005	2006
	(in millions, except percentages)		
Minutes from domestic long distance calls	5,621	5,131	4,643
Growth rate (compared to the same period in the prior year)	(9.3)%	(8.7)%	(9.5)%

Minutes of use for domestic long distance calls have been declining as a result of traffic migration to cellular services, competition from other fixed line operators and increased use of VoIP. We expect the decline minutes of use for fixed line services to continue in the future because of the same reasons.

The following table sets forth information with respect to the average domestic long distance usage charge per minute for the periods indicated:

	Year ended December 31,		
	2004	2005	2006
Average domestic long distance usage charge (per minute)	NT$1.65	NT$1.65	NT$1.65
Growth rate (compared to the same period in the prior year)	1.2%	0%	0%

All domestic long distance calls, regardless of the distance between the calling parties, have the same tariff. We changed the unit of billing from a per-minute basis to a per-second basis effective February 1, 1999. In addition, we reduced our peak hour domestic long distance rate in April 2001 from NT$0.045 per second to our current rate of NT$0.035 per second. Our current domestic long distance rate for off peak hours is NT$0.025 per second. The rates for both peak hours and off peak hours are the same for residential and business customers. Our average domestic long distance usage charge per minute remained flat between 2004, 2005 and 2006.

We provide so-called "intelligent" network services over our domestic long distance network, including toll free calling, universal number, televoting, premium rate service and virtual private networks. We also focus on offering our customers an increasing number of value-added services and flexible tariff packages.

International Long Distance Telephone

We provide international long distance telephone services in Taiwan. Revenues from international long distance telephone services comprised approximately 8.2%, 7.9% and 7.6% of our revenues in 2004, 2005 and 2006, respectively. Residential customers generated approximately 33.0% of our international long distance revenues during 2006. In addition, we provide wholesale international long distance services to international simple resale operators who do not possess their own telephone network or infrastructure.

Since fixed line services have been open for competition since 2001, we expect competition in this line of business will continue to intensify. We believe other fixed line operators consider the international long distance market to be their primary focus. Our average market share of the international long distance market was approximately 61.3%, 57.8% and 58.3% in 2004, 2005 and 2006, respectively. Our market share increased in 2006 primarily because of a slight increase in our sales of wholesale minutes. Our international long distance services consist primarily of international direct dial services and our discounted "Super eCall" services, which we introduced in April 2000. Under Super eCall, we use VoIP technology through international dedicated circuits which connect to our major correspondent carriers that route calls internationally. Super eCall customers are offered rates that are approximately 30% lower than those for our international direct dial service. Calls made over Super eCall represented approximately 7.2% and 7.8% of our total outgoing international traffic in 2005 and 2006, respectively.

We commenced the wholesale of international long distance minutes to licensed international resale operators and other international carriers in 2001. International resale operators require a fixed line operator in Taiwan to complete their long distance telephone services originating in Taiwan. In addition, other international carriers often find it less expensive to route international calls through Taiwan. These resale operators and carriers purchase from us large numbers of minutes at discounted rates. Our international long distance wholesale business has grown rapidly since its introduction. In 2004, 2005 and 2006, we sold 595.4 million, 781.9 million and 1,041.5 million of wholesale outgoing minutes, which represented approximately 32.1%, 39.0% and 46.5% of our total outgoing international long distance minutes, respectively. Revenues from the wholesale of international long distance minutes increased by approximately 28.7% from NT$1,124 million in 2005 to NT$1,447 million in 2006 As the international long distance market becomes more competitive, we believe the wholesale business will allow us to generate increases in international minutes without accelerating the decline in international long distance rates in the more profitable retail segment.

International calls to and from our top five destinations represented approximately 60.2% our international long distance call traffic in 2006.

The following table shows the percentage of total outgoing and incoming international long distance minutes for our top five outgoing destinations in 2006.

Destination	Percentage of total outgoing minutes	Percentage of total incoming minutes
Mainland China	31.8%	32.0%
United States	9.6	15.2
Hong Kong	6.0	4.9
Japan	3.3	5.6
Philippines	10.7	0.6
Total of top five destinations	61.4%	58.3%

The following table sets forth information with respect to usage of our international long distance services for the periods indicated.

	As of December 31,		
	2004	2005	2006
	(in thousands, except percentages and incoming/outgoing ratio)		
Incoming minutes	1,291	1,289	1,354
Growth rate (compared to the same period in the prior year)	8.5%	(0.2)%	5.0%
Outgoing minutes	1,855	2,004	2,239
Growth rate (compared to the same period in the prior year)	0.4%	8.0%	11.7%
Total minutes	3,146	3,293	3,593
Incoming/outgoing ratio	0.70	0.64	0.60

Total outgoing international long distance minutes increased by 8.0% from 2004 to 2005 and by 11.7% from 2005 to 2006, primarily due to promotions and increased wholesale minutes. Our incoming call volume slightly decreased by 0.2% from 2004 to 2005 due to increased competition resulting from lower priced calls offered by our competitors, which reduced our incoming international call volume and increased by 5.0% from 2005 to 2006 due to active expansion of international wholesale incoming call services through overseas points of presence.

Outgoing calls made by customers in Taiwan and by customers from foreign destinations using Taiwan direct service are billed in accordance with our international long distance rate schedule for the destination called. Rates vary depending on the time of day at which a call is placed. Customers are billed on a per minute basis for Super eCall services, whereas customers are billed on a six second unit basis for international direct dial services.

The following table sets forth information with respect to the average international long distance usage charge per minute that we received for outgoing international calls during the periods indicated:

	Year ended December 31,		
	2004	2005	2006
Average international long distance usage charge (per minute)	NT$ 6.1	NT$ 5.4	NT$ 4.7
Growth rate (compared to the same period in the prior year)	(1.6)%	(11.5)%	(13.0)%

Tariffs for international long distance calls have generally been declining worldwide and we expect this trend to continue. We do not expect the increase in international call traffic to fully offset the decline in tariffs. In anticipation of new competition, we substantially reduced our international tariffs by an average of 37% in April 2001 to defend our business and market share. In addition, we offered our customers significant promotional packages and discounts during off-peak hours in 2004, 2005 and 2006 to maintain their loyalty. In particular, we increased the discounts offered to our high-usage international long distance customers in each of these three years.

We pay for the use of networks of carriers in foreign destinations for outgoing international calls and receive payments from foreign carriers for the use of our network for incoming international calls. Traditionally, these payments have been made pursuant to settlement arrangements under the general auspices of the International Telecommunications Union. Settlement payments are generally denominated in U.S. dollars and are made on a net basis.

The following table sets forth information with respect to our gross settlement receipts and payments during the periods indicated.

	Year ended December 31,		
	2004	2005	2006
		(in billions)	
	NT$	NT$	NT$
Gross international settlement receipts	3.5	3.3	3.1
Gross international settlement payments	5.3	4.5	3.8

Our payments on an aggregate basis to international carriers have been more than our receipts from these carriers, primarily because our customers' outgoing minutes exceeded incoming minutes. As international settlement rates have fallen, our international settlement receipts and our international settlement payments have both declined.

In order to compete more effectively in the international long distance market, we have implemented innovative and customized discount calling plans and marketing campaigns directed at high-usage business customers. We also continue to promote our intelligent network services, including international virtual private networks, international toll free calling and calling card services, and our international long distance minutes wholesale business. We also plan to launch phone-to-phone voice VoIP after the National Communications Commission authorizes the 070 prefix for our phone-to-phone VoIP service. We plan to target specific customers for these services and offer bundled services to increase customer retention in the competitive business environment.

Cellular Services

Cellular service, is one of our principal business activities. We are Taiwan's largest provider of cellular services in terms of both revenues and subscribers. In 2004, we generated revenues of NT$70.3 billion, or approximately 38.0% of our revenues, from cellular services. In 2005, we generated revenues of NT$73.0 billion, or approximately 39.5% of our revenues, from cellular services. In 2006, we generated revenues of NT$73.0 billion (US$2.3 billion), or approximately 39.2% of our revenues, from cellular services.

The following table sets forth our revenues from cellular services for the periods indicated.

	Year ended December 31,		
	2004	2005	2006
		(in billions)	
	NT$	NT$	NT$
Cellular revenues:			
Usage[1]	60.0	60.8	59.7
Interconnection	6.3	7.0	7.3
Mobile data	2.3	3.2	4.2
Other	1.7	2.0	1.8
Total cellular	70.3	73.0	73.0

(1) Includes monthly fees.

As the market for cellular services has continued to expand, we have experienced substantial growth in our cellular customer base. We are the largest cellular operator in Taiwan in terms of revenues and number of subscribers. We had 8.49 million cellular subscribers, for a market share of approximately 36.5% of total 2G cellular subscribers and approximately 35.7% of total 2G cellular services revenues in Taiwan, as of December 31, 2006. Revenues from cellular services comprised approximately 38.0%, 39.5% and 39.2% of our revenues in 2004, 2005 and 2006, respectively. Mobile data revenues as a percentage of total cellular revenues were 3.3%, 4.4% and 5.7% for the years ended December 31, 2004, 2005 and 2006, respectively.

We offer digital cellular service through our dual band GSM network. We are one of the three national licensed providers of GSM services. We have been allocated 15 MHz in the 900 MHz frequency band and 11.25 MHz in the 1800 MHz frequency band for GSM services and general packet-switched radio services, or GPRS, and 15 MHz paired spectrum plus 5 MHz unpaired spectrum in the 2 GHz frequency band for 3G cellular services. This is the largest frequency spectrum allocation to any cellular operator in Taiwan. In February 2002, the Ministry of Transportation and Communications granted 3G cellular services concessions to five companies, including us. In March 2002, we paid NT$10.2 billion to the government for our concession. Our 3G cellular services license is valid to December 31, 2018. In July 2005, we launched our 3G cellular telephone services using WCDMA technology. We also offer the largest international roaming network among Taiwan cellular service providers. In particular, our 2G subscribers have access to 312 networks in 164 countries through our GSM service roaming network and 126 networks in 69 countries through our GPRS roaming network. In addition, our 3G service system includes 37 networks in 22 counties.

As of December 31, 2006, we had approximately 12,234 cellular base stations (including both GSM base stations and 3G cellular base stations) covering substantially all of Taiwan's population. We use these base stations to support both our GSM network and our GPRS network. In 2006, we also selectively upgraded 82 base stations in downtown Taipei, Taiwan Taoyuan International Airport and certain industrial parks areas with HSDPA capability. We will continue this process of implementing HSDPA upgrades in the following five major areas in Taiwan: Taipei City, Taipei County, Taoyuan County, Taichung City and Kaohsiung City.

The following table sets forth information regarding our cellular service operations and our cellular subscriber base for the periods indicated.

	As of or for the year ended December 31,		
	2004	2005	2006
Taiwan population (in thousands)(1)	22,689	22,770	22,877
Total cellular subscribers in Taiwan (in thousands)(2)	21,528	19,876	23,249
Penetration (as a percentage of the population)(2)	94.9%	87.3%	101.6%
Total cellular revenues in Taiwan—2G (in billions)(3)	NT$ 198.2	NT$ 205.2	NT$ 185.2
Number of our cellular subscribers (in thousands)(2)(4)	8,191	8,158	8,487
Our market share by subscribers—2G(2)	38.0%	39.6%	40.9%
Our market share by revenues—2G	35.4%	35.0%	35.7%
Number of our prepaid subscribers (in thousands)	968	603	636
Our prepaid subscribers as a percentage of our total subscribers	11.8%	7.4%	7.5%
Annualized churn rate(5)	22.9%	16.8%	11.6%
Minutes of usage (in millions of minutes)			
Incoming	9,352	9,720	10,403
Outgoing	8,668	8,921	9,227
Average minutes of usage per cellular subscriber per month(2)(6)	182	190	197
Average revenue per cellular subscriber per month(2)(7)	NT$ 712	NT$ 744	NT$ 731

(1) Data from the Department of Population, Ministry of the Interior, Republic of China
(2) The number of cellular subscribers is based on the number of subscriber identification module cards. From 2004, the number of our cellular subscribers excludes prepaid subscription accounts that are inactive for more than three months. In 2006, the total number of cellular subscribers in Taiwan included personal handy-phone system and 3G customers.
(3) Data from the statistical monthly release by Ministry of Transportation and Communications, Republic of China.
(4) Includes GSM, GPRS and 3G services.
(5) Measures the rate of subscriber disconnections from cellular service, determined by dividing (a) our aggregate voluntary and involuntary deactivations (excluding deactivations due to subscribers switching from one of our cellular services to another) during the relevant period by (b) the average number of subscribers during the period (calculated by averaging the number of subscribers at the beginning of the period and the end of the period), and multiplying the result by the fraction where (c) the numerator is 12 and (d) the denominator is the number of months in that period.
(6) Average minutes of usage per cellular subscriber per month is calculated by dividing the total minutes of usage during the period by the average of the number of our cellular subscribers on the first and last days of the period and dividing the result by the number of months in the relevant period.
(7) Average revenue per subscriber per month is calculated by dividing our aggregate cellular telecommunications services revenue during the relevant period by the average of the number of our cellular subscribers on the first and last days of the period and dividing the result by the number of months in the relevant period.

The cellular market in Taiwan has grown rapidly since the liberalization of the market in 1997. Total cellular subscribers in Taiwan has reached approximately 23.2 million as of December 31, 2006. Cellular penetration was approximately 101.6% on the same date. We expect the subscriber growth to continue to slow as a result of market saturation. In addition, the overall cellular services market experienced a slowdown in terms of revenue in 2006. We believe that any future growth in the number of cellular subscribers will depend largely upon continuing improvements in wireless technologies and wireless data applications and the availability of advanced cellular handsets.

We began offering prepaid card services in October 2000. As of December 31, 2006, we had approximately 0.6 million prepaid customers representing approximately 7.5% of our total cellular subscribers. Prepaid customers do not pay monthly fees but pay a higher usage charge on a per second basis. Once the prepayment has been fully utilized, a prepaid customer can make additional prepayments to continue the services. Alternatively, the customer may convert to become a post-paid customer while retaining the same telephone number.

We offer handset incentives to third party dealers when new subscribers agree to sign a two-year service contract with us or when existing subscribers renew their contracts with us for a period of two years. We generally offer incentives on handsets equipped with more advanced data functions to promote the expansion of our GPRS and 3G cellular services. In 2006, the average handset incentives we offered was NT$2,631 per subscriber up from NT$2,380 per subscriber in 2005 primarily due to an increase in the number of subsidized 3G customers. We expect the level of our average handset incentives to slightly decline in the foreseeable future, with a decrease in incentives for handsets generally offset by higher incentives for 3G handsets.

Traffic growth has also been strong as pricing has declined and the number of post-paid subscribers have increased. We have also experienced a significant increase in the number of short messaging service messages sent by our subscribers, which continued to have a positive impact on traffic volume. The average minutes of usage per subscriber rose in 2004 because of a decline in prepaid customers as a percentage of total cellular customers, primarily as a result of accelerated closing of inactive prepaid customer accounts. In contrast, the average minutes of usage per subscriber increased in 2005 because of a decrease in the number of prepaid customers. However, the average minutes of usage per subscriber increased in 2006 because of low pricing packages, such as the "Energy Plan" which have stimulated usage.

Our tariffs for post-paid cellular subscribers primarily consist of usage fees and monthly fees. When our subscribers are outside Taiwan, they pay roaming charges plus international long distance charges and, where applicable, local charges in roaming destinations. We charge a flat fee per transaction for our short messaging service and a fee per packet for our GPRS based on the volume of data transmitted. We also offer discounts on usage fees for calls made between our cellular subscribers to encourage subscription to our cellular service. Our 3G service also provides a monthly flat rate service to our customers using our 3G service for internet purposes.

The decrease in the number of our prepaid subscribers in 2005 was primarily the result of our increased attention to closing inactive accounts. Our average revenue per subscriber per month increased from NT$712 in 2004 to NT$744 in 2005, primarily due to an increase in the number of postpaid subscribers and an increase in the revenues of cellular value-added services. In 2006, average revenue per subscriber further decreased to NT$731 due to price cuts in SMS, or short message service, reduction of the tariff for mobile calls to fixed-line numbers in 2005 and 3G promotion programs during 2006. In order to continue to increase average revenue per subscriber reduce the negative impact caused by the April 2007 GSM price adjustment, we intend to continue introducing new value-added services and promote our 3G and 3.5G and wireless internet services.

In addition to our basic cellular services, we also offer a broad range of value-added telecommunications and information services. In August 2001, we introduced a platform of integrated cellular value added services under the brand name "emome." Our "emome" services offer a broad range of value-added services, including financial information, transaction services, emergency services access numbers, directory information, time, weather and traffic reports. In addition, we have launched other cellular value-added services, such as JAVA games, unstructured supplementary service data, mobile internet and multimedia messaging services. After the launch of our 3G cellular services, we have provided video phone, video on demand and other related 3G cellular value-added services as well. In addition to creating additional sources of revenue, we believe these services enhance customer loyalty and satisfaction and increase cellular traffic. Revenues from mobile data services represented approximately 3.3%, 4.4% and 5.7% of our total cellular revenues in 2004, 2005 and 2006, respectively.

Internet and Data Services

We have experienced continued growth in our internet and data services. Our internet and data revenues represented approximately 21.2%, 22.8% and 24.9% of our revenues in 2004, 2005 and 2006, respectively. We provide:

- Internet services, including HiNet (our internet service provider), ADSL internet access, internet value-added services, wireless local area networks and fiber-to-the-building services; and
- data services, including leased line services, managed data services and internet data center services.

The following table sets forth our revenues from internet and data services for the periods indicated.

	Year ended December 31,		
	2004	2005	2006
		(in billions)	
	NT$	NT$	NT$
Internet and data revenues:			
Internet	29.5	32.1	35.5
Data	9.8	10.1	10.8
Total Internet and data	39.3	42.2	46.3

Internet Services

HiNet and Internet Access

The following table sets forth our revenues from internet services for the periods indicated.

	Year ended December 31,		
	2004	2005	2006
		(in billions)	
	NT$	NT$	NT$
Internet revenues:			
Narrowband access	0.7	0.3	0.1
Narrowband Internet service	0.7	0.5	0.3
Broadband access (ADSL only)	14.7	16.2	18.0
Broadband Internet service (ADSL only)	10.8	12.1	13.2
Other Internet	2.6	3.0	3.9
Total Internet	29.5	32.1	35.5

We are the largest internet service provider in Taiwan, with a market share of 61.2% as of December 31, 2006. As of December 31, 2006, HiNet had approximately 4.3 million subscribers, and our number of subscribers increased by a 6.1% compound annual growth rate over the two years ended December 31, 2006.

The following table sets forth HiNet's subscribers as of each of the dates indicated.

	As of December 31,		
	2004	2005	2006
	(in thousands, except percentages)		
Total Internet access subscribers in Taiwan	8,036	7,271	7,037
HiNet subscribers			
HiNet dial-up subscribers	1,376	1,166	1,043
HiNet ADSL subscribers	2,413	2,909	3,063
Other access technology subscribers	32	38	199
Total HiNet subscribers	3,821	4,113	4,305
Market share(1)	47.5%	56.6%	61.2%

(1) Based on data provided by the MOTC.

We have maintained our leading market position despite a highly competitive market with over 181 internet service providers in Taiwan. We expect the competitive conditions currently prevailing in the internet service provider market to continue to intensify.

Customers can access HiNet through various technologies. We provide narrowband dial-up internet access through connections based on standard telephone modems. We provide broadband internet access through connections based on ADSL and our fiber-to-the-building technology. As of December 31, 2006, approximately 79.5%, or 3.1 million, of subscribers who access the internet through our ADSL are our HiNet subscribers, and we expect this ratio to increase as a result of recent promotions to attract dial-up customers to upgrade to broadband internet access.

We are the largest broadband internet access provider in Taiwan in terms of subscribers. We began providing our ADSL service in August 1999 and had approximately 3.9 million subscribers as of December 31, 2006. Our market share of Taiwan's broadband market was approximately 83.0%, 85.3% and 85.5% in 2004, 2005 and 2006, respectively. Our ADSL service allows for transmission of data at high access rates and offers high-speed broadband internet access services. We also provide ADSL services to other internet service providers that do not have their own network infrastructure. By the end of 2006, the total number of our FTTB customers reached approximately 185,000. In addition, 179,621 of the subscribers who access the internet through FTTB are Hinet subscribers. As of December 31, 2006, approximately 4.2% of subscribers who access the internet through our FTTB were also HiNet subscribers, and we expect this ratio to increase as a result of recent promotions to attract ADSL and dial-up customers to upgrade to FTTB internet access.

The following table sets forth our ADSL service subscribers as of each of the dates indicated.

	As of December 31,		
	2004	2005	2006
Our ADSL service subscribers (in thousands)	3,071	3,654	3,851
Average downlink speed (Mbps)(1)	1.60	2.14	2.56

(1) Average downlink speed is calculated by dividing the total downlink speed subscribed by the total number of subscribers as of the relevant date.

Our ADSL service offers downlink speeds that range from 256 kilobits per second to 12 megabits per second and uplink speeds that range from 64 kilobits per second to 1 megabit per second. In December 2001, we began providing symmetrical digital service with uplink and downlink speeds of 512 kilobits per second. After our promotions in 2004 to increase customer access speeds, including our promotions for subscribers to upgrade to higher-speed access, the average uplink and downlink speeds of our subscribers have increased substantially. As of December 31, 2005, approximately 59% of our subscribers had subscribed for downlink speeds of over

2Mbps per second and our average downlink speed was 2.14 Mbps. As of December 31, 2006, over 62.5% of our subscribers had subscribed for downlink speeds of over 2 Mbps and our average downlink speed was 2.56 Mbps. Our FTTB service offers downlink speeds of 10 megabit per second and uplink speeds of 2 megabit per second.

We have experienced limited competition in the ADSL service market because other fixed line operators and cable operators have not established a nationwide network infrastructure to provide this service.

Our revenues from providing internet access are generated from installation fees, monthly subscription fees and usage fees from fixed line telephone calls made to access HiNet, which are recorded as internet services revenues rather than as fixed line revenues. Usage fees from fixed line telephone calls made to access internet service providers other than HiNet are recorded as local fixed line revenues.

Charges for our HiNet dial-up service include a monthly fee entitling the subscriber to a fixed number of minutes of service, with an additional charge per minute when the fixed number of minutes is exceeded. Alternatively, we offer our subscribers an unlimited number of minutes for a fixed monthly fee. Charges for our ADSL service include one-time installation charges and monthly subscription fees. These charges vary based on connection speed.

The following table sets forth our average revenues per user for each of the periods indicated.

	Year ended December 31,		
	2004	2005	2006
	NT$	NT$	NT$
Average revenue per HiNet dial-up subscriber per month(1)	81	50	33
Average revenue per ADSL subscriber per month(2)	863	780	768
Average revenue per FTTB subscriber per month(3)	3,695	3,795	1,165

(1) Average revenue per HiNet dial-up subscriber per month is calculated by dividing the total local telephone usage revenues generated by HiNet dial-up subscribers and internet access revenues by the average of the number of our HiNet dial-up subscribers on the first and last days of the period and dividing the result by the number of months in the relevant period.

(2) Average revenue per ADSL service subscriber per month is calculated as the sum of (a) ADSL access revenues for the relevant period divided by the average of the number of our ADSL service subscribers on the first and last days of the period divided by the number of months in the relevant period and (b) HiNet ADSL internet service provider revenue divided by the average of the number of HiNet ADSL subscribers on the first and last days of the period divided by the number of months in the relevant period.

(3) Average revenue per FTTB service subscriber per month is calculated as the sum of (a) FTTB access revenues for the relevant period divided by the average of the number of our FTTB service subscribers on the first and last days of the period divided by the number of months in the relevant period and (b) HiNet FTTB internet service provider revenue divided by the average of the number of HiNet FTTB subscribers on the first and last days of the period divided by the number of months in the relevant period.

Our average revenues per subscriber have declined over the last three years due to increasing competition. In addition, we were required by the regulatory authority at that time, the Directorate General of Telecommunications, to decrease our tariffs by an average of 24% in June 2004. However, we expect our average revenue per subscriber for broadband services to decline more gradually going forward, as subscribers migrate towards more expensive, higher bandwidth internet services.

Internet Value-added Services

Our HiNet portal at *www.hinet.net* provides value-added services to our subscribers, such as network security, Blog, travel, gaming, e-learning, financial information, music, video, anti-virus and links to other portals. We charge fees for some of these services. We also receive commissions for transactions completed on some of these other portals. Our broadband internet portal at *www.hichannel.hinet.net* offers online entertainment services through the internet. In particular, our HiNet broadband (ADSL and FTTB) customers can access music, television programs, movies and other multi-media content on demand. We charge access fees for some of this content. We expect the revenues generated from these value-added services to grow as a percentage of our total internet and data services revenues. The information contained in our HiNet portal and broadband internet portal is not a part of this annual report. Our internet value-added services revenues as a percentage of total internet revenues were 5.8%, 6.9% and 6.4% in 2004, 2005 and 2006, respectively.

Wireless Local Area Network Service

We launched our wireless local area network service in May 2002. As of December 31, 2006, we had a total of approximately 30,262 residential and business customers that lease our access points. In addition, we have established 1,009 hot spots in public areas, such as airports and international convention centers, where individuals can access our wireless local area network.

Data Services

The following table sets forth our revenues from data services for the periods indicated.

	Year ended December 31,		
	2004	2005	2006
		(in billions)	
	NT$	NT$	NT$
Data revenues:			
Leased line	7.6	7.6	8.0
Other	2.2	2.5	2.8
Total data	9.8	10.1	10.8

Leased Line Services

We are the leading provider of domestic leased line services in Taiwan. We are also a leading provider of overseas leased line services. Leased line services involve offering exclusive lines that allow point-to-point connection for voice and data traffic. Leased lines are used by business customers to assemble their own private networks and by telecommunications service providers to establish networks to offer telecommunications services.

We provide data transmission services to major corporate customers in Taiwan. We also provide leased lines to other cellular and fixed line service operators for interconnection with our fixed line network and for connection within their networks. Since August 2001, licenses have been awarded to four undersea cable operators to engage in leased line services. Demand for high-speed data transmission services has been growing rapidly, as a result of growing consumer demand and lower tariffs due to increased competition. In particular, the total bandwidth of our lines leased decreased by 3.3% over the two years ended December 31, 2006.

The following table shows the bandwidth of lines leased to third parties as of each of the dates indicated.

	As of December 31,		
	2004	2005	2006
		(in gigabits per second)	
Total bandwidth	501.7	495.8	469.4

Rental fees for local leased lines are generally based on transmission speed while domestic long distance and international long distance leased line rental fees are generally based on transmission speed and distance.

We continue to experience a decline in rental fees for all of our leased line products. The decline in rental fees since 2000 has been substantial, particularly for international leased lines, partly as a result of competition from new international leased line service providers. In response, we continue to implement marketing and service campaigns to retain our high-value corporate customers.

Managed Data Services

We provide a wide range of managed data services, including frame relay services, asynchronous transfer mode services, and virtual private network services. Frame relay services provide high-speed data communications linking remote sites. Asynchronous transfer mode services are used to handle high-bandwidth, integrated voice, video, data and internet traffic between sites.

Internet Data Center Services

Internet data centers are facilities providing the physical environment necessary to keep computer network servers running at all times. These facilities are custom-designed with high-volume air conditioning temperature control systems, secure access, reliable electricity supply and connections to high-bandwidth internet and data networks. Data centers house, protect and maintain network server computers that store and deliver internet and other network content, such as web pages, applications and data. We currently have 13 internet data centers in Taiwan. We offer co-location, web hosting and application service provider services. To expand our internet data center services and strengthen our cooperation with international telecommunications operators, we acquired 70% equity from Chief Telecom, which increased our internet data center market share to 51%.

Other Telecommunications Services

We provide other telecommunications services, including MOD services, satellite services, telephone directories, corporate solution services and billing handling services and paging services. In 2004, we generated NT$3.5 billion, or approximately 1.9% of our revenues. In 2005, we generated NT$3.2 billion or approximately 1.8% of our revenues, from these various other telecommunications services. In 2006, we generated NT$4.1 billion, or approximately 2.1% of our revenues, from these various other telecommunications services. We also lease real estate owned by us to third parties.

To expand our internet data center services and strengthen our cooperation with international telecommunications operators, we acquired 70% equity from Chief Telecom, which increased our internet data center market share to 51%.

Multimedia on Demand Services

We launched our multimedia on demand, or MOD, service in Taipei County and Keelung City in March 2004. We expanded this service to cover 13 counties and cities of Taiwan by the end of 2006. Using video streaming technology through a set top box that connects to our ADSLs, our customers can access TV programs and other services. We had 33 broadcasting channels, and over 1,600 on-demand programs and served approximately 249,203 subscribers as of December 31, 2006. In addition, our video-on-demand service provides movies, e-learning and music programs for home entertainment. We also plan to introduce popular channels and bundle them with other pay channels in order to enhance our service content and satisfy our customers' needs.

Satellite Services

We are a 50% owner of the ST-1 telecommunications satellite. Singapore Telecommunications Ltd. owns the remaining 50%. ST-1 was launched on August 26, 1998 and began commercial operations on December 1, 1998. We lease out transponder capacity on ST-1 and provide satellite lease circuits. In addition, we have two satellite communication centers that enable us to provide satellite value-added services and back up systems for use in major emergencies. We also provide satellite services to Southeast Asia.

Telephone Directories

We are the largest provider of classified advertising directory and associated products and services in Taiwan with over 60 years of experience in publishing and distributing telephone directories to households and businesses in Taiwan. Our yearly circulation is approximately 6.3 million copies. To address the needs of advertisers and users for multiple platforms of directory search, we offer buyers and sellers related directory products and services in print, through online directories and by operator-assisted search services. In addition, we established Chunghwa International Yellow Pages Corporation in 2007, changing previous paper search business into a more advanced search service combining electronic yellow page and telephone voice cross-platform services.

Paging Services

We offered nationwide and regional paging services in Taiwan. In addition to traditional paging services, we offered a broad range of wireless information services, including stock quotes on our "InterMessenger" service, weather information, news and agricultural information. We had approximately 35,520 and 23,620 paging subscribers as of December 31, 2005 and 2006.

Interconnection

We provide interconnection of our fixed line network with other cellular operators and, since July 2001, with other fixed line operators.

The following table sets forth our interconnection fee revenues and costs for the periods indicated. These revenues and costs are included, depending on the nature of the call made, in local, domestic long distance services or cellular revenues and expenses, respectively.

	Year ended December 31		
	2004	2005	2006
		(in billions)	
	NT$	NT$	NT$
Interconnection fee revenues:			
Local	3.1	3.0	2.9
Domestic long distance	1.3	1.1	1.0
Cellular	6.3	7.0	7.3
Interconnection costs:			
Fixed line	0.7	0.4	0.2
Cellular	5.6	6.2	6.7

Currently, tariffs for telephone calls between our fixed line subscribers and cellular subscribers of other cellular operators are set by the cellular operators. The cellular operators pay us interconnection fees based on minutes of usage, regardless of who initiated the call. The former regulatory authority, the Directorate General of Telecommunications, and the current regulatory authority, the National Communications Commission, has consulted with the public regarding a change to the regulation that would allow us to set and collect tariffs for telephone calls made by our fixed line subscribers to cellular subscribers of other cellular operators. For such calls, cellular operators will no longer pay us interconnection fees, but we will be required to pay them termination charges. On September 5, 2006, the National Communications Commission announced that it proposes to make changes to the collection structure in two phases. In phase one, fixed line operators other than us would be able to set and collect tariffs for telephone calls made by their fixed line subscribers to cellular subscribers of other cellular operators. In phase two, we would be allowed to set and collect tariffs for telephone calls initiated by our subscribers if (i) the market share of our local telephone services falls to and under 90% or (ii) the transfer acceptance rate of our number portability service and the acceptance rate for leasing out local loop both reach 85% every month for six consecutive months and we share our telecom switching centers with other fixed line operators. If and when such proposal may be implemented is uncertain.

The start of many happy returns.

In the interim, the former regulatory authority, the Directorate General of Telecommunications has approved, effective January 2004, an interconnection rate of NT$0.59 per minute for calls initiated by cellular subscribers, and NT$0.814 per minute for calls initiated by fixed line subscribers. The interconnection rate between our fixed line subscribers and other fixed line subscribers is approximately NT$0.32 per minute. The interconnection rate between our cellular subscribers and other cellular subscribers is approximately NT$2.15 per minute.

All interconnections by the networks of cellular operators and other fixed line operators with our fixed line network are made through dedicated lines that these operators lease from us. We record the revenue for these leased lines as part of our internet and data revenues.

We expect an increase in interconnection revenue due to an increase in traffic between different fixed line networks as a result of the competition from other fixed line operators.

In accordance with governmental regulations, the contracts governing our interconnection arrangements must specifically address a number of prescribed issues. For example, our interconnection charge should reflect our cost with respect to the network elements used. In addition, cost increases are subject to approval by the regulatory authorities. We expect that our interconnection contracts will generally be reviewed annually, although we may also enter into long-term contracts.

Marketing, Sales and Distribution

Marketing Strategy

In order to retain and expand our large customer base and to encourage our customers to increase their use of our services and products, we continue to focus our marketing strategy on the following areas.

- *Services, Products and Bundled Offerings*. We continually develop new value-added services and products, and bundle our services and products based on different market segments, with the aim of increasing our high-usage customers and enhancing customer loyalty.
- *Pricing and Promotions*. We design flexible pricing packages that allow customers to select structures best tailored to their usage patterns, and design special promotional packages to encourage usage. For example, we have provided our "Friends and Family" and "Energy Plan" promotion package to attract cellular subscribers.
- *Distribution Channels*. We seek to facilitate customer subscription by adding more service points. In addition, we seek to broaden our *distribution* reach by strengthening our cross-industry alliances and marketing relationships. Furthermore, we seek to expand our sales channels by implementation of a sales agent system. We have also developed staff incentive programs to better motivate our sales staff.
- *Business Customers*. We have expanded our customer focus to include small- and medium-sized enterprises in addition to large corporations. We seek to serve the needs of large corporate customers by devoting a project manager or project engineer to *service* these customers. These account managers are responsible for developing customized solutions and tariff packages to meet the specific needs of our customers. We continually update and expand our service offerings so that we can remain a one-stop telecommunications services provider to our corporate customers and provide for all of their telecommunications needs. Our dedicated local teams serve the needs of small- and medium-sized enterprises. These teams also use our data bank to identify and target potential clients for promoting our e-commerce and cellular services. In addition, we help our corporate customers improve their efficiency and competitiveness by creating information systems for them.
- *Advertising*. We are committed to further strengthening the Chunghwa Telecom brand and image as well as strengthening and expanding market recognition *of* our specialized product brands, such as HiNet and emome. We plan to leverage our leading market position and status to strengthen the overall advantage of our product brands.

Sales and Distribution

Our marketing department at our corporate headquarters in Taipei is responsible for central business planning and formulating our marketing strategies and objectives. We have six business divisions, each of which has its own marketing department that is responsible for business and marketing planning.

We also have 24 operations offices, 322 service centers and 121 exclusive service stores located throughout Taiwan that are responsible for operations, sales and customer service in their local areas.

Customer Service and Billing

We believe our reputation for quality customer service has helped us attract new customers and maintain customer loyalty. We regularly survey our customers to improve our service and better understand market demand and subscriber preferences, and seek to develop products and services accordingly.

We provide the following services to our customers:

- 24-hour customer service and technical support through our service centers, call centers and website;
- English billing documents available upon request;
- free of charge itemized billing for international and domestic long distance calls;
- bill payment services at 24-hour convenience stores, bank service counters, automatic teller machines, direct debit, over the phone, website (www.cht.com.tw), cellphone emome and service centers throughout Taiwan;
- online information and bill payment services at our website, *www.cht.com.tw*, and customer service hotline for telephone payment; and
- consolidated and automated billing for all services.

Network Infrastructure

Our network infrastructure consists of transmission networks that convey voice and data traffic, switching networks that route traffic between networks, and cellular, paging, internet, leased line and data switching networks.

We purchase most of our network equipment from well-known international suppliers. As part of the purchase contract, these suppliers deliver and install the equipment for us. We also purchase from local suppliers a variety of components such as transmission lines, switches, telephone sets and radio transmitters.

Approximately 15,086 of our employees were engaged in network infrastructure development, maintenance, operation and planning as of December 31, 2006.

Internet Protocol Broadband Backbone Network

Our internet protocol broadband backbone network consists of a core network and edge networks. We completed the construction of our high-speed internet protocol backbone network at the end of 2006 with 14 sets of 640 Gbps gigabit switch routers for the core network and more than 54 sets of 320 Gbps and 80 Gbps gigabit switch routers for the edge networks. We believe this network will enable us to meet the increasing demand for broadband access and broadband multimedia services. Moreover, this network will also serve as the backbone for our 3G cellular services and VoIP services.

Transmission Networks

As of December 31, 2006, our transmission networks consisted of 1,005,180 fiber kilometers of fiber optic cable for trunking and 1,036,437 fiber kilometers of fiber optic cable for local loop.

Between 1999 and 2002, we made significant progress in the upgrading of our plesiochronous digital hierarchy network transmission facilities to synchronous digital hierarchy network transmission facilities. Plesiochronous digital hierarchy is the traditional technology for voice network transmission systems. Synchronous digital hierarchy architecture is an advanced technology that allows for instantaneous rerouting and eliminates downtime in the event of a fiber cut. In addition, synchronous digital hierarchy offers better reliability and performance for optical fiber transmissions at a lower operating cost. In December 2002 we installed synchronous transport module 64 multiplexer and 10 gigabit capacity 32-wavelength dense wavelength division multiplexing equipment on our long-haul backbone network. Our synchronous transport module 64 multiplexer can multiplex several low speed signals into a 10 gigabit per second high-speed signal. Dense wavelength division multiplexing equipment uses a technology that puts data from different sources together on an optical fiber with each signal carried on its own separate wavelength. Both synchronous transport module 64 multiplexer and dense wavelength division multiplexing equipment can increase our network capacity. Furthermore, between 2003 and 2006, we deployed twenty-five 32-wavelength optical add-drop multiplexer rings in Taipei, Taichung, Tainan and Kaohsiung, metropolitan areas in order to provide new data services such as gigabit Ethernet, fiber channel, 2.5 gigabit packet over synchronous digital hierarchy and 10 gigabit Ethernet. To meet the demand for broadband services, we completed the deployment of a next generation synchronous digital hierarchy network in June 2005. The next generation synchronous digital hierarchy network can provide gigabit Ethernet over synchronous digital hierarchy service.

Based on the transmission network described above, we launched connection circuit service of 10 gigabit packet over synchronous digital hierarchy and 10 gigabit Ethernet to the government's Taiwan Advanced Research and Education Network in 2003.

As part of our strategic focus on the internet and data markets, our local loop connections use ADSL technology. This enables us to deliver high-speed internet, multimedia and other data services to our customers. Substantially all of our installed telephone lines are capable of delivering ADSL services. As of December 31, 2006, we have constructed approximately 5.13 million lines of ADSL and had 3.85 million ADSL users. In addition, the ethernet-based fiber to the building system is also introduced into our access network to provide broadband services, such as MOD, high speed internet access and virtual private network, or VPN.

As of December 31, 2006, we have constructed approximately 300,000 ports of VDSL and had 165,000 users. Our FTTB (VDSL) can offer high-speed broadband Internet access rates up to 100 Mbps.

Switching Networks

Domestic telecommunications network. Our domestic public switched telephone network consists of 19 message areas connected by a long distance network. As of December 31, 2006, we had 66 long distance exchanges, which are interconnection points between our telecommunications network.

We currently have intelligent networks installed over our public switched telephone networks for our domestic long distance and international networks, as well as a local intelligent network in the Taipei, Taichung and Kaohsiung metropolitan areas. Our intelligent network is designed to facilitate the use of value-added services by providing more information about calls and allowing greater management of those calls.

As of December 31, 2006, our domestic network included 17.4 million installed telephone lines, and reached virtually all homes and businesses in Taiwan.

International network. Our international transmission infrastructure consists of both submarine cable and satellite transmission systems, which link our national network directly to 103 telecommunications service providers in 59 international destinations.

International calls are routed between Taiwan and international destinations through one of our two international switching centers, one located in Taipei and the other in Kaohsiung. Each center had two international gateway switches. In total, we had a trunks capacity of 85,040 channels as of December 31, 2006.

We currently have invested in 20 submarine cables, six of which land in Taiwan. Our aggregate total capacity in the undersea cables in which we have invested is 104 gigabits per second.

Cellular Services Network

Our cellular services network consists of:

- cell sites, which are physical locations equipped with a base station consisting of transmitters, receivers and other equipment used to communicate through radio channels with subscribers' cellular telephone handsets within the range of a cell;
- base station controllers, which connect to, and control, the base station within each cell site;
- mobile switching service centers, which control the base station controllers and the processing and routing of telephone calls;
- gateway GPRS support nodes, which connect our GPRS network to the internet;
- serving GPRS support nodes, which connect the GPRS network to the base station controllers; and
- transmission lines, which link (1) with respect to the GSM network, the mobile switching service centers, base station controllers, base stations and the public switched telephone network, and (2) with respect to the GPRS network, the base station controllers, the support nodes and the internet.

The following table sets forth selected information regarding our cellular networks as of the dates indicated.

	As of December 31,		
	2004	2005	2006
GSM system			
GSM base stations	8,207	8,413	8,597
Switches	54	54	54
Lines of capacity (in thousands)	8,500	8,500	8,500
Taiwan population coverage	99.9%	99.9%	99.9%
Taiwan geographical coverage	90.0%	90.0%	90.0%
GPRS gateway support nodes	25	25	25
GPRS Serving support nodes	20	20	20
GPRS System capacity (in thousands)	1,000	2,000	2,000

	As of December 31, 2006
3G system	
3G base stations	3,637
Switches	8
Lines of capacity (in thousands)	2,400
Taiwan population coverage	80%
Taiwan geographical coverage	65%
GPRS gateway support nodes	16
Serving support nodes	11
System capacity (in thousands)	2,400

We provide cellular services based on the GSM network standards. We have dual band 900 MHz and 1800 MHz frequency spectrums for our GSM services. In addition, we have installed an intelligent network on our cellular services network infrastructure to enable us to provide prepaid services as well as a wide range of advanced call features and value-added services. We have also installed wireless application protocol gateways on our cellular services network that enable us to provide wireless application protocol services. We began providing cellular communications services based on the GPRS network standards in August 2001, using "emome" as the portal name.

As our subscriber base has continued to grow, we have increased the capacity of our intelligent network to more than 1.5 million subscribers. We also completed a system expansion of our cellular services network to accommodate more than 8.5 million subscribers (including 2 million GPRS subscribers) at the end of 2003. We have GPRS and 15 MHz paired spectrum plus 5 MHz unpaired spectrum in the 2 GHz frequency band for our 3G cellular services. In preparation for the launch of 3G cellular services, we contracted with Nokia Corporation to provide the core network, radio access network, service network, transmission network and maintenance network for approximately NT$12 billion over three years. As of December 31, 2006, we have completed the construction of approximately 3,637 third generation base stations with a network capacity of 2.4 million lines. Our 3G cellular network is comprised of 3,637 base stations, with a capacity of 2.4 million lines upon completion of contract. We launched our 3G cellular services on July 26, 2005. As of December 31, 2006, we had approximately 943,000 3G cellular services customers.

In September of 2006, we also selectively upgraded our third generation cellular network to provide HSDPA capabilities, with 82 base stations in downtown Taipei, Taiwan Taoyuan International Airport and certain industrial parks where the mobile internet usage is higher. We also plan to extend the HSDPA coverage to three metropolitan areas, Taipei, Taichung and Kaohsiung, in 2007, with data rates starting from the current 384kbps to the future 1.8Mbps, 3.6Mbps or higher, to attract more high average revenue per user, or ARPU, users.

Paging Network

The primary components of our paging network are:

- paging control systems, which receive and encode incoming messages; and
- base stations, which transmit messages to the subscriber's pager.

Our paging network uses, among other technologies, the open paging protocol developed by Motorola. This technology provides higher data rate, larger content capacity, longer battery life and better error correction capabilities than other existing paging technologies.

Internet Network

HiNet, our internet service provider, has the largest internet access network in Taiwan, with 35 points of presence, approximately 3,496 dial-up ports, approximately 4,535,050 broadband remote access server ports and a backbone bandwidth of approximately 424 gigabits per second as of December 31, 2006. We plan to increase HiNet's points of presence and backbone bandwidth to approximately 599 gigabits per second by the end of 2007.

HiNet's total international connection bandwidth is 51.3 gigabits per second as of December 31, 2006. As we expect that internet traffic flows to and from the United States will continue to increase, we plan to expand our bandwidth to the United States. We also plan to increase our links to other countries, including Japan, Korea, Hong Kong, Singapore, Mainland China, Malaysia and Australia.

Leased Line and Data Switching Networks

We operate leased line networks on both a managed and unmanaged basis. In addition, we operate a number of switched digital networks used principally for the provision of packet-switched, frame relay, asynchronous transfer mode technology and a multi protocol label switching internet protocol virtual private network. We have completed the construction of a digital cross connect system for provisioning and managing voice-grade data services throughout Taiwan with a total of 50 nodes. As of December 31, 2006, we had 2,623 frame relay ports, 5,441 X.25 ports, 7,867 asynchronous transfer mode ports and approximately 50,000 multi protocol label switching internet protocol virtual private network virtual ports.

Our data networks support a variety of transmission technologies, including X.25 protocol, frame relay and asynchronous transfer mode technology. We have also built up our HiLink virtual private network that combines internet protocol and asynchronous transfer mode technologies. The advantage of a HiLink virtual private network based on multi protocol label switching technology is that it can carry different classes of services, such as video, voice and data together to provide services with various qualities of service, high performance transmission and fast forward solution in an enhanced security network. A HiLink virtual private network can be accessed by an ADSL and can include built-in mechanisms that can deal with overlapping internet protocol addresses. Therefore, the network potentially is less costly and requires less management for business applications.

In 2006, we also selectively upgraded 82 base stations in downtown Taipei, Taoyuan International Airport and certain industrial park areas to provide HSDPA capability.

Competition

We face competition in virtually all aspects of our business.

Fixed Line

We are the largest fixed line service provider in Taiwan, with a market share of approximately 97.4% in terms of subscribers for local telephone services, approximately 83.6% in terms of traffic for domestic long distance telephone services and approximately 58.3% in terms of traffic for international long distance telephone services in 2006. Three new providers, namely, Taiwan Fixed Network, New Century Infocomm Tech. Co., Ltd. and Asia Pacific Broadband Telecom Co. Ltd., have provided fixed line services since June 2001. We believe these operators are primarily focused on international long distance services. In addition, we anticipate that these operators will focus on corporate customers, which typically generate higher profit margins than residential customers. Since August 2001, four undersea cable services licenses have been granted. These undersea cable operators, as well as internet service providers and international simple resale operators, have begun offering international leased line services to other fixed line operators, internet service providers and international simple resale operators.

We are required by Republic of China regulations to provide number portability and unbundled local loop access.

Our domestic long distance services compete with cellular services as people increasingly use cellular telephones. In addition, our international long distance services compete with international long distance resale services and alternative mediums for making international calls, including VoIP technologies, such as those provided by Skype. One of our competitors has sought an alliance with Taiwan Railway Administration to use its infrastructure to deliver telecommunications services. We believe that the fixed line competition in Taiwan will be primarily based on price, quality of service, network coverage and customer services, such as call centers and unified billing.

Cellular

There are currently three major GSM cellular operators in Taiwan, namely, Taiwan Mobile Co., Ltd., Far EasTone Telecommunications Co., Ltd. and us. Based on data provided by the National Communications Commission, as of December 31, 2006, we were the largest cellular operator, with a 40.9% market share in terms of 2G subscribers. In addition, there are two new 3G cellular operators in Taiwan, namely Asia Pacific Broadband Wireless Communications Inc. and Vibo Telecom Inc., as well as one personal handyphone system operator, First International Telecom. Furthermore, the government issued 12 mobile virtual network operator licenses to New Century InfoComm Tech. Co., Ltd., KGEx.com, Hicall Telecom Co., Ltd., China Motion Telecom (Taiwan) Limited, Taiwan Fixed Network, 10net, INFOTECH International Corp., Network Telecommunication Co., Ltd., AURORA Telecom Corporation, ARCOA Communication Co., Ltd., Chung-Hwa

Wideband Best Network and Chia Hsin Food & Synthetic Fiber Co., Ltd. which allow operators without a spectrum allocation to provide cellular services by leasing the capacity and facilities of a cellular service network from a licensed cellular service provider. We may cooperate with other mobile virtual network operators in Taiwan in future. We compete in the wireless services market primarily on the basis of price, quality of service, network reliability and attractiveness of service packages.

Internet and Data

Our primary competitors in internet and data services include:

Internet services:

- Internet services providers: SeedNet, Asia Pacific Online, GigaMedia and So-net Taiwan;
- Broadband internet access providers: Asia Pacific Broadband Telecom Co., Ltd., GigaMedia, Taiwan Fixed Network and New Century Infocomm Tech. Co., Ltd.; and
- Cable operators: Eastern Multimedia Co., Ltd., China Network Systems Co., Ltd., Taiwan Broadband Communications Co., Ltd., Pacific Broadband Co., Ltd., and Taiwan Infrastructure Technology Co., Ltd.

Data services:

- Leased line service providers: Taiwan Fixed Network, New Century Infocomm Tech. Co., Ltd., Asia Pacific Broadband Telecom Co. Ltd., Asia Netcom, Reach Global Services Ltd., FLAG Telecom and Taiwan International Gateway Corporation.

We are the largest provider of internet services in Taiwan. As of December 31, 2006, we had a 61.2% share of the internet service market in terms of subscribers and a 85.5% share of the broadband internet access market in terms of subscribers. We compete in the internet and data services market primarily on the basis of price, technology, speed of transmission, amount of bandwidth available for use, network coverage and value-added services.

Properties

Our properties consist mainly of land, land improvements and buildings located throughout Taiwan. We have recently begun investing in real estate revitalization projects as part of our efforts to make more productive use of certain undeveloped or underdeveloped properties that we own. Our revitalization projects include the development of high-tech residences, commercial offices and resorts. As of the date of this annual report, we have six such projects underway relating to properties in and around Taipei and other parts of Taiwan.

Insurance

We do not carry comprehensive insurance for our properties or any insurance for business disruptions. We do, however, maintain in-transit insurance for key materials, such as cables, equipment and equipment components. We also carry insurance for the ST-1 satellite while it is in orbit. As part of our efforts to enhance our risk management capabilities, we have been assessing our equipment that requires the most time and cost to repair or replace, in order to determine whether and to what extent we should carry fire insurance for such equipment.

Employees

Please refer to "Item 6. Directors, Senior Management and Employees—D. Employees" for a discussion of our employees.

Our Pension Plans

We have two types of employee retirement plans, which are administered in accordance with the Republic of China Labor Standards Act and the Republic of China Labor Pension Act.

Legal Proceedings

A portion of the land that we used during the period from July 1, 1996 to December 31, 2004 was co-owned by us and Taiwan Post Co., Ltd. (the former Chunghwa Post Co., Ltd, Directorate General of Postal Service). In accordance with the claims process in Taiwan, on July 12, 2005, the Taiwan Taipei District Court sent a claim notice to us to reimburse Taiwan Post Co., Ltd. in the amount of $768 million for land usage compensation due to the portion of land usage area in excess of our ownership, along with interest calculated at 5% interest rate from April 1, 2002 to the payment date. However, we believe that the computation used to derive the land usage compensation amount is inaccurate because most of the compensation amount has expired as a result of the expiration clause. Therefore, we have filed an appeal at the Taiwan Taipei District Court. As of the date of this annual report, the case is still in the appeals process. While we cannot accurately predict the eventual resolution of this litigation, we believe that the final outcome will not have a material adverse effect on our results of operations or our financial condition.

We are also involved in other litigation, arbitration or administrative proceedings in the ordinary course of our business. Although we cannot accurately predict the outcome of these matters, we do not expect any proceeding, if determined adversely against us, to have a material adverse effect on our business, financial condition or results of operation.

Capital Expenditures

See "Item 5. Operating and Financial Review and Prospects—B. Liquidity and Capital Resources—Capital Expenditures" for a discussion of our capital expenditures.

Enforceability of Judgments in Taiwan

We are a company limited by shares and incorporated under the Republic of China Company Law and the Statute of Chunghwa Telecom Co., Ltd. All of our directors and executive officers, our supervisors and some of the experts named in this annual report are residents of Taiwan and a substantial portion of our assets and the assets of those persons are located in Taiwan. As a result, it may not be possible for investors to effect service of process upon us or those persons outside of Taiwan, or to enforce against them judgments obtained in courts outside of Taiwan. We have been advised by our Republic of China counsel that in their opinion any final judgment obtained against us in any court other than the courts of the Republic of China in connection with any legal suit or proceeding arising out of or relating to the ADSs will be enforced by the courts of the Republic of China without further review of the merits only if the court of the Republic of China in which enforcement is sought is satisfied that:

- the court rendering the judgment has jurisdiction over the subject matter according to the laws of the Republic of China;
- the judgment and the court procedure resulting in the judgment are not contrary to the public order or good morals of the Republic of China;
- if the judgment was rendered by default by the court rendering the judgment, we were served within a reasonable period of time in accordance with the laws and regulations of the jurisdiction of the court or process was served on us with judicial assistance of the Republic of China; and
- judgments at the courts of the Republic of China are recognized and enforceable in the court rendering the judgment on a reciprocal basis.

A party seeking to enforce a foreign judgment in the Republic of China would be required to obtain foreign exchange approval from the Central Bank of the Republic of China (Taiwan) for the payment out of Taiwan of any amounts recovered in connection with the judgment denominated in a currency other than NT dollars if a conversion from NT dollars to a foreign currency is involved.

Regulation

Overview

Before March 1, 2006, the Taiwan telecommunications industry was subject to extensive regulation by and under the supervision of the former competent authorities, the Ministry of Transportation and Communications and the Directorate General of Telecommunications pursuant to the provisions of the Telecommunications Act and various other telecommunications laws and regulations, as well as regulations under various laws of general application. Since March 1, 2006, regulatory authority over the Taiwan telecommunications industry has been transferred from the Ministry of Transportation and Communications and the Directorate General of Telecommunications to the National Communications Commission.

We were subject to the Statute of Chunghwa Telecom Co., Ltd. prior to our privatization. Although we have been privatized, the Legislative Yuan has not yet abolished the Statute of Chunghwa Telecom Co., Ltd., and at this time, the Statute of Chunghwa Telecom Co., Ltd. is still applicable to us.

Regulatory Authorities

Prior to March 1, 2006, we were under the supervision of the Ministry of Transportation and Communications and the Directorate General of Telecommunications. On March 1, 2006, the National Communications Commission was formed in accordance with the National Communications Commission Organization Law, or Organization Law, which was intended to transfer regulatory authority over the Taiwan telecommunications industry from the Ministry of Transportation and Communications and the Directorate General of Telecommunications to the National Communications Commission. The National Communications Commission is to be comprised of thirteen commissioners and is currently comprised of nine commissioners who have been recommended by the government and opposition political parties in the Legislative Yuan, as well as recommended by the Executive Yuan and approved by the Legislative Yuan. However, the Executive Yuan considered the composition of the National Communications Commission unconstitutional and petitioned the Grand Justices of the Republic of China, or the Grand Justices, to interpret the constitutionality of the formation of the National Communications Commission and the procedure for nominating commissioners to serve on the National Communications Commission. On July 21, 2006, the Grand Justices rendered an interpretation and held that the relevant provisions under the Organization Law as to the nomination procedures for the commissioners of the National Communications Commission were unconstitutional. However, the Grand Justices granted a grace period allowing such provisions of the Organization Law to remain in effect until December 31, 2008. Consequently, the National Communications Commission will have the authority at least until the end of 2008.

In accordance with the National Communications Commission Organization Law, the National Communications Commission is responsible for:

- formulating, implementing and interpreting telecommunications laws and regulations;
- issuing telecommunications licenses and regulating the operation of telecommunications industry participants;
- assessing and testing telecommunication systems and equipment;
- drafting and promulgating technical standards for telecommunications and broadcasting;
- classifying and censoring the contents of telecommunications and broadcasting;
- managing telecommunications and media resources in Taiwan;

- maintaining competition order in the telecommunication and broadcasting industries;
- governing technical standards in connection with the safety of information communications;
- managing and facilitating the resolution of disputes pertaining to the Taiwan telecommunications and broadcasting industries;
- managing offshore matters relating to Taiwan's telecommunications and broadcasting industries including matters of international cooperation;
- managing funds allocated for the development of Taiwan's telecommunications and broadcasting industries;
- monitoring, investigating and determining matters in relating to Taiwan's telecommunications and broadcasting industries;
- enforcing restrictions under telecommunications and broadcasting laws and punishing violators; and
- supervising other matters in relation to communications and media.

Prior to our privatization, in each fiscal year, the Legislative Yuan approved the annual budget prepared by us, as a state-owned enterprise, and the Ministry of Audit under the Control Yuan audited, and adjusted, our consolidated financial statements, including our earnings and losses. Our annual budget is no longer subject to Legislative Yuan or Control Yuan approval or audit.

Telecommunications Act

The Telecommunications Act and the regulations under the Telecommunications Act establish the framework and govern the various aspects of the Taiwan telecommunications industry, including:

- licensing of telecommunications services;
- restrictions on dominant telecommunications service providers;
- tariff control and price cap regulation;
- accounting separation system;
- interconnection arrangements;
- bottleneck facilities;
- spectrum allocation;
- provision of universal services;
- equal access;
- number portability; and
- ownership limitations.

Each of these aspects is described below. The Telecommunications Act also establishes a non-auction pricing system for assignment of radio frequencies.

Licensing of Telecommunications Services

Type I and Type II Service Providers

Under the Telecommunications Act, telecommunications service providers are classified into two categories:

Type I. Type I service providers are providers that install network infrastructure, such as network transmission, switching and auxiliary equipment for the provision of telecommunications services. Type I services include fixed line services such as local, domestic long distance and international long distance services, as well as interconnection, leased line, ADSL and satellite services and wireless services such as cellular, including 3G cellular, paging, mobile data and trunked radio services.

Type II. Type II service providers are defined as all telecommunications service providers other than Type I service providers. Type II services are divided into special services and general services. Special services include simple resale, VoIP international leased circuit and other services specified by the Ministry of Transportation and Communications before March 1, 2006 or by the National Communications Commission from March 1, 2006. General services include any Type II service other than special services.

Until 1996, we were the sole provider of Type I services in Taiwan. In 1996, the government opened the market for cellular, paging and trunked radio, mobile data and digital low power cordless telephone services. In 1998, the government opened the market for fixed line and mobile satellite services. In June 2001, the government granted licenses to three operators for establishing fixed line services, thereby opening the market for fixed line services. Since August 2000, the government has permitted four undersea cable operators to engage in the undersea cable leased-circuit business.

Commencing in 2007, the National Communications Commission began accepting applications for licenses to provide fixed line services in March, June, September and December of each year. The National Communications Commission also announced that it would accept applications for fixed line services on a monthly basis beginning in 2008. There is no limit on the number of fixed line licenses that they may decide to issue.

Granting of Licenses

Type I

Type I service providers are more closely regulated than Type II service providers. The government has broad powers to limit the number of providers and their business scope and to ensure that they meet their facilities roll-out obligations. Under the Telecommunications Act, Type I service providers are subject to pre-licensing merit review of their business plans and tariff rates.

Before March 1, 2006, licenses for Type I services were granted by the Ministry of Transportation and Communications through a three-step procedure. Applicants obtained a concession from the Ministry of Transportation and Communications. After obtaining a concession, the applicant obtained a network construction permit and an assignment of spectrum, in the case of cellular telephone services and satellite services, from the Directorate General of Telecommunications or the Ministry of Transportation and Communications prior to applying for a license. Upon completion of construction of its network and review by the Directorate General of Telecommunications, the applicant was granted a Type I license. The Ministry of Transportation and Communications had the authority to grant Type I licenses for each of fixed line services, wireless services and satellite services. Type I licenses have different minimum paid-in capital requirements for applicants and varying durations depending on the particular type of service.

Since March 1, 2006, the same procedure applies except that the licenses are granted by the National Communications Commission.

The Telecommunications Act further authorizes the competent authority, now the National Communications Commission to promulgate separate regulations governing each Type I service including the business scope of the Type I service provider, as well as the procedures and conditions for granting special permits and the length of the period of the special permits of each Type I service. Each holder of a Type I license will pay a fee ranging from 0.5% to 2% of the annual revenues generated from the particular Type I service for which a license has been granted.

Fixed Line Services. Under the Telecommunications Act, the Fixed Network Regulations adopted by the Ministry of Transportation and Communications continue to govern the issuance of fixed line service licenses and the business scope of fixed line providers. Fixed line service licenses are subdivided into the following categories:

- integrated services, including local, domestic long distance, international long-distance telephone services;
- local telephone services;
- domestic long distance telephone services;
- international long distance telephone services; and
- local, domestic long distance and international long distance leased line services.

We conduct our fixed line services through a license for integrated services.

Licenses for local telephone and integrated services are valid for 25 years. Licenses for domestic long distance and international long distance telephone services are valid for 20 years. Licenses for leased line services are valid for 15 years. The minimum paid-in capital requirement for integrated services providers and international undersea leased cable service providers is NT$40 billion and NT$800 million, respectively. The minimum paid-in capital requirement for both domestic and international long distance telephone service providers is NT$2 billion. The minimum paid-in capital requirement for local telephone service providers is NT$12 billion multiplied by the Local Network Operation Weights for the regions in which local network managerial rights have been granted to the service provider. The Local Network Operation Weights are calculated as the population of the region as a proportion of the entire population of Taiwan and are announced by the competent authority every three years.

In March 2000, the government granted three new concessions to fixed line services providers for integrated services. Recipients of these concessions are required to apply for a network construction permit to deploy broadband local access networks. Each recipient of these concessions is required to have capacity for 150,000 subscribers before they are able to apply for a fixed line license to launch their proposed services. The three fixed line service providers have since obtained fixed line licenses and are required to achieve capacity for one million subscribers by the sixth year following the date of the grant of the network construction permit awarded. Operators that applied for integrated service provider licenses after June 30, 2004 must achieve a capacity for 400,000 subscribers, ports or a combination of both by the fourth year following the date of the grant of the network construction permit.

Wireless Services. Under the Telecommunications Act, the Wireless Regulations promulgated by the Ministry of Transportation and Communications before March 1, 2006 or by the National Communications Commission from March 1, 2007 continue to govern the issuance of wireless services licenses and the business scope of wireless service providers. Wireless service licenses are subdivided into the following categories:

- cellular services;
- paging services;
- mobile data services;
- digital low-power cordless telephone services; and
- trunked radio services.

Wireless service licenses are granted to both regional and national service providers through review and bidding procedures.