



This summary is based on the provisions of the Internal Revenue Code of 1986, as amended (the “Code”), and regulations, rulings and judicial decisions thereunder as of the date hereof, and such authorities may be replaced, revoked or modified so as to result in U.S. federal income tax consequences different from those discussed below. It is for general purposes only and you should not consider it to be tax advice. In addition, it is also based in part on representations made by the depositary and assumes that each obligation under the deposit agreement and any related agreement will be performed in accordance with its terms. This summary does not represent a detailed description of all the U.S. federal income tax consequences to you in light of your particular circumstances and does not address the effects of any state, local or non-U.S. tax laws (or other U.S. federal tax consequences, such as U.S. federal estate or gift tax consequences). In addition, it does not represent a detailed description of the U.S. federal income tax consequences applicable to you if you are subject to special treatment under the U.S. federal income tax laws, including if you are:

- a dealer in securities or currencies;
- a trader in securities if you elect to use a mark-to-market method of accounting for your securities holdings;
- a financial institution or an insurance company;
- a regulated investment company;
- a real estate investment trust;
- a tax-exempt organization;
- a person liable for alternative minimum tax;
- a person holding shares or ADSs as part of a hedging, integrated or conversion transaction, constructive sale or straddle;
- a person owning, actually or constructively, 10% or more of our voting stock;
- a partnership or other pass-through entity for U.S. federal income tax purposes; or
- a U.S. holder whose “functional currency” is not the United States dollar.

We cannot assure you that a later change in law will not alter significantly the tax considerations that we describe in this summary.

If a partnership holds our shares or ADSs, the tax treatment of a partner will generally depend upon the status of the partner and the activities of the partnership. If you are a partner of a partnership holding our shares or ADSs, you should consult your tax advisor.

You should consult your own tax advisor concerning the particular U.S. federal income tax consequences to you of the ownership and disposition of the shares or ADSs, as well as the consequences to you arising under the laws of any other taxing jurisdiction.

In general, for U.S. federal income tax purposes, a U.S. person who is the beneficial owner of an ADS will be treated as the owner of the shares underlying its ADS. Deposits or withdrawals of shares, actually or constructively, by U.S. holders for ADSs will not be subject to U.S. federal income tax. The U.S. Treasury has expressed concerns that parties through whom ADSs are pre-released may be taking actions that are inconsistent with the claiming of foreign tax credits by U.S. holders of ADSs. Such actions would also be inconsistent with the claiming of the reduced rate of tax, described in “—Taxation of Dividends” below, applicable to dividends received by certain non-corporate holders. Accordingly, the availability of the reduced tax rate for dividends received by certain non-corporate holders, each described in “—Taxation of Dividends” below, could be affected by actions taken by parties through whom the ADSs are released.

Taxation of Dividends

The amount of distributions (other than certain pro rata distributions of shares to all shareholders) you receive on your shares or ADSs, including net amounts withheld in respect of Republic of China withholding taxes, will generally be treated as dividend income to you to the extent the distributions are made from our current and accumulated earnings and profits as calculated according to U.S. federal income tax principles. These amounts (including withheld taxes) will be includible in your gross income as ordinary income on the day you actually or constructively receive the distributions, which in the case of an ADS will be the date received by the depository. You will not be entitled to claim a dividends received deduction allowed to corporations under the Code with respect to distributions you receive from us.

With respect to U.S. holders who are individuals, certain dividends received from a foreign corporation in taxable years beginning before January 1, 2011, on shares (or ADSs backed by such shares) that are readily tradable on an established securities market in the United States may be subject to reduced rates of taxation, provided further that the foreign corporation was not, in the year prior to the year in which the dividends are paid, and is not, in the year in which the dividends are paid, a passive foreign investment company (see “Passive Foreign Investment Company” below). Under current U.S. Treasury Department guidance, our ADSs, which are listed on the New York Stock Exchange, but not our common shares, are treated as readily tradable on an established securities market in the United States. Thus, we do not believe that dividends that we pay on our common shares that are not backed by ADSs currently meet the conditions required for these reduced tax rates. There can be no assurance that our ADSs will continue to be readily tradable on an established securities market in later years (or that our shares will be readily tradable on an established securities market in any given year). Individuals that do not meet a minimum holding period requirement during which they are not protected from the risk of loss, or that elect to treat the dividend income as “investment income” pursuant to Section 163(d)(4) of the Code, will not be eligible for the reduced rates of taxation regardless of the trading status of our shares or ADSs. In addition, the rate reduction will not apply to dividends if the recipient of a dividend is obligated to make related payments with respect to positions in substantially similar or related property. This disallowance applies even if the minimum holding period has been met. You should consult your own tax advisor regarding the application of these rules given your particular circumstances.

The amount of any dividend paid in NT dollars will equal the U.S. dollar value of the NT dollars you receive, calculated by reference to the exchange rate in effect on the date you actually or constructively receive the dividend, which in the case of an ADS will be the date received by the depository, regardless of whether the NT dollars are actually converted into U.S. dollars. If the NT dollars received as a dividend are not converted into U.S. dollars on the date of receipt, you will have a basis in the NT dollars equal to their U.S. dollar value on the date of receipt. Any gain or loss you realize if you subsequently sell or otherwise dispose of the NT dollars will be ordinary income or loss from sources within the United States for foreign tax credit limitation purposes.

Subject to certain conditions and limitations under the Code, you may be entitled to a credit or deduction against your U.S. federal income taxes for the net amount of any Republic of China taxes that are withheld from dividend distributions made to you. In determining the amounts withheld in respect of Republic of China taxes, any reduction of the amount withheld on account of a Republic of China credit in respect of the 10% retained earnings tax imposed on us is not considered a withholding tax and will not be treated as distributed to you or creditable by you against your U.S. federal income tax. The limitation on foreign taxes eligible for credit is calculated separately with respect to specific classes of income. For purposes of calculating the foreign tax credit, dividends we pay with respect to shares or ADSs will generally be considered passive income from sources outside the United States. Further, a U.S. holder that

- has held shares or ADSs for less than a specified minimum period during which it is not protected from risk of loss, or
- is obligated to make payments related to the dividends,

may not be allowed a foreign tax credit for foreign taxes imposed on dividends paid on shares or ADSs. The rules governing the foreign tax credit are complex. We therefore urge you to consult your tax advisor regarding the availability of the foreign tax credit under your particular circumstances.



To the extent that the amount of any distribution you receive exceeds our current and accumulated earnings and profits for a taxable year, as determined under U.S. federal income tax principles, the distribution will first be treated as a tax-free return of capital, causing a reduction in your adjusted basis in the shares or ADSs and thereby increasing the amount of gain, or decreasing the amount of loss, you will recognize on a subsequent disposition of the shares or ADSs. The balance in excess of adjusted basis, if any, will be taxable to you as capital gain recognized on a sale or exchange. However, we do not expect to keep earnings and profits in accordance with U.S. federal income tax principles. Therefore, you should expect that a distribution will generally be treated as a dividend.

It is possible that pro rata distributions of shares or ADSs to all shareholders may be made in a manner that is not subject to U.S. federal income tax. The basis of any new shares or ADSs so received will generally be determined by allocating your basis in the old shares or ADSs between the old shares or ADSs and the new shares or ADSs, based on their relative fair market values on the date of distribution.

For U.S. tax purposes, any such tax-free share distribution and any distributions in excess of current and accumulated earnings and profits generally would not result in foreign source income to you. Consequently, you may not be able to use the foreign tax credit associated with any Republic of China withholding tax imposed on such distributions unless you can use the credit (subject to applicable limitations) against U.S. federal income tax due on other foreign source income in the appropriate category for foreign tax credit purposes.

Taxation of Capital Gains

When you sell or otherwise dispose of your shares or ADSs, you will generally recognize capital gain or loss in an amount equal to the difference between the U.S. dollar value of the amount realized for the shares or ADSs and your basis in the shares or ADSs, determined in U.S. dollars. For foreign tax credit limitation purposes, such gain or loss will generally be treated as U.S. source gain or loss. If you are an individual, and have held the shares or ADSs being sold or otherwise disposed of for more than one year, your gain recognized will be eligible for reduced rates of taxation. Your ability to deduct capital losses is subject to limitations.

Any Republic of China securities transaction taxes that you pay generally will not be creditable foreign taxes for U.S. federal income tax purposes, but you may be able to deduct such taxes, subject to certain limitations under the Code. You are urged to consult your tax advisors regarding the U.S. federal income tax consequences of these taxes.

Passive Foreign Investment Company

We believe that we were not a “passive foreign investment company” (“PFIC”) for U.S. federal income tax purposes for 2006. In addition, based on the projected composition of our income and valuation of our assets, including goodwill, we do not expect to be a PFIC for 2007. However, since PFIC status depends upon the composition of our income and assets and the market value of our assets (including, among others, goodwill) from time to time, there can be no assurance that we will not be considered a PFIC for any taxable year. If we were treated as a PFIC for any taxable year during which you held our shares or ADSs, you could be subject to additional U.S. federal income taxes on gain recognized with respect to the shares or ADSs and on certain distributions, plus an interest charge on certain taxes treated as having been deferred under the PFIC rules. Non-corporate U.S. holders will not be eligible for reduced rates of taxation on any dividends received from us in taxable years beginning before January 1, 2011, if we are a PFIC in the taxable year in which such dividends are paid or in the preceding taxable year.

Information Reporting and Backup Withholding

In general, dividend payments, or other taxable distributions, made within the United States to you will be subject to information reporting requirements if you are a non-corporate U.S. person. Such payments may also be subject to backup withholding if you:

- fail to provide an accurate taxpayer identification number;

- are notified by the U.S. Internal Revenue Service that you have failed to report all interest or dividends required to be shown on your federal income tax returns; or
- in certain circumstances, fail to comply with applicable certification requirements.
- If you sell your shares or ADSs to or through a United States office of a broker, the payment of the proceeds is subject to both United States backup withholding and information reporting unless you establish an exemption. If you sell your shares or ADSs outside the United States through a non-U.S. office of a non-U.S. broker, and the sales proceeds are paid to you outside the United States, then United States backup withholding and information reporting requirements generally will not apply to that payment. However, United States information reporting, but not backup withholding, will apply to a payment of sales proceeds, even if that payment is made outside the United States, if you sell your shares or ADSs through a non-U.S. office of a broker that:
 - is a U.S. person;
 - derives 50% or more of its gross income for a specified three-year period from the conduct of a trade or business in the United States;
 - is a “controlled foreign corporation” as to the United States;
 - is a foreign partnership, if at any time during its tax year one or more of its partners are U.S. persons, as defined in U.S. Treasury regulations, who in the aggregate hold more than 50% of the income or capital interest in the partnership; or
 - the foreign partnership is engaged in a United States trade or business,

unless you establish an exemption.

You generally may obtain a refund of any amounts withheld under the backup withholding rules that exceed your income tax liability by filing a refund claim with the U.S. Internal Revenue Service.

F. Dividends and Paying Agents

Not applicable.

G. Statement by Experts

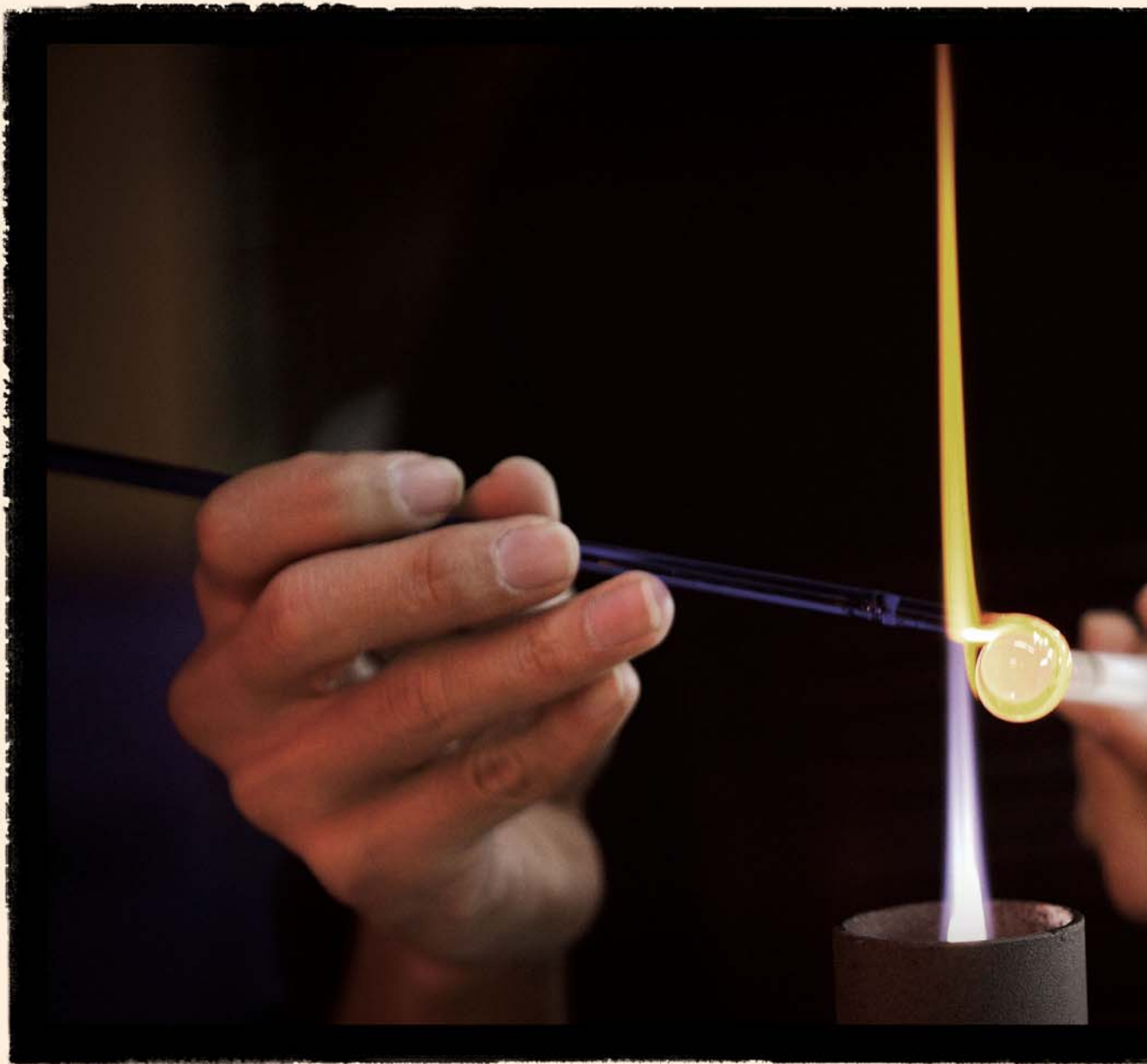
Not applicable.

H. Documents on Display

We have filed this annual report on Form 20-F, including exhibits, with the SEC. As allowed by the SEC, in Item 19 of this annual report, we incorporate by reference certain information we filed with the SEC. This means that we can disclose important information to you by referring you to another document filed separately with the SEC. The information incorporated by reference is considered to be part of this annual report.

You may read and copy this annual report, including the exhibits incorporated by reference in this annual report, at the SEC’s Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549 and at the SEC’s regional offices in New York, New York and Chicago, Illinois. You can also request copies of this annual report, including the exhibits incorporated by reference in this annual report, upon payment of a duplicating fee, by writing information on the operation of the SEC’s Public Reference Room.

The SEC also maintains a website at www.sec.gov that contains reports, proxy statements and other information regarding registrants that file electronically with the SEC. Our annual report and some of the other information submitted by us to the SEC may be accessed through this web site.



Impressive results come from meticulous planning.







I. Subsidiary Information

Not applicable.

ITEM 11. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk is the risk of loss related to adverse changes in market prices, including interest rates and foreign exchange rates, of financial instruments. In the normal course of business, we are routinely subject to a variety of risks, including market risk associated with interest rate movements, currency rate movements on non-NT dollar denominated assets and liabilities and equity price movements on our portfolio of equity securities.

We regularly assess these financial instruments and their ability to address market risk and have established policies and business practices to protect against the adverse effects of these and other potential exposures.

Interest Rate Sensitivity

We are subject to market rate risks due to fluctuations in interest rates for our short-term and long-term loans, but we do not expect these risks to have a material impact on our company. We have not used any derivative financial instruments to hedge interest rate risk. We have not been exposed nor do we anticipate being exposed to material risks due to changes in interest rates. The risk associated with fluctuating interest rates is principally confined to our cash deposits in banks, and, therefore, we believe our exposure to interest rate risk is minimal.

We had 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, consisting of a loan with a five-year term payable in three annual installments beginning in March 2005 and ending in March 2007. This loan was repaid in full in March 2007. On November 18, 2005, our subsidiary Chief Telecom Inc. obtained a two-year secured loan in the amount of NT\$23 million from Chinatrust Commercial Bank at an annual interest rate of 3.05%, with interest and principle payable monthly. 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. We do not expect interest rate risk to have a material impact on our financial condition and results of operations.

Foreign Currency Risk

We are exposed to foreign currency risk as a result of our telecommunications equipment being sourced from overseas suppliers and from our international settlement payments associated with our services for international calls and roaming traffic. Specifically, our foreign currency exposure relates primarily to our foreign-currency denominated purchase agreements, settlement of roaming and international traffic contracts in foreign currencies, and to a limited extent, cash and cash equivalents denominated in foreign currencies. We have entered into foreign exchange forward contracts and index future contracts designed to mitigate our exposure to foreign currency risks. We expect our foreign currency hedging activities to increase in the future. Net losses arising from these derivative financial instruments for the year ended December 31, 2006 were NT\$52 million including realized settlement losses of NT\$32 million and valuation losses of NT\$20 million. We do not believe the gains and losses from these transactions to be material on our financial condition and results of operations.

Equity Price Risk

We are exposed to equity price risk as a result of the equities that we hold. Many of these equities are listed on stock market exchanges, and the value of our equity holdings fluctuates depending on the market conditions. During the year ended December 31, 2006, we entered into hedging transactions to manage the equity price risk exposure by purchasing index future contracts. We do not expect the gains and losses in the values of the equities that we hold to have a material impact on our financial condition and results of operations.

ITEM 12. DESCRIPTION OF SECURITIES OTHER THAN EQUITY SECURITIES

Not applicable.

PART II

ITEM 13. DEFAULTS, DIVIDEND ARREARAGES AND DELINQUENCIES

None of these events occurred in any of fiscal 2004, 2005 and 2006.

ITEM 14. MATERIAL MODIFICATIONS TO THE RIGHTS OF SECURITY HOLDERS AND USE OF PROCEEDS

None.

ITEM 15. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

As of the end of the period covered by this annual report, an evaluation has been carried out under the supervision and with the participation of our management, including our chief executive officer and our chief financial officer, of the effectiveness of the design and operation of our disclosure controls and procedures, as such term is defined under Rules 13a-14(c) and 15d-14(c) promulgated under the Securities Exchange Act of 1934, as amended. Based on that evaluation, our chief executive officer and chief financial officer have concluded that our disclosure controls and procedures are effective in ensuring that material information required to be disclosed in this annual report is recorded, processed, summarized and reported to them for assessment, and required disclosure is made within the time period specified in the rules and forms of the Securities and Exchange Commission.

Management's Annual Report on Internal Control Over Financial Reporting.

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Rule 13a—15(f) under the Securities Exchange Act of 1934, as amended, for our company. Internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements in accordance with generally accepted accounting principles and includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of a company's assets, (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of consolidated financial statements in accordance with generally accepted accounting principles, and that a company's receipts and expenditures are being made only in accordance with authorizations of a company's management and directors, and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of a company's assets that could have a material effect on the consolidated financial statements.

Because of its inherent limitations, a system of internal control over financial reporting can provide only reasonable assurance with respect to consolidated financial statement preparation and presentation and may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

As required by Section 404 of the Sarbanes-Oxley Act of 2002 and related rules as promulgated by the Securities and Exchange Commission, management assessed the effectiveness of the our internal control over financial reporting as of December 31, 2006 using criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

Based on this assessment, management concluded that the our internal control over financial reporting was effective as of December 31, 2006 based on the criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.



Our management's assessment, as well as the effectiveness of internal control over financial reporting has been audited by Deloitte & Touche, an independent registered public accounting firm, who has also audited our consolidated financial statements for the year ended December 31, 2006. Deloitte & Touche has issued an attestation report on management's assessment of the effectiveness of our internal control over financial reporting under Auditing Standard No. 2 of the Public Company Accounting Oversight Board.

Attestation Report of the Registered Public Accounting Firm

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Stockholders
Chunghwa Telecom Co., Ltd.

We have audited management's assessment, included in the accompanying Management's Annual Report on Internal Control Over Financial Reporting, that Chunghwa Telecom Co., Ltd. and subsidiaries (the Company) maintained effective internal control over financial reporting as of December 31, 2006, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company's management is responsible, for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed by, or under the supervision of, the company's principal executive and principal financial officers, or persons performing similar functions, and effected by the company's board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the Company's assets that could have a material effect on the consolidated financial statements.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management's assessment that the Company maintained effective internal control over financial reporting as of December 31, 2006, is fairly stated, in all material respects, based on the criteria

established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2006, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements as of and for the year ended December 31, 2006 of the Company and our report dated March 13, 2007 expressed an unqualified opinion on those financial statements and included an explanatory paragraph regarding the effect for the Company's adoption of U.S. FASB Statement No. 158, Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans.

/s/ Deloitte & Touche

Deloitte & Touche
Taipei, Taiwan
The Republic of China

March 13, 2007

Changes in Internal Control Over Financial Reporting

There were no changes in our internal control over financial reporting that occurred during the year ended December 31, 2006 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

ITEM 16A. AUDIT COMMITTEE FINANCIAL EXPERT

Jing-Twen Chen is our audit committee financial expert and an independent director. See "Item 6. Directors, Senior Management and Employees—C. Board Practices."

ITEM 16B. CODE OF ETHICS


We have adopted a code of ethics that applies to our directors, supervisors, employees and officers, including our chief executive officer and chief financial officer. We have included a copy of code of ethics as an exhibit to this annual report.

ITEM 16C. PRINCIPAL ACCOUNTANT FEES AND SERVICES

The following table sets forth the aggregate fees by categories specified below in connection with certain professional services rendered by Deloitte & Touche, our principal accountant for the years indicated. We did not pay any other fees to our auditors during the periods indicated below.

	For the year ended December 31,			
	2004	2005	2006	
Audit fees ⁽¹⁾	NT\$27,664	NT\$42,287	NT\$59,014	US\$1,811
Audit-related fees ⁽²⁾	—	—	—	—
Tax fees ⁽³⁾	319	—	—	—
All other Fees ⁽⁴⁾	—	—	—	—

- (1) "Audit fees" means the aggregate fees billed in each of the fiscal years listed for professional services rendered by our principal accountant for the audit of our annual consolidated financial statements or services that are normally provided by the auditors in connection with statutory and regulatory filings or engagements.

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- (2) "Audit-related fees" means the aggregate fees billed in each of the fiscal years listed for assurance and related services by our principal accountant that are reasonably related to the performance of the audit or review of our consolidated financial statements and are not reported under "Audit fees." Services comprising the fees disclosed under the category of "Audit-related fees" involve principally the issuance of agreed upon procedures letters.
 - (3) "Tax fees" means the aggregate fees billed in each of the fiscal years listed for professional services rendered by our principal accountant for tax compliance, tax advice and tax planning. Services comprising the fees disclosed under the category of "Tax Fees" involve tax advice.
 - (4) "All other fees" means the aggregate fees billed in each of the last two fiscal years for products and services provided by our principal accountant other than the services reported in items (1) to (3) above.

Prior to forming an audit committee, our board of directors is responsible for the oversight of the work performed by our principal accountant. The policy of our board of directors is to pre-approve all audit and non-audit services provided by Deloitte & Touche, including audit services, audit-related services, tax services and other services as described above. After our audit committee was established in September 2004, all audit and non-audit services provided by Deloitte & Touche were pre-approved by our audit committee.

ITEM 16D. EXEMPTIONS FROM THE LISTING STANDARDS FOR AUDIT COMMITTEES

None.

ITEM 16E. PURCHASES OF EQUITY SECURITIES BY THE ISSUER AND AFFILIATED PURCHASERS

The table below details our purchases of our own equities pursuant to the share repurchase program announced on February 9, 2006. Our share repurchase program authorized the purchase of a maximum of 250,000,000 shares of our common stock before the expiration of the program on April 9, 2006. Under this share repurchase program, we purchased 192,000,000 shares of our common stock before the expiration of the program.

Issuer Purchases of Equity Securities

Period	(a) Total Number of Shares Purchased	(b) Average Price Paid per Share	(c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	(d) Maximum Number (or Approximate Dollar Value) of Shares that May Yet Be Purchased Under the Plans or Programs
February 10, 2006 – February 28, 2006	51,545,000	NT\$58.43	51,545,000	198,455,000
March 1, 2006 – March 31, 2006	97,613,000	NT\$59.54	97,613,000	100,842,000
April 1, 2006 – April 7, 2006	42,842,000	NT\$59.96	42,842,000	58,000,000

PART III

ITEM 17. FINANCIAL STATEMENTS

The Registrant has elected to provide the consolidated financial statements and related information specified in Item 18 in lieu of Item 17.

ITEM 18. FINANCIAL STATEMENTS

The following is a list of the audited consolidated financial statements and report of independent registered public accounting firm included in this annual report beginning on page F-1.

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ITEM 19. EXHIBITS

<u>Exhibit Number</u>	<u>Description of Exhibits</u>
1.1	Statute of Chunghwa Telecom Co., Ltd. as last amended on November 29, 2000 (English translation) (incorporated by reference to Exhibit 1.1 to the Registrant's Annual Report on Form 20-F for the fiscal year ended December 31, 2003 (File No. 001-31731) filed with the Commission on May 17, 2004).
1.2*	Articles of incorporation of the Company as last amended on May 30, 2006 (English Translation).
2.1	Form of Deposit Agreement among the Company, The Bank of New York, as depositary, and Holders and Beneficial Owners of American Depositary Shares issued thereunder, including the form of American Depositary Shares (incorporated by reference to Exhibit (a) to the Registrant's Registration Statement on Form F-6 (File No. 333-106416) filed with the Commission on July 15, 2003).
8.1*	List of Subsidiaries.
11.1	Code of Ethics (English translation), as amended (incorporated by reference to Exhibit 11.1 to the Registrant's Annual Report on Form 20-F for the fiscal year ended December 31, 2005 (File No. 001-31731) filed with the Commission on May 26, 2006).
12.1*	Certification of our Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
12.2*	Certification of our Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
13.1*	Certification of our Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

* Filed herewith.



SIGNATURES

The registrant hereby certifies that it meets all of the requirements for filing on Form 20-F and that it has duly caused and authorized the undersigned to sign this annual report on its behalf.

CHUNGHWA TELECOM CO., LTD.

By: /s/ Tan Ho Chen
Name: **Tan Ho Chen**
Title: **Chairman and Chief Executive Officer**

Date: April 23, 2007

MEMO





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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Stockholders
Chunghwa Telecom Co., Ltd.

We have audited the accompanying consolidated balance sheets of Chunghwa Telecom Co., Ltd. and subsidiaries (the Company) as of December 31, 2005 and 2006, and the related consolidated statements of operations and comprehensive income, changes in stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2006, all expressed in New Taiwan dollars. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Chunghwa Telecom Co., Ltd. and subsidiaries as of December 31, 2005 and 2006 and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2006 in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 2 to the consolidated financial statements, the Company adopted SFAS No. 158 on December 31, 2006 and the impact on accumulated other comprehensive income is NT\$226 million.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of the Company's internal control over financial reporting as of December 31, 2006, based on the criteria established in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 13, 2007 expressed an unqualified opinion on management's assessment of the effectiveness of the Company's internal control over financial reporting and an unqualified opinion on the effectiveness of the Company's internal control over financial reporting.

Our audits also comprehended the translation of New Taiwan Dollar amounts into U.S. dollar amounts and, in our opinion, such translation has been made in conformity with the basis stated in Note 4. Such U.S. dollar amounts are presented for the convenience of the readers.

/s/ Deloitte & Touche

Deloitte & Touche
Taipei, Taiwan
The Republic of China

March 13, 2007



CHUNGHWA TELECOM CO., LTD. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(Amounts in Millions, Except Shares and Par Value Data)

	Notes	December 31		
		2005	2006	
		NT\$	NT\$	US\$ (Note 4)
ASSETS				
CURRENT ASSETS				
Cash and cash equivalents	2,5,24	\$ 41,891	\$ 70,673	\$ 2,169
Short-term investments	2,6,24	14,171	6,951	213
Trade notes and accounts receivable, net	2,7,20	12,839	12,630	388
Inventories	2,8	2,120	2,183	67
Prepaid expenses		1,149	907	28
Deferred income taxes	2,19	3,353	1,271	39
Other current assets	18,19	5,805	6,287	192
Total current assets		81,328	100,902	3,096
LONG-TERM INVESTMENTS	2,9,24	3,391	3,546	109
INVESTMENT IN PRIVATE MUTUAL FUND	2,10	481	—	—
PROPERTY, PLANT AND EQUIPMENT, NET	2,11,20	293,525	277,426	8,513
INTANGIBLE ASSETS				
3G concession, net	2	9,732	8,983	276
Patents and computer software, net	2	184	210	6
Goodwill	2	—	73	2
Total intangible assets		9,916	9,266	284
OTHER ASSETS				
Deferred income taxes, non-current	2,19	2,626	3,457	106
Other	21,24	3,901	4,184	128
Total other assets		6,527	7,641	234
TOTAL		\$395,168	\$398,781	\$ 12,236
LIABILITIES AND STOCKHOLDERS' EQUITY				
CURRENT LIABILITIES				
Short-term loans	14,24	\$ —	\$ 126	\$ 4
Trade notes and accounts payable	20	10,673	9,906	304
Income tax payable	2,19	997	12,469	383
Accrued expenses	12,20	16,010	19,937	612
Current portion of deferred income	2	8,907	8,354	256
Current portion of long-term loan	15,24	200	323	10
Customers' deposits	24	7,392	6,654	204
Other current liabilities	13,20	12,507	9,344	286
Total current liabilities		56,686	67,113	2,059
LONG-TERM LIABILITIES				
Deferred income, net of current portion	2	10,147	9,350	287
Long-term loan, net of current portion	15,24	300	—	—
Accrued pension liabilities	2,18	—	1,612	50
Other		207	561	17
Total long-term liabilities		10,654	11,523	354
Total liabilities		67,340	78,636	2,413
MINORITY INTEREST		—	98	3
COMMITMENTS AND CONTINGENCIES	21,23	—	—	—
STOCKHOLDERS' EQUITY				
Capital stock—NT\$10 (US\$0.3) par value	16	—	—	—
Authorized—9,647,724,900 common shares at December 31, 2005; 12,000,000,000 common shares at December 31, 2006				
Issued and outstanding—9,647,724,900 common shares at December 31, 2005; 9,667,845,093 common shares at December 31, 2006				
		96,477	96,678	2,967
Capital surplus		157,490	164,330	5,042
Retained earnings		73,864	58,727	1,801
Other comprehensive income		(3)	312	10
Total stockholders' equity		327,828	320,047	9,820
TOTAL		\$395,168	\$398,781	\$ 12,236

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

CHUNGHWA TELECOM CO., LTD. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME

(Amounts in Millions, Except Shares and Per Share and Per ADS Data)

	Notes	Year Ended December 31			
		2004 NT\$	2005 NT\$	2006 NT\$	US\$ (Note 4)
REVENUES	20	\$ 185,163	\$ 184,696	\$ 186,342	\$ 5,718
OPERATING COSTS AND EXPENSES	2				
Costs of revenues, excluding depreciation and amortization	20	58,664	68,073	62,606	1,921
Marketing, excluding depreciation and amortization	2	19,298	23,650	20,651	633
General and administrative, excluding depreciation and amortization		2,550	3,505	3,314	102
Research and development, excluding depreciation and amortization	2	2,476	3,144	2,824	87
Depreciation and amortization — cost of revenues		38,358	38,800	38,353	1,177
Depreciation and amortization — other operating expenses		2,345	2,363	2,297	70
Total operating costs and expenses		123,691	139,535	130,045	3,990
INCOME FROM OPERATIONS		61,472	45,161	56,297	1,728
OTHER INCOME					
Interest		224	452	804	25
Other income		901	1,527	735	22
Total other income		1,125	1,979	1,539	47
OTHER EXPENSES					
Interest		5	2	6	—
Impairment loss on long-term investments		—	740	—	—
Other expense		415	366	490	15
Total other expenses		420	1,108	496	15
INCOME BEFORE INCOME TAX AND MINORITY INTEREST		62,177	46,032	57,340	1,760
INCOME TAX	2,19	11,259	12,733	15,281	469
INCOME BEFORE MINORITY INTEREST		50,918	33,299	42,059	1,291
MINORITY INTEREST		—	—	13	—
NET INCOME		\$ 50,918	\$ 33,299	\$ 42,072	\$ 1,291
NET INCOME PER SHARE	2	\$ 5.18	\$ 3.39	\$ 4.34	\$ 0.13
WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING		9,836,839,398	9,836,839,398	9,686,928,910	9,686,928,910
NET INCOME PER PRO FORMA EQUIVALENT ADS	2	\$ 51.76	\$ 33.85	\$ 43.43	\$ 1.33
WEIGHTED AVERAGE NUMBER OF PRO FORMA EQUIVALENT ADSs OUTSTANDING		983,683,940	983,683,940	986,692,891	986,692,891
COMPREHENSIVE INCOME					
Net income	2	\$ 50,918	\$ 33,299	\$ 42,072	\$ 1,291
Cumulative translation adjustments		(5)	2	—	—
Unrealized gain on available-for-sale securities	2,6	—	—	541	16
Comprehensive income		\$ 50,913	\$ 33,301	\$ 42,613	\$ 1,307

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



CHUNGHWA TELECOM CO., LTD. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

(Amounts in Millions, Except Shares Data)

	Capital Stock			Retained Earnings				Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Total Stockholders' Equity
	Common Shares	Amount NT\$	Capital Surplus NT\$	Legal Reserve NT\$	Losses on Reserve NT\$	Unappropriated Earnings NT\$	Total NT\$			
BALANCE, DECEMBER 31, 2003 (IN NT\$)	9,647,724,900	\$ 96,477	\$135,873	\$ 29,437	\$ 2,675	\$ 46,293	\$ 78,405	\$ —	\$ —	\$ 310,755
Additional capital contributed by government	—	—	32	—	—	—	—	—	—	32
Additional capital contributed by the MOTC through selling shares to employees at a discounted price	—	—	457	—	—	—	—	—	—	457
Appropriations and distributions of 2003 earnings:										
Legal reserve	—	—	—	4,850	—	(4,850)	—	—	—	—
Special reserve	—	—	—	—	1	(1)	—	—	—	—
Dividends declared	—	—	—	—	—	(43,414)	(43,414)	—	—	(43,414)
Net income	—	—	—	—	—	50,918	50,918	—	—	50,918
Cumulative translation adjustment for foreign-currency investments in unconsolidated companies	—	—	—	—	—	—	—	(5)	—	(5)
BALANCE, DECEMBER 31, 2004 (IN NT\$)	9,647,724,900	96,477	136,362	34,287	2,676	48,946	85,909	(5)	—	318,743
Additional capital contributed by government	—	—	6	—	—	—	—	—	—	6
Additional capital contributed by the MOTC through selling shares to employees at a discounted price	—	—	12,770	—	—	—	—	—	—	12,770
Additional capital contributed by MOTC—pension	—	—	8,352	—	—	—	—	—	—	8,352
Appropriations and distributions of 2004 earnings:										
Legal reserve	—	—	—	4,986	—	(4,986)	—	—	—	—
Special reserve	—	—	—	—	4	(4)	—	—	—	—
Dividends declared	—	—	—	—	—	(45,344)	(45,344)	—	—	(45,344)
Net income	—	—	—	—	—	33,299	33,299	—	—	33,299
Cumulative translation adjustment for foreign-currency investments in unconsolidated companies	—	—	—	—	—	—	—	2	—	2
BALANCE, DECEMBER 31, 2005 (IN NT\$)	9,647,724,900	96,477	157,490	39,273	2,680	31,911	73,864	(3)	—	327,828
Additional capital contributed by the MOTC through selling shares to employees at a discounted price (Note 17)	—	—	503	—	—	—	—	—	—	503
Employee stock bonus (Note 16)	23,005,695	230	1,151	—	—	—	—	—	—	1,381
Appropriations and distributions of 2005 earnings:										
Legal reserve	—	—	—	4,765	—	(4,765)	—	—	—	—
Cash dividends—NT\$4.3 per share	—	—	—	—	—	(40,660)	(40,660)	—	—	(40,660)
Stock dividends—NT\$0.2 per share	189,114,498	1,891	9,456	—	—	(11,347)	(11,347)	—	—	—
Consolidated net income	—	—	—	—	—	42,072	42,072	—	—	42,072
Purchase treasury stock—192,000 thousand shares	—	—	—	—	—	—	—	—	(11,392)	(11,392)
Cancellation of treasury stock—192,000 thousand shares	(192,000,000)	(1,920)	(4,270)	—	—	(5,202)	(5,202)	—	11,392	—
Unrealized gain on available-for-sale securities	—	—	—	—	—	—	—	541	—	541
Adjustment to initially apply SFAS No. 158, net of tax	—	—	—	—	—	—	—	(226)	—	(226)
BALANCE, DECEMBER 31, 2006 (IN NT\$)	9,667,845,093	\$ 96,678	\$164,330	\$44,038	\$ 2,680	\$ 12,009	\$ 58,727	\$ 312	\$ —	\$ 320,047
BALANCE, DECEMBER 31, 2006 (IN US\$) (Note 4)	9,667,845,093	\$ 2,967	\$ 5,042	\$ 1,351	\$ 82	\$ 368	\$ 1,801	\$ 10	\$ —	\$ 9,820

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

CHUNGHWA TELECOM CO., LTD. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Amounts in Millions)

	Year Ended December 31			
	2004 NT\$	2005 NT\$	2006 NT\$	US\$ (Note 4)
CASH FLOWS FROM OPERATING ACTIVITIES				
Net income	\$50,918	\$33,299	\$ 42,072	\$1,291
Adjustments to reconcile net income to net cash provided by operating activities:				
Provision for doubtful accounts	1,565	920	617	19
Depreciation and amortization	40,703	41,163	40,650	1,247
Impairment loss on long-live assets	—	343	—	—
Impairment loss on long-term investments	—	740	—	—
Loss (gain) on sales of short-term investments	12	(232)	(93)	(3)
Loss on sale of investments in private mutual fund	—	—	7	—
Net loss (gain) on disposal of scrap inventories and property, plant and equipment	168	(305)	(751)	(23)
Equity in earnings of unconsolidated companies	(70)	(160)	(97)	(3)
Cash dividends received from equity investees	56	66	42	1
Unrealized losses on investment in private mutual fund	—	19	—	—
Stock compensation expenses for shares sold to employees at a discount	457	12,770	503	16
Employee stock bonus	—	—	1,151	35
Deferred income taxes	157	9,689	1,406	43
Minority interest	—	—	(13)	—
Changes in operating assets and liabilities:				
Decrease (increase) in:				
Trade notes and accounts receivable	(382)	(72)	(298)	(9)
Inventories	(326)	(831)	580	18
Prepaid expenses	(108)	(547)	243	8
Other current assets	134	(4,210)	(474)	(14)
Other assets	742	(274)	285	8
Increase (decrease) in:				
Trade notes and accounts payable	2,879	(4,002)	(1,500)	(46)
Income tax payable	109	(4,035)	11,472	352
Accrued expenses	162	1,642	4,120	126
Customers' deposits	(2,421)	(1,012)	(738)	(23)
Other current liabilities	464	587	774	24
Accrued pension liabilities	(1,229)	1,381	1,269	39
Deferred income	(2,385)	(778)	(1,377)	(42)
Other liabilities	(40)	4	301	9
Net cash provided by operating activities	91,565	86,165	100,151	3,073

(Continued)



CHUNGHWA TELECOM CO., LTD. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS — (Continued)
(Amounts in Millions)

	Year Ended December 31			
	2004 NT\$	2005 NT\$	2006 NT\$	US\$ (Note 4)
CASH FLOWS FROM INVESTING ACTIVITIES				
Acquisitions of available-for-sale securities	\$ (9,127)	\$ (4,824)	\$ (4,149)	\$ (128)
Proceeds from disposal of available-for-sale securities	—	—	12,001	368
Acquisition of long-term investments	(530)	—	(97)	(3)
Acquisition of investment in private mutual fund	—	(500)	—	—
Proceeds from disposal of investments in private mutual fund	—	—	474	14
Acquisitions of property, plant and equipment	(22,889)	(22,930)	(27,681)	(849)
Proceeds from disposal of property, plant and equipment	215	374	779	24
Acquisitions of patents and computer software	(122)	(139)	(170)	(5)
Acquisition of subsidiary, net of cash and cash equivalents acquired	—	—	(283)	(8)
Net cash used in investing activities	<u>(32,453)</u>	<u>(28,019)</u>	<u>(19,126)</u>	<u>(587)</u>
CASH FLOWS FROM FINANCING ACTIVITIES				
Increase in short-term loans	—	—	11	—
Payments on principal of long-term loans	—	(200)	(202)	(6)
Cash dividends paid	(43,414)	(45,344)	(40,660)	(1,247)
Additional capital contributed by government	32	6	—	—
Purchase of treasury stock	—	—	(11,392)	(350)
Net cash used in financing activities	<u>(43,382)</u>	<u>(45,538)</u>	<u>(52,243)</u>	<u>(1,603)</u>
NET INCREASE IN CASH AND CASH EQUIVALENTS	<u>15,730</u>	<u>12,608</u>	<u>28,782</u>	<u>883</u>
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	<u>13,553</u>	<u>29,283</u>	<u>41,891</u>	<u>1,286</u>
CASH AND CASH EQUIVALENTS, END OF YEAR	<u>\$ 29,283</u>	<u>\$ 41,891</u>	<u>\$ 70,673</u>	<u>\$ 2,169</u>
SUPPLEMENTAL INFORMATION				
Interest paid	\$ 4	\$ 2	\$ 7	\$ —
Income tax paid	<u>\$ 10,993</u>	<u>\$ 11,419</u>	<u>\$ 1,287</u>	<u>\$ 39</u>
SUPPLEMENTAL SCHEDULE OF NONCASH INVESTING				
Acquisition of subsidiary, net of cash and cash equivalents acquired is shown as follows:				
Asset acquired			\$ 456	\$ 14
Goodwill			73	2
Liabilities assumed			(246)	(8)
Acquisitions of subsidiary, net of cash and cash equivalents acquired			<u>\$ 283</u>	<u>\$ 8</u>

(Continued)

CHUNGHWA TELECOM CO., LTD. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS—(Continued)

(Amounts in Millions)

	Year Ended December 31			
	2004	2005	2006	
	NT\$	NT\$	NT\$	US\$ (Note 4)
NON-CASH FINANCING ACTIVITIES				
Current portion of long-term loans	\$ 200	\$ 200	\$ 323	\$ 10
Activities related to the settlement of the pension obligations upon privatization:				
Accrued pension liabilities	\$ —	\$ 46,915	\$ —	\$ —
Deferred pension cost	—	(34,504)	—	—
Deferred income taxes	—	(4,059)	—	—
Additional capital contributed by MOTC- pension	\$ —	\$ 8,352	\$ —	\$ —

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

(Concluded)



CHUNGHWA TELECOM CO., LTD. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Amounts in Millions of New Taiwan Dollars, Unless Stated Otherwise)

1. GENERAL

Chunghwa Telecom Co., Ltd. ("Chunghwa" or "the Company") was incorporated on July 1, 1996 in the Republic of China ("ROC") pursuant to the Telecommunications Act No. 30. The Company is a company limited by shares and, prior to August 2000, was wholly owned by the Ministry of Transportation and Communications ("MOTC"). Prior to July 1, 1996, the current operations of Chunghwa were carried out under the Directorate General of Telecommunications ("DGT"). The DGT was established by the MOTC in June 1943 to take primary responsibility in the development of telecommunications infrastructure and to formulate policies related to telecommunications. On July 1, 1996, the telecom operations of the DGT were spun-off as Chunghwa which continues to carry out the business and the DGT continues to be the industry regulator.

As a telecommunications service provider of fixed-line and cellular telephone services, within the meaning of applicable telecommunications regulations of the ROC, the Company is subject to requirements imposed by the MOTC.

Effective August 12, 2005, the MOTC had completed the process of privatizing the Company by reducing the government ownership to below 50%. Portions of the MOTC's common share holdings had been sold, in connection with the foregoing privatization plan, in domestic public offerings at various dates from August 2000 to July 2003. Portions of the MOTC's common share holdings had also been sold to the Company's employees at various dates from October 2000 to July 2005. In July 2003, the MOTC sold the Company's common shares in an international offering of securities in the form of American Depositary Shares ("ADS"). In August 2005, the MOTC sold 289,431,000 common shares in the ROC and 1,350,682,000 common shares in an international offering of securities in the form of ADS. As of August 12, 2005, the MOTC owned 47.84% shares of the Company and the privatization plan was completed. The MOTC and Taiwan Mobile Co. sold 505,388,900 and 58,959,000 common shares of the Company, respectively, to third parties in the form of ADS amounting to 56,435 thousand units in total on October 4, 2006. As of December 31, 2006, the MOTC owns 35.48% shares of the Company.

The Company's common shares were listed and traded on Taiwan Stock Exchange and New York Stock Exchange on October 27, 2000 and on July 17, 2003, respectively.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

Prior to August 12, 2005, the effective date of privatization, the Company maintained its accounting books and records based on the ROC government regulations for state-owned enterprises, ROC government regulations governing the preparation of financial statements of public companies and accounting principles generally accepted in the ROC ("ROC GAAP"). Subsequent to August 12, 2005, the Company is no longer required to follow the ROC government regulations for state-owned enterprises. The accompanying consolidated financial statements have been prepared to present its financial positions, results of operations and cash flows in accordance with accounting principles generally accepted in the United States of America ("US GAAP").

Principles of Consolidation

The accompanying consolidated financial statements consolidate the results and assets and liabilities of all entities within the scope FASB Interpretation No. 46R, "Consolidation of Variable Interest Entities—an Interpretation of Accounting Research Bulletin (ARB) No. 51" ("FIN46R") which are Variable Interest

Entities (VIEs) where the Company is the primary beneficiary. For entities which are not VIEs the Company consolidates all directly and indirectly majority owned subsidiaries of the Company applying the criteria in FASB Statement No. 94 “Consolidation of All Majority-Owned Subsidiaries”. All significant intercompany balances and transactions are eliminated upon consolidation.

The Company has established New Prospect Investments Holdings, Ltd. (B.V.I.) and Prime Asia Investments Group Ltd. (B.V.I.) in March, 2006. Both holding companies are operating as investment companies and the Company has 100% ownership right in an amount of US\$1 in each holding company. Beginning from September 2006, the Company acquired 70% ownership of CHIEF Telecom Co., Ltd and consolidated the accounts from that date.

Use of Estimates

The preparation of financial statements requires management to make certain estimates and assumptions that affect the recorded amounts of assets, liabilities, revenues and expenses of the Company. The Company continually evaluates these estimates, including those related to allowances for doubtful accounts, useful lives of long term assets, pension plans, valuation allowances on deferred income taxes, customer service periods, impairment of assets and the fair value of financial instruments. The Company bases its estimates on historical experience and other assumptions, which it believes to be reasonable under the circumstances. Actual results may differ from these estimates.

Foreign Currency Transactions

The functional currency of the Company is the local currency, the New Taiwan dollar (NT\$) as it is the currency of the primary economic environment. Thus, the transactions of the Company that are denominated in currencies other than the New Taiwan dollars (the “foreign currency”) are recorded in New Taiwan dollars at the exchange rates prevailing on the transaction dates. Gains or losses realized upon the settlement of a foreign currency transaction are included in the period in which the transaction is settled. The balances, at the balance sheet dates, of the foreign currency assets and liabilities are adjusted to reflect the prevailing exchange rates and the resulting differences are recorded as follows:

- a. Long-term stock investments accounted for by the equity method—as cumulative translation adjustment in stockholders’ equity.
- b. Financial assets and liabilities—credited or charged to current income.

Business Combination

The acquisition of subsidiaries is accounted for using the purchase method. The cost of the acquisition is measured at the aggregate of the fair values, at the date of exchange, of assets given and liabilities incurred or assumed, by the Company in exchange for control of the acquiree, plus any costs directly attributable to the business combination. The acquiree’s identifiable assets and liabilities are recognized at their fair values at the acquisition date.

Goodwill arising on acquisition is recognized as an asset and initially measured at cost, being the excess of the cost of the business combination over the Company’s interest in the net fair value of the identifiable net assets.

The interest of minority stockholders in the acquiree is initially measured at historical cost.

Cash Equivalents

Cash equivalents include negotiable certificates of deposit and commercial paper purchased with maturities of three months or less from the date of acquisition.



Short-term Investments

Short-term investments include open-ended mutual funds, real estate investment trust funds and listed stocks which are classified as available-for-sale securities. When subsequently measured at fair value, the changes in fair value are excluded from earnings and reported as a separate component of stockholders' equity. Unrealized losses are recorded as a charge to income when deemed other than temporary.

The credit linked investment was an interest-rate-risk financial instrument with an embedded derivative linked to credit risk in order to gain a higher rate of return. The hybrid financial instrument is remeasured at fair value with changes in fair value reported in earnings. As such, the Company does not bifurcate the embedded derivative from the host contract.

Inventories

Inventories, consisting mainly of telecommunication cables, are stated at the lower of cost (weighted- average cost method) or market value (replacement cost or net realizable value). If the market value is below cost, the Company writes down the inventory to the market value which then becomes the new cost basis.

Long-term Investments

Investments in shares of stock in companies where the Company exercises significant influence over operating and financial policy decisions are accounted for using the equity method of accounting. The difference between the investment cost and the Company's proportionate share in the fair value of the net assets of the investee at the date of acquisition is recognized as equity method goodwill which is not amortized. Any cash dividends received are recognized as a reduction in the carrying value of the investment. Profits and losses arising from equipment purchases from equity investees are eliminated. For other-than-temporary declines in the value of investments accounted for using the equity method, the investment is reduced to its fair value and an impairment loss is recognized.

Investments in shares of stock with no readily determinable market values are accounted for using the cost method when the ownership is less than 20%. Cash dividends received are recorded as income and stock dividends received are accounted for as increases in the number of shares held but not recognized as income.

Property, Plant and Equipment

Property, plant and equipment are stated at cost. Depreciation expense is determined based upon the assets' estimated useful life using the straight-line method.

The estimated useful lives are as follows:

	Useful Life (Years)
Buildings and improvements	10-60
Telecommunications equipment:	
Transmission equipment	9-30
Exchange equipment	5-20
Miscellaneous equipment	3-10

Cost of maintenance and repairs, including the cost of replacing minor items not constituting substantial improvements, is charged to current income.

Gains and losses on the sale or disposal of property, plant and equipment are recorded as costs of revenues.

Valuation of Long-lived Assets

Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable in accordance with Statement of Financial Accounting Standards (“SFAS”) No. 144 “Accounting for the Impairment or Disposal of Long-Lived Assets”. If the total of the expected future cash flows (undiscounted and without interest charges) is less than the carrying amount of the assets, a loss is recognized for the excess of the carrying amount over the fair value of the asset.

3G Concession

3G Concession represents the amount paid by the Company on March 11, 2002 to the ROC government in connection with the grant of a concession to provide various telecommunication services using spectrum assigned by the MOTC that utilizes the International Mobile Telecommunication—2000: The Global Standard for Third Generation Wireless Communications technical standards as announced by the International Telecommunications Union (the “3G concession”). Licenses for 3G mobile telecommunication services are granted by the MOTC through a three-step procedure. Applicants first obtain a concession from the MOTC through a bidding process. The holder of the concession must then obtain a network construction permit from the DGT. Once the network construction is complete, the applicant may apply for a 3G license from the MOTC. The Company received a 3G license from MOTC on May 26, 2005 and commenced operations of the network on the same day. The 3G license is valid through December 31, 2018. The 3G Concession and any additional licensing fees are amortized on a straight-line basis from the date operations commence through the date the license expires. Amortization expense for the years ended December 31, 2005 and 2006 was NT\$447 million and NT\$749 million, respectively.

Patents and Computer Software

Patents are amortized using the straight-line method over the estimated useful lives ranging from 10 to 20 years. Computer software costs are capitalized and amortized using the straight-line method over the estimated useful lives of three years. Amortization expenses for the years ended December 31, 2004, 2005 and 2006 were NT\$166 million, NT\$154 million and NT\$145 million, respectively. Accumulated amortization was NT\$1,133 million and NT\$1,278 million as of December 31, 2005 and 2006, respectively.

Goodwill

Goodwill represents the excess of the cost of an acquisition over the Company’s interest in the net fair value of the identifiable assets, liabilities and contingent liabilities of the entity recognized at the date of acquisition. Goodwill is initially recognized as an asset at cost and is subsequently measured at cost less any accumulated impairment losses. Goodwill is held in the currency of the acquired entity and revalued to the closing rate at each balance sheet date.

Goodwill is not subject to amortization but is tested for impairment in accordance with statement of Financial Accounting Standard (“SFAS”) No. 142, “Goodwill and other Intangible Assets.”

Revenue Recognition

The Company recognizes revenue when they are realized or realizable and earned. Revenues are realized or realizable and earned in accordance with Securities and Exchange Commission, or SEC, Staff Accounting Bulletin No. 104, Revenue Recognition. When the Company has persuasive evidence of an arrangement, the goods have been delivered or the services have been rendered to the customer, the sales price is fixed or determinable and collectibility is reasonably assured.

The following describes the application of that general policy to particular revenue streams.

The Company records service revenues as follows. Usage revenues from fixed-line services, cellular services, internet and data services, and inter-connection 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.

The costs of providing services are recognized as incurred. The cost includes incentives to third party dealers which are payable when the end user enters into an airtime contract.

Deferred income represents one-time connection fees from subscribers and advance received fees of service usage revenues from subscribers and Internet set up fees from enterprises. The deferred income related to one-time connection fees is recognized over the average expected customer service periods showed as follows:

	As of December 31	
	2005	2006
Fixed-line	16	16
Cellular	4	4
Paging	2	2
Internet	4	4

Deferred income related to advance received fees of service usage revenues from subscribers and Internet set up fees from enterprises is recognized as revenues when it is earned and realized or realizable.

The Company expenses the direct cost related to deferred income as incurred.

Where the Company enters into transactions which involve both the provision of air time bundled with products such as 3G data card and handset, 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.

Where the Company sells products to third party cellular phone stores the Company records the direct sale of the products, typically handsets, as gross revenue when the Company is the primary obligor in the arrangement and when title is passed and the products are accepted by the stores. Where the Company also pays the third party cellular phone stores incentives to connect 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.

Concentrations

For all periods presented, no individual customer or supplier constituted more than 10% of the Company's revenues, trade notes and accounts receivables, purchases or trade notes and accounts payable. The Company invests its cash with several high-quality financial institutions. The Company also does not have concentrations of available sources of labor, services or other rights that could, if suddenly eliminated, severely impact its operations. However, telecommunications franchises and licenses are issued solely by authority of the ROC government. The withdrawal or the revocation of the franchise and licenses by the ROC government would severely impact the Company's operations.

Pension Costs

Pension costs are recorded on the basis of actuarial calculations. As a foreign private issuer, the Company adopted SFAS No. 87, "Employers' Accounting for Pensions," on July 1, 1996 as it was not feasible for the Company to obtain the information necessary to adopt SFAS No. 87 as of July 1, 1989. The Company had

allocated a portion of the transition obligation directly to equity on the date of adoption based on the ratio of: (a) the years elapsed between the effective date in SFAS No. 87 and the adoption date, to (b) the remaining service period of employees expected to receive benefits as estimated at the adoption date.

The projected benefit obligation had been determined by actuarial methods based on the related employees' service through the date of privatization. An intangible asset representing the unrecognized net losses and unrecognized transition obligations had been recorded on the balance sheet as deferred pension cost. Such amounts represented an additional minimum pension liability and were recorded as an asset as such costs represent a receivable from the MOTC and was fully realized upon privatization.

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 applied 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, the Company adopted SFAS No. 158, "Employer's Accounting for Defined Benefit Pensions and Other Postretirement Benefits" (SFAS 158). In accordance with this standard, the Company recorded the funded status of its defined benefit pension as an asset or liability on its 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.

The following table shows the effects of adopting SFAS 158 at December 31, 2006 on individual line items in the consolidated balance sheet at December 31, 2006:

	Before Application of SFAS 158 NT\$	Adjustments NT\$	After Application of SFAS 158 NT\$
Deferred income taxes assets, non-current	\$ 3,344	\$ 108	\$ 3,452
Accrued pension liability	1,278	334	1,612
Accumulated other comprehensive income	538	(226)	312
Total stockholders' equity	320,268	(226)	320,042

Advertising and Promotional Expenses

Advertising and promotional expenses are charged to income as incurred. These expenses were NT\$2,526 million, NT\$2,610 million and NT\$2,350 million for the years ended December 31, 2004, 2005 and 2006, respectively.

Research and Development Costs

Research and development costs are charged to income as incurred.

Employee Stock Compensation

The MOTC made an offer to the Company's employees to purchase shares of common stock of the Company at a discount from the quoted market price. The Company records compensation expense for this offer as the difference between the fair value of common stock offered less the amount of the discounted price at the grant date.

Derivative Financial Instruments

The Company enters into forward contracts to reduce its exposure to foreign currency risk and variability in operating results due to fluctuations in exchange rates underlying the value of liabilities denominated in foreign currencies until such liabilities are paid. A forward contract obligates the Company to exchange predetermined amounts of specified foreign currencies at specified exchange rates on specified dates. These



foreign currency forward exchange contracts are denominated in the same currency in which the underlying foreign currency liabilities are denominated and bear a contract value and maturity date that approximate the value and expected settlement date, respectively, of the underlying transactions. Gains and losses on forward contracts and foreign denominated liabilities are included in other income (expense), net.

Derivatives are recognized at fair value and included in either other current liabilities or other current assets on the balance sheet.

Income Tax

The Company is subject to income tax in the ROC. The Company accounts for income tax using the asset and liability method. Under this method, deferred income tax is recognized for losses carried forward and the future tax consequences attributable to differences between financial statement carrying amounts and their respective tax bases, using enacted laws. The Company treats the investment tax credit as a reduction of current income taxes of the year in which the credit arises and defers unutilized tax credit as deferred income tax assets. A valuation allowance is recognized if, based on the weight of available evidence, it is more likely than not that a portion or the entire deferred tax asset will not be realized.

Under ROC tax regulations, the current year's tax-basis earnings that are not distributed in the following year are subject to a 10% additional income tax, however, the tax regulations was amended to change 10% income tax from to tax on tax-basis undistributed earnings to tax on book-basis undistributed earnings in May 2006. This 10% additional income tax is recognized in the period during which the related income is generated. The Company adjusts the amount of accrued undistributed earnings tax after the Company's stockholders approve the distribution of earnings in the following year.

Earnings Per Share and Per Equivalent ADS

Net income per share is computed by dividing net income by the weighted-average number of common shares outstanding during the periods. Net income per equivalent ADS is calculated by multiplying the above net income per share by ten as each ADS represents ten common shares.

Per share data has been restated for all periods presented to reflect the declaration of the stock dividends in 2006.

Comprehensive Income

Comprehensive income includes net income plus the results of certain changes in stockholders' equity during a period from non-owner sources that are not reflected in the statement of operations. Other comprehensive income consists of cumulative translation adjustment, unrealized gain on available-for-sale securities and adjustment to initially apply SFAS No. 158, net of tax, and such amounts were (NT\$3) million, NT\$541 million and (NT\$226) million, respectively, for the year ended December 31, 2006. Under the ROC tax laws, income tax on gains derived from the securities transactions was ceased to be imposed effective beginning after January 1, 1990, at the same time, losses on securities transactions are no longer deductible from income derived from such transactions. As a result, no deferred income tax for unrealized gains or losses on available-for-sale securities has been recorded.

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 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 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. The Company will adopt FIN 48 as of January 1, 2007. 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 financial statements on fiscal years ending after November 15, 2006. Adoption of this guidance did not materially impact on the Company's financial statements.

On February 15, 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.

3. RECLASSIFICATION

Certain accounts of 2004 and 2005 have been reclassified to conform to the 2006 financial statements presentation.

4. U.S. DOLLAR AMOUNTS

The Company maintains its accounts and expresses its consolidated financial statements in the New Taiwan dollars. For convenience only, the U.S. dollar amounts presented in the accompanying consolidated financial statements have been translated at the noon buying rate for cable transfers as certified for customs purposes by the Federal Reserve Bank of New York as of December 31, 2006, which was NT\$32.59 to US\$1.00. The convenience translations should not be construed as representations that the New Taiwan dollar amounts have been, could have been, or could in the future be, converted into U.S. dollars at this or any other rate of exchange.

5. CASH AND CASH EQUIVALENTS

	December 31	
	2005	2006
	NT\$	NT\$
Cash and bank deposits	\$ 2,355	\$ 7,986
Negotiable Certificate of Deposit	10,907	25,751
Commercial paper purchased	28,629	36,936
	<u>\$41,891</u>	<u>\$70,673</u>

6. SHORT-TERM INVESTMENTS

	December 31			
	2005		2006	
	Carrying Amount NT\$	Unrealized Gain (Loss) NT\$	Carrying Amount NT\$	Unrealized Gain (Loss) NT\$
Credit linked investment	\$ 35	\$ —	\$ —	\$ —
Available-for-sale securities				
Open-end mutual funds	13,959	61	5,789	431
Real estate investment trust fund	104	4	179	29
Listed stocks	73	4	983	81
	14,136	69	6,951	541
	<u>\$14,171</u>	<u>\$ 69</u>	<u>\$ 6,951</u>	<u>\$ 541</u>

The Company's gross realized gains and losses on the sale of investments for the year ended December 31, 2006 were NT\$206 million and NT\$81 million, respectively.

The Company entered into investment management agreements with one well-known financial institution (fund managers) to manage its investment portfolios in 2006. In accordance with the investment guidelines and terms specified in these agreements, the securities invested by the fund managers cannot be below a pre-defined credit rating. As of December 31, 2006, the Company's investment portfolios managed by these fund managers aggregated to an original amount of US\$100 million. The investment portfolios included securities such as open-end bond mutual fund, listed stocks and others.

The Company entered into a contract with Citibank Taiwan Branch ("Citibank") to invest NT\$35 million in a credit-linked investment in October 2005. The Company received interest on a quarterly basis commencing from December 2005 through March 2007, the maturity date. In addition to the quarterly interest, Citibank paid an additional amount based on the embedded credit derivative. The embedded credit derivative was linked to credit events of Quanta Display Inc., a Taiwan Stock Exchange listed company. The credit events included bankruptcy, failure to pay certain obligations, acceleration of obligations, repudiation, moratorium and restructuring. If a credit event had occurred on any day prior to the maturity date, Citibank might at its option declare a credit event, designate a cash settlement date and pay the cash settlement amount equal to 30% of the outstanding contract amount to the Company in New Taiwan Dollars. The contract also granted a call provision to Citibank enabling it to early terminate the contract. Following the exercise of the call provision, the Bank paid the Company the terminated contract amount and any accrued interest.

The contract was accounted for as a hybrid financial instrument and remeasured at fair value at the balance sheet date and any gain or loss is charged to income. On January 9, 2006, the Company sold the contract to a third party and recognized an investment loss of NT\$0.2 million.

7. ALLOWANCE FOR DOUBTFUL ACCOUNTS

The changes in the allowance for doubtful accounts are summarized as follows:

	Year Ended December 31		
	2004 NT\$	2005 NT\$	2006 NT\$
Balance, beginning of period	\$ 7,786	\$ 4,473	\$3,626
Provision for doubtful accounts charged to income	1,522	906	623
Accounts receivable written off	(4,835)	(1,774)	(699)
Balance, end of period	<u>\$ 4,473</u>	<u>\$ 3,605</u>	<u>\$3,550</u>

8. INVENTORIES

	December 31	
	2005 NT\$	2006 NT\$
Supplies	\$1,276	\$1,580
Work in process	20	73
Merchandise	—	161
Materials in transit	824	369
	<u>\$2,120</u>	<u>\$2,183</u>

The insurance coverage on inventories as of December 31, 2006 amounted to NT\$1,338 million.

9. LONG-TERM INVESTMENTS

The long-term investments comprise the following:

	December 31			
	2005		2006	
	Carrying Value NT\$	% of Ownership	Carrying Value NT\$	% of Ownership
Equity investees:				
Chunghwa Investment ("CHI")	\$ 950	49	\$ 975	49
Taiwan International Standard Electronics ("TISE")	575	40	609	40
Spring House Entertainment Inc.	—	—	17	30
	<u>1,525</u>		<u>1,601</u>	
Cost investees:				
Taipei Financial Center ("TFC")	1,790	12	1,790	12
iD Branding Ventures ("iDBV")	—	—	75	8
RPTI International ("RPTI")	71	12	71	12
Siemens Telecommunication Systems ("Siemens")	5	15	5	15
3-Link Information Service ("3-Link")	—	—	4	12
	<u>1,866</u>		<u>1,945</u>	
	<u>\$ 3,391</u>		<u>\$ 3,546</u>	

The Company invested Spring House in October, 2006, for a purchase price of NT\$22 million. Spring House engages mainly in internet services.

The Company invested iDBV on November 13, 2006, for a purchase price of NT\$75 million. iDBV engages mainly in investment in companies dealing with brand marketing.

CHI invests in companies engaged in telecom and software businesses. No dividends were declared by CHI for the years ended December 31, 2005 and 2006, respectively.

TISE designs, manufactures and sells telecommunications equipment. It also provides maintenance services on such telecommunications equipment. Dividends of NT\$66 million and NT\$42 million were declared by TISE for the years ended December 31, 2005 and 2006, respectively.

The Company evaluates the investments in TFC, iDBV, RPTI, Siemens and 3-Link for impairment annually. There were no indicators of impairment noted in iDBV, RPTI, Siemens and 3-Link for the years

ended December 31, 2005 and 2006, respectively. In 2005, the Company identified an impairment indicator in TFC and determined the investment in TFC was impaired due to an adverse change in the market condition of the industry in which TFC operates. The Company recognized an impairment loss of NT\$740 million in 2005.

The Company received dividends of NT\$58 million and NT\$29 million from Siemens during the years ended December 31, 2005 and 2006, respectively.

10. INVESTMENT IN PRIVATE MUTUAL FUND

The Company invested NT\$500 million in a private placement fund managed by First Global Investment Trust Company Limited ("FGIT") from September 27, 2005 to September 28, 2008. FGIT, on-behalf of the Company, invested 95% of the total investment principle in a three-year structured time deposit issued by Far Eastern International Bank and invested the rest of the investment principal in a currency swap with Ta Chong Bank. The Company marks to market the private placement fund without distinguishing and presenting the underlying investment assets separately on its balance sheets. This is because the majority of the fair value of the private placement fund is generated from the three-year structured time deposit and the fair value of the currency swap is nominal. On June 28, 2006, the Company sold the private placement fund and recognized an investment loss of NT\$7 million.

11. PROPERTY, PLANT AND EQUIPMENT, NET

	December 31	
	2005 NT\$	2006 NT\$
Cost		
Land	\$ 42,463	\$ 42,483
Buildings and improvements	57,687	59,259
Telecommunications equipment	620,377	629,451
Miscellaneous equipment	27,317	26,666
	<u>747,844</u>	<u>757,859</u>
Accumulated depreciation		
Buildings and improvements	13,235	14,268
Telecommunications equipment	447,888	468,325
Miscellaneous equipment	21,077	21,329
	<u>482,200</u>	<u>503,922</u>
Construction in progress	27,856	23,462
Advances related to acquisition of equipment	25	27
Property, plant and equipment, net	<u>\$293,525</u>	<u>\$277,426</u>

Because of the improvements of telecommunication technology and changes in the market, the paging division is at risk of obsolescence. If the total expected future cash flows (undiscounted and without interest charges) is less than the carrying amount of the assets of paging division, a loss is recognized for the excess of the carrying amount over the fair value. The Company performed an impairment analysis as required by SFAS No. 144 and concluded that the paging division assets were impaired. An impairment loss of NT\$343 million (US\$10 million) was recognized in 2005 and was charged to cost of revenues.

No interest expense was capitalized for the years ended December 31, 2004, 2005 and 2006.

The Company carries insurance on certain buildings and certain telecom equipment with carrying values of NT\$1,796 million and NT\$6,475 million as of December 31, 2005 and 2006, respectively. The Company does not carry comprehensive insurance on all properties.

12. ACCRUED EXPENSES

	December 31	
	2005	2006
	NT\$	NT\$
Accrued compensation	\$10,339	\$12,995
Accrued franchise fees	2,539	2,413
Other accrued expenses	3,132	4,529
	<u>\$16,010</u>	<u>\$19,937</u>

13. OTHER CURRENT LIABILITIES

	December 31	
	2005	2006
	NT\$	NT\$
Amounts collected from subscribers on behalf of other telecommunications companies and carriers	\$ 3,323	\$3,364
Payable to equipment suppliers	4,142	1,661
Payables to construction suppliers	2,406	1,073
Other	2,636	3,246
	<u>\$12,507</u>	<u>\$9,344</u>

14. SHORT-TERM LOANS

	December 31	
	2005	2006
	NT\$	NT\$
Bank loans—annual yield rate—2.955%	<u>\$ —</u>	<u>\$126</u>

15. LONG-TERM LOANS (INCLUDING CURRENT PORTION OF LONG-TERM LOANS)

	December 31	
	2005	2006
	NT\$	NT\$
Loan from the Fixed-Line Fund	\$500	\$ 300
Bank loans—annual yield rate—3.05%	—	23
	500	323
Less: Current portion of long-term loans	200	323
	<u>\$300</u>	<u>\$ —</u>

The loan from the Fixed-Line Fund was obtained pursuant to a long-term loan agreement with the Fixed-Line Fund managed by the Ministry of Interior that allows the Company to obtain unsecured interest-free credit up to the original amount contributed to the fund. The outstanding principal is carried at its



undiscounted amount and is payable in three annual installments (NT\$200 million, NT\$200 million and NT\$300 million) starting on March 12, 2005 until March 12, 2007.

CHIEF obtained a secured loan from Chinatrust Commercial Bank. Interest and principal are payable monthly and the secured loan is due by November 18, 2007.

As of December 31, 2006, the Company has unused credit line of approximately NT\$31,924 million, which are available for short-term and long-term borrowings.

16. STOCKHOLDERS' EQUITY

Under the Company's Articles of Incorporation revised on May 30, 2006, the Company's authorized capital is NT\$120,000,000,020. The Company's Articles of Incorporation and the Republic of China Telecommunications Act provide that the MOTC has the right to purchase two redeemable preferred shares at NT\$10 (par value) in the event its ownership of the Company falls below 50% of the outstanding common shares. On March 28, 2006, the board of directors approved the issuance of the 2 preferred shares, and the MOTC purchased the 2 preferred shares at par value on April 4, 2006.

The MOTC, as the holder of those preferred shares is entitled to the same rights as holders of common shares and certain additional rights as specified in the Company's Articles of Incorporation as follows:

- a. The holder of the preferred shares, or its nominated representative, will act as a director and/or supervisor during the entire period in which the preferred shares are outstanding.
- b. The holder of preferred shares has the same pre-emptive rights as holders of common shares when the Company raises capital by issuing new shares.
- c. The holder of the preferred shares will have the right to veto on any change in the name of the Company or the nature of its business and any transfer of a substantial portion of the Company's business or property.
- d. The holder of the preferred shares may not transfer the ownership. The Company must redeem all outstanding preferred shares within three years from the date of their issuance.

As the preferred shares are mandatory redeemable in 2009, the shares are classified as other long-term liabilities. The redemption value of preferred shares is NT\$20.

For the purpose of privatizing the Company, the MOTC sold 1,109,750 thousand common shares of the Company in an international offering of securities in the form of ADS amounting to 110,975 thousand units (one ADS represents ten common shares) on the New York Stock Exchange on July 17, 2003. Subsequently, the MOTC sold 1,350,682 thousand common shares in the form of ADS amounting to 135,068 thousand units on August 10, 2005. Afterwards, the MOTC and Taiwan Mobile Co., Ltd sold 505,389 thousand and 58,959 thousand common shares of the Company, respectively, to third parties in the form of ADS amounting to 56,435 thousand units in total on October 4, 2006. As of December 31, 2006, the MOTC and Taiwan Mobile Co., Ltd. have sold 3,024,780 thousand common shares in the form of ADS amounting to 302,478 thousand units.

The ADS holders generally have the same rights and obligations as other common stockholders, subject to the provision of relevant laws. The exercise of such rights and obligations shall comply with the related regulations and deposit agreement, which stipulate, among other things, that ADS holders can, through deposit agents, exercise their voting rights, sell their ADSs, and receive dividends declared and subscribe to the issuance of new shares.

As of December 31, 2005 and December 31, 2006, the outstanding ADSs were 246,043 thousand units and 307,399 thousand units (including stock dividends), which equaled approximately 2,460,431 thousand and 3,073,988 thousand common shares and represented 25.50% and 31.8% of the Company's total outstanding common shares, respectively.

Under the ROC Company Law, capital surplus may only be utilized to offset deficits or be declared as stock dividends. Also, such capital surplus can only be declared as a stock dividend by the Company at an amount calculated in accordance with the provisions of existing regulations.

In addition, before distributing a dividend or making any other distribution to stockholders, the Company must pay all outstanding taxes, recover any past losses and set aside a legal reserve equal to 10% of its net income, and depending on its business needs or requirements, may also set aside a special reserve. In accordance with the Articles of Incorporation, no less than 50% of the earnings comprising remaining balance of net income, if any, plus cumulative undistributed earnings, shall be distributed in the following:

- a. From 2% to 5% of distributable earnings shall be distributed to employees as employee bonus.
- b. No more than 0.2% of distributable earnings shall be distributed to board of directors and supervisors as remuneration in the following years after privatization.
- c. Cash dividends to be distributed shall not be less than 50% of the total amount of dividends to be distributed.

During the year of privatization, the distributable earnings are limited to the earnings generated after privatization. The remaining distributable earnings can be distributed to the stockholders based on the resolution of stockholders' meeting.

If cash dividends to be distributed is less than NT\$0.10 per share, such cash dividend shall be distributed in the form of common shares.

Under the ROC Company Law, the appropriation for legal reserve shall be made until the accumulated reserve equals the aggregate par value of the outstanding capital stock of the Company. This reserve can only be used to offset a deficit, or when reaching 50% of the aggregate par value of the outstanding capital stock of the Company, up to 50% of the reserve may, at the option of the Company, be declared as a stock dividend and transferred to capital.

The appropriations and distributions of the 2005 earnings of the Company have been approved and resolved by the stockholders on May 30, 2006 as follows:

	<u>Amount</u> <u>NT\$</u>
Legal reserve	\$ 4,765
Cash dividends—NT\$4.3 per share	40,660
Stock dividends—NT\$0.2 per share	1,891
Employee bonus—cash	230
Employee bonus—stock (at par value)	230
Remuneration to board of directors and supervisors	15
	<u>\$47,791</u>

The amount of compensation expense related to employee stock bonus is determined based on the market value of the Company's common stock at the date of approval of distribution by the shareholders on May 30, 2006. For the year ended December 31, 2006, the compensation expense related to employee stock bonus was NT\$1,151 million in addition to NT\$230 million which had been recognized in prior year.

17. EMPLOYEE STOCK COMPENSATION

The MOTC provided employees with two stock purchase plans: The market discount plan and the par value plan.

Market discount plan—under the market discount plan, the MOTC sold shares of stock at discounted prices to employees at various times from October 2000 to September 2005. The employees purchased the



common shares at discounts of 10% and 20% and 50% from the quoted market price in consideration for their commitment to hold the common shares for two, three and four years (the “holding periods”), respectively. The common shares are held by an escrow agent on behalf of the employees/stockholders. There are no circumstances under which the MOTC or the Company would be required to repurchase these common shares. Also, the employees are not required to remain employed with the Company during the duration of the holding periods. The Company recognized nil and NT\$12,542 million as compensation expense for the discounted shares purchased by employees for the years ended December 31, 2004, and 2005, respectively. There were no market discount plan offerings during the year ended December 31, 2006.

Par value plan—under the par value plan, the MOTC sold shares of stock to employees at par value (NT\$10). The difference between the market price of the stock on the offering dates and the par value was recognized as compensation expense. The total shares sold to employees by the MOTC for the year ended December 31, 2005 and 2006 were 4,126,928 shares and 10,411,955 shares, respectively. The MOTC received total proceeds of NT\$41 million and NT\$104 million for the years ended December 31, 2005 and 2006, respectively, from these sales.

The Company recognized NT\$457 million, NT\$228 million and NT\$503 million as compensation expense for the discounted shares purchased by employees under the par value plan for the years ended December 31, 2004, 2005 and 2006, respectively.

The basic earnings per share were reduced NT\$0.05, NT\$1.30 and NT\$0.05 for years ended December 31, 2004, 2005 and 2006, respectively, after the Company recognized the aforementioned compensation expenses under market discount plan and par value plan. There was no income tax benefit recognized in the statement of operation for share-based compensation arrangements and there was no effect on the statements of cash flow.

18. PENSION PLAN

At the time of its incorporation on July 1, 1996, the Company continued the existing two noncontributory defined benefit pension plans covering all its employees, as previously adopted by the DGT. The first plan (hereinafter referred to as “Plan A”) covered civil service eligible employees (i.e., employees who meet the necessary qualifications set by the ROC Government) and the second plan (hereinafter referred to as “Plan B”) covered all other employees of the Company (hereinafter referred to as “non-civil service eligible employees”). The adoption of two pension plans was necessary as different pension laws apply to civil service eligible and non-civil service eligible employees.

Plan A provided benefits equal to the sum of: (a) the lump-sum payment equivalent to one benefit unit per year for the first twenty service years rendered and one-half benefit unit per service year rendered thereafter, with one benefit unit equivalent to a portion of the salary of the employee at the time of retirement (referred to hereinafter as “pensionable salary”), and (b) annuity payments payable monthly equivalent to a certain percentage of the benefit unit. Plan B provided benefits equal to the lesser of: (a) forty-five benefit units, or (b) two benefit units per service year rendered for the first fifteen years, and one-half benefit unit per service year exceeding fifteen years rendered before August 1, 1984 and one benefit unit per service year for services rendered after August 1, 1984, with one benefit unit equivalent to the monthly average base salary (consisting of regular salary items plus overtime salary). Plan A was funded based on amounts included in budgets approved by the Legislative Yuan and supplementary budgets approved by the Executive Yuan while Plan B was funded by the Company at an amount equivalent to 2% to 15% of the monthly salary.

The Company adopted SFAS No. 87 on July 1, 1996 (adoption date), the date of its incorporation. The unrecognized net transition obligation recorded to stockholders’ equity on July 1, 1996 was NT\$6,571 million which represents the difference in the net pension cost for the period from the issuance of SFAS No. 87 and the date of adoption. The remaining unrecognized net transition obligation of NT\$16,790 million is amortized over the estimated remaining service period of the employees as determined on July 1, 1996, which is a period of twenty-five years for civil service eligible employees and seventeen years for non-civil service eligible employees.

As required by the ROC Government for state-owned enterprises instructed to undergo privatization plans effective on the privatization date, except for those employees who reached the mandatory retirement age (the age of 65 for Plan A participants and age 60 for Plan B participants) by that day, employees received pension benefit payments calculated in accordance with the Guidelines on Payments of Severance Benefits to Employees of State-Owned Enterprises ("Guidelines").

Under the Guidelines, on the privatization date, settlement benefit payments were distributed to both Plan A and Plan B participants as follows: (a) employees who voluntarily left the Company on the privatization date (hereinafter referred to as "separated employees") received a service clearance payment which is calculated similar to the benefit formula under the original Plan B as mentioned above plus an additional six-month salary and one-month advance notice pay (hereinafter referred to as the "additional separation payments"); and (b) employees who opted to remain with the privatized company after the privatization date (hereinafter referred to as "privatized company employees") would receive an amount equivalent to those received by the separated employees without the additional separation payments. Privatized company employees who are involuntarily terminated by the Company within five years from the date of privatization (hereinafter referred to as "redundant employees") will receive redundancy benefits equivalent to the pension amount as computed based on one benefit unit for every year of service after privatization plus the additional separation payments (hereinafter referred to as "redundancy benefit payments"). The six-month portion of the additional separation payments was paid by the MOTC. The accrued pension amount after privatization and the one-month advance notice pay were paid by the Company.

The unrecognized prior service costs, which amounted to NT\$30,018 million, related to the increased benefits provided under the Guidelines described in the preceding paragraph were amortized through June 30, 2001. The unrecognized prior service costs excluded any costs expected to be incurred for the additional separation payments or redundancy benefit payments. The additional separation payments under the Guidelines were accounted for as special termination benefits and were recognized in the period when the employee accepted the offer while the redundancy benefit payments will be recognized in the period management approves a plan of termination.

In order to increase operational efficiency, the Company approved a Special Retirement Incentive Program ("Program A"). Program A allowed eligible employees who voluntarily left the Company on February 1, 2005 to receive benefit payments based on the respective original plan (meaning Plan A or Plan B) plus the additional separation payments. The present value of such amount over and above the lump sum amount was NT\$821 million and was accounted for as special termination benefits in the statement of income for the year ended December 31, 2005. A portion of the Program A benefits amounting to NT\$243 million were recognized in 2004 when employees formally accepted the terms of Program A.

In order to provide employees with additional consideration, the Company approved another Special Retirement Incentive Program ("Program B") in May 2005. Program B allowed eligible employees who voluntarily left the Company on August 11, 2005, the day before privatization, to also receive benefit payments based on the respective original plan (meaning Plan A or Plan B) plus the additional separation payments. The present value of such amount over and above the lump sum amount was NT\$1,325 million and was accounted for as special termination benefits in the statement of income for the year ended December 31, 2005.

The Company also approved another Special Retirement Incentive Program ("Program C") in December 2005. Program C allowed eligible employees who voluntarily applied to leave the Company from March 1 to March 31, 2006 to also receive benefit payments based on the respective original plan plus the additional separation payments. The approval procedure took up to 15 days after applications were submitted therefore, if employees applied for the voluntary retirement on March 31, 2006, they were eligible to retire from the Company on or before April 14, 2006. The present value of such amount over and above the lump sum amount that would have been paid to the eligible employees was accounted for as special termination benefits. Accordingly, such benefits were recognized as a liability and charged to income when employees formally accepted the terms of Program C. The Company recognized expense of NT\$2,302 million for Program C during 2006. The New Plan B vested benefit obligations for the majority of the employees



electing Program C were settled; the remaining employees have accumulated benefits under New Plan B but were not eligible to receive the benefits and the election of Program C terminated their employment earlier than expected, thereby reducing their expected years of future service.

Under applicable ROC regulations, upon the privatization, the obligation related to annuity payments due after the date of privatization for civil serve eligible employees who retire prior to that date would be born by the MOTC. The Company completed its privatization plan on August 12, 2005. On the date of privatization, the MOTC settled all employees' past service costs. The portion of the pension obligations that was settled by the MOTC, represented by the difference between the accrued pension liabilities and the deferred pension cost and related deferred income tax assets and was accounted for as contributed capital and recorded in stockholders' equity as of August 12, 2005. The non-cash financing activities and related amounts of the pension obligation settlement as of the date of privatization are disclosed on the face of the statement of cash flows.

Upon privatization, the MOTC settled all accrued pension obligations for Plan A and Plan B including service clearance payment, lump sum payment under civil plan, additional separation payments, and other related obligations upon the completion of the privatization in accordance with the Statute Governing Privatization of Stated-Owned Enterprises. After paying all pension obligations for privatization, the plan assets will be transferred to the Fund for Privatization of Government-owned Enterprises (the "Privatization Fund") under the Executive Yuan. According to the instructions of MOTC, the Company has been requested to administer the distributions to employees for pension obligations including service clearance payment, lump sum payment under civil service plan, additional separation payments, and other related obligations upon the completion of the privatization on the MOTC's behalf acting as the MOTC's agent merely in an administrative capacity with no rights or duties received or owed for a six-month transition period. In August 2006, CHT transferred the remaining funds to be disbursed to employees to the Privatization Fund.

Upon privatization and settlement of the related obligations, Plan A and Plan B ceased to exist. A new plan ("New Plan B"), having similar terms and benefits as Plan B, was established and offered to employees. Employees choosing to enter into New Plan B were not credited with any prior service nor did they receive any accumulated benefits from prior service and benefits begin to accrue to them under this plan commencing from the privatization date. The components of net periodic benefit costs before privatization are for both Plan A and Plan B. The effect of privatization relates to both Plan A and Plan B. The amounts of plan assets remaining after privatization and the components of net periodic benefit costs after privatization relate to New Plan B.

The Company's subsidiary—CHIEF Telecom has its own pension plan, which is similar to New Plan B of the Company.

Before Privatization

The components of net periodic benefit costs are as follows:

	Year Ended December 31, 2004 NT\$	Period Ended August 12, 2005 NT\$
Service cost	\$ 1,943	\$ 1,253
Interest cost	1,887	1,232
Expected return on plan assets	(1,226)	(798)
Termination benefit under the Program A	243	—
Amortization of unrecognized net transition obligation	939	575
Amortization of unrecognized net loss	907	996
Net periodic benefit pension cost	<u>\$ 4,693</u>	<u>\$ 3,258</u>

The changes in benefits obligation and plan assets and the reconciliation of funded status are as follows:

	Year Ended December 31, 2004 NT\$	Period Ended August 12, 2005 NT\$
Change in benefits obligation:		
Projected benefits obligation, beginning of year	\$ (126,126)	\$ (134,911)
Services cost	(1,943)	(1,253)
Interest cost	(1,887)	(1,232)
Termination benefit under the Program A	(243)	—
Actuarial gain (loss)	(8,038)	2,294
Benefits paid	3,326	2,126
Projected benefits obligation, end of period	<u>\$ (134,911)</u>	<u>\$ (132,976)</u>
Change in plan assets:		
Fair value of plan assets, beginning of year	\$ 82,578	\$ 85,870
Actual return on plan assets	696	441
Employer contributions	5,922	2,956
Benefits paid	(3,326)	(2,126)
Fair value of plan assets, end of period	<u>\$ 85,870</u>	<u>\$ 87,141</u>
Reconciliation of funded status:		
Funded status	\$ (49,041)	\$ (45,835)
Unrecognized net transition obligation	8,811	8,237
Unrecognized actuarial loss	29,200	26,267
Net amount recognized	<u>\$ (11,030)</u>	<u>\$ (11,331)</u>
The weighted-average asset allocations by asset category are:		
Time deposit	85%	
Short-term notes	15%	
	<u>100%</u>	

(Concluded)

The target asset allocations are established through an investment policy established by the Chunghwa Telecom's Employee Pension Fund Committee and agreed to by the Ministry of Finance ("MOF"). As increased liquidity of the fund is necessary due to the privatization of the Company, the current policy for plan assets is to place funds in time deposit accounts of the financial and postal institutions, non-designated trust funds in an investing company or financial institution and government bonds. In addition, the pension fund may invest in beneficial certificates of equity securities.

Effect of Privatization

	Before Privatization NT\$	Effect of Privatization NT\$	After Privatization NT\$
Projected benefits obligation	\$ (132,976)	\$ 132,976	\$ —
Plan assets at fair value	87,141	(86,061)	1,080
Funded status	(45,835)	46,915	1,080
Unrecognized net transition obligation	8,237	(8,237)	—
Unrecognized net loss	26,267	(26,267)	—
Net amount recognized	<u>\$ (11,331)</u>	<u>\$ 12,411</u>	<u>\$ 1,080</u>

The plan assets and net period benefit costs after privatization represent those assets and costs of New Plan B.

After Privatization

The components of net periodic benefit costs of New Plan B for the period from August 13, 2005 through December 31, 2005, and of New Plan B and the pension plan of subsidiary as of December 31, 2006 are as follows:

	Period from August 13 to December 31, 2005	Year Ended December 31, 2006
	NT\$	NT\$
Service cost	\$ 1,192	\$ 3,073
Interest cost	—	59
Expected return on plan assets	(14)	(66)
Amortization of unrecognized net loss	—	45
Curtailment/settlement loss to be recognized	—	161
Net periodic benefit pension cost	<u>\$ 1,178</u>	<u>\$ 3,272</u>

The changes in benefits obligation and plan assets and the reconciliation of funded status for New Plan B and the pension plan of subsidiary are as follows:

	Period from August 13 to December 31, 2005	Year Ended December 31, 2006
	NT\$	NT\$
Change in benefits obligation:		
Projected benefits obligation, beginning of year	\$ —	\$ (1,683)
Services cost	(1,192)	(3,073)
Interest cost	—	(59)
Curtailment/settlement effect	—	270
Actuarial (loss) gain	(501)	19
Benefits paid	10	6
Impact on acquisition of subsidiary	—	(14)
Projected benefits obligation, end of year	<u>\$ (1,683)</u>	<u>\$ (4,534)</u>
Change in plan assets:		
Fair value of plan assets, beginning of year	\$ 1,080	\$ 1,637
Actual return on plan assets	(18)	66
Employer contributions	585	1,544
Benefits paid—settlement	—	(326)
Benefits paid	(10)	(6)
Impact on acquisition of subsidiary	—	7
Fair value of plan assets, end of year	<u>\$ 1,637</u>	<u>\$ 2,922</u>

(Continued)

	Period from August 13 to December 31, 2005 NT\$	Year Ended December 31, 2006 NT\$
Reconciliation of funded status		
Funded status	\$ (46)	\$ (1,612)
Unrecognized actuarial loss	504	—
Net amount recognized—prepaid current asset (liability)	<u>\$ 458</u>	<u>\$ (1,612)</u>
Amounts recognized in accumulated other comprehensive income		
Net actuarial loss, pretax		\$ 334
Deferred tax asset		(108)
Net impact in accumulated other comprehensive loss		<u>\$ 226</u>
The weighted-average asset allocations by assets category are:		
Time deposit	49%	45%
Short-term notes	33%	27%
Taiwan government securities and loans	18%	28%
	<u>100%</u>	<u>100%</u>

(Concluded)

The amounts recognized in the accompanying balance sheets at December 31 are as follows:

	Year Ended December 31	
	2005 NT\$	2006 NT\$
Amounts recognized		
Accrued pension liability	\$ —	\$1,612
Intangible assets—deferred pension cost	—	—
Net amount recognized	<u>\$ —</u>	<u>\$1,612</u>
Prepaid pension (included in other current assets)	<u>\$ 458</u>	<u>\$ —</u>

Actuarial assumptions:

	Before Privatization	After Privatization
<i>Year ended December 31, 2004</i>		
Discount rate used in determining present value	1.50%	—
Rate of compensation increase		
All employees	3.50%	—
Annuity increase for retirees	3.00%	—
Rate of return on plan assets		
Plan A	1.50%	—
Plan B	1.50%	—

(Continued)



	Before Privatization	After Privatization
<i>Year ended December 31, 2005</i>		
Discount rate used in determining present value	—	2.25%
Rate of compensation increase—all employees	—	2.00%
Rate of return on plan assets—all employees		3.00%
<i>Year ended December 31, 2006</i>		
Discount rate used in determining present value	—	2.00-2.75%
Rate of compensation increase—all employees	—	1.50-3.00%
Rate of return on plan assets—all employees		2.75-3.00%

(Concluded)

The Labor Pension Act of ROC (“Act”) was effective beginning July 1, 2005 and this pension mechanism was considered as a defined contribution plan. The employees who were subject to the Labor Standards Law prior to the enactment of the Act may choose to be subject to the pension mechanism under the Act or continue to remain subject to the pension mechanism under the Labor Standards Law. For those employees who were subject to the Labor Standards Law prior to July 1, 2005 and still work for the same company after July 1, 2005 and choose to be subject to the pension mechanism under the Act, their seniority as of July 1, 2005 shall be maintained. The rate of contribution by an employer to the Labor Pension Fund per month shall not be less than 6% of each employee’s monthly salary or wage. The Company has contributed 6% of each employee’s monthly salary per month beginning July 1, 2005. For the year ended December 31, 2005 and 2006, total contributions were NT\$16 million (US\$0.49 million) and NT\$67 million (US\$2.06 million), respectively.

19. INCOME TAXES

The components of income taxes are as follows:

	Year Ended December 31		
	2004	2005	2006
	NT\$	NT\$	NT\$
Current	\$11,102	\$ 3,044	\$13,875
Deferred	157	9,689	1,406
	<u>\$11,259</u>	<u>\$12,733</u>	<u>\$15,281</u>

A reconciliation between income tax expense computed by applying the statutory income tax rