Wireless services licenses for cellular and paging services are valid for 15 years, and licenses for mobile data, digital low-power cordless telephone and trunked radio are valid for ten years. The minimum paid-in capital requirement for regional cellular service providers and national cellular service providers is NT$2 billion and NT$6 billion, respectively.

We are licensed to provide cellular and paging services in Taiwan.

Third Generation Cellular Services. The Ministry of Transportation and Communications promulgated the Third Generation Mobile Telecommunications Services Regulations on October 15, 2001 and these regulations were last amended on November 17, 2005. The regulations govern voice and non-voice telecommunications services provided using the spectrum assigned by the Ministry of Transportation and Communications, and now governed by the National Communications Commission, that utilizes the IMT-2000 technical standards as announced by the International Telecommunications Union. Licenses for 3G cellular services were granted by the Ministry of Transportation and Communications. We have received our 3G cellular services license, which is valid from May 26, 2005 to December 31, 2018.

Satellite Services. Under the Telecommunications Act, the Satellite Regulations promulgated by the Ministry of Transportation and Communications govern the issuance of satellite services licenses and the business scope of satellite service providers. Satellite services licenses are subdivided into fixed satellite services licenses and mobile satellite services licenses.

Satellite services licenses are valid for 10 years. Minimum paid-in capital requirements for fixed satellite services providers and mobile satellite services providers are NT$100 million and NT$500 million, respectively.

We currently hold a fixed satellite services license, valid from December 10, 1998 to December 9, 2008.

Type II

The Telecommunications Act was amended in 1996 to open the market for all Type II services. Under the Type II Services Regulations as last amended on November 15, 2005, Type II services are divided into special services and general services. Special services include simple resale, VoIP, network telephone service of E.164 and non-E.164 user numbers (IP Phone Numbers), international leased circuit and other services previously specified by the Ministry of Transportation and Communications and now by the National Communications Commission. General services include any Type II service other than special services. The policy for granting a Type II service license is as follows:

- there is no limit on the number of licenses to be issued;
- licenses were granted by the Directorate General of Telecommunications before March 1, 2006 and are now granted by the National Communications Commission; and
- no bidding procedure is required.

We hold a license to operate all Type II services. Type II service licenses issued before November 15, 2005 are valid for ten years and may be renewed by application made two months prior to the expiration date. Type II service licenses issued or renewed on or after November 15, 2005 are valid for three years and may be renewed during the period commencing two months prior to the expiration date. There is no minimum paid-in capital requirement for Type II service providers. Our license to operate Type II services is included in our license to operate integrated services, and is valid from July 29, 2000 to July 28, 2025.

On December 27, 2005, the Ministry of Transportation and Communications promulgated regulations governing the fees payable for Type II licenses. Under these regulations, operators of simple resale or network telephone services of E.164 or non-E.164 user numbers must pay an annual license fee equal to 1% of annual revenues generated from these services during the previous year. Type II service operators providing services other than simple resale or network telephone services of E.164 or non-E.164 user numbers must pay license fees ranging from NT$6,000 to NT$150,000 depending on their respective paid-in capitals. The regulations do not apply to integrated services providers who are permitted to provide Type II services without additional Type II Licenses. The annual license fee for an integrated services provider operating Type II businesses is 1% of its annual revenues generated from its Type II services.

The Directorate General of Telecommunications started to process the applications for allocating E.164 and non-E.164 user numbers (IP phone numbers) on November 15, 2005. A few operators, including our company, have applied for IP phone numbers. We believe after these operators obtain the numbers and begin offering their services, competition in this area will become intense. We plan to provide VoIP service after we obtain IP phone numbers.

Restrictions on Dominant Telecommunications Services Providers

Under the Telecommunications Act, the regulations governing dominant telecommunications services providers apply only to Type I service providers. A Type I service provider is deemed to be dominant if it meets any of the following criteria and was declared by the Ministry of Transportation and Communications or now the National Communications Commission as dominant:

- controls key basic telecommunications infrastructure;
- has dominant power over market price; or
- has more than a 25% market share in terms of customers or revenues.

We have been declared by the former competent authority Ministry of Transportation and Communications as a dominant Type I service provider for fixed line and cellular services.

Under the Telecommunications Act, a dominant Type I service provider must not engage in the following activities:

- directly or indirectly hinder a request for interconnection with its proprietary technology by other Type I service providers;
- refuse to release to other Type I service providers the calculation methods of its interconnection fees and other relevant materials;
- improperly determine, maintain or change its tariffs or means of services;
- reject, without due cause, a request for leasing network components by other Type I service providers;
- reject, without due cause, a request for leasing lines by other service providers or subscribers;
- reject, without due cause, a request for negotiation or testing by other service providers or subscribers;
- reject, without due cause, a request for negotiation for co-location by other service providers;
- discriminate, without due cause, against other service providers or subscribers; or
- abuse its position as a dominant provider, or engage in other unfair competition activities as determined by the regulatory authorities.

In addition, a dominant Type I service provider is subject to special regulations limiting its tariff changes.

Tariff Control and Price Cap Regulation

In order to promote competition in the telecommunications market, and as part of the government's overall policy toward deregulation, the Telecommunications Act was amended in 1999 to abolish the former rate of return system on tariff setting in favor of price cap regulation of Type I services.

Under the Regulations Governing Tariffs of Type I Service Providers promulgated and last amended by the Ministry of Transportation and Communications on January 11, 2006, a dominant Type I service provider must submit its proposed adjustment in primary tariffs and promotional packages to the Directorate General of Telecommunications for onward submission to the Ministry of Transportation and Communications or, from March 1, 2006, directly to the National Communications Commission from for approval at least 14 days prior to the date of the proposed tariff changes and announce such change on media, website and business locations on the next day after the Ministry of Transportation and Communications or National Communications Commission grants the approval. The tariff change will come into effect seven days after the announcement.

Primary tariffs include:

- for fixed line local telephone services: monthly fees, usage fees, monthly rental fees of leased lines and pay telephone usage fees;
- for fixed line domestic long distance telephone services: usage fees and monthly rental fees of leased lines;
- for fixed line international long distance telephone services: usage fees and leased line monthly rental fees;
- for wireless services, including third generation cellular services: monthly rental fees and usage fees; and
- other fees or tariffs announced by the Directorate General of Telecommunications before March 1, 2006 or by the National Communications Commission from March 1, 2006.

In addition, a dominant Type I service provider is required to set wholesale prices for the provision of its telecommunication services to other telecommunication enterprises. The wholesale prices set by a dominant Type I service provider may be the retail price less fees and expenses which need not be incurred, but shall not higher than its promotional pricing. The Regulations Governing Tariffs of Type I Service Providers further prohibits a dominant Type I service provider from practising unfair competition against other telecommunication enterprises.

In comparison, all non-dominant Type I service providers are required to notify the Directorate General of Telecommunications or the National Communications Commission from March 1, 2006 and the public of their proposed tariff adjustments seven days prior to the date of the proposed tariff change with respect to all tariffs. In addition, changes in tariffs charged by Type I service providers (notwithstanding the type of their respective services) may not, in any event, be greater than the annual growth rate of the consumer price index in Taiwan adjusted by a set constant, which will be periodically determined and announced by the National Communications Commission. For example, if:

- the annual growth rate of the consumer price index in Taiwan minus the set constant is positive, the increased percentage of tariffs must not exceed such positive figure;
- the annual growth rate of the consumer price index in Taiwan minus the set constant is negative, the decreased percentage of tariffs must be at least the absolute value of such negative figure, and the tariffs used in the given year must not be higher than the decreased tariff; and
- the annual growth rate of the consumer price index in Taiwan minus the set constant equals to zero, no increase in tariffs is allowed to be made by any Type I service providers.

In December 2006, the National Communications Commission announced that effective from April 1, 2007 to March 31, 2010:

- the set constant to be applied to the tariff adjustment for leasing of ADSL under the fixed line integrated service and the local telephone service is the annual growth rate of the consumer price index in Taiwan plus 5.35%;

- the set constant to be applied to the tariff adjustment of call charges for call made from local telephones to the 900 MHZ and 1800 MHZ cellular services is the annual growth rate of the consumer price index in Taiwan plus 4.88%;
- the set constant to be applied to the tariff adjustment for the minimum monthly subscription fee charged for 900 MHZ and 1800 MHZ cellular services is the annual growth rate of the consumer price index in Taiwan plus 4.88%;
- the set constant to be applied to the tariff adjustment for prepaid phone card fees and other prepaid service fees charged for 900 MHZ and 1800 MHZ cellular services is the annual growth rate of the consumer price index in Taiwan plus 4.88%; and
- the set constant to be applied to the tariff adjustment for other services is equal to the annual growth rate of the consumer price index in Taiwan.

Type II service providers are free to establish their own tariff schemes, but are required to notify the Directorate General of Telecommunications or, from March 1, 2006 the National Communications Commission and the public upon adoption and upon any subsequent adjustments.

Accounting Separation System

The Telecommunications Act requires that a Type I service provider, including one who concurrently offers Type II services, separately calculate the profits and losses for its different services and prohibits any cross-subsidization among services that will impede fair competition.

Interconnection Arrangements

The Telecommunications Act requires all Type I service providers to allow other Type I service providers access to their networks. It further requires Type I service providers, within three months upon request by the other Type I service provider, to reach an agreement on the relevant terms for the interconnection. Prices charged for interconnection must be based on cost. If the parties fail to reach an agreement within three months, the National Communications Commission may, either at the request of the parties or on its own accord, arbitrate and determine the interconnection terms for the parties. According to the Administrative Rules for Network Interconnection Between Telecommunication Service Providers, the tariffs for communications (except for international communications) between a cellular telecommunications network and a fixed line telecommunications network) shall be collected by the call-originating services provider from its subscribers pursuant to the tariff schedules set by the cellular services provider, and the revenue or any uncollectible accounts from such tariffs shall go to the cellular services provider. In addition, tariffs for communications within cellular telecommunications networks shall be collected by the call-originating services provider from its subscribers pursuant to the tariff schedules set by such provider, and the revenue or any uncollectible accounts from such tariffs shall be for the account of to the call-originating services provider.

When a Type I service provider leases unbundled network components to another Type I service provider, the parties are required to negotiate the rental fee. Unbundled network components include:

- local loops;
- local switch transmission equipment;
- local trunks;
- toll switch transmission equipment;
- long-distance trunks;
- international switch transmission equipment;
- network interfaces;

- directory equipment and services; and
- signaling network equipment.

The Telecommunications Act authorizes the Directorate General of Telecommunications or, from March 1, 2006, the National Communications Commission to issue rules and regulations pertaining to interconnection. Under the Administrative Rules for Network Interconnection issued by the Directorate General of Telecommunications, as last amended on November 17, 2005, we, as a dominant Telecommunication service provider for fixed line and cellular services, are required to unbundle our network and provide cost-based interconnection charges calculated with reference to the total element long-run incremental cost incurred by us. We are required to submit our proposed calculations of the total element long-run incremental cost to the Directorate General of Telecommunications or, from March 1, 2006, the National Communications Commission, for its approval each year. Local loop unbundlings for both voice and data have been completed.

Bottleneck Facilities

Under the Telecommunications Act, when a Type I service provider cannot construct bottleneck facilities within a reasonable period of time or substitute those facilities by other available technologies, it may request for co-location on a fee basis from the owner of the facilities located at the bottleneck of the relevant telecommunications network. The owner of the facilities so requested may not reject these requests without due cause. The Ministry of Transportation and Communications had the authority, now held by the National Communications Commission, to prescribe facilities as bottleneck facilities, and has prescribed bridges, tunnels, lead-in tubes and telecommunications chambers located within buildings and horizontal and vertical telecommunications cables and lines as bottleneck facilities in relation to fixed line telecommunications networks. The National Communications Commission made an announcement on December 21, 2006, defining the local loop as bottleneck facilities.

Spectrum Allocation

The Ministry of Transportation and Communications previously and now the National Communications Commission allocates all telecommunications related frequencies primarily according to the standards set by the International Telecommunications Union. The 900 MHz and 1,800 MHz frequency bands have been allocated for cellular applications. A total of 40 MHz spectrum around the 800 MHz frequency band and a total of 130 MHz of spectrum around the 2 GHz band have been allocated for 3G cellular services.

Frequency allocation for fixed wireless platforms, such as wireless local loop and local multipoint distribution services, has already been set. Only some bands of the spectrum made available for these services are completely clear and there is partial usage in all other bands. The cost of frequency usage will be based on quantity.

Provision of Universal Services

A Type I service provider may be required by the Ministry of Transportation and Communications previously and now the National Communications Commission under the Telecommunications Act, to provide universal telecommunications services in remote or unprofitable areas. All Type I service providers and certain Type II service providers designated by the Ministry of Transportation and Communications previously and now the National Communications Commission will be required to contribute a fixed portion of their annual revenues to a universal services fund. Such a fund will be used to compensate any losses and management fees incurred by the relevant Type I service provider in providing the universal services. In April 2005, the Ministry of Transportation and Communications amended the Regulations on Telecommunications Universal Services, pursuant to which Type I service providers are required to provide universal telecommunications services and contribute to the costs and expenses of providing such services on a pro rata basis according to their respective revenues. The same regulation was further amended by the National Communications Commission in late 2006 to exclude certain services, such as coastline station reporting for ship accidents, from the provision of universal telecommunications services and revise the scope of access to data communications services.

Equal Access

As a result of the liberalization of Taiwan's telecommunications industry, a Type I service provider, including a 3G cellular services provider, is required to provide its subscribers with equal access to the domestic and international long distance telephone services provided by other service providers. A Type I service provider may provide equal access through pre-selection or call-by-call selection. Before July 1, 2005, all Type I service providers, including us, provide equal access only through call-by-call selection. When a subscriber makes a call using call-by-call selection, such subscriber has the option to select a service provider by dialing the network identification prefix assigned to the service provider of his choice. This will result in the automatic selection of the preferred service provider for the provision of relevant telecommunication services. Starting from July 1, 2005, all Type I service providers also provide equal access through pre-selection in Keelung City, Taipei City/County, Taichung City/County and Kaohsiung City/County. Equal access through pre-selection is available throughout Taiwan since January 1, 2006. The pre-selection function allows any subscriber to select in advance a long distance or international service provider of his or her choice. When such subscriber makes a call using this function, the communications network will automatically interconnect to the long distance or international network previously selected by such subscriber.

Number Portability

The Ministry of Transportation and Communications has adopted principles on fixed line number portability to enable customers to migrate their local and toll free fixed line telephone numbers. Under these regulations, we are required to provide fixed line number portability in seven major cities and counties in Taiwan upon the grant of the first fixed line license to a new entrant. We are also required to provide such number portability in other service areas no later than 181 days from the grant of such license and upon six months' advanced written notification received from the new fixed line service provider. Since May 2002, fixed line number portability has been made available to all customers in accordance with the then prevailing Fixed Network Regulations.

In November 2003, the Directorate General of Telecommunications promulgated the Administration Rules Governing Number Portability governing both fixed line and cellular services and the Fixed Network Regulations were revised to reflect such new regulation. Under the Administration Rules Governing Number Portability, which rules were amended on September 22, 2005, subscribers may migrate their telephone numbers when changing Type I service providers. The number portability for wireless services commenced on October 15, 2005.

Local Loop Unbundling

In December 2006, the National Communications Commission 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.

Co-location

We have been declared by the former competent authority Ministry of Transportation and Communications as a dominant Type I service provider for fixed line and cellular services. According to the Telecommunication Act, the Regulations Governing Fixed Network Telecommunications Businesses and the Administrative Rules for Network Interconnection between Telecommunication Service Providers, if any other service provider requests for co-location, we must negotiate with them, unless otherwise provided by laws or regulations. In 2005, the other three Type I fixed line service providers, Asia Pacific Broadband Telecom, Taiwan Fixed Network and

New Century InfoComm Co., requested co-location for 12 point of interconnect, or POI, sites and one cable station. In 2006, after negotiations, we completed all 12 POI sites and the one cable station. In addition, another Type I cellular service provider, Taiwan Mobile, also requested co-location for 15 POI sites. After negotiations, we completed 9 POI sites in 2006, with 6 other sites completed in March 2007.

Ownership Limitations

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. It is currently unclear whether the Ministry of Transportation and Communications has such authority to increase our foreign ownership limitation. If it is determined that the Ministry of Transportation and Communications did not have such authority and our foreign ownership is above 40%, we could be deemed in violation of the foreign ownership limitations and as a result we may be subject to monetary fines and our licenses to operate some of our businesses could be revoked. However, according to a draft amendment to the Telecommunications Act proposed by the National Communications Commission on August 31, 2006, the power to prescribe the limits on foreign ownership of our shares under the Telecommunications Act is to remain with the Ministry of Transportation and Communications.

Under the current Telecommunications Act, the Chairman of a Type I service provider is required to be a citizen of the Republic of China.

Administrative Fee Law

According to the Administrative Fee Law promulgated in December 2002, central and local governments, government agencies and schools are empowered to collect administrative fees from us and other telecommunications services providers for the telecommunications facilities built on public roads and properties. Under the Administrative Fee Law, Urban Road Act and Local Road Act, road authorities of municipal governments may collect usage fees from users of local roads, including us, for establishing lines along with the local roads. The fee schedule is set up in the Standard for Usage Fees of Local Roads.

In addition, under the Public Road Law, as amended in July 2003, administrative authorities of public roads may collect usage fees from the users of public roads. According to the Rules Governing Collection of Usage Fees on Public Roads, the relevant collection agencies, including agencies designated by the Ministry of Transportation and Communications and municipal governments, depending on the types of public roads, may collect usage fees from users, including us, for establishing lines along with the public roads.

Laws and Regulations Relating to State-Owned Enterprises and Our Privatization; Statute Governing Privatization of State-Owned Enterprises

On the date of our privatization, we were required to make termination payments in accordance with the pension payment determined under the Labor Standards Law plus six months' salary and one month's wages in lieu of prior notice of termination to our employees who chose not to continue their employment. The government is responsible for paying the six months' salary to our employees who chose not to continue their employment.

Upon the completion of our privatization, we were required to make a settlement payment to our employees who chose to remain with us, based on their seniority and in accordance with the pension payment determined under the Labor Standards Law as if they have retired at the time of privatization. Those employees who remained with us and who are laid off within five years after the completion of our privatization will be entitled to a payment equal to the pension benefit accrued from the date of our privatization to the date of termination, six months' salary and one month's wages (including salary, bonuses, allowances and other regular payments) in lieu of prior notice of termination. The government has agreed to assume the cost of paying the six months' salary to the laid-off employees.

The government will indemnify those employees who have suffered from any losses and damages due to our privatization, such as losses arising from change of an insurance program.

Part of the funds realized from our privatization will be allocated to the Privatization Fund, and the rest of the funds will go to the Treasury of the Republic of China. Indemnification payments by the government will be made from the Privatization Fund.

Statute of Chunghwa Telecom Co., Ltd.

In light of the privatization of our company, the Executive Yuan, on May 1, 2006, proposed a motion for the abolishment of the Statute of Chunghwa Telecom Co., Ltd. for legislative approval. We cannot determine when this motion will be approved by the Legislative Yuan. Under Republic of China law, the Statute of Chunghwa Telecom Co., Ltd will continue in effect until the Legislative Yuan formally approves the motion and the President of the Republic of China pronounces the abolishment of the law.

Approval of Ministry of Transportation and Communications

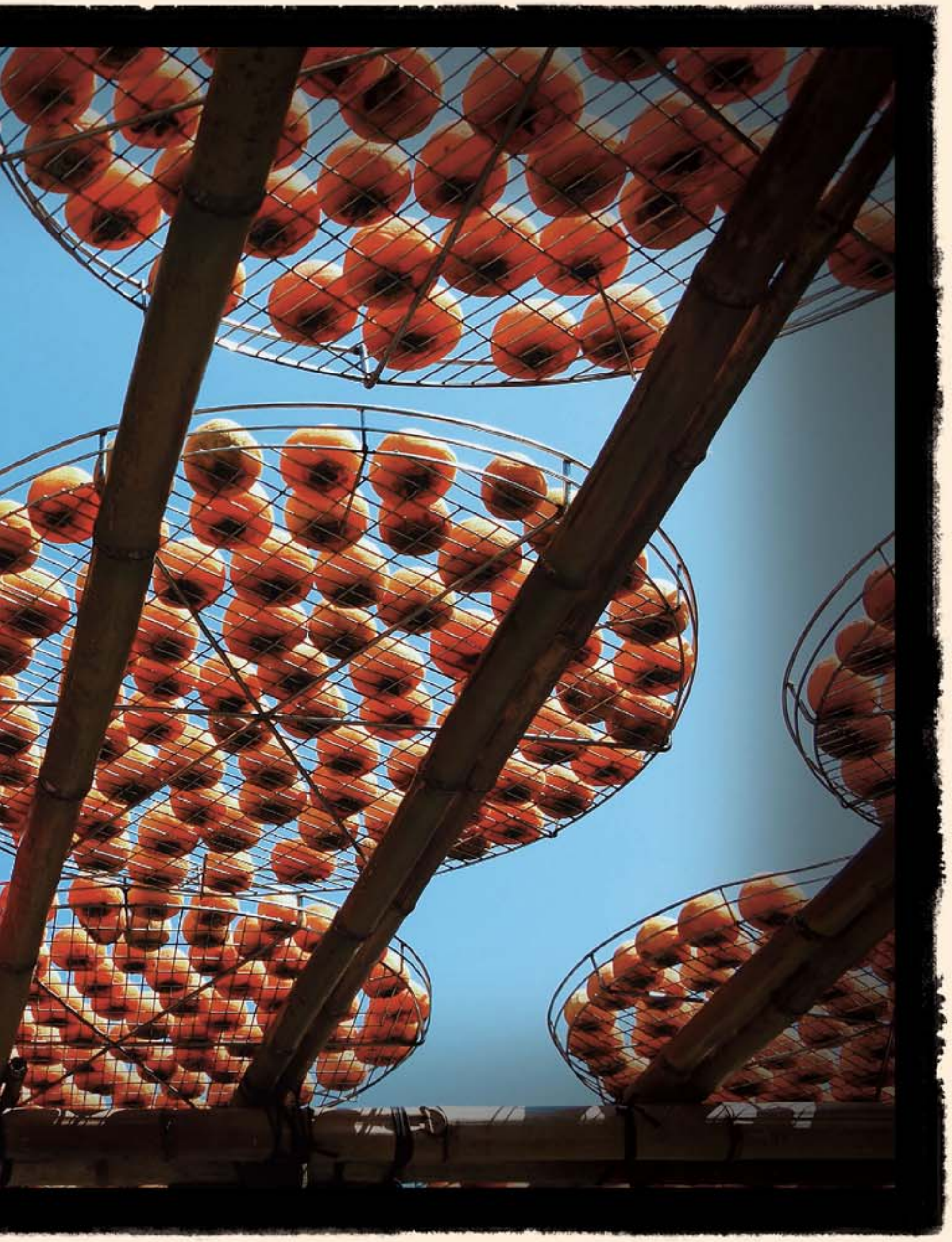
While the continued application of the Statute of Chunghwa Telecom Co., Ltd. remains unclear and it may be abolished in the near future, under that statute we are required to obtain approval of the Ministry of Transportation and Communications for:

- the adoption of and any changes to our articles of incorporation and board of directors organization rules;
- any changes to our authorized capital and any issuance of our common shares;
- any changes to primary tariffs for Type I services; and
- any changes to operational procedures of Type I services.

Employee Subscription Rights for New Issues of Our Common Shares

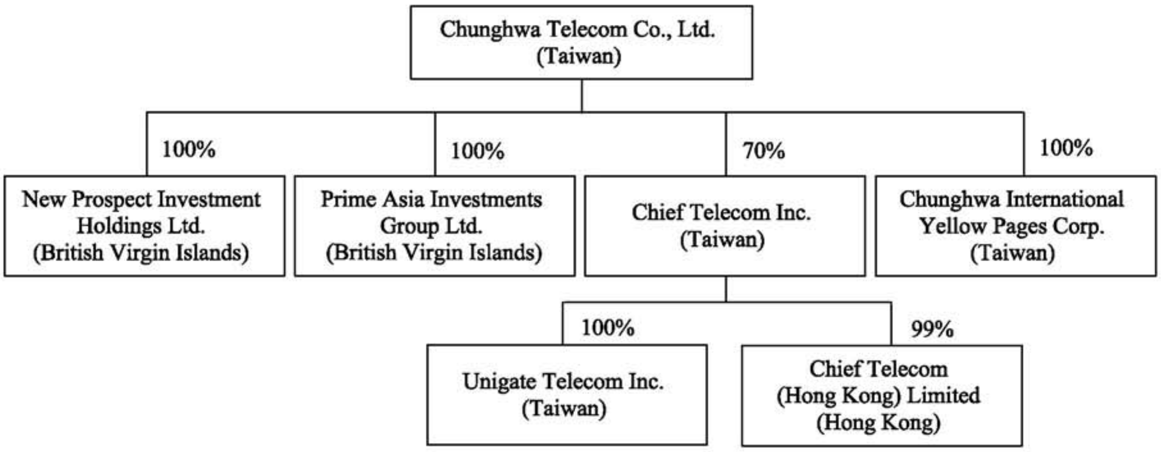
In accordance with the Statute of Chunghwa Telecom Co., Ltd., our employees have rights to subscribe for not more than 10% of a new issuance of our common shares at favorable terms in accordance with subscription rules which were to be announced by the Ministry of Transportation and Communications. However, no such rules were ever announced. In addition, under the Republic of China Company Law, employees of Republic of China companies have pre-emptive rights to subscribe for between 10-15% of any new issue of shares by the company.

Participating, interacting, sharing, and nurturing.



C. Organizational Structure

Set forth below is a diagram indicating our organization structure as of the date of this annual report.



D. Property, Plant and Equipment

Please refer to "—B. Business Overview" for a discussion of our property, plant and equipment.

ITEM 4A. UNRESOLVED STAFF COMMENTS

None.

ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS

You should read the following discussion of our financial condition and results of operations together with the consolidated financial statements and the notes to such statements included in this annual report.

For the convenience of readers, NT dollar amounts used in this section for, and as of, the year ended December 31, 2006 have been translated into U.S. dollar amounts using US$1.00=NT$32.59, the noon buying rate of the Federal Reserve Bank of New York on December 29, 2006. The US dollar translation appears in parentheses next to the relevant NT dollar amount.

Overview

A number of recent and expected future developments have had, and in the future may have, a material impact on our financial condition and results of operations. These developments include:

- changes in our revenue composition and sources of revenue growth;
- increased competition in the fixed line, leased line and cellular services markets, including the 3G cellular services market;
- tariff adjustments;
- capital expenditures as a result of technological improvements and changes in our business;
- provisions for pension payments and other stock-based compensations to our employees; and
- taxation.

Each of these developments is discussed below.

Changes in our revenue composition and sources of revenue growth

Our fixed line revenues are derived primarily from the provision of local, domestic long distance and international long distance telephone services. In addition, we also derive fixed line revenues from providing interconnection services to other carriers. Our revenues from cellular services are principally derived from the provision of voice services and, to a lesser extent, from SMS and other data services. Our revenues from internet and data services are generated principally from HiNet, our internet service provider, from our ADSL services, and from the provision of dedicated leased lines for our business customers and other operators.

The table below sets forth the revenues from our principal lines of business as a percentage of revenues for the periods indicated.

	Year ended December 31,		
	2004	2005	2006
Revenues:			
Fixed line	38.9%	35.9%	33.8%
Cellular(1)	38.0	39.5	39.2
Internet and data	21.2	22.8	24.9
Other(1)	1.9	1.8	2.1
Total	100.0%	100.0%	100.0%

(1) Beginning with the fiscal year ended December 31, 2006, we no longer combine cellular and paging services in one business segment. Instead, revenues from paging services are included in Other. For this reason, revenues for 2004 and 2005 have been reclassified on a comparable basis.

Over the past three years, the composition of our revenue base has undergone a significant change as a result of our strategy to diversify our revenues and focus on generating increased revenues from higher growth businesses, such as internet and data services.

Internet and data services have been our fastest growing sources of revenue over the last three years. Most of our increased revenues have come from internet access services, with our ADSL services accounting for a significant portion of such increase. We launched our ADSL services in August 1999, and we had approximately 3.9 million subscribers as of December 31, 2006 Increasing internet penetration in Taiwan and higher data traffic have contributed to a significant increase in our revenues from internet and data services over this period. We believe that internet and data services will continue to generate an increasing percentage of our revenues. Revenues from our local telephone and domestic long distance telephone and paging services have declined during this period, mainly due to traffic migration to cellular services. Revenues from our international long distance services have also declined, as international long distance tariffs have declined worldwide. Revenues from our mobile phone services remained flat in 2006 and in 2005, but the percentage of mobile phone services in total revenue declined in 2006 due to increasing market competition and the tariff reductions in SMS and calls from mobile phones to fixed-line numbers.

Increased competition in the fixed line, leased line and cellular services markets, including the 3G cellular services market

Three operators in addition to us have been providing fixed line services in Taiwan since June 2001. We believe that these competitors are largely targeting business subscribers, which generally generate higher revenues per subscriber as compared with residential customers. We are facing significant competition, particularly in the international long distance telephone services market, from these competitors.

Since August 2001, the Ministry of Transportation and Communications has awarded undersea cable service licenses to four additional operators. Moreover, in February 2002, the Ministry of Transportation and

Communications awarded five concessions to provide 3G cellular services. Two of these new concessions were awarded to new cellular operators. In addition, the government issued six mobile virtual network operator licenses in 2004, and began to allow mobile number portability services in October 2005. As of the date of this annual report, there are 12 mobile virtual network operators. The increased competition in the areas of fixed line, leased line and cellular services has led to, and may continue to lead to, further declines in our tariffs, which may result in a decrease in our revenues from these services. At the same time, the increased competition has stimulated consumer demand for telecommunications services, with results including higher international telephone usage and increased international bandwidth demand. We seek to minimize loss of customers from the increased competition by continuing to offer handset incentives, more competitive pricing packages, our "Friends and Family" packages and mobile virtual private networks for our corporate customers.

Tariff adjustments

We adjust our tariffs and offer promotional packages from time to time primarily in response to market conditions. We also from time to time are required to adjust our pricing in line with domestic regulations.

In July 2003, we reduced monthly rental fees for our ADSL services by an average of 16%.

In June 2004, we:

- reduced monthly rental fees for our ADSL services by an average of 24%;
- reduced the tariff for HiNet ADSL services by an average of 22%; and
- reduced the short messaging service fee from NT$2 to NT$1.5 per message for messages sent between our customers and from NT$2.5 to NT$2 per message for messages sent to users of other service providers.

In April 2005, we reduced monthly rental fees for part of our ADSL services by an average of 2%. For downlink speeds of 256k services, the reduction rate was as high as 47%.

In June 2005, we reduced short messaging service fees from NT$1.5 to NT$1.3 per message for messages sent between our customers and from NT$2 to NT$1.7 per message for messages sent to users of other service providers.

In December 2005, we reduced mobile dialing fees for calls to local telephone numbers by an average of 7%.

In December 2006, we began providing wholesale prices for the following services: ATM domestic leased lines, TWIX domestic leased lines and peering bandwidth, domestic type I carriers, interconnection leased lines and other domestic leased lines, to facilitate the National Communications Commission's request that market leaders provide wholesale prices to Type I and Type II telecommunications operators.

The National Communications Commission adopted a price reduction plan on December 21, 2006 that came into effect on April 1, 2007, setting a 4.88% price reduction in the tariff for fixed-line to GSM mobile phone dialing, a 4.8875% price reduction in the GSM highest tariff package and a 5.2% price reduction in prepayment cards. The NCC also requested us on April 1, 2007 to reduce the tariffs for ADSL service, and we are awaiting approval from the NCC on our plan to reduce the ADSL tariff by 5.35%. The price reduction plan also required us to stop collecting NT$5.0 monthly maintenance fee from our fixed-line customers and a NT$70.0 fixed-line basic charge from our ADSL users who only use data services.

We expect to continue to adjust tariffs and offer a variety of promotional packages from time to time in response to increasing competition and in order to take advantage of our pricing power from economies of scale. We may also be required to adjust our pricing due to changes in domestic regulations.

Capital expenditures as a result of technological improvements and changes in our business

In recent years, we have focused on modernizing and upgrading our cellular services network, and on developing our ADSL network, which enables transmission of digital information at a high-bandwidth over existing telephone lines. In particular, we have enhanced our telecommunications services through:

- the introduction of a VoIP exchange system in our long distance telephone network;
- the implementation of a network modernization program, including a gradual transfer from our public switched telephone network to a system based on internet protocol, to remain at the forefront of new technologies;
- the development of an intelligent network for fixed line services;
- the deployment of a high-capacity long-haul dense wavelength division multiplexing system and a nationwide internet protocol backbone network with 320 Gbps gigabit switching routers for internet and internet protocol virtual private network services;
- the expansion and upgrade of our cellular services network, including the rollout of GRPS; and
- the construction of our 3G cellular services network.

As a result, we incurred aggregate capital expenditures of NT$105.7 billion over the period from January 1, 2003 to December 31, 2006

Our long-term goal is to optimize our capital expenditures by focusing on investing in innovative products and services with attractive return profiles. We evaluate our investment opportunities by benchmarking them against internal return requirements. We are currently finalizing plans for the gradual upgrade of 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 increased operational efficiencies from reduced switching centers, and related property, materials and personnel costs. We have also devoted resources toward the effective rollout of our 3G cellular network and the continuing build-out of our fiber-to-the-building infrastructure.

Provisions for pension payments and other stock-based compensations to our employees

Personnel expenses constitute a significant portion of our operating costs and expenses. In 2004, 2005 and 2006 personnel expenses represented 32.8%, 39.4% and 34.8% respectively, of our total operating costs and expenses, and pension costs represented 11.3%, 7.8% and 7.1%, respectively, of our personnel expenses. The table below sets forth information regarding personnel expenses, depreciation and amortization and other operating costs and expenses in the aggregate and as a percentage of our total operating costs and expenses for the periods indicated.

	For the year ended December 31,					
	2004		2005		2006	
	(in billions of NT$, except for percentages)					
Operating costs and expenses:						
Personnel expenses						
Pension[1]	4.6	3.7%	4.3	3.1%	3.2	2.5%
Salaries and bonus	36.0	29.1	50.6	36.3	42.0	32.3
Total personnel expenses	40.6	32.8	54.9	39.4	45.2	34.8
Depreciation and amortization—costs of services	38.4	31.0	38.8	27.8	38.4	29.5
Depreciation and amortization—operating expenses	2.3	1.9	2.4	1.7	2.3	1.8
Other	42.4	34.3	43.5	31.1	44.1	33.9
Total operating costs and expenses	123.7	100.0%	139.6	100.0%	130.0	100.0%

(1) Does not include NT$129 million, NT$183 million and NT$142 million of pension costs associated with employees engaged in construction projects that were capitalized and not treated as personnel expenses in 2004, 2005 and 2006, respectively.

The following table sets forth our personnel expenses (divided into pension and non-pension portions) allocated by categories of operating costs and expenses:

	For the year ended December 31,					
	2004		2005		2006	
	(in billions of NT$, except for percentages)					
Personnel expenses						
Cost of Revenues						
Pension	2.8	6.9%	2.5	4.6%	1.9	4.3%
Non-pension	22.5	55.4	30.8	56.1	25.4	56.1
Total	25.3	62.3	33.3	60.7	27.3	60.4
Sales and Marketing						
Pension	1.2	3.1	1.3	2.3	0.9	1.9
Non-pension	9.6	23.6	14.4	26.2	11.9	26.4
Total	10.8	26.7	15.7	28.5	12.8	28.3
General and Administration						
Pension	0.3	0.6	0.2	0.5	0.2	0.4
Non-pension	2.0	5.0	2.9	5.2	2.5	5.5
Total	2.3	5.6	3.1	5.7	2.7	5.9
Research and Development						
Pension	0.3	0.6	0.2	0.4	0.2	0.4
Non-pension	1.9	4.8	2.6	4.7	2.2	5.0
Total	2.2	5.4	2.8	5.1	2.4	5.4
Total personnel expenses	40.6	100.0%	54.9	100.0%	45.2	100.0%

At the time of our privatization, our then existing defined benefit pension obligations were settled in full. After completion of our privatization, our continuing employees were deemed to have commenced employment as of the date our privatization was completed for seniority purposes under our pension plans in effect after privatization. Under applicable Republic of China regulations, upon our privatization, the Ministry of Transportation and Communications assumed the obligation to make annuity payments to our employees who retired before our privatization. Under US GAAP reporting, the portion of the pension obligations that was settled by the Ministry of Transportation and Communications, was represented by the difference between the accrued pension liabilities, the deferred pension cost and related deferred income tax assets was accounted for as contributed capital and recorded under our stockholders' equity as of August 12, 2005.

As of December 31, 2006, we adopted SFAS 158 and recorded the under-funded status of our defined benefit pension plans as a liability with a corresponding offset, net of taxes, recorded in accumulated other comprehensive income within stockholders' equity.

We expect our pension costs for the fiscal year 2007 to be approximately NT$3.0 billion.

Increases in our costs and expenses in recent years were also attributable to purchases of our common shares by our employees at discounts. We recognize compensation expenses when our employees purchase our common shares at discounts under the priority share subscription program. We recognized such compensation expenses in the amounts of NT$0.5 billion, NT$12.8 billion and NT$0.5 billion (US$15 million) in 2004, 2005 and 2006, respectively.

Under a program established pursuant to a regulation adopted by the Ministry of Transportation and Communications, our employees were able to subscribe for up to approximately 476.9 million of our common shares from the Ministry of Transportation and Communications in offerings conducted by the Ministry of Transportation and Communications prior to our privatization. As long as our employees agree not to transfer or pledge these shares for either two or three years, are eligible to receive a discount of 10% or 20%, respectively, from the offering price. Pursuant to a June 2005 amendment to the terms of this program, the majority of our employees who continued their employment with us after our privatization are also eligible to receive a 50% discount if they agree not to transfer or pledge the shares for four years.

At the time when we were privatized, the Ministry of Transportation and Communications implemented another stock subscription program, allocating up to approximately 476.9 million common shares, or 4.9% of our then outstanding common shares, for a one-time subscription by our employees. Under this program, a majority of our employees will be eligible to receive a discount of 10%, 20% or 50% from the offering price of the shares if they agree not to transfer or pledge these shares for two, three or four years, respectively.

As of the date of this annual report, 762,886,886 of our common shares, representing 7.9% of our outstanding common shares were sold under the two programs mentioned above.

Taxation

The current corporate income tax rate in the Republic of China is 25%. We benefit from tax incentives generally available to technology companies in the Republic of China, including tax credits of up to 30% of the amount of some of our research and development, automation and employee training expenditures. Starting in 2001, we also qualified for tax benefits at the rate of 5% to 20% of the amount of our investment in qualified equipment and technology. As a result, our effective tax rate was 18.1%, 27.7% and 26.6% in 2004, 2005 and 2006, respectively.

In 1997, the Income Tax Law of the Republic of China was amended to integrate corporate income tax and shareholder dividend tax to eliminate the double taxation effect for resident shareholders of Taiwan companies. Under the amendment, all retained earnings generated from January 1, 1998 and not distributed to shareholders as dividends in the following year are assessed with a 10% retained earnings tax. See "Item 10. Additional Information—E. Taxation—Republic of China Taxation—Dividends." Historically, this has not had an impact on our financial results of operations, because the majority of our earnings was distributed to the government by way of dividends. If we decide to distribute our earnings in the future, we may need to reserve the retained earnings tax recorded in the period during which the related income is generated.

Segment Operating Losses

Our local telephone services had operating losses of NT$7.2 billion, NT$14.2 billion and NT$13.7 billion (US$0.4 billion) in 2004, 2005 and 2006, respectively. See Note 25 to our audited consolidated financial statements included elsewhere in this annual report. We expect our local telephone services to continue incurring operating losses as competition in the local telephone services market further intensifies and traffic continues to migrate from fixed line services to cellular and broadband services.

Critical Accounting Policies

Our consolidated financial statements are prepared in accordance with US GAAP. The preparation of these consolidated financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses as well as the disclosure of contingent assets and liabilities. We continually evaluate these estimates and judgments, including those related to revenue recognition, allowance for doubtful accounts, estimated useful lives of long-lived assets, investments in unconsolidated companies, pension benefits and accounting for income taxes. We base these estimates and judgments on our historical experience and other factors that we believe to be reasonable under the circumstances. Actual results may differ from these estimates.

Revenue Recognition

We recognize revenues for our services in accordance with the Securities and Exchange Commission Staff Accounting Bulletin No. 104. We record service revenues over the periods they are earned. The costs of providing services are recognized as incurred. Handset incentives are paid to third party dealers when they sell handsets to customers that enter into service contracts, and these are recognized as a cost of service when incurred. Usage revenues from fixed line services, cellular services, internet and data services, and interconnection and call transfer fees from other telecommunications companies and carriers are billed in arrears and are recognized based upon minutes of traffic processed when the services are provided in accordance with contract terms.

One-time subscriber connection fees, primarily in relation to fixed line service revenues, are deferred and recognized over the average expected customer service periods, which we evaluate on a continual basis. For example, the average expected customer service period for fixed line service revenues has increased over time from 13 years at December 31, 2004 to 16 years at December 31, 2006, and the average expected customer service period for cellular service revenues has declined over time from five years at December 31, 2004 to four years at December 31, 2006 and the average expected customer service period for internet service revenues increased from three years in 2004 to four years in 2006, while the average expected customer service periods for other service lines have remained relatively the same over the same period. If our estimates of these customer service periods become longer, the amortization of our deferred income could be materially and adversely affected.

When we enter into transactions which involve the provision of airtime bundled with products such as 3G data cards or handsets, the bundled arrangement is accounted for in accordance with the Emerging Issues Task Force, or EITF, Issue No. 00-21, Revenue Arrangements with Multiple Deliverables. Total consideration received from handsets in these arrangements is allocated and measured using units of accounting within the arrangement based on relative fair values limited to the amount that is not contingent upon the delivery of other items or services. Total consideration received from 3G data cards does not have objective and reliable fair values for delivered and undelivered items; therefore, the recognition of revenues follows one unit of accounting.

When we sell products to third party cellular phone stores, we record the direct sale of the products, typically handsets, as gross revenue when we are the primary obligor in the arrangement and when title is passed and the products are accepted by the stores. When we also pay the third party cellular phone stores incentives to attract new customers and such incentives are identifiable, these incentives are accounted for as a reduction of revenue in accordance with EITF, Issue No. 01-09, Accounting for Consideration Given by a Vendor to a Customer or a Reseller of the Vendor's Products.

Allowance for Doubtful Accounts

We maintain allowance for doubtful accounts for estimated losses that result from the inability of our customers to make required payments. We base our allowances on the likelihood of recoverability of accounts receivable by operating segment based on past experience and current collection trends that we expect to continue. Our evaluation also includes the length of time the receivables are past due, geographic concentrations and the general business environment. If changes in these factors occur, or the historical data we use to calculate the allowance provided for doubtful accounts does not reflect the future ability to collect outstanding receivables, additional provisions for doubtful accounts may be needed and our future results of operations could be materially and adversely affected. Even as revenues have increased in recent years, the allowance for doubtful accounts has decreased due to stricter credit investigations for new subscribers and more efficient collection activities for outstanding accounts.

Estimated Useful Lives of Long-Lived Assets

A significant portion of our total assets consists of long-lived assets, primarily property, plant and equipment and definite-lived intangibles. We estimate the useful lives of property, plant and equipment and other long-lived assets with finite lives in order to determine the amount of depreciation and amortization expense to be recorded during the reported period. The useful lives are estimated at the time assets are acquired and are based on historical experience with similar assets as well as the anticipated technological evolution or other environmental changes. If technological changes were to occur more rapidly than anticipated or in a different form than anticipated, the useful lives assigned to these assets may need to be shortened, resulting in the recognition of increased depreciation and amortization in the relevant periods. Alternatively, technological obsolescence could result in a write-down in the value of the assets to reflect impairment. We review these types of assets for impairment annually, or when events or circumstances indicate that the carrying amount may not be recoverable over the remaining life of an asset. In assessing impairments, we use estimated cash flows that take into account management's estimates of future operations. We performed an impairment analysis and concluded that the paging division assets were impaired and recognized an impairment loss of NT$343 million in 2005.

If at January 1, 2006 we would have determined that the remaining useful lives for our property, plant and equipment were shorter or longer by one year than what we used in the preparation of our consolidated financial statements, our recorded depreciation expense in 2006 would have increased by approximately NT$12.9 billion or decreased by approximately NT$8.1 billion, respectively.

Investments in Unconsolidated Companies

We hold investments in other companies that we account for under the equity method or cost method of accounting, depending on our ability to exert significant influence over the investee company. The amounts for our equity method investments generally represent our cost of the initial investment adjusted for our share of the investee company's income or loss and any dividends received. The amounts for our cost method investments where the securities are not publicly traded generally represent our cost of the initial investment less any adjustments we make when we determine that an investment's net realizable value is less than its carrying cost.

The process of assessing whether a particular cost method investment's net realizable value is less than its carrying cost requires a significant amount of judgment. We periodically evaluate these long-term investments based on quoted market prices, if available, the financial condition of the investee company, economic conditions in the industry and our intent and ability to hold the investment for a long period of time. If quoted market prices are not available, we estimate the fair value using the net asset values as well as the financial condition of the investee company. This information may be based on information that we request from the investee companies and may not be subject to the same disclosure and audit requirements as required of U.S. companies, and as such, the reliability and accuracy of the information may vary. If we deem the fair value of an investment to be less than the book value based on the above factors, and the decline in value is deemed to be other than temporary, we record the difference as impairment in the period of occurrence. In 2005, we recognized a loss of NT$740 million, accounted for using the cost method, in relation to our investment in Taipei Financial Center Corporation due to lower than expected leasing rates for office and retail space in Taipei 101.

Estimating the net realizable value of investments in privately held companies can be inherently subjective and may contribute to significant volatility in our reported results of operations. For example, if the investment environment worsens in 2007, we may incur an impairment in our equity or cost method investments.

Pension Benefits

The amounts recognized in our consolidated financial statements related to pension benefits are determined on an actuarial basis that utilizes several different assumptions in the calculation of such amounts. Significant assumptions used in determining our pension benefits are the discount rate, the expected long-term rate of return on plan assets, the rate of increase in compensation levels, and the average remaining years of service for employees, which prior to 2005 included an estimate for the number of employees that will retire upon our privatization. In addition, because we were required to fully fund our pension plans on or prior to the date of our privatization to enable us to meet the requirements of making full benefit payments to our then existing employees, prior to 2005 we made an assumption of our privatization date in determining the amount of the pension benefits.

We use long-term historical actual return information and estimate future long-term investment returns by reference to external sources to develop the expected long-term return on plan assets. The discount rate is assumed based on the rates available on high-quality fixed-income debt instruments with the same period to maturity as the estimated period to maturity of the pension benefit. We assume the rate of increase in compensation levels and average remaining years of service based on historical data. Any changes in one or more of these assumptions could impact our pension benefits.

A decrease in the discount rate or in the expected return on assets would increase the reported obligation. For example, if the discount rate in 2006 used in determining this obligation were 0.25% lower, it would generate a NT$125.4 million increase in the obligation reported on the balance sheet and a NT$66.7 million increase in the benefit costs. Similarly, if the expected return on assets assumption were 0.25% lower, it would generate a NT$7.6 million increase in 2007 benefit costs. A minor change in the estimate of health care cost assumptions would not materially affect our pension obligations or related benefit costs. The MOTC settled related pension obligations on the privatization date and recorded the difference between accrued pension liabilities, deferred pension cost and related deferred income tax assets as contributed capital in stockholders' equity by applying the guidance in AICPA Interpretation 39 to APB 16 "Business combinations" and FASB Implementation Guide, SFAS 88 Q&A 40.

As of December 31, 2006, we adopted SFAS No. 158, "Employers' Accounting for Defined Benefit Pensions and Other Postretirement Benefits". In accordance with this standard, we recorded the funded status of our defined benefit pension as an asset or liability on our consolidated balance sheet with a corresponding offset, net of taxes, recorded in accumulated other comprehensive income (loss) within stockholders' equity, resulting in an after-tax decrease in equity of NT$226 million. Any changes in the pension obligation will have an equivalent impact on the funded status. The accumulated other income (loss) will also be impacted by the tax-adjusted amount.

Accounting for Income Taxes

Deferred income taxes represent the effect of temporary differences between the amounts of assets and liabilities recognized for financial reporting purposes and the amounts recognized for income tax purposes. We measure deferred tax assets and liabilities using statutory tax rates that, if changed, would result in either an increase or a decrease in the provision for income taxes in the period of change. A one-percentage point increase in the statutory income tax rate as of December 31, 2006 would have decreased our net income by approximately NT$573.4 million.

We record a valuation allowance to reduce our deferred tax assets to the amount of future tax benefit that is more likely than not to be realized. While we have considered future taxable income and ongoing prudent and feasible tax planning strategies in assessing the need for the valuation allowance, we cannot assure you that we would not need to increase the valuation allowance to cover additional deferred tax assets that may not be realizable. Any increase in the valuation allowance could have a material adverse effect on our income tax provision and net income in the period in which such determination is made.

We had a valuation allowance of NT$110 million on our deferred tax asset balance as of December 31, 2006. We do not have a full valuation allowance on the deferred tax asset, as we believe these benefits will be fully realizable based on our projection of future operating income. If we experience a significant decrease in our future operating income, the realizability of our deferred tax assets could be negatively impacted, and thus an increase in the valuation allowance might be required.

Our Financial Reporting Obligations

Our audited consolidated financial statements included in this annual report are prepared under US GAAP. We intend to transition into financial reporting under ROC GAAP, with reconciliation to US GAAP, beginning in 2008. In the interim, we expect to continue to make available our quarterly and annual consolidated financial statements prepared in accordance with US GAAP.

A. Operating Results

The following table sets forth our revenues, operating costs and expenses, income from operations and other financial data for the periods indicated.

	For the year ended December 31,			
	2004	2005	2006	
	(in billions)			
	NT$	NT$	NT$	US$
Revenues:				
Fixed line				
Local	44.9	40.7	39.0	1.2
Domestic long distance	12.0	11.0	9.9	0.3
International long distance	15.2	14.6	14.0	0.4
Total fixed line	72.1	66.3	62.9	1.9
Cellular	70.3	73.0	73.0	2.3
Internet and data:				
Internet	29.5	32.1	35.5	1.1
Data	9.8	10.1	10.8	0.3
Total Internet and data	39.3	42.2	46.3	1.4
Other(1)	3.5	3.2	4.1	0.1
Total revenues	185.2	184.7	186.3	5.7
Operating costs and expenses:				
Costs of revenues(2)	58.7	68.1	62.6	1.9
Marketing(2)	19.3	23.7	20.6	0.6
General and administrative(2)	2.5	3.5	3.3	0.1
Research and development(2)	2.5	3.1	2.8	0.1
Depreciation and amortization—costs of revenues	38.4	38.8	38.4	1.2
Depreciation and amortization—other operating expenses	2.3	2.4	2.3	0.1
Total operating costs and expenses	123.7	139.6	130.0	4.0
Income from operations	61.5	45.1	56.3	1.7
Other income	1.1	2.0	1.6	0.1
Other expenses	0.4	1.1	0.5	0.0
Income before income tax	62.2	46.0	57.4	1.8
Income tax	11.3	12.7	15.3	0.5
Net income	50.9	33.3	42.1	1.3

(1) Beginning with the fiscal year ended December 31, 2006, we no longer combine cellular and paging services in one business segment. Instead, revenues from paging services are included in Other. For this reason, revenues for 2004 and 2005 have been reclassified on a comparable basis.

(2) Excludes related depreciation and amortization which are presented separately.

The following table sets forth our revenues, operating costs and expenses, income from operations and other financial data as a percentage of our total revenues for the periods indicated.

	For the year ended December 31,		
	2004	2005	2006
	(as percentages of total revenues)		
Revenues:			
Fixed line			
Local	24.3%	22.1%	20.9%
Domestic long distance	6.4	5.9	5.3
International long distance	8.2	7.9	7.6
Total fixed line	38.9	35.9	33.8
Cellular	38.0	39.5	39.2
Internet and data:			
Internet	15.9	17.3	19.1
Data	5.3	5.5	5.8
Total Internet and data	21.2	22.8	24.9
Other(1)	1.9	1.8	2.1
Total revenues	100.0	100.0	100.0
Operating costs and expenses:			
Costs of revenues(2)	32.6	36.9	33.6
Marketing(2)	10.4	12.8	11.1
General and administrative(2)	1.4	1.9	1.8
Research and development(2)	1.3	1.7	1.5
Depreciation and amortization—costs of revenues	20.7	21.0	20.6
Depreciation and amortization—other operating expenses	1.3	1.3	1.2
Total operating costs and expenses	67.7	75.6	69.8
Income from operations	32.3	24.4	30.2
Other income	1.5	1.1	0.8
Other expenses	0.2	0.6	0.2
Income before income tax	33.6	24.9	30.8
Income tax	6.1	6.9	8.2
Net income	27.5%	18.0%	22.6%

(1) Beginning with the fiscal year ended December 31, 2006, we no longer combine cellular and paging services in one business segment. Instead, revenues from paging services are included in Other. For this reason, revenues for 2004 and 2005 have been reclassified on a comparable basis.
(2) Excludes related depreciation and amortization which are presented separately.

Year ended December 31, 2005 compared with year ended December 31, 2006

Revenues

Our revenues increased by 0.9% from NT$184.7 million in 2005 to NT$186.3 billion (US$5.7 billion) in 2006. This increase was primarily due to an increase in operating revenues of internet and data services.

Fixed Line Services

Fixed line revenues comprised 35.9% and 33.8% of our revenues in 2005 and 2006, respectively. Our fixed line revenues decreased by 5.0% from NT$66.3 billion in 2005 to NT$62.9 billion (US$1.9 billion) in 2006.

Local telephone services. Our local telephone revenues decreased by 4.3% from NT$40.7 billion in 2005 to NT$39.0 billion (US$1.2 billion) in 2006. This decrease was principally a result of a 12.0% decline in traffic volume from 21.1 billion minutes in 2005 to 18.6 billion minutes in 2006. This decline in traffic volume was primarily due to the continued migration of non-HiNet internet subscribers from dial-up to broadband internet access, the continued traffic migration from fixed line services to broadband and cellular services, and increasing market competition. We expect this trend to continue as broadband and cellular services become more widely adopted in Taiwan. However, we believe the rate of traffic migration from fixed-line services to broadband and cellular services is slowing. This decline in traffic volume was partially offset by a 2.9% increase in average local usage fees, reflecting a continued decrease in the number of users of our discounted internet tariff package. Our local interconnection revenues decreased by NT$0.1 billion between these two years because of a decrease in local interconnection volume.

Domestic long distance telephone services. Our domestic long distance telephone revenues decreased by 9.7% from NT$11.0 billion in 2005 to NT$9.9 billion (US$303 million) in 2006. This decrease was mainly due to a decrease in traffic volume from 5.1 billion minutes in 2005 to 4.6 billion minutes in 2006. The decrease in traffic volume was primarily due to the continued traffic migration from fixed line services to cellular services and increased competition from other fixed line operators and VoIP. The rate of migration from fixed line services to cellular services has been slowing in the past two years as the cellular market becomes increasingly saturated. Our interconnection revenues also decreased as a result of more direct connections between private operators.

International long distance telephone services. Our international long distance telephone revenues decreased by 3.7% from NT$14.6 billion in 2005 to NT$14.0 billion (US$431 million) in 2006. This decrease was mainly due to intense market competition and a decrease in the average per minute usage charge due to promotional packages to encourage usage. This was partially offset by an 11.7% increase in outgoing traffic volume from 2005 to 2006. Our international settlement revenues decreased by 8.1% from NT$3.3 billion in 2005 to NT$3.1 billion (US$94 million) in 2006. This decrease was primarily due to the continued decline in international settlement rates.

Cellular Services

Cellular revenues comprised 39.5% and 39.2% of our revenues in 2005 and 2006, respectively. Our cellular revenues remained flat at NT$73.0 billion (US$2.3 billion) in 2005 and in 2006. While we experienced an increase in volume in 2006 from 2005, this was largely offset by tariff reductions which came into effect in June 2005 for SMS and in December 2005 for calls from mobile to fixed-line numbers. Outgoing traffic volume increased 3.4% from 8.9 billion minutes in 2005 to 9.2 billion minutes in 2006, as a result of an increase in the number of customers using cellular service.

Internet and Data Services

Internet and data revenues comprised 22.8% and 24.9% of our revenues in 2005 and 2006, respectively. Our internet and data revenues increased by 9.9% from NT$42.2 billion in 2005 to NT$46.3 billion (US$1.4 billion) in 2006 due primarily to an increase in our internet services.

Internet services. Our revenues attributable to internet services increased by 11.0% from NT$32.1 billion in 2005 to NT$35.5 billion (US$1.1 billion) in 2006. This increase was largely due to an increase in the number of our ADSL subscribers from 3.7 million as of December 31, 2005 to 3.9 million as of December 31, 2006. This increase was also due to a 4.7% increase in the number of our HiNet subscribers from 4.1 million as of December 31, 2005 to 4.3 million as of December 31, 2006. There was an increase in the number of FTTB customers from 20,000 in 2005 to 185,000 in 2006. However, the number of dial-up customers decreased from 1,166,092 in 2005 to 1,042,797 in 2006. Calls to HiNet are recorded as part of our internet and data services and are not included in our local minutes or revenues. We include usage fees from fixed line telephone calls to access our HiNet service in our internet and data revenues. Usage fees from fixed line telephone calls to access internet service providers other than HiNet are recorded as fixed line revenues.

Data services. Revenues from our data services increased by 6.6% from NT$10.1 billion in 2005 to NT$10.8 billion (US$0.3 billion) in 2006. This increase was principally due to an increase in revenues from leased line services and additional operating revenue from our new subsidiary, Chief Telecom, in which we acquired a 70% interest in September 2006. We continue to derive a substantial portion of our data revenues from leased line services. While demand for higher speed lease lines continues to increase, our overall leased line tariffs have continued to be adversely affected by competition from other fixed line operators and international leased line service providers, as well as the continued migration of domestic leased line users to ADSL services.

Other

Other revenues comprised 1.8% and 2.1% of our revenues in 2005 and 2006, respectively.

Our other revenues increased by 24.1% from NT$3.2 billion in 2005 to NT$4.1 billion (US$124 million) in 2006. This increase in other revenues was primarily due to an NT$0.9 billion increase in revenues from our corporate solution business, MOD, real estate leasing and sales of 3G cellular handsets and data cards. This increase was partially offset by a NT$66 million decrease from paging services, which beginning in 2006 is accounted for under "Other".

Operating Costs and Expenses

Our operating costs and expenses decreased by 6.8% from NT$139.6 billion in 2005 to NT$130.0 billion (US$4.0 billion) in 2006. This decrease was primarily due to decreases in stock compensation expenses. As a percentage of revenues, operating costs and expenses decreased from 75.5% in 2005 to 69.8% in 2006.

Costs of Revenues

Costs of revenues include personnel expenses, international settlement costs, handset incentives, spectrum usage and license fees, costs of materials and maintenance and interconnection fees among cellular operators.

Our costs of revenues decreased by 8.0% from NT$68.1 billion in 2005 to NT$62.6 billion (US$1.9 billion) in 2006. This decrease was principally a result of: an NT$7.2 billion decrease in employees' purchases of our common shares at discounts under our priority share subscription program; a NT$438 million profit increase resulting from sales of fixed assets; NT$383 million increase in contractual penalty payments from third-party contractors relating to project delays and a NTS369 million income increase due to sales of scrap inventory. This decrease was partially offset by an NT$1.2 billion increase in our handset incentives and an NT$1.2 billion increase in special termination benefits under our early retirement program. We recognize compensation expense when our employees purchase our common shares at discounts under the priority share subscription program.

Marketing

Our marketing expenses, which include personnel expenses, provisions for bad debt and expenses relating to advertising and other marketing-related activities, decreased by 12.7% from NT$23.7 billion in 2005 to NT$20.6 billion (US$0.6 billion) in 2006. This decrease was mainly due to an NT$4.0 billion decrease in employees' purchases of our common shares at discounts under our priority share subscription program, and partially offset by an NT$0.8 billion increase in special termination benefits under our early retirement program.

General and Administrative

Our general and administrative expenses decreased by 5.4% from NT$3.5 billion in 2005 to NT$3.3 billion (US$0.1 billion) in 2006. This decrease was primarily due to a decrease of NT$0.7 billion in compensation expense due to a decrease in employees' purchases of our common shares at discounts under our employee priority share subscription program. This decrease was partially offset by an increase of NT$0.2 billion in special termination benefits under our early retirement program and an NT$0.2 billion increase in donations to non-profit organizations.

Research and Development

Our research and development expenses decreased by 10.2% from NT$3.1 billion in 2005 to NT$2.8 billion (US$87 million) in 2006. This decrease was primarily due to a decrease of NT$0.5 billion in compensation expense due to a decrease in employees' purchase of our common shares at discounts under our employee priority share subscription program, and partially offset by an increase of NT$53 million in special termination benefit under early retirement program. Our research and development expenses decreased as a percentage of our revenues from 1.7% in 2005 to 1.5% in 2006.

Depreciation and Amortization

Our depreciation and amortization expenses decreased by 1.2% from NT$41.2 billion in 2005 to NT$40.7 billion (US$1.2 billion) in 2006. This decrease was mainly due to decreases in capital expenditure since 2002, and partially offset by the amortization of our 3G license.

Operating Costs and Expenses by Business Segment

	Local	Domestic Long Distance	International Long Distance	Cellular Service(1)	Internet and Data	Other(1)	Total
			(in billions of NT$)				
As of and for the year ended December 31, 2006							
Operating costs and expenses	34.7	1.2	7.0	23.1	15.8	3.3	85.1
Unallocated corporate expenses							4.3
Total operating costs and expenses							89.4
Depreciation and amortization	18.0	0.7	0.5	8.2	12.4	0.8	40.6
Unallocated corporate expenses							0.1
Total depreciation and amortization							40.7
As of and for the year ended December 31, 2005							
Operating costs and expenses	36.0	1.5	7.6	22.8	22.4	3.2	93.5
Unallocated corporate expenses							4.9
Total operating costs and expenses							98.4
Depreciation and amortization	19.0	0.7	0.7	7.4	12.4	0.8	41.0
Unallocated corporate expenses							0.2
Total depreciation and amortization							41.2

(1) Beginning with the fiscal year ended December 31, 2006, we no longer combine cellular and paging services in one business segment. Instead, operating costs and expenses from paging services are included in Other. For this reason, operating costs and expenses for 2005 have been reclassified on a comparable basis.

Local telephone services

Our local telephone operating expenses, excluding depreciation and amortization, decreased by 3.5% from NT$36.0 billion in 2005 to NT$34.7 billion (US$1.1 billion) in 2006, primarily due to an NT$4.4 billion decrease in employees' purchases of our common shares at discount under our employee priority share subscription program, partially offset by an NT$1.6 billion increase in special termination benefits under our early retirement program, an NT$1.1 billion increase in bonus for employees and remuneration for directors and supervisors and an NT$0.6 billion increase in performance-based bonuses. Our depreciation and amortization expenses relating to local telephone services decreased by 5.6% from NT$19.0 billion in 2005 to NT$18.0 billion (US$0.6 billion) in 2006. The decrease was primarily due to a decrease in depreciation expenses because of an increase in obsolete equipment.

Domestic long distance telephone services

Our domestic long distance telephone operating expenses, excluding depreciation and amortization, decreased by 17.8% from NT$1.5 billion in 2005 to NT$1.2 billion (US$38 million) in 2006,primarily due to an NT$0.2 billion decrease in the employees' purchases of our common shares at discount under our employee priority share subscription program. Our depreciation and amortization expenses relating to domestic long distance telephone services remained flat at NT$0.7 billion in 2005 and in 2006.

International long distance telephone services

Our international long distance telephone operating expenses, excluding depreciation and amortization, decreased by 8.4% from NT$7.6 billion in 2005 to NT$7.0 billion (US$0.2 billion) in 2006. The decrease was primarily due to an NT$0.4 billion decrease in the employees' purchase of our common shares at discounts and an NT$0.8 billion decrease in international long distance telephone settlement fees; partially offset by an NT$0.2 billion increase in material expenses and an NT$0.2 billion increase in interconnection fees. Our depreciation and amortization expenses relating to international long distance telephone services decreased by 16.8% from NT$0.7 billion in 2005 to NT$0.5 billion (US$17 million) in 2006. The decrease in depreciation and amortization expenses was mainly due to a decrease in expenditures relating to equipment upgrades.

Cellular Services

Our cellular operating expenses, excluding depreciation and amortization, increased by 1.5% from NT$22.8 billion in 2005 to NT$23.1 billion (US$0.7 billion) in 2006. This increase was primarily due to an NT$1.1 billion increase in marketing expenses, an NT$0.2 billion increase in bonus for employees and remuneration for directors and supervisors and a NT$0.2 billion increase in special termination benefits under our early retirement program partially offset by an NT$1.2 billion decrease in the employees' purchases of our common shares at discounts under our employee priority share subscription program. Our depreciation and amortization expenses relating to cellular services increased by 10.9% from NT$7.4 billion in 2005 to NT$8.2 billion (US$0.3 billion) in 2006. The increase was mainly due to an NT$0.5 billion increase in depreciation caused by purchases of new equipment such as mobile exchangers and signal transmitters and receivers; and an NT$0.3 billion increase in amortization of 3G license fees.

Internet and Data Services

Our internet and data operating expenses, excluding depreciation and amortization, decreased by 29.2% from NT$22.4 billion in 2005 to NT$15.8 billion (US$0.5 billion) in 2006. This decrease was primarily due to an NT$5.3 billion decrease in the employees' purchases of our common shares at discounts under our employee priority share subscription program; and an NT$1.1 billion decrease in printing and mailing expenses of bills after the business was relocated to local telephone services. Our depreciation and amortization expenses relating to internet and data services remained flat at NT$12.4 billion in 2005 and in 2006.

Operating Income and Operating Margin

As a result of the foregoing, our operating income increased by 24.7% from NT$45.1 billion in 2005 to NT$56.3 billion (US$1.7 billion) in 2006. Our operating margin increased from 24.5% in 2005 to 30.2% in 2006.

The following table sets forth certain information regarding our operating income by business segment for the periods indicated.

	Local	Domestic Long Distance	International Long Distance	Cellular Service[1]	Internet and Data	Other[1]	Total
			(in billions of NT$)				
As of and for the year ended December 31, 2006							
Income from operations	0.5	7.1	2.9	30.2	20.6	(0.5)	60.8
Elimination of intersegment income	(14.1)	0.9	3.6	11.5	(2.5)	0.6	0
	(13.6)	8.0	6.5	41.7	18.1	(0.1)	60.8
Unallocated corporate expenses							(4.5)
Total income from operations							56.3
As of and for the year ended December 31, 2005							
Income from operations	(0.9)	7.7	3.1	30.2	11.4	(1.3)	50.2
Elimination of intersegment income	(13.3)	1.0	3.2	12.6	(4.0)	0.5	0
	(14.2)	8.7	6.3	42.8	7.4	(0.8)	50.2
Unallocated corporate expenses							(5.1)
Total income from operations							45.1

(1) Beginning with the fiscal year ended December 31, 2006, we no longer combine cellular and paging services in one business segment. Instead, income from operations from paging services are included in Other. For this reason, income from operations for 2005 have been reclassified on a comparable basis.

As a result of the foregoing, in 2005 compared to 2006 operating loss for our local telephone services decreased by 4% from NT$14.2 billion to NT$13.6 billion (US$0.4 billion); operating income for our domestic long distance telephone services decreased by 8.4% from NT$8.7 billion to NT$8.0 billion (US$0.2 billion); operating income for our international long distance telephone services increased by 3.4% from NT$6.3 billion to NT$6.5 billion (US$0.2 billion); operating income for our cellular services decreased by 2.7% from NT$42.8 billion to NT$41.7 billion (US$1.3 billion); and operating income for our internet and data services increased by 145% from NT$7.4 billion to NT$18.1 billion (US$0.6 billion).

Our management evaluates our business segments taking into account internal and inter-segment costs and revenues. All of our business lines, particularly local telephone, domestic long distance telephone and international long distance telephone services, operate as an integrated business unit. Therefore, we have shown the inter-segment income in the above table.

Other Income and Other Expenses

Our other income decreased by 22.2% from NT$2.0 billion in 2005 to NT$1.6 billion (US$47 million) in 2006. This decrease was primarily due to an NT$0.2 billion decrease in rental income as rental income was recategorized from other income in 2005 to revenue—other in 2006 and an NT$0.1 billion decrease in foreign exchange loss. We recategorized rental income from other income to revenues—other in 2006 as we have 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 and therefore expect rental income will increase in future years.

Our other expenses decreased by 55.2% from NT$1.1 billion in 2005 to NT$0.5 billion (US$15 million) in 2006. This decrease was largely due to a NT$740 million impairment loss on our long-term investment in the Taipei 101 building in 2005.

Income Tax

Our income tax was NT$12.7 billion in 2005, compared to NT$15.3 billion (US$469 million) in 2006. Our effective tax rate was 27.7% in 2005 and 26.6% in 2006.

Net Income

As a result of the foregoing, our net income increased by 26.3% from NT$33.3 billion in 2005 to NT$42.1 billion (US$1.3 billion) in 2006. Our net margin was 18.0% in 2005 and 22.6% in 2006.

Year ended December 31, 2004 compared with year ended December 31, 2005

Revenues

Our revenues decreased by 0.3% from NT$185.2 million in 2004 to NT$184.7 billion (US$5.6 billion) in 2005. This decrease was primarily due to a continuous decline in fixed network business and an expansion of the average expected customer service period which affects the revenue from fixed network.

Fixed Line Services

Fixed line revenues comprised 38.9% and 35.9% of our revenues in 2004 and 2005, respectively. Our fixed line revenues decreased by 8.0% from NT$72.1 billion in 2004 to NT$66.3 billion (US$2.0 billion) in 2005.

Local telephone services. Our local telephone revenues decreased by 9.3% from NT$44.9 billion in 2004 to NT$40.7 billion (US$1.2 billion) in 2005. This decrease was principally a result of a 14.0% decline in traffic volume from 24.5 billion minutes in 2004 to 21.1 billion minutes in 2005. This decline in traffic volume was primarily due to the continued migration of non-HiNet internet subscribers from dial-up to broadband internet access, the continued traffic migration from fixed line services to broadband and cellular services, and increasing market competition. We expect this trend to continue as broadband and cellular services become more widely adopted in Taiwan. However, we believe the rate of traffic migration from fixed-line services to broadband and cellular services is slowing. This decline in traffic volume was partially offset by a 2.9% increase in average local usage fees, reflecting a continued decrease in the number of users of our discounted internet tariff package. The decrease was also due to the expansion of the customer service period from an average of 13 years to 16 years, which has caused a substantial decline in revenues in local telephone connection fees. Our local interconnection revenues decreased by NT$0.1 billion between these two years because of a decrease in local interconnection volume.

Domestic long distance telephone services. Our domestic long distance telephone revenues decreased by 8.3% from NT$12.0 billion in 2004 to NT$11.0 billion (US$0.3 billion) in 2005. This decrease was mainly due to a decrease in traffic volume from 5.6 billion minutes in 2004 to 5.1 billion minutes in 2005. The decrease in traffic volume was primarily due to the continued traffic migration from fixed line services to broadband and cellular services and increased competition from other fixed line operators. The rate of migration from fixed line services to cellular services has been slowing in the past two years as the cellular market becomes increasingly saturated. Our interconnection revenues also decreased as a result of more direct connections between private operators.

International long distance telephone services. Our international long distance telephone revenues decreased by 4.1% from NT$15.2 billion in 2004 to NT$14.6 billion (US$0.4 billion) in 2005. This decrease was mainly due to intense market competition and a decrease in the average per minute usage charge due to promotional packages to encourage usage. This was partially offset by an 8% increase in outgoing traffic volume from 2004 to 2005. Our international settlement revenues decreased by 5.6% from NT$3.5 billion in 2004 to NT$3.3 billion (US$0.1 billion) in 2005. This decrease was primarily due to the continued decline in international settlement rates and translation losses due to fluctuations in foreign exchange rates.

Cellular Services

Our cellular services grew as a percentage of our revenues from 38.0% in 2004 to 39.5% in 2005. Our cellular services revenues increased by 3.9% from NT$70.3 billion in 2004 to NT$73.0 billion (US$2.2 billion) in 2005. This increase was mainly a result of an increase in outgoing traffic volume of 2.9% from 8.7 billion minutes in 2004 to 8.9 billion minutes in 2005, as a result of an increase in the number of customers using monthly rental service.

Internet and Data Services

Internet and data revenues comprised 21.2% and 22.8% of our revenues in 2004 and 2005, respectively. Our internet and data revenues increased by 7.2% from NT$39.3 billion in 2004 to NT$42.2 billion (US$1.3 billion) in 2005 due primarily to an increase in our internet services.

Internet services. Our revenues attributable to internet services increased by 8.6% from NT$29.5 billion in 2004 to NT$32.1 billion (US$1.0 billion) in 2005. This increase was largely due to an increase in the number of our ADSL subscribers from 3.1 million as of December 31, 2004 to 3.7 million as of December 31, 2005. This increase was also due to a 7.6% increase in the number of our HiNet subscribers from 3.8 million as of December 31, 2004 to 4.1 million as of December 31, 2005. Calls to HiNet are recorded as part of our internet and data services and are not included in our local minutes or revenues. We include usage fees from fixed line telephone calls to access our HiNet service in our internet and data revenues. Usage fees from fixed line telephone calls to access internet service providers other than HiNet are recorded as fixed line revenues.

Data services. Revenues from our data services increased by 3.0% from NT$9.8 billion in 2004 to NT$10.1 billion (US$0.3 billion) in 2005. This increase was principally due to an increase in revenues from our hiLink virtual private network service. We continue to derive a substantial portion of our data revenues from leased line services. While demand for higher speed lease lines continues to increase, our overall leased line tariffs have continued to be adversely affected by competition from other fixed line operators and international leased line service providers, as well as the continued migration of domestic leased line users to ADSL services. The effects of tariff decreases were generally offset by the continued increase in the usage of our leased line services in 2005.

Other

Other revenues comprised 1.9% and 1.8% of our revenues in 2004 and 2005, respectively.

Our other revenues decreased by 6.7% from NT$3.5 billion in 2004 to NT$3.2 billion (US$99.7 million) in 2005. This decrease in other revenues was primarily due to an NT$0.3 billion decrease in revenues from our corporate solution business and a decrease in revenues of NT$0.2 billion from our paging services.

Operating Costs and Expenses

Our operating costs and expenses increased by 12.8% from NT$123.7 billion in 2004 to NT$139.6 billion (US$4.3 billion) in 2005. This increase was primarily due to increases in stock compensation expenses and performance-based bonuses. As a percentage of revenues, operating costs and expenses increased from 66.8% in 2004 to 75.5% in 2005.

Costs of Revenues

Costs of revenues include personnel expenses, international settlement costs, handset incentives, spectrum usage and license fees, costs of materials and maintenance and interconnection fees among cellular operators.

Our costs of revenues increased by 16.0% from NT$58.7 billion in 2004 to NT$68.1 billion (US$2.1 billion) in 2005. This increase was principally a result of: an NT$7.2 billion increase in employees' purchase of our common shares at discounts; an NT$0.9 billion increase in our handset incentives; an NT$0.8 billion increase in performance-based bonuses; and an NT$0.3 billion impairment loss on long-term assets. We recognize compensation expense when our employees purchase our common shares at discounts under the priority share subscription program.

Marketing

Our marketing expenses, which include personnel expenses, provisions for bad debt and expenses relating to advertising and other marketing-related activities, increased by 22.6% from to NT$19.3 billion in 2004 to NT$23.7 billion (US$0.7 billion) in 2005. This increase was mainly due to an NT$4.0 billion increase in employees' purchase of our common shares at discounts and an NT$0.4 billion increase in performance-based bonuses. We recognize compensation expense when our employees purchase our common shares at discounts under the priority share subscription program.

General and Administrative

Our general and administrative expenses increased by 37.5% from NT$2.5 billion in 2004 to NT$3.5 billion (US$0.1 billion) in 2005. This increase was primarily due to an increase of NT$0.7 billion in compensation expense arising under our employee priority share subscription program; and an increase of NT$76 million in performance-based bonuses. We recognize compensation expense when our employees purchase our common shares at discounts under the priority share subscription program. The higher compensation expense in 2005 was largely due to an increase in such purchases by our employees compared to 2004.

Research and Development

Our research and development expenses increased by 27.0% from NT$2.5 billion in 2004 to NT$3.1 billion (US$0.1 billion) in 2005. This increase was primarily due to an increase of NT$0.5 billion in compensation expense as a result of an increase in employees' purchases of our common shares at a discount under our employee priority share subscription program and an increase of NT$74 million in performance-based bonuses. Our research and development expenses increased as a percentage of our revenues from 1.3% in 2004 to 1.7% in 2005.

Depreciation and Amortization

Our depreciation and amortization expenses increased by 1.1% from NT$40.7 billion in 2004 to NT$41.2 billion (US$1.3 billion) in 2005. This increase was mainly due to the amortization of our 3G licence.

Operating Costs and Expenses by Business Segment

	Local	Domestic Long Distance	International Long Distance	Cellular Service	Internet and Data	Other(1)	Total
			(in billions of NT$)				
As of and for the year ended December 31, 2005							
Operating costs and expenses	36.0	1.5	7.6	22.8	22.4	3.2	93.5
Unallocated corporate expenses							4.9
Total operating costs and expenses							98.4
Depreciation and amortization	19.0	0.7	0.7	7.4	12.4	0.8	41.0
Unallocated corporate expenses							0.2
Total depreciation and amortization							41.2
As of and for the year ended December 31, 2004							
Operating costs and expenses	32.2	1.2	7.5	19.9	16.2	2.0	79.0
Unallocated corporate expenses							4.0
Total operating costs and expenses							83.0
Depreciation and amortization	20.0	0.8	0.7	5.9	12.4	0.8	40.6
Unallocated corporate expenses							0.1
Total depreciation and amortization							40.7

(1) Beginning with the fiscal year ended December 31, 2006, we no longer combine cellular and paging services in one business segment. Instead, operating costs and expenses from paging services are included in Other. For this reason, operating costs and expenses for 2004 and 2005 have been reclassified on a comparable basis.

Local telephone services

Our local telephone operating expenses, excluding depreciation and amortization, increased by 11.8% from NT$32.2 billion in 2004 to NT$36.0 billion (US$1.1 billion) in 2005. This increase was primarily due to an NT$4.5 billion increase in employees' purchase of our common shares at discount. Our depreciation and amortization expenses relating to local telephone services decreased by 4.9% from NT$20.0 billion in 2004 to NT$19.0 billion (US$0.6 billion) in 2005. The decrease was a result of a decrease in depreciation and amortization expenses because of an increase in obsolete equipment.

Domestic long distance telephone services

Our domestic long distance telephone operating expenses, excluding depreciation and amortization, increased by 23.2% from NT$1.2 billion in 2004 to NT$1.5 billion (US$46 million) in 2005. The increase was primarily due to an NT$0.2 billion increase in the employees' purchase of our common shares at discount. Our depreciation and amortization expenses relating to domestic long distance telephone services decreased by 12.7% from NT$0.8 billion in 2004 to NT$0.7 billion (US$21.9 million) in 2005. The decrease in depreciation and amortization expenses was mainly due to a slow-down of our upgrading equipment.

International long distance telephone services

Our international long distance telephone operating expenses, excluding depreciation and amortization, increased by 1.0% from NT$7.5 billion in 2004 to NT$7.6 billion (US$0.2 billion) in 2005. The increase was primarily due to an NT$0.35 billion increase in the employees' purchase of our common shares at discounts. Our depreciation and amortization expenses relating to international long distance telephone services remained flat at NT$0.7 billion in 2004 and in 2005.

Cellular Services

Our cellular operating expenses, excluding depreciation and amortization, increased by 14.3% from NT$19.9 billion in 2004 to NT$22.8 billion (US$0.7 billion) in 2005. This increase was primarily due to an NT$1.2 billion increase in the employees' purchase of our common shares at discounts and an NT$1 billion increase in marketing expenses. Our depreciation and amortization expenses relating to cellular services increased by 25.8% from NT$5.9 billion in 2004 to NT$7.4 billion (US$0.2 billion) in 2005. The increase was mainly due to an NT$1.0 billion increase in depreciation caused by purchases of new equipment such as mobile exchangers and signal transmitters and receivers and an NT$0.4 billion increase in amortization of 3G license fees.

Internet and Data Services

Our internet and data operating expenses, excluding depreciation and amortization, increased by 37.8% from NT$16.2 billion in 2004 to NT$22.4 billion (US$0.7 billion) in 2005. This increase was primarily due to an NT$5.3 billion increase in the employees' purchase of our common shares at discounts. Our depreciation and amortization expenses relating to internet and data services remained flat at NT$12.4 billion in 2004 and in 2005.

Operating Income and Operating Margin

As a result of the foregoing, our operating income decreased by 26.5% from NT$61.5 billion in 2004 to NT$45.1 billion (US$1.4 billion) in 2005. Our operating margin decreased from 33.2% in 2004 to 24.5% in 2005.

The following table sets forth certain information regarding our operating income by business segment for the periods indicated.

	Local	Domestic Long Distance	International Long Distance	Cellular Service	Internet and Data	Other[(1)]	Total
			(in billions of NT$)				
As of and for the year ended December 31, 2005							
Income from operations	(0.9)	7.7	3.1	30.2	11.4	(1.3)	50.2
Elimination of intersegment income	(13.3)	1.0	3.2	12.6	(4.0)	0.5	—
	(14.2)	8.7	6.3	42.8	7.4	(0.8)	50.2
Unallocated corporate expenses							(5.1)
Total income from operations							45.1
As of and for the year ended December 31, 2004							
Income from operations	6.1	8.5	3.9	32.7	14.0	0.4	65.6
Elimination of intersegment income	(13.3)	1.4	3.1	11.8	(3.3)	0.3	—
	(7.2)	9.9	7.0	44.5	10.7	0.7	65.6
Unallocated corporate expenses							(4.1)
Total income from operations							61.5

(1) Beginning with the fiscal year ended December 31, 2006, we no longer combine cellular and paging services in one business segment. Instead, income from operations from paging services are included in Other. For this reason, income from operations for 2004 and 2005 have been reclassified on a comparable basis.

As a result of the foregoing, in 2004 compared to 2005 operating loss for our local telephone services increased by 96.6% from NT$7.2 billion to NT$14.2 billion (US$434.3 million); operating income for our domestic long distance telephone services decreased by 11.8% from NT$9.9 billion to NT$8.7 billion (US$265.9 million);

operating income for our international long distance telephone services decreased by 9.9% from NT$7.0 billion to NT$6.3 billion (US$192.1 million); operating income for our cellular services decreased by 3.7% from NT$44.5 billion to NT$42.8 billion (US$1.3 billion); and operating income for our internet and data services decreased by 31.1% from NT$10.7 billion to NT$7.4 billion (US$225.4 million).

Our management evaluates our business segments taking into account internal and inter-segment costs and revenues. All of our business lines, particularly local telephone, domestic long distance telephone and international long distance telephone services, operate as an integrated business unit. Therefore, we have shown the inter-segment income in the above table.

Other Income and Other Expenses

Our other income increased by 75.9% from NT$1.1 billion in 2004 to NT$2.0 billion (US$60 million) in 2005. This increase was primarily due to an NT$228 million increase in interest income, an NT$128 million increase in gains on sales of short-term investment and an NT$90 million increase resulting from equity in earnings of unconsolidated companies.

Our other expenses increased by 163.8% from NT$0.4 billion in 2004 to NT$1.1 billion (US$34 million) in 2005. This increase was largely due to a NT$740 million impairment loss on our long-term investment in the Taipei 101 building in 2005.

Income Tax

Our income tax was NT$11.3 billion in 2004, compared to NT$12.7 billion (US$388 million) in 2005. Our effective tax rate was 18.1% in 2004 and 27.7% in 2005.

Net Income

As a result of the foregoing, our net income decreased by 34.6% from NT$50.9 billion in 2004 to NT$33.3 billion (US$1.0 billion) in 2005. Our net margin was 27.5% in 2004 and 18.0% in 2005.

B. Liquidity and Capital Resources

Liquidity

The following table sets forth the summary of our cash flows for the periods indicated:

	For the year ended December 31,			
	2004	2005	2006	
		(in billions)		
	NT$	NT$	NT$	US$
Net cash provided by operating activities	91.6	86.2	100.1	3.1
Net cash used in investing activities	(32.4)	(28.0)	(19.1)	(0.6)
Net cash used in financing activities	(43.4)	(45.6)	(52.2)	(1.6)
Net increase in cash and cash equivalents	15.8	12.6	28.8	0.9
Cash and cash equivalents at end of period	29.3	41.9	70.7	2.2

Our primary source of liquidity is cash flow from operations, which represents operating profit adjusted for non-cash items, primarily depreciation and amortization and changes in current assets and liabilities. We believe that our working capital is sufficient for our present requirements.

In 2006, our net cash provided by operating activities totaled NT$100.1 billion (US$3.1 billion), compared with NT$86.2 billion in 2005. This increase was primarily due to an NT$10.1 billion decrease in income tax expenditure. In 2005, our net cash provided by operating activities totaled NT$86.2 billion compared with NT$91.6 billion in 2004. This decrease was primarily due to a decrease in net income.

Historically, net cash provided by operating activities has been sufficient to cover our capital expenditures, including the ongoing expansion and modernization of our networks. Our net cash used in investing activities decreased from NT$28.0 billion in 2005 to NT$19.1 billion (US$0.6 billion) in 2006, principally as a result of an NT$12.7 billion increase in purchases and sales of short-term investments offset by NT$4.8 billion increase in acquisition of property, plant and equipment. Our net cash used in investing activities decreased from NT$32.4 billion in 2004 to NT$28.0 billion in 2005, principally as a result of an NT$4.3 billion decrease in purchases and sales of short-term investments.

In 2006, our net cash used in financing activities totaled NT$52.2 billion (US$1.6 billion), which reflected NT$40.7 billion of payment of dividends and NT$11.4 billion of purchase of treasury stock during that period. In 2005, our net cash used in financing activities totaled NT$45.6 billion, which reflected NT$45.3 billion of payment of dividends during that period. In 2004, our net cash used in financing activities totaled NT$43.4 billion, which reflected NT$43.4 billion of payment of dividends during that period.

Capital Resources

We have historically financed our capital expenditure requirements with our cash flows from operations.

In future years, we expect to have capital expenditure requirements for the ongoing expansion and upgrade of our networks combined with anticipated outlays for the introduction of new services, including our 3G cellular services. We also expect to make dividend payments on an ongoing basis. See "Item 8. Financial Information—A. Consolidated Statements and Other Financial Information." Furthermore, we may require working capital from time to time to finance purchases of materials for our maintenance and other overhead expenses. We expect to primarily rely on cash generated from operations and, to a lesser extent, loans from commercial banks to meet our planned capital expenditures, make our planned dividend payments, repay debts and fulfill other commitments over the next 12 months.

As of December 31, 2006, our primary source of liquidity was NT$70.7 billion (US$2.2 billion) of cash and cash equivalents. We had a portfolio of interest-free debt of approximately NT$0.7 billion, NT$0.5 billion and NT$0.3 billion (US$9.2 million) as of December 31, 2004, 2005 and 2006, respectively. Our only long-term loan has a five-year term with three annual installment payments due beginning in March 2005 and ending in March 2007. We are not subject to any covenants under any of our long-term loan facilities.

On November 18, 2005, our subsidiary Chief Telecom Inc. obtained a secured loan in the amount of NT$23 million from Chinatrust Commercial Bank at an annual interest rate of 3.05%. Interest and principle are payable monthly and the secured loan is due by November 18, 2007. Chief Telecom Inc. also has short-term loans in the amount of NT$126 million at a floating rate equivalent to the two-year time deposit interest rate plus 0.7%, which will be due on October 11, 2007.

In 1995, we and several other public utilities companies in Taiwan were required by the Republic of China government to contribute funds as a part of the government's effort to upgrade the existing telecommunication and other infrastructure in Taiwan. As of December 31, 2006, we have contributed NT$2.0 billion to the funds, and the contributions were accounted for as "Other assets- Other" on our balance sheets. If the contributions to the funds are not sufficient to finance the construction of the new underground fixed lines and conduits, the contributors to the funds and the governmental agencies will determine if and when to raise additional capital and the amounts of such contributions from each party. This fund allows us to obtain unsecured interest-free loans up to the original amount contributed to the fund. As of December 31, 2006, we had total outstanding borrowings of NT$0.3 billion from this fund, which is due within one year. We are not required to provide any collateral to secure these borrowings.

We have a revolving credit facility with a term of one year. As of December 31, 2006, we had not made any drawdowns under this facility. We are not subject to any covenants for borrowings under this facility. In the past, we had from time to time issued commercial paper to fund our working capital needs. In 2006, we did not issue any commercial paper. We may issue commercial paper in the future for our short-term cash requirements.

We have not entered into any financial guarantees or similar commitments to guarantee the payment obligations of third parties. In addition, we do not have any written options on non-financial assets.

Capital Expenditures

The following table sets forth a summary of our capital expenditures for the periods indicated.

	For the year ended December 31,					
	2004		2005		2006	
	(NT$ in million, except percentages)					
Capital Expenditures						
Wireline equipment[1]	16,611	72.6%	17,857	77.9%	17,898	64.7%
Cellular equipment	5,512	24.1	4,449	19.4	9,405	34.0
Others	766	3.3	624	2.7	377	1.3
Total capital expenditures	22,889	100.0%	22,930	100.0%	27,680	100.0%

(1) Wireline equipment used to provide fixed line services and data and internet services. Some wireline equipment is jointly used by fixed line and data and internet services.

The following table sets forth a summary of our planned capital expenditures for the year ending December 31, 2007.

	For the year ending December 31, 2007	
	(in millions of NT$, except percentages)	
Capital Expenditures		
Wireline equipment	22,490	75.0%
Cellular equipment	6,377	21.3
Others	1,128	3.7
Total capital expenditures	29,995	100.0%

We expect our total capital expenditures to be approximately NT$30 billion in 2007. In future periods, we expect our total capital expenditures to rise due to the launch of new businesses, internet protocol next generation network migration, and 3G cellular network expansion. We expect to finance these capital expenditures with our cash flows from operations.

Inflation/Deflation

We do not believe that deflation or inflation in Taiwan has had a material impact on our results of operations.

Recent Accounting Pronouncements

In June 2006, the FASB issued SFAS No. 157, "Fair Value Measurements," to define fair value, establish a framework for measuring fair value in accordance with accounting principles generally accepted in the United

States of America, and expand disclosures about fair value measurements. SFAS No. 157 will be effective for consolidated financial statements issued for fiscal years beginning after November 15, 2007, the beginning of the Company's 2008 fiscal year. The Company is assessing the impact the adoption of SFAS No. 157 will have on the Company's consolidated financial position and results of operations.

In July 2006, the FASB issued FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes"—an interpretation of FASB Statement No. 109 (FIN 48), which clarifies the accounting for uncertainty in tax positions. The Interpretation prescribes a recognition threshold and a measurement attribute for the consolidated financial statement recognition and measurement of tax positions taken or expected to be taken in a tax return. FIN 48 is effective for fiscal years beginning after December 15, 2006. On January 1, 2007, the Company adopted FIN 48. The Company expects that the adoption of FIN48 will not have a significant impact on the Company's consolidated financial position, results of operations and effective tax rate.

In September 2006, the Securities and Exchange Commission ("SEC") issued Staff Accounting Bulletin ("SAB") No. 108. This Bulletin provides the Staff's views on the consideration of the effects of prior year misstatements in quantifying current year misstatements for the purpose of a materiality assessment. The guidance in SAB No. 108 is effective for consolidated financial statements on fiscal years ending after November 15, 2006. Adoption of this guidance did not materially impact on the Company's consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities" (SFAS 159). Under this Standard, the Company may elect to report financial instruments and certain other items at fair value on a contract-by-contract basis with changes in value reported in earnings. This election is irrevocable. SFAS 159 provides an opportunity to mitigate volatility in reported earnings that is caused by measuring hedged assets and liabilities that were previously required to use a different accounting method than the related hedging contracts when the complex provisions of SFAS 133 hedge accounting are not met. There is no impact to the Company as a result of the adoption of this standard.

C. Research, Development, Patents and Licenses, Etc.

Research and Development

Our research and development efforts are focused on the development of advanced network services and operation technologies as well as the development of core technologies for the domestic telecommunications market. For 2004, 2005 and 2006, our research and development expenses excluding depreciation and amortization were approximately NT$2.5 billion, NT$3.1 billion and NT$2.8 billion (US$87 million), respectively, or 1.3%, 1.7% and 1.5% of our revenues, respectively.

We currently have more than 1,187 researchers focusing on the following areas:

- wireless communication;
- broadband transmission and access;
- Internet and multimedia applications;
- network operation support;
- customer service information;
- advanced technologies research; and
- customer premises equipment.

We have developed a number of advanced network services, operation technologies and applications and value-added services, including our ADSL deployment, internet-based call center, e-commerce platform, global standard for mobile communications billing system, a new telecommunications operation service system for all business units of our company, government public key infrastructure, a leased line testing and monitoring system and an intelligent transportation system. As of March 31, 2007, we have been granted 257 domestic patents and 27 foreign patents.

D. Trend Information

See "—Overview" for a discussion of the most significant recent trends that have had, and in the future may have, a material impact on our results of operations, financial condition and capital expenditures. In addition, see discussions included in this Item for a discussion of known trends, uncertainties, demands, commitments or events that we believe are reasonably likely to have a material effect on our net operating revenues, income from continuing operations, profitability, liquidity or capital resources, or that would cause reported financial information not necessarily to be indicative of future operating results or financial condition.

E. Off-Balance Sheet Arrangements

As of December 31, 2006, we did not have any off-balance sheet arrangements.

F. Tabular Disclosure of Contractual Obligations

Set forth below are our total contractual obligations as of December 31, 2006.

	Total	2007	2008	2009	2010	After 2010
Contractual Obligations						
Long-term debt[1]	0.3	0.3	—	—	—	—
Operating leases	3.1	1.2	0.9	0.6	0.3	0.1
Total	3.4	1.5	0.9	0.6	0.3	0.1

(1) Amounts do not include interest payments as the majority of our long-term debt is interest-free.

As of December 31, 2006, we had remaining commitments under non-cancelable contracts with various parties as follows: acquisition of lands and buildings of NT$1.6 billion and acquisition of telecommunications equipment of NT$15.5 billion. We do not have any capital lease obligations or other long-term liabilities.

G. Foreign Exchange

Our revenues and costs and expenses are largely denominated in NT dollars. Our principal expenses denominated in foreign currencies are capital expenditures on telecommunications equipment and settlement payments for the use of networks of carriers in foreign countries for outgoing international calls. Settlement receipts have been a principal source of foreign currency for us. While future fluctuations of the NT dollar against foreign currencies could impact our financial condition and results of operations, we have not to date been materially affected by the fluctuation of the NT dollar against foreign currencies.

Devotion and diligence are what drive us.

ITEM 6. DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES

A. Directors and Senior Management

The following table sets forth the name, age, position and tenure of each of our directors, supervisors and executive officers and such person's position as of March 31, 2007. There is no family relationship among any of these persons. All of our directors and supervisors were elected at our annual general shareholders' meeting held on June 25, 2004 and have terms from June 25, 2004 to June 24, 2007.

Name	Age	Position	Tenure with us
Tan Ho Chen	57	Chairman and Chief Executive Officer	4 years
Shyue-Ching Lu	58	Director and President	29 years
Oliver F.L. Yu	61	Director	5 years
Yu-Huei Jea	64	Director	9 years
Jeng-Tsuen Liaw	64	Director	3 years
Chao-I Hsieh	59	Director	5 months
Neng-Pai Lin	54	Director	1.5 years
Chiu-Kuei Huang	53	Director	4 years
Lo-Ming Chung	56	Director	4 years
Chien-Cheng Lin	50	Director	3 years
Jing-Twen Chen(1)	53	Director	6 years
Zse-Hong Tsai(1)	46	Director	5 years
Joyce H.Y. Jen(1)	50	Director	3 years
Shih-Peng Tsai(2)	58	Director	34 years
Hsu-Chung Simon Chang(2)	48	Director	30 years
Judy Fu-meei Ju	50	Supervisor	5 years
Ming-Daw Chang	54	Supervisor	4 years
Yu-Hsien Lin	50	Supervisor	4 years
Yeong-Chwan Hwang	52	Supervisor	8 years
Feng-Hsiung Chang	63	Senior Executive Vice President	37 years
Joseph C.P. Shieh	47	Chief Financial Officer and Senior Vice President	2 months
Shaio-Tung Chang	60	Senior Vice President	38 years
John C.C. Hsueh	62	Senior Vice President	35 years
Hank Han-Chao Wang	58	Senior Vice President	32 years
Tsung-Yen Chang	58	Senior Vice President	33 years
Chun-Ming Hsieh	63	Executive Vice President	39 years
Chi-Mao Hsieh	53	Executive Vice President	30 years
Jen-Hung Lin	61	Executive Vice President	38 years
Hsiang-Yi Chen	55	Executive Vice President	31 years
Yen-Sung Lee	58	Executive Vice President	33 years
Cheng-Lang Huang	58	Executive Vice President	35 years

(1) Independent director.

(2) Shih-Peng Tsai was replaced by Hsu-Chung Simon Chang on March 9, 2006.

Tan Ho Chen is our Chairman and Chief Executive Officer. Mr. Ho Chen is also currently an Executive Officer of The National Land Policy Advisory Committee, Office of the President, Republic of China. Mr. Ho Chen was the Executive Vice Minister of the Ministry of Transportation and Communications from 2000 to 2001. Mr. Ho Chen holds a Master's degree in regional and urban planning from Virginia Polytechnic Institute & State University and a Bachelor's degree in civil engineering from the National Chung-Hsing University in Taiwan and studied urban planning while on a Humphrey Fellowship at Hunter College in New York.

Shyue-Ching Lu is a director and the President of our company. Dr. Lu was the Director General of the Department of Posts and Communications of the Ministry of Transportation and Communications from 1993 to 1994 and the Deputy Director General of the Directorate General of Telecommunications from 1994 to 1996. Dr. Lu holds a Ph.D. degree in electrical engineering from the University of Hawaii and a Bachelor's degree in engineering from the National Cheng Kung University in Taiwan.

Oliver F.L. Yu is a director of our company. Mr. Yu is also currently the Vice Minister of the Ministry of Transportation and Communications. Mr. Yu was the Director of Kaohsiung Harbor Bureau from 1996 to 2001 and the Director General of Civil Aeronautics Administration, Ministry of Transportation and Communications from 2001 to 2002. Mr. Yu holds a Master of Business Administration degree from the Institute of Management Science, National Chiao Tung University and a Bachelor's degree in transportation and communications management science from the National Cheng Kung University in Taiwan.

Yu-Huei Jea is a director of our company. Dr. Jea is also a Senior Counselor of the Ministry of Transportation and Communications. Dr. Jea was the Director General of the Department of Posts and Telecommunications from 1994 to 1996 and the Director General of the Directorate General of Telecommunications from 1996 to 1997. Dr. Jea holds a Ph.D. degree in electrical engineering from the University of Texas at Austin.

Jeng-Tsuen Liaw is a director of our company. Mr. Liaw is also a Director of Personnel Department, the Ministry of Transportation and Communications. He was the Director General of the Department of Manpower of Central Personnel Administration, Executive Yuan from 1995 to 2001. He graduated from the Department of Public Administration and Policy with a Bachelor's degree from the National Chung-Hsing University in Taiwan. His specialty field is human resources management.

Chao-I Hsieh is a director of our company. Mr. Hsieh is also a Senior Counselor of the Ministry of Transportation and Communications. He holds a Ph.D. degree from Pennsylvania University, and he majored in city and regional planning.

Neng-Pai Lin is a director of our company. Mr. Lin is also a Professor of Health Care Organization Administration at the National Taiwan University. He holds a Ph.D. degree from Ohio State University in business administration.

Chiu-Kuei Huang is a director of our company. Ms. Huang is also currently the Director of Labor Relations, Department of the Council of Labor Affairs. Ms. Huang was the Director of the Labor Condition Department from 2002 to 2003. She graduated from the Institute of Labor Science, Chinese Culture University, with a Master's degree in labor science.

Lo-Ming Chung is a director of our company. Mr. Chung is also currently the Executive Vice President of China Steel Corporation. He holds a Master of Business Administration degree from Arizona State University.

Chien-Cheng Lin is a director of our company. Since 1991, Dr. Lin has been a Professor of the Department of Materials Science and Engineering, National Chiao Tung University. He is also the Dean of General Affairs at the National Chiao Tung University. He holds a Ph.D. degree in materials science and engineering from the University of Illinois at Urbana-Champaign, a Bachelor of Science degree in mechanical engineering from the National Taiwan University, and a Master of Science degree in materials science and engineering from the National Sun Yat-Sen University in Taiwan.

Jing-Twen Chen is a director of our company. Dr. Chen is also a Professor at the Department of Finance of the National Central University in Taiwan. Dr. Chen holds a Ph.D. degree in finance from the National Taiwan University of Science and Technology.

Zse-Hong Tsai is a director of our company. Dr. Tsai is also currently a Professor of Electrical Engineering at the National Taiwan University. His research interest includes broadband networking, performance evaluation and telecommunication regulations. Dr. Tsai holds a Ph.D. degree and a Master of Science degree in electrical engineering from the University of California at Los Angeles, and a Bachelor of Science degree in electrical engineering from the National Taiwan University.

Joyce H.Y. Jen is a director of our company. Ms. Jen is the founder and a senior partner of Serenity Law Office. She graduated from the National Taiwan University with Bachelor's and Master's degrees in law. She also studied at the Law School of University College London, Great Britain, and the University of Wisconsin. She specializes in commercial law, business law and corporate transactions, construction and public contracts law, intellectual property law and real estate law.

Shih-Peng Tsai is a director of our company. Mr. Tsai is also currently a representative of Member's Convention, Chunghwa Telecom Workers Union and serves as Manager of our SeeKoo Service Center. Mr. Tsai graduated from Ta Tung Junior Technological College of Commerce in Taiwan.

Hsu-Chung Simon Chang is a director of our company. Mr. Chang is also President of Chunghwa Telecom Workers Union. He holds a Master's degree in public affairs management from National Sun Yat-Sen University, ROC and a Bachelor's degree in Foreign Languages & Literature from National Cheng Kung University. Mr. Chang is currently a student in the Ph.D. program at the Institute of Public Affair Management of National Sun Yat-Sen University.

Judy Fu-Meei Ju is a supervisor of our company. Ms. Ju also serves as the Third Department Director General of the Executive Yuan and as a public prosecutor in the Taiwan Superior Court Prosecutor's Office. Ms. Ju holds a Ph.D. degree in law from the National Taiwan University.

Ming-Daw Chang is a supervisor of our company. Mr. Chang is currently the Deputy Director General of Examination Bureau of Financial Supervisory Commission. Mr. Chang has worked for the Ministry of Finance since 1985, the Banking Bureau since 1991 and the Financial Examination Bureau since 2004. Mr. Chang holds a Master's degree in law from the Law Department of the Chinese Culture University in Taiwan.

Yu-Hsien Lin is a supervisor of our company. Mr. Lin is currently the Director of the Department of Accounting of the Ministry of Transportation and Communications. Mr. Lin was previously the Director of General Affairs of Directorate General of Budget, Accounting & Statistics, the Executive Yuan. Mr. Lin holds a Master's degree in Statistics from the National Chung-Hsing University in Taiwan.

Yeong-Chwan Hwang is a supervisor of our company. Mr. Hwang is also currently the Director of Accounting Office and the Deputy Director of Accounting Management Center of the Directorate General of Budget, Accounting and Statistics of the Executive Yuan. Mr. Hwang holds a Master's degree from Soochow University and a Bachelor's degree in accounting from the Fu Jen Catholic University, both in Taiwan.

Feng-Hsiung Chang is a Senior Vice President of our company. Mr. Chang is also a director of Siemens Telecommunications Systems and Chunghwa Investment Co., Ltd. Mr. Chang served as Deputy Managing Director of the Northern Taiwan Telecommunications Administration from 1994 to 1996. Mr. Chang holds a Bachelor's degree in business administration from Chung-Hsing University and a Master of Business Administration degree from the National Chiao Tung University, both in Taiwan.

Joseph C.P. Shieh is our Chief Financial Officer. Mr. Shieh served as an Executive Vice President and spokesman of Mega Financial Holding Company from February 2003 to January 2007. He was the Chairman of Mega Venture Investment Co. Ltd. from October 2004 to January 2007 and the CEO of the Investment Banking Business Group at Mega Financial Holding Company from July 2004 to January 2007. Dr. Shieh holds a Ph.D. degree in finance from Kent State University, Ohio.

Shaio-Tung Chang is a Senior Vice President of our company. Mr. Chang is also a director of Chunghwa Investment Co., Ltd. Mr. Chang served as Executive Vice President of our company and manager of our Mobile Business Group from July 2004 to March 2007. He also served as Executive Vice President of our company and manager of our International Business Group from December 2002 to July 2004. Mr. Chang holds a Master of Business Administration degree from the National Chiao Tung University in Taiwan.

John C.C. Hsueh is a Senior Vice President of our company. Mr. Hsueh is also a Board of Director of Taipei Financial Center Corp. He served as a President of Telecom Laboratories from October 1998 to October 2000. He also served as Executive Vice President of our company and as a manager of our Northern Taiwan Business Group from October 2000 to September 2006. Dr. Hsueh holds a Ph.D. degree in electric engineering and computer science.

Hank Han-Chao Wang is a Senior Vice President of our company. Mr. Wang is also a supervisor of Siemens Telecommunication System Limited. Mr. Wang served as the Senior Managing Director of the Finance Department of our company from 2001 to 2005, as Chief Financial Officer from April 2005 to January 2007 and has a total working experience of 32 years in our company. Mr. Wang holds a Master's Degree in management science from the National Chiao Tung University in Taiwan.

Tsung-Yen Chang is a Senior Vice President of our company. Mr. Chang is also a director of the Taiwan International Standard Electronics Ltd. Mr. Chang served as Assistant Vice President of our company and deputy manager of our Northern Taiwan Business Group from August 2003 to January 2006. Prior to that, he was a Manager of the Banciao Operation Department. Mr. Chang holds a Master of Science degree from the National Chiao Tung University.

Chun-Ming Hsieh is an Executive Vice President of our company and a manager of our Northern Taiwan Business Group. He served as an Executive Vice President of our company and a manager of our Central Taiwan Business Group from July 2004 to September 2006. He holds a Bachelor's degree in management science from National Chiao Tung University.

Chi-Mao Hsieh is an Executive Vice President of our company and a manager of our Southern Taiwan Business Group. Mr. Hsieh is also a manager of our Central Taiwan Business Group. He served as a president of the Department of Network from September 2001 to January 2004. He also served as Assistant Vice President of our company and deputy manager of our Central Taiwan Business Group from January 2004 to September 2006. Mr. Hsieh holds a Master of Business Administration degree from the National Taiwan University.

Jen-Hung Lin is an Executive Vice President and general manager of our Mobile Business Group of our company. Mr. Lin is also a director of the RPTI International Co., Ltd. Mr. Lin served as Assistant Vice President and deputy manager of our Mobile Business Group from July 1996 to January 2006. He also served as Executive Vice President of our company and manager of our International Business Group from January 2006 to March 2007. Mr. Lin graduated from New York Institute of Technology with Master's degree in electrical engineering.

Hsiang-Yi Chen is an Executive Vice President and Manager of our Data Communications Business Group. Mr. Chen is also a director of the RPTI International Co., Ltd. Mr. Chen was the President of our Value-added Service Department of our Data Communications Business Group from May 1997 to January 2005 and was an Assistant Vice President of our company and Deputy Manager of our Data Communications Business Group from January 2005 to September 2006. Mr. Chen holds a Master's degree in electronic engineering from National Taiwan University.

Yen-Sung Lee is an Executive Vice President and Manager of our Industrial Customer Group of our company. Mr. Lee was an Executive Vice President Manager of the Data Communications Business Group of our company from January 2002 to April 2005 and was the President of the Telecom Laboratories from April 2005 to February 2007. Mr. Lee holds a Ph. D. degree in information engineering from National Chiao Tung University.

Cheng-Lang Huang is an Executive Vice President of our company. Mr. Huang served as Assistant Vice President of our company and deputy manager of our Northern Taiwan Business Group from January 2005 to March 2007. He served as a president of the Department of Human Resources from June 2001 to January 2005. Mr. Huang holds a Master's degree in computer engineering from the National Chiao Tung University in Taiwan.

B. Compensation

The compensation plan for our directors and supervisors, approved at our annual general shareholders' meeting in 2006, stipulates that:

- the chairman of our board of directors may receive a fixed monthly income of NT$330,000 and his non-fixed income such as performance-related bonuses may not exceed his fixed income each year, and the chairman will not receive any extra compensation for directors;
- independent directors who serve in military, public office or hold teaching or administrative post may receive a fixed monthly compensation of NT$8,000, and those who do not service in military or public office or hold teaching or administrative post may receive a monthly compensation of NT$50,000;
- directors and supervisors who serve in military, public office or hold teaching or administrative post may receive a monthly compensation of NT$8,000, and those directors and supervisors who do not serve in military and public office or hold teaching or administrative post may receive a monthly compensation of NT$30,000;
- the labor union director only receives his fixed monthly income, and will not receive any extra compensation for directors.

Furthermore, the monthly compensation for our president, approved by our board of directors meeting in 2006, is NT$300,000, and his non-fixed income such as performance-related bonuses may not exceed his fixed income each year. If the president is also a director of the board, he will not receive any extra compensation for directors.

The compensation plan was put into practice on January 1, 2006. The aggregate amount of compensation that we paid to our directors, supervisors and executive officers in 2005 and 2006 was NT$35,601,063 and NT$91,281,404 respectively. The aggregate amount of compensation in 2006 includes an NT$68,839,752 salary payment for directors, supervisors and executive officers, an NT$15,337,128 bonus for directors and supervisors and an NT$7,104,524 bonus for executive officers and a labor union director. The 2006 compensation of our directors and supervisors may not exceed 0.2% of our distributable earnings and must be approved at our 2007 annual general shareholders' meeting.

We do not have any service contracts with any directors providing for any benefits upon termination of employment.

C. Board Practices

All of our directors were elected in June 2004 for a three-year term, which may be renewed for any number of consecutive terms. Pursuant to the Republic of China Company Law, however, the directors may be removed from office at any time by a resolution adopted at a shareholders' meeting. The chairman of our board of directors is elected by our directors. Our chairman presides at all meetings of our board of directors and also has the authority to act as our representative. We have not entered into any contract with any of our directors and supervisors by which our directors or supervisors are expected to receive benefits upon termination of their employment.

Our articles of incorporation provide for a 7-to-15-member board of directors. Three independent directors were elected during our annual general shareholders' meeting held on June 25, 2004. Pursuant to the Republic of China Securities and Exchange Act, as amended in January 2006, the Financial Supervisory Commission on

March 28, 2006 published a rule requiring listed non-financial-institution companies with paid-in capital exceeding NT$50 billion to appoint independent directors to their board of directors in accordance with the Act. This requirement shall apply to us upon expiry of the current term of our directors. The term "independent director" may have a different meaning when used in Taiwan than in other jurisdictions. The number of independent directors shall be not less than one-fifth of the total number of directors and not less than two in number. Pursuant to the relevant Republic of China regulations, our company is required to adopt the candidate-nomination-system as specified in the Republic of China Company Law to elect independent directors and both the board and shareholders holding one percent of our total outstanding shares or more will have the right to submit names for inclusion in the roster of independent director candidates. With respect to certain material decisions to be made by our company as specified in the Republic of China Securities and Exchange Act, including the adoption or amendment to our internal control system, material loans or guarantees, the issuance of equity-type securities, matters in which directors and supervisors have personal interests, the appointment and discharge of auditors, approval of financial reports, the appointment and discharge of financial, accounting or internal auditing officers and other matters prescribed by the Republic of China Financial Supervisory Commission, the dissenting opinion or qualified opinion of an independent director is required to be noted in the minutes of the board of directors' meeting. After our privatization on August 12, 2005, the number of labor union representatives on our board was reduced from three to one. As a result, our board currently is composed of 14 directors.

In accordance with our articles of incorporation, we are required to have 3 to 5 supervisors. We currently have 4 supervisors. In accordance with the Republic of China Company Law, our supervisors are elected by our shareholders and may not concurrently serve as our directors, executive officers or other staff members. The term of office for our supervisors is three years and their term may be renewed for any number of consecutive terms. Supervisors' duties and powers include, but are not limited to, supervision of our business operations, investigation of our financial condition, inspection of corporate records, verification of statements prepared by the board of directors prior to the annual general shareholders' meeting, calling of and giving reports at shareholders' meetings, representation of us in negotiations with our directors and giving notification, when appropriate, to the board of directors to cease acting in contravention of applicable law or regulations, our articles of incorporation or the resolutions adopted by our shareholders. The supervisors may be also removed from office at any time by a resolution adopted at a shareholders' meeting.

In the event preferred shares are outstanding, the holder of these preferred shares will be entitled to appoint one director and one supervisor. Under the Telecommunications Act of the Republic of China, the preferred shares may only be issued to the Ministry of Transportation and Communications. See "Item 10. Additional Information—B. Memorandum and Articles of Association—Preferred Shares."

Under the Republic of China Company Law, a person may serve as our director or supervisor in his personal capacity or as the representative of another legal entity. A director or supervisor who serves as the representative of a legal entity may be removed or replaced at any time at the discretion of that legal entity, and the replacement director or supervisor may serve the remainder of the term of office of the replaced director or supervisor. Except for our three independent directors, all of our directors and supervisors are representatives of the Ministry of Transportation and Communications. However, in accordance with the Republic of China Securities and Exchange Act, as amended, except with the approval of the Competent Authority (i.e. The Financial Supervisory Commission), a representative of the government or of a juristic person, as a shareholder of our company, may not be concurrently selected or serve as the director or supervisor from the time of expiration of the term currently being served by our directors or supervisors.

The business address of our directors, supervisors and executive officers is the same as our registered address.

Our audit committee was established in September 2004 and is comprised of our three independent directors: Joyce H.Y. Jen, Dr. Jing-Twen Chen and Dr. Zse-hong Tsai. Our audit committee is responsible for overseeing: (i) the review of and discussion with management regarding our consolidated financial statements and other financial reports and disclosure; (ii) the appointment of our principal accounting firm and approval of non-audit services provided by the principal accounting firm; (iii) the review and assessment of our internal control policy, procedures and functions; (iv) assisting management and our principal accounting firm to resolve any difficulties encountered in the course of audit work; (v) our compliance with legal and regulatory requirements impacting our financial reporting; (vi) the review and approval of procedures relating to major financial actions and related party transactions; and (vii) the assessment and management of our existing and potential risk exposure. Our board of directors has concluded that Dr. Jing-Twen Chen is our audit committee financial expert.

In addition to our audit committee, we also have a corporate strategy committee and drafting committee. Our corporate strategy committee is composed of five directors and is responsible for reviewing and advising on the budgets, capital requirements, financial forecasts, matters related to investments, business license matters, corporate reorganization, development plans and other major issues affecting our development. The conclusions of the corporate strategy committee are considered at a subsequent board of directors meeting. Our drafting committee is composed of three directors and is responsible for reviewing proposals to be considered by the board of directors in advance of the board of directors meeting. Approved proposals will be reported, discussed and resolved at the subsequent board of directors meeting. The board of directors passed a resolution on November 8, 2005 to set up a compensation committee, which is composed of five directors. The compensation committee will draft compensation proposals for the chairman, vice chairman, directors, supervisors, chief executive officer and general manager.

In November 2003, the Securities and Exchange Commission approved changes to the New York Stock Exchange's listing standards related to the corporate governance practices of listed companies. Under these rules, listed foreign private issuers, like us, must disclose any significant ways in which their corporate governance practices differ from those followed by New York Stock Exchange-listed U.S. companies under the New York Stock Exchange's listing standards. A copy of the significant differences between our corporate governance practices and New York Stock Exchange corporate governance rules applicable to U.S. companies is available on our website *http://www.cht.com.tw*. The information contained on our website is not a part of this annual report.

D. Employees

All of our employees are located in Taiwan and all are employed on a full-time basis. As of December 31, 2006, approximately 68.7% of our employees had university, graduate or post-graduate degrees. To improve our operational efficiency by reducing personnel costs, we offered a number of voluntary retirement programs between June 1, 2000 and April 30, 2006, which resulted in a reduction in our workforce of approximately 10,190 employees.

	2004	2005	2006
Employees			
Technical	15,367	14,710	15,086
Operations	11,293	10,920	9,245
Administrative	1,858	1,779	1,542
Total	28,518	27,409	25,873

As of December 31, 2006, approximately 99% of our employees were members of our principal labor union. Our collective agreement sets forth work rules, grievance procedures and provides for union participation in performance evaluations and promotion decisions. Our union members also occupy a majority of the seats on our employee welfare and pension fund committees. In addition, we will continue to maintain a good relationship with our labor union. We strive to have good communication with our employees and the labor union by inviting representatives of our labor union to attend various meetings related to the performance of our employees.

Commencing in 2005, in which our privatization was completed, prior to distributing any dividends to our shareholders, we were required to first distribute (1) not less than 1% of the distributable earnings to employees as bonuses and (2) not more than 0.2% of the distributable earnings to directors and supervisors as compensation. Pursuant to our articles of incorporation, as last amended at our 2006 annual general shareholders' meeting, prior to distributing any dividends to our shareholder, we must now distribute (1) between 2% and 5% of the distributable earnings to employees as bonuses and (2) not more than 0.2% of the distributable earnings to directors and supervisors as compensation. See "Item 10. Additional Information—B. Memorandum and Articles of Association—Dividends and Distributions."

Employee Stock Subscription Program

Under the Statue Governing Privatization of State-Owned Enterprises, a certain portion of our shares were required to be reserved for purchase by our employees at favorable terms, in accordance with regulations issued by the Ministry of Transportation and Communications and approved by the Executive Yuan in the process of privatization.

Under a program established pursuant to a regulation adopted by the Ministry of Transportation and Communications, our employees may subscribe for up to 476,858,252 of our common shares from the Ministry of Transportation and Communications in offerings conducted by the Ministry of Transportation and Communications prior to our privatization. As long as our employees agree not to transfer or pledge these shares for two or three years, they will be eligible to receive a discount of 10% or 20%, respectively, from the offering price. Pursuant to an amendment in June 2005 to the terms of this program, a majority of our employees who continued their employment with us after our privatization will also be eligible to receive a 50% discount if they agree not to transfer or pledge the shares for four years.

At the time we were privatized, the Ministry of Transportation and Communications implemented another stock subscription program, allocating up to 476,858,252 common shares, or 4.9% of our then outstanding common shares, for a one-time subscription by our employees. Under this program, a majority of our employees will be eligible to receive a discount of 10%, 20% or 50% from the offering price of the shares if they agree not to transfer or pledge these shares for two, three or four years, respectively.

As of the date of this annual report, 762,886,886 of our common shares, representing 7.89% of our outstanding common shares, were sold under the two programs mentioned above.

In addition, the Ministry of Transportation and Communications has sold 47,126,272 of our common shares to our employees at par value, representing 0.49% of our outstanding shares.

Under the Statute of Chunghwa Telecom Co., Ltd. and our articles of incorporation, whenever we issue new shares for cash, we must reserve up to 10% of the new shares to be issued on a favorable term for subscription by our employees.

E. Share Ownership

As of December 31, 2006, our directors, supervisors and executive officers personally held an aggregate 912,679 of our common shares, representing less than 0.01% of our outstanding common shares. As of the same date, we do not have any outstanding or unexercised options.


The sheer delight of bountiful harvests.

ITEM 7. MAJOR SHAREHOLDERS AND RELATED PARTY TRANSACTIONS

A. Major Shareholders

The following table sets forth information known to us with respect to the beneficial ownership of our shares (i) as of April 1, 2007, the most recent practicable date and (ii) as of certain record dates in each of the preceding three years, for the shareholders known by us to own at least 5.0% of our outstanding common shares. Beneficial ownership is determined in accordance with Securities and Exchange Commission's rules.

	As of July 9, 2004		As of April 20, 2005		As of April 1, 2006		As of April 1, 2007	
Name	**Number**	**Percent**	**Number**	**Percent**	**Number**	**Percent**	**Number**	**Percent**
The Republic of China government(1)	6,444,356,056	66.80	6,298,539,234	65.29	4,034,057,591	41.37	3,473,946,787	35.93
The Ministry of Transportation and Communications	6,265,072,056	64.94	6,256,292,234	64.85	3,991,572,591	41.37	3,423,082,447	35.41

(1) Includes shares held through the Ministry of Transportation and Communications and other government-controlled entities

The Ministry of Transportation and Communications owned 6,259,973,541, or 64.89%, 4,001,984,546, or 41.48% and 3,430,403,286, or 35.48% of our outstanding common shares as of December 31, 2004, 2005 and 2006, respectively. Under our articles of incorporation, the Ministry of Transportation and Communications has the right to subscribe for two preferred shares when the government's ownership of our outstanding common shares falls below 50%, and the Ministry of Transportation and Communications exercised such right on April 4, 2006. Under our articles of incorporation, the holder of preferred shares is entitled to certain rights, including 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.

B. Related Party Transactions

Related Party Transactions Policies

We have not extended any loans or credit to any of our directors, supervisors or executive officers, and we have not provided guarantees for borrowings by any of these persons. We have not entered into any fee-paying contract with any of these persons for them to provide services not within his or her capacity as a director, supervisor or executive officer of our company, except that three of our directors who are also our employees receive salaries from our company in their capacity as our employees.

We currently own 40% of Taiwan International Standard Electronics, 49% of Chunghwa Investment Co., Ltd. and 30% of Spring House Entertainment Inc. We have purchased telecommunications exchange facilities and related supplies and replacement parts from Taiwan International Standard Electronics for approximately NT$0.9 billion in 2004, NT$0.5 billion in 2005 and NT$0.9 billion (US$28 million) in 2006. We acquired from Chunghwa System Integration, a subsidiary of Chunghwa Investment Co., Ltd., network equipment and related supplies for approximately NT$0.2 billion in 2004, NT$0.3 billion in 2005 and NT$0.3 billion (US$9 million) in 2006. We believe that these transactions with Taiwan International Standard Electronics and Chunghwa System Integration have been conducted on arm's length terms.

In 2005, our subsidiary Chief Telecom Inc. agreed to provide compensation to its board member Tai Zhong He for providing assets that were pledged as collateral in connection with a financing arrangement during the period from 2002 to 2005. The total compensation payable to Tai Zhong He for this pledge was NT$20 million. The amount was based on the number of days that the pledged assets were used by Chief Telecom Inc. as collateral and was calculated at an interest rate below 5%.

On January 15, 2007, we purchased a 31.5% stake, or 70,373,000 shares, of Senao International Co., Ltd, or Senao, a distributor of cellular handsets in Taiwan. On April 1, 2007, we entered into an agreement with Senao making Senao the exclusive distributor of cellular handsets to our retail outlets. Under the terms of the agreement, Senao will also provide cellular handset sales services in our retail outlets and exclusively sell our SIM cards in Senao's own retail stores.

C. Interests of Experts and Counsel

Not applicable.

ITEM 8. FINANCIAL INFORMATION

A. Consolidated Statements and Other Financial Information

See Item 18 for a list of all consolidated financial statements filed as part of this annual report on Form 20-F.

Except as described in "Item 4. Information on the Company—B. Business Overview—Legal Proceedings," we are not currently involved in material litigation or other proceedings that may have or have had in the recent past, significant effects on our financial position or profitability.

For our policy on dividend distributions, see "Item 10. Additional Information—B. Memorandum and Articles of Association—Dividends and Distributions." The following table sets forth the dividends declared on each of our common shares and in the aggregate for each of the fiscal years ended June 30, 1998 and 1999, for the 18 months ended December 31, 2000, and the years ended December 31, 2001, 2002, 2003, 2004, 2005 and 2006. All of these dividends were paid, in the fiscal year following the period with respect to which the dividends relate, to the Republic of China government and, in the case of our dividend distribution for the 18 months ended December 31, 2000, the years ended December 31, 2001, 2002, 2003, 2004, 2005 and 2006, also to our public shareholders.

	Dividends per common share[(1)]	Total dividends[(1)]
		(in billions)
Fiscal year ended June 30, 1998	NT$ 4.99	NT$ 48.1
Fiscal year ended June 30, 1999	4.76	45.9
18 months ended December 31, 2000	5.80	56.0
Year ended December 31, 2001	3.50	33.8
Year ended December 31, 2002	4.00	38.6
Year ended December 31, 2003	4.50	43.4
Year ended December 31, 2004	4.70	45.3
Year ended December 31, 2005	4.50[(2)]	42.6[(2)]
Year ended December 31, 2006	—[(3)]	—[(3)]

(1) Cash dividend unless otherwise indicated.
(2) Includes stock dividends of NT$0.20 per common share (equivalent to 20 shares for every 1,000 shares held) representing total stock dividends of NT$1.9 billion.
(3) Dividends for 2006 are expected to be declared at our annual general shareholders' meeting scheduled for June 2007.

We have historically distributed cash dividends to our shareholders equal to approximately 90% of our annual net income. We intend to maintain this dividend payout ratio in the future, subject to a number of commercial factors, including the interests of our shareholders, cash requirements for future capital expenditures and investments, as well as relevant industry and market practice. Prior to our privatization, the amount of our net income was determined for these purposes in accordance with Chunghwa Telecom Internal Accounting Principles, which took into account ROC GAAP and relevant laws and regulations and government guidelines applicable to state-owned enterprises. Our net income after our privatization is determined in accordance with ROC GAAP and relevant laws and regulations, but not subject to the government guidelines applicable to state-owned enterprises. The amount of our net income determined for purposes of calculating our annual dividend payout may differ from the amount of our net income determined in accordance with US GAAP.

B. Significant Changes

Other than as disclosed elsewhere in this annual report, we have not experienced any significant changes since the date of the annual consolidated financial statements included in this annual report.

ITEM 9. THE OFFER AND LISTING

A. Offer and Listing Details

Market Price Information for Our Common Shares

Our common shares have been listed on the Taiwan Stock Exchange since October 27, 2000. There is no public market outside Taiwan for our common shares. The table below shows, for the periods indicated, the high and low closing prices and the average daily volume of trading activity on the Taiwan Stock Exchange for our common shares. The closing price for our common shares on the Taiwan Stock Exchange on April 20, 2007 was NT$64.0 per share.

	Closing price per common share		Average daily trading volume
	High	Low	
	(NT$)	(NT$)	(in thousands)
2000 (from October 27)	100.50	75.00	8,393
2001	84.00	39.60	3,382
2002	55.00	43.20	2,398
2003	58.00	46.00	5,568
2004	64.00	49.40	8,995
2005	66.00	56.10	9,358
First Quarter	65.50	62.50	9,385
Second Quarter	65.30	59.00	8,052
Third Quarter	66.00	56.50	12,058
Fourth Quarter	58.10	56.10	7,962
2006	62.00	53.70	9,348
First Quarter	61.30	55.10	11,351
Second Quarter	62.00	58.50	7,825
Third Quarter	61.00	53.70	9,418
Fourth Quarter	60.60	54.70	8,929
October	58.00	54.70	7,427
November	59.40	56.90	11,035
December	60.60	59.20	8,154
2007			
First Quarter	64.20	59.60	9,357
January	63.20	59.60	7,901
February	64.20	62.10	9,715
March	64.10	60.80	10,455
Second Quarter (through April 20)	65.2	63.4	6,283
April (through April 20)	65.2	63.4	6,283

Market Price Information for Our American Depositary Shares

Our ADSs have been listed on the New York Stock Exchange under the symbol "CHT" since July 17, 2003. The outstanding ADSs are identified by the CUSIP number 17133Q205. The table below shows, for the periods indicated, the high and low closing prices and the average daily volume of trading activity on the New York Stock Exchange for our ADSs. The closing price for our ADSs on the New York Stock Exchange on April 20, 2007 was US$20.27 per ADS. Each of our ADSs represents the right to receive ten shares.

	Closing Price Per ADS		Average ADS Daily Trading Volume
	High	Low	
	US$	US$	(in thousands)
2003 (from July 23)	16.10	13.38	680
2004	21.09	14.93	326
First Quarter	17.85	14.93	431
Second Quarter	18.09	15.85	417
Third Quarter	17.73	15.73	206
Fourth Quarter	21.09	17.85	261
2005	22.17	16.88	942
First Quarter	23.04	20.30	400
Second Quarter	21.54	19.57	306
Third Quarter	22.12	17.50	1,756
Fourth Quarter	18.46	16.95	1,286
2006	22.65	16.75	1,214
First Quarter	19.98	17.79	1,138
Second Quarter	22.65	18.38	966
Third Quarter	18.90	16.75	1,381
Fourth Quarter	20.00	17.34	1,371
October	18.44	17.34	1,695
November	20.00	18.25	1,355
December	19.96	18.98	1,032
2007	20.84	19.06	918
First Quarter	20.84	19.06	882
January	20.71	19.39	924
February	20.84	19.06	966
March	20.53	19.09	771
Second Quarter (through April 20)	20.38	19.30	1,079
April (through April 20)	20.38	19.30	1,079

As of April 15, 2007, a total of 307,398,771 ADSs and 9,667,845,093 of our common shares were outstanding. With certain limited exceptions, holders of shares that are not Republic of China persons are required to hold these shares through a brokerage or custodial account in the Republic of China. As of April 15, 2007, 3,073,988,523 shares were registered in the name of a nominee of The Bank of New York, the depositary under the deposit agreement.

B. Plan of Distribution

Not applicable.

C. Markets

The principal trading market for our common shares is the Taiwan Stock Exchange and the principal trading market for our ADSs is the New York Stock Exchange.

D. Selling Shareholders

Not applicable.

E. Dilution

Not applicable.

F. Expenses of the Issue

Not applicable.

ITEM 10. ADDITIONAL INFORMATION

A. Share Capital

Not applicable.

B. Memorandum and Articles of Association

Set forth below is information relating to our capital structure, including brief summaries of material provisions of our articles of incorporation, the Republic of China Securities and Exchange Law, the Republic of China Company Law, the Statute of Chunghwa Telecom Co., Ltd. and the Telecommunications Act, all as currently in effect. The following summaries are qualified in their entirety by reference to our articles of incorporation, the Republic of China Securities and Exchange Law, the Republic of China Company Law, the Statute of Chunghwa Telecom Co., Ltd. and the Telecommunications Act.

Objects and Purpose

The scope of business of Chunghwa Telecom Co., Ltd. as set forth in Article 2 of our articles of incorporation, includes (i) Telecommunications Enterprise Type 1 and Type 2 businesses pursuant to the Telecommunications Act of the Republic of China, (ii) installation of the computer equipment and radio-frequency equipment whose operation is controlled by the telecommunication business, (iii) telecommunications equipment wholesale, retail and engineering businesses, (iv) design, engineering and operation of information software and hardware service businesses and (v) other businesses, except any business requiring a special permit or otherwise restricted by law or regulation.

General

Under our articles of incorporation as last amended on May 30, 2006, our authorized capital was increased to NT$120,000,000,020, divided into 12,000,000,000 common shares and two preferred shares, with par value of NT$10 per share. Our paid-in capital is NT$96,678,450,950, divided into 9,667,845,093 common shares and two non-transferable preferred shares. Since the preferred shares must be redeemed by the company in 2009, the shares are classified as other long-term liabilities. The redemption value of the preferred shares is NT$20. The Ministry of Transportation and Communications has the right to subscribe for two preferred shares in the event the government owns less than 50% of our common shares. On April 4, 2006, we issued two preferred shares to the Ministry of Transportation and Communications. We currently do not have any other equity in the form of convertible bonds or otherwise outstanding as of the date of this annual report.

The Ministry of Transportation and Communications, on behalf of the government of the Republic of China, owned approximately 35.41% of our outstanding common shares as of March 31, 2007. The remainder of our outstanding shares is held by public shareholders and other investors.

Directors

Under Republic of China Company Law, our board of directors, in conducting our business, shall act in accordance with laws and regulations, our articles of incorporation and the resolutions adopted at the meetings of shareholders. Where any resolution adopted by our board of directors contravenes laws, our articles of incorporation and the resolutions adopted at the meetings of shareholders, thereby causing loss or damage to us, all directors taking part in the adoption of such resolution shall be liable to compensate us for such loss or damage; however, those directors whose disagreement appears on record or is expressed in writing shall be exempted from liability.

If our board of directors decides, by resolution, to commit any act in violation of any law or our articles of incorporation, a supervisor or any shareholder who has continuously held our shares for a period of one year or longer may request our board of directors to discontinue such act. One or more shareholders who have held more than 3% of our issued and outstanding shares for over a year may require a supervisor to bring an action on our behalf against a director for losses suffered by us as a result of the director's unlawful actions or failure to act by sending a written request to a supervisor. In addition, if our shareholders' meeting resolves to institute an action against a director, we shall, within 30 days from the date of such resolution, institute such an action. In the case of a lawsuit between us and a director, a supervisor shall act on our behalf, unless otherwise provided by law; and our shareholders meeting may also appoint some other person to act on our behalf in a lawsuit.

In addition, our board of directors owes fiduciary duty to us. Our directors are liable to compensate us if they breach their fiduciary duty.

According to the Republic of China Company Law, a director who has a personal interest in a matter to be discussed at the meeting of the board of directors, the outcome of which may conflict with his interests, shall abstain from voting on such matter. Our articles of incorporation also provide that commencing in the fiscal year in which our privatization is completed, we may make compensation to all directors and supervisors and such compensation shall not exceed 0.2% of our distributable earnings and may be approved only by a validly convened shareholders' meeting. Our articles of incorporation do not impose a mandatory retirement age for our directors. Furthermore, our articles of incorporation do not impose a shareholding qualification for each director. According to our current internal Loan Procedures, we may not extend any loan to our directors or our supervisors.

Preferred Shares

Under our articles of incorporation, the holder of preferred shares is entitled to the same rights as holders of common shares with respect to receiving distributions of dividends and bonuses, remaining assets available for distribution upon our dissolution, liquidation or winding up, distribution of retained earnings or capital reserve, or capital allocation.

In addition, the holder of preferred shares will be entitled to the same voting rights as holders of common shares at any of our meetings of holders of common shares.

The holder of preferred shares, or its nominated representative, will act as our director and supervisor during the existing period of the preferred shares. Any such representative is subject to removal and replacement by the holder of the preferred shares from time to time.

When we issue new shares for cash, the holder of preferred shares will be entitled to the same pre-emptive rights as holders of common shares.

Without the prior consent of the holder of preferred shares, we may not:

- change our corporate name;
- change our business; or
- transfer the whole or the main portion of our business or property.

The holder of preferred shares may not transfer its preferred shares. We must redeem all outstanding preferred shares at par value three years from the date of their issuance. We are required to cancel these preferred shares immediately after their redemption.

Dividends and Distributions

At each annual general shareholders' meeting, our board of directors submits to the shareholders for their approval any proposal for the distribution of dividend or the making of any other distribution to shareholders from our net income for the preceding fiscal year. All common shares outstanding and fully paid as of the relevant record date are entitled to share equally in any dividend or other distribution so approved. Dividends may be distributed in cash, in the form of common shares or a combination of the two, as determined by the shareholders at the meeting.

We are not permitted to distribute dividends or make other distributions to shareholders in any year in which we do not have any net income or retained earnings (excluding reserves). The Republic of China Company Law also requires that 10% of our annual net income, less prior years' losses and outstanding tax, if any, be set aside as a legal reserve until the accumulated legal reserve equals our paid-in capital. We may also set aside special reserve as determined by our shareholders at a shareholders' meeting. In addition, our articles of incorporation provide that at least 50% of the remaining portion of the net income, less prior years' losses, outstanding taxes, the legal reserve and any special reserve, plus undistributed retained earnings from prior years will be distributed as dividends to shareholders. Under our articles of incorporation as last amended on May 30, 2006, not less than 50% of the total amount of the distributed dividends must be in cash, but if the cash dividends to be distributed are less than NT$0.10 per share, the dividends may be distributed in the form of shares. Commencing in 2005, in which our privatization was completed, prior to distributing any dividends to our shareholders, we were required to first distribute (1) not less than 1% of the distributable earnings to employees as bonuses and (2) not more than 0.2% of the distributable earnings to directors and supervisors as compensation. Pursuant to our articles of incorporation, as last amended at our 2006 annual general shareholders' meeting, prior to distributing any dividends to our shareholder, we must now distribute (1) between 2% and 5% of the distributable earnings to employees as bonuses and (2) not more than 0.2% of the distributable earnings to directors and supervisors as compensation. However, registration of the amended articles is still pending as the Ministry of Economic Affairs has requested that we make certain wording changes to one of the amendments relating to employee bonuses. We will revise the wording accordingly and submit the revised amendment to the shareholders at our next shareholders' meeting for approval. Distributions for the year in which the privatization is completed will be distributed out of the profits generated from the date of privatization to the end of that fiscal year. The above percentages may be adjusted, with our shareholders' approval, according to our actual profits, capital budget and funding conditions of that year.

However, registration of the amended articles is still pending as the Ministry of Economic Affairs has requested that we make certain wording changes to one of the amendments relating to employee bonuses. We will revise the wording accordingly and submit the revised amendment to the shareholders at our next shareholders' meeting for approval.

Under the Republic of China Audit Law, the earnings and losses of a state-owned enterprise are audited by the Ministry of Audit under the Control Yuan of the Republic of China. As a result, if the amount of our earnings or loses decided by the auditing authority is different from the amount approved at our shareholders' meeting, the latter amount shall be adjusted accordingly to be identical with the former amount, and the dividends and bonuses approved at our shareholders' meeting will be adjusted accordingly and reported to the shareholders at the next shareholders' meeting. However, following our privatization, we are no longer considered a state-owned enterprise for proposes of the Audit Law, and we are no longer subject to the Audit Law and audit by the Ministry of Audit.

Under our articles of incorporation, if we do not have current or retained earnings (excluding reserves) but our legal reserve exceeds 50% of our paid-in capital, we may use the excess amount to distribute dividends. In addition, under the Republic of China Company Law, if we do not incur a loss, we are also permitted to make distributions to our shareholders of additional common shares by capitalizing reserves (including the legal reserve, the premium derived from the issuance of new shares and the income from endowments received by us). However, amounts payable by capitalizing our legal reserve are limited to 50% of the total accumulated legal reserve and this capitalization can only be effected when the accumulated legal reserve exceeds 50% of our paid-in capital.

Changes in Share Capital

Under the Republic of China Company Law, any change in our authorized share capital requires an amendment to our articles of incorporation, which in turn requires approval at our shareholders' meeting. Authorized but unissued common shares may be issued, subject to applicable Republic of China law, upon terms as our board of directors may determine.

Preemptive Rights

Under the Republic of China Company Law and our articles of incorporation, when we issue new shares for cash, existing shareholders who are listed on the shareholders' register as of the record date have preemptive rights to subscribe for the new issue in proportion to their existing shareholdings. Under our articles of incorporation as last amended on May 30, 2006, the company's employees, whether or not they are our shareholders, have rights to subscribe for between 10 and 15% of any new issue. However, registration of our amended articles (including article relating to our employee preemptive rights) is still pending as the Ministry of Economic Affairs has requested that we make certain wording changes to the amendment. We will revise the wording accordingly and submit the revised amendment to the shareholders at our next shareholders' meeting for approval.

In addition, in accordance with the Republic of China Securities and Exchange Law, a public company that intends to offer new shares for cash must offer to the public at least 10% of the shares to be sold except in certain limited circumstances. This percentage can be increased by a resolution passed at a shareholders' meeting, held in accordance with the Company Law and our articles of incorporation which would diminish the number of new shares subject to the preemptive rights of existing shareholders.

Meetings of Shareholders

We are required by the Republic of China Company Law and our articles of incorporation to hold a general meeting of our shareholders within six months following the end of each fiscal year. These meetings are generally held in Taipei, Taiwan. Special shareholders' meetings may be convened by resolution of the board of directors or by the board of directors upon the written request of any shareholder or shareholders who have held 3% or more of the outstanding common shares for more than one year. Shareholders' meetings may also be convened by a supervisor. Notice in writing of general meetings of shareholders, stating the place, time and agenda must be dispatched to each shareholder at least 30 days, in the case of general meetings, and 15 days, in the case of special meetings, before the date set for each meeting. Except in certain circumstances described below, a majority of the holders of all issued and outstanding common shares present at a shareholders' meeting constitutes a quorum for meetings of shareholders. Shareholders of 1% or more our issued and outstanding shares are entitled to submit one written proposal each year for consideration at our annual general shareholders' meeting in accordance with the Republic of China Company Law.

Voting Rights

As previously required by the Republic of China Company Law, our articles of incorporation provide that a holder of common shares has one vote for each common share. Cumulative voting applies to the election of our directors and supervisors. Separate ballots may be held for the election of independent directors.

In general, a resolution can be adopted by the holders of at least a majority of the common shares represented at a shareholders' meeting at which the holders of a majority of all issued and outstanding common shares are present. Under the Republic of China Company Law, the approval by at least a majority of the common shares represented at a shareholders' meeting in which a quorum of at least two-thirds of all issued and outstanding common shares are represented is required for major corporate actions, including:

- amendment to our articles of incorporation;
- entering into, modification or termination of any contracts regarding leasing of all business, outsourcing of operations or joint operations;
- transfer of the whole or substantial part of our business or assets;
- taking over of the whole of the business or assets of any other company which would have significant impact on our operations;
- distribution of any share dividend;
- dissolution;
- merger or spin-off; and
- removing of directors or supervisors.

Alternatively, the Republic of China Company Law provides that in the case of a public company, such as us, a resolution may be adopted by the holders of at least two-thirds of the common shares represented at a meeting of shareholders at which holders of at least a majority of issued and outstanding common shares are present.

A shareholder may be represented at a general or special meeting by proxy if a valid proxy form is delivered to us five days before the commencement of the general or special shareholders' meeting. Except for trust enterprises or share registrar approved by the Securities and Futures Bureau, where one person is appointed as proxy by two or more shareholders who together hold more than 3% of the total issued common shares, the votes of those shareholders in excess of 3% of the outstanding common shares shall not be counted.

Any shareholder who has a personal interest in the matter under discussion at a shareholders' meeting, the outcome of which may impair our interests, shall not vote or exercise voting rights on behalf of another shareholder.

Holders of our ADSs generally will not be able to exercise voting rights on the common shares underlying ADSs on an individual basis.

Other Rights of Shareholders

Under the Republic of China Company Law, dissenting shareholders are entitled to appraisal rights in certain major corporate actions, such as a planned transfer of the whole or part of the business or a proposed merger by the company. A dissenting shareholder may request the company to purchase back all of the shares owned by the shareholder at a fair price determined by mutual agreement or determined by the court if a mutual agreement cannot be reached. Shareholders may exercise their appraisal rights by serving notice in writing to the company prior to the related shareholders' meeting and/or by raising his objection at the shareholders' meeting. Moreover, a shareholder has the right to file a petition in the court for annulment of any resolution adopted at a shareholders' meeting where the procedures for convening the shareholders' meeting or the method of adopting the resolutions at the meeting is contrary to law or our Articles of Incorporation. One or more shareholders who have held more than 3% of the issued and outstanding shares of a company continuously for more than one year may require a supervisor to institute, on behalf of the company, an action against a director. In addition, one or more shareholders who has/have continuously held 3% or more of the total number of the outstanding shares of our company for more than one year may require the board of directors to convene a special shareholders' meeting by sending a written request to the board of directors.

The Republic of China Company Law has been recently amended to allow shareholders holding 1% or more of the total issued shares of a company to submit, during the period of time prescribed by the company, one proposal in writing for discussion at the general meeting of shareholders. The amendment also provided that a company may adopt a nomination procedure for election of directors or supervisors. We have adopted a nomination procedure for election of independent directors as stipulated in our articles of incorporation which provides that shareholders holding 1% or more of our total issued shares may submit to us a list of candidates for independent director, along with relevant information and supporting documents.

Register of Shareholders and Record Dates

Our share registrar, Taiwan Securities Co., Ltd., maintains our register of shareholders at its offices in Taipei, Taiwan, and enters transfers of common shares in our register upon presentation of, among other documents, certificates representing the common shares transferred. Under the Republic of China Company Law and our articles of incorporation, we may, by giving advance public notice, set a record date and close the register of shareholders for a specified period in order for us to determine the shareholders or pledgees that are entitled to rights pertaining to the common shares. The specified period required is as follows:

- general shareholders' meeting—60 days;
- special shareholders' meeting—30 days; and
- relevant record date—five days.

Annual Consolidated Financial Statements

At least ten days before the annual general shareholders' meeting, our annual consolidated financial statements must be available at our principal office in Taipei, Taiwan for inspection by the shareholders.

Transfer of Common Shares

The transfer of common shares in registered form is effected by endorsement and delivery of the related share certificates but, in order to assert shareholders' rights against us, the transferee must have his name and address registered on our register of shareholders. Shareholders are required to file their respective specimen seals, also known as chops, with us. Chops are official stamps widely used in Taiwan by individuals and other entities to authenticate the execution of official and commercial documents.

Acquisition of Our Own Common Shares

Under the Republic of China Company Law, with minor exceptions, we cannot acquire our own common shares. Any common shares acquired by us, under certain of such minor exceptions, must be sold at the market price within six months after their acquisition.

In addition, under the Republic of China Securities and Exchange Law, a company whose shares are listed on the Taiwan Stock Exchange or traded on the GreTai Securities Market may, pursuant to a board resolution adopted by a majority consent at a meeting attended by more than two-thirds of the directors and pursuant to the procedures prescribed by the Securities and Futures Bureau, purchase its shares for the following purposes on the Taiwan Stock Exchange, the GreTai Securities Market or by a tender offer:

- for transfers of shares to its employees;
- for conversion into shares from bonds with warrants, preferred shares with warrants, convertible bonds, convertible preferred shares or certificates of warrants issued by the company; and
- for maintaining its credit and its shareholders' equity, provided that the shares so purchased shall be cancelled thereafter.

The total shares purchased by the company shall not exceed 10% of its total issued and outstanding shares. In addition, the total amount for purchase of the shares shall not exceed the aggregate amount of the retained earnings, the premium from shares issues and the realized portion of the capital reserve.

The shares purchased by the company pursuant to items (1) and (2) above shall be transferred to the intended transferees within three years after the purchase, otherwise the same shall be cancelled. For the shares to be cancelled pursuant to item (3) above, the company shall complete amendment registration for such cancellation within six months after the purchase.

The shares purchased by the company shall not be pledged or hypothecated. In addition, the company may not exercise any shareholders' rights attaching to these shares. The company's affiliates (as defined in Article 369-1 of the Republic of China Company Law), directors, supervisors, managers and their respective spouses and minor children and/or nominees are prohibited from selling the shares of the company held by them during the purchase period of such shares reported by the company to the Securities and Futures Bureau.

Liquidation Rights

In the event of our liquidation, the assets remaining after payment of all debts, liquidation expenses and taxes will be distributed pro rata to the shareholders in accordance with the relevant provisions of the Republic of China Company Law and our articles of incorporation.

Substantial Shareholders and Transfer Restrictions

The Republic of China Securities and Exchange Law currently requires (1) each director, supervisor, manager, as well as their respective spouses, minor children and nominees, and substantial shareholder (i.e., a shareholder who together with his or her spouse, minor children or nominees, holds more than 10% of the shares of a public company) to report any change in that person's shareholding to the issuer of the shares on a monthly basis and (2) each director, supervisor, manager or substantial shareholder holding such common shares for more than a six month period to report his or her intent to transfer any shares listed on the Taiwan Stock Exchange or traded on the GreTai Securities Market to the Securities and Futures Bureau at least three days before the intended transfer, unless the number of shares to be transferred is less than 10,000 shares. ADS holders holding more than 10% of our common shares, including common shares represented by ADSs, may be subject to the reporting obligation in above item (1).

In addition, the number of shares that can be sold or transferred on the Taiwan Stock Exchange or GreTai Securities Market by any person subject to the restrictions described above on any given day may not exceed:

- 0.2% of the outstanding shares of the company in the case of a company with no more than 30 million outstanding shares;
- 0.2% of 30 million shares plus 0.1% of the outstanding shares exceeding 30 million shares in the case of a company with more than 30 million outstanding shares; or
- in any case, 5% of the average daily trading volume (number of shares) on the Taiwan Stock Exchange or the GreTai Securities Market for the ten consecutive trading days preceding the reporting day on which day the director, supervisor, manager or substantial shareholder or their respective spouse, minor child or nominee reports the intended share transfer to the Securities and Futures Bureau.

These restrictions do not apply to block trading, auction sale, purchase by auction, after-hour trading and sales or transfers of our ADSs. However, these restrictions will apply to sales of common shares upon withdrawal.

C. Material Contracts

We have not entered into any material contracts other than in the ordinary course of business and other than those described elsewhere in this annual report.

D. Exchange Controls

Foreign Investment and Exchange Controls in Taiwan

We have extracted from publicly available documents the information presented in this section. Please note that citizens of the People's Republic of China and entities organized in the People's Republic of China are subject to special Republic of China laws, rules and regulations, which are not discussed in this section.

General

Historically, foreign investments in the securities market of Taiwan were restricted. However, commencing in 1983, the Taiwan government has from time to time enacted legislation and adopted regulations to make foreign investment in the Taiwan securities market possible. Initially, only overseas investment trust funds of authorized securities investment trust enterprises established in Taiwan were permitted to invest in the Taiwan securities market. Since January 1, 1991, qualified foreign institutional investors are allowed to make investments in the Taiwan listed securities market. Since March 1, 1996, overseas Chinese, non-resident foreign institutional and individual investors (other than qualified foreign institutional investors), called "general foreign investors," are permitted to make direct investments in the Taiwan securities market.

Foreign Investment in Taiwan Securities Market

On December 28, 1990, the Executive Yuan, the cabinet of the Republic of China government, approved guidelines drafted by the Securities and Futures Commission (the predecessor of the Securities and Futures Bureau), which, since January 1, 1991, has allowed direct foreign investment in Taiwan's securities that are listed on the Taiwan Stock Exchange or other Taiwan securities approved by the Securities and Futures Bureau by certain eligible qualified foreign institutional investors.

In addition to qualified foreign institutional investors, certain individual and foreign institutional investors which meet certain qualifications set by the Securities and Futures Bureau may invest in the shares of Taiwan Stock Exchange-listed companies, GreTai Securities Market (formerly known as Over-The-Counter Securities Exchange) traded companies, emerging market companies or other Taiwan securities approved by the Securities and Futures Bureau up to a limit of US$50 million (in the case of institutional investors) and US$5 million (in the case of individual investors) after obtaining permission from the Taiwan Stock Exchange.

On September 30, 2003 and June 15, 2004, the Securities and Futures Bureau issued amendments to the "Guideline Governing Investment in Securities by Overseas Chinese and Foreign Nationals" and relevant regulations, in which the Securities and Futures Bureau lifted certain restrictions and simplified the procedures required for foreign investments in Taiwan's securities market. The amendment focuses mainly on the following aspects:

- The concept of "qualified foreign institutional investors" no longer exists. Foreign investors are reclassified as "off-shore foreign institutional investors", "on-shore foreign institutional investors", "off-shore general foreign investors", and "on-shore general foreign investors" based on whether they are institutions or natural persons, and whether they have presence in Taiwan.
- For foreign investors to invest in Taiwan's securities market, registration with the Taiwan Stock Exchange, instead of the approval of the Securities and Futures Bureau, is required. The Taiwan Stock Exchange may withdraw or rescind the registration if the application documents submitted by foreign investors are untrue or incomplete, or if any material violation of the relevant regulations exists.
- Off-shore foreign investors may provide the securities they hold as the underlying shares of depositary receipts and act as selling shareholders in depositary receipts offerings.
- Off-shore foreign institutional investors are required to appoint their agent or nominee to attend the shareholders' meeting of the invested company.

Currently, subject to the specific restriction imposed by relevant regulations, the off-shore foreign institutional investors may invest in the Taiwan securities market without any amount restriction. However, a ceiling will be separately determined by the Securities and Futures Bureau after consultation with the Central Bank of the Republic of China (Taiwan) for investment by offshore oversea Chinese and foreign individual investors.

Foreign Investment Approval

Other than:

- foreign institutional investors;
- foreign individual investors; and
- investors in overseas convertible bonds and depositary receipts,

foreign investors who wish to make direct investments in the shares of Taiwan companies may submit a "foreign investment approval" application to the Investment Commission of the Ministry of Economic Affairs of Taiwan or other government authority to qualify for benefits granted under the Statute for Investment by Foreign Nationals. The Investment Commission or other government authority reviews each foreign investment approval application and approves or disapproves the application after consultation with other governmental agencies. Any non-Taiwan person possessing a foreign investment approval may remit capital for the approved investment and repatriate annual net profits and interests and cash dividends attributable to an approved investment. Stock dividends, investment capital and capital gains attributable to the investment may be repatriated with approval of the Investment Commission or other government authority.

In addition to the general restrictions against direct investment by non-Taiwan persons in Taiwan companies, non-Taiwan persons are currently prohibited from investing in prohibited industries in Taiwan under the Negative List promulgated by the Executive Yuan from time to time. The prohibition on direct foreign investment in the prohibited industries in the Negative List is absolute with the consequence of certain specific exemption from the application of the Negative List. Under the Negative List, some other industries are restricted so that non-Taiwan persons may directly invest only up to a specified level and with the specific approval of the relevant authority which is responsible for enforcing the legislation which the negative list is intended to implement. The telecommunication industry is a restricted industry under the Negative List.

Depositary Receipts

In April 1992, the Securities and Futures Bureau began allowing Taiwan companies listed on the Taiwan Stock Exchange, with the prior approval of the Securities and Futures Bureau, to sponsor the issuance and sale of depositary receipts evidencing depositary shares. In December 1994, the Republic of China Ministry of Finance began allowing companies whose shares are traded on the GreTai Securities Market also to sponsor the issuance and sale of depositary receipts evidencing depositary shares representing shares of its capital stock. Approvals for these issuances are still required.

After the issuance of a depositary share, a holder of the depositary receipt evidencing the depositary shares may request the depositary issuing the depositary share to cause the underlying shares to be sold in Taiwan and to distribute the proceeds of the sale to or to withdraw the shares and deliver the shares to the depositary receipt holder. A citizen of the People's Republic of China is not permitted to withdraw and hold our shares.

If you are an offshore foreign institutional investor holding the depositary receipts, you must register with the Taiwan Stock Exchange as a foreign investor before you will be permitted to withdraw the shares represented by the depositary receipts. In addition to obtaining registration with the Taiwan Stock Exchange, you must also (1) appoint a qualified local agent 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, (2) appoint a custodian bank to hold the securities and cash proceeds, confirm transactions, settle trades and report and declare other relevant information and; (3) appoint a tax guarantor as guarantor for the full compliance of the withdrawing depositary receipt holders' tax filing and payment obligations in the Republic of China. A depositary receipt holder not registered as a foreign investor with the Taiwan Stock Exchange, or not have made the necessary appointments as outlined above, will be unable to hold or subsequently transfer the shares withdrawn from the depositary receipt facility.

No deposits of shares may be made in a depositary receipt facility and no depositary shares may be issued against deposits without specific Securities and Futures Bureau approval, unless they are:

(1) stock dividends;

(2) free distributions of shares;

(3) due to the exercise by the depositary receipt holder preemptive rights in the event of capital increases for cash; or

(4) if permitted under the deposit agreement and custody agreement and within the amount of depositary receipts which have been withdrawn, due to the direct purchase by investors or purchase through the depositary on the Taiwan Stock Exchange or the GreTai Securities Market or delivery by investors of the shares for deposit in the depositary receipt facility. In this event, the total number of depositary receipts outstanding after an issuance cannot exceed the number of issued depositary receipts previously approved by the Securities and Futures Bureau in connection with the offering plus any ADSs issued pursuant to the events described in (1), (2) and (3) above.

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.

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 payment for rights offerings. The depositary may be required to obtain foreign exchange payment 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.

Exchange Controls

Taiwan's Foreign Exchange Control Statute and regulations provide that all foreign exchange transactions must be executed by banks designated to handle foreign exchange transactions by the Financial Supervisory Commission and by the Central Bank of the Republic of China (Taiwan). Current regulations favor trade-related foreign exchange transactions. Consequently, foreign currency earned from exports of merchandise and services may now be retained and used freely by exporters. All foreign currency needed for the importation of merchandise and services may be purchased freely from the designated foreign exchange banks.

Aside from trade-related foreign exchange transactions, Taiwan companies and residents may remit to and from Taiwan foreign currencies of up to US$50 million (or its equivalent) and US$5 million, (or its equivalent), respectively, in each calendar year. These limits apply to remittances involving a conversion between New Taiwan dollars and U.S. dollars or other foreign currencies. A requirement is also imposed on all private enterprises to register all medium and long-term foreign debt with the Central Bank of the Republic of China (Taiwan).

In addition, a foreign person without an alien resident card or an unrecognized foreign entity may remit to and from Taiwan foreign currencies of up to US$100,000 per remittance if required documentation is provided to Taiwan authorities. This limit applies only to remittances involving a conversion between New Taiwan dollars and U.S. dollars or other foreign currencies.

E. Taxation

Republic of China Taxation

The discussion below describes the principal Republic of China tax consequences of the ownership and disposition of ADSs representing common shares and of common shares. It applies to you only if you are:

- an individual who is not a citizen of the Republic of China, who owns ADSs or common shares and who is not physically present in Taiwan for 183 days or more during any calendar year; or
- a corporation or a non-corporate body that is organized under the laws of a jurisdiction other than the Republic of China for profit-making purposes and has no fixed place of business or other permanent establishment in Taiwan.

You should also consult your tax advisors concerning the tax consequences of owning ADSs and common shares in the Republic of China and any other relevant taxing jurisdiction to which they are subject.

Dividends

Dividends declared by us out of our retained earnings and distributed to you are subject to Republic of China withholding tax, currently at the rate of 20%, on the amount of the distribution in the case of cash dividends or on the par value of the common shares in the case of stock dividends. However, a 10% Republic of China retained earnings tax paid by us on our undistributed after-tax earnings, if any, would provide a credit of up to 10% of the gross amount of any dividends declared out of such earnings that would reduce the 20% Republic of China tax imposed on these distributions.

Share dividends paid by us out of our capital reserves which are derived from the issuance of shares at a premium are not subject to Republic of China withholding tax.

Capital Gains

Gains from the sale of property in the Republic of China are generally subject to Republic of China income tax. However, under current Republic of China law, capital gains on securities transactions (including sale of common stock) are exempt from income tax.

Sales of ADSs by you are regarded as transactions relating to property located outside the Republic of China and thus any gains derived therefrom are currently not subject to Republic of China income tax.

Preemptive Rights

Distributions of statutory preemptive rights for common shares in compliance with Republic of China law are not subject to any Republic of China tax. Proceeds derived from sales of statutory preemptive rights evidenced by securities are exempted from income tax but are subject to securities transaction tax at the rate of 0.3% of the gross amount received. Proceeds derived from sales of statutory preemptive rights which are not evidenced by securities are subject to capital gains tax at the rate of:

- 35% of the gains realized if you are a natural person; or
- 25% of the gains realized if you are an entity that is not a natural person.

Subject to compliance with Republic of China law, we, at our sole discretion, can determine whether statutory preemptive rights shall be evidenced by issuance of securities.

Securities Transaction Tax

A securities transaction tax, at the rate of 0.3% of the gross amount received, payable by the seller will be withheld upon a sale of common shares in Taiwan. Transfers of ADSs are not subject to Republic of China securities transaction tax. According to a letter issued by the Ministry of Finance of the Republic of China in 1996, withdrawal of common shares from the deposit facility will not be subject to Republic of China securities transaction tax.

Estate Taxation and Gift Tax

Republic of China estate tax is payable on any property within Taiwan of a deceased person who is a non-resident individual, and Republic of China gift tax is payable on any property within Taiwan donated by any such person. According to the tax ruling dated December 27, 2006, from January 1, 2007, estate tax is payable at rates ranging from 2% of the first NT$670,000 to 50% of amounts over NT$111,132,000, and gift tax is payable at rates ranging from 4% of the first NT$670,000 to 50% of amounts over NT$50,090,000. Under Republic of China estate and gift tax laws, common shares issued by Taiwan companies are deemed located in Taiwan regardless of the location of the owner. It is not clear whether the ADSs will be regarded as property located in Taiwan under Republic of China estate and gift tax laws.

Tax Treaty

The Republic of China does not have an income tax treaty with the United States. On the other hand, the Republic of China has income tax treaties with Indonesia, Singapore, South Africa, Australia, Vietnam, New Zealand, Malaysia, Macedonia, Swaziland, the Netherlands, United Kingdom, Gambia, Senegal, Sweden, Belgium and Denmark, which may limit the rate of Republic of China withholding tax on dividends paid with respect to common shares in Taiwan companies. It is unclear whether if you hold ADSs, you will be considered to hold common shares for the purposes of these treaties. Accordingly, if you may otherwise be entitled to the benefits of the relevant income tax treaty, you should consult your tax advisors concerning your eligibility for the benefits with respect to the ADSs.

Retained Earnings Tax

Under the Republic of China Income Tax Laws, a 10% retained earnings tax will be imposed on a company for its after-tax earnings generated after January 1, 1998 which are not distributed in the following year. The retained earnings tax so paid will further reduce the retained earnings available for future distribution. When the company declares dividends out of those retained earnings, up to a maximum amount of 10% of the declared dividends will be credited against the 20% withholding tax imposed on the non-resident holders of its shares.

U.S. Federal Income Tax Considerations For U.S. Persons

The following is a summary of the material U.S. federal income tax consequences of the ownership and disposition of our shares and ADSs. The discussion set forth below is applicable to beneficial owners of our shares or ADSs that hold the shares or ADSs as capital assets and that are U.S. holders and non-residents of the Republic of China. You are a U.S. holder if you are:

- an individual who is a citizen or resident of the United States;
- a corporation or other entity taxable as a corporation for U.S. federal income tax purposes created or organized in or under the laws of the United States, any state thereof or the District of Columbia;
- an estate the income of which is subject to U.S. federal income taxation regardless of its source;
- a trust that is subject to the primary supervision of a court within the United States and the control of one or more U.S. persons; or
- a trust that has a valid election in effect under applicable U.S. Treasury regulations to be treated as a U.S. person.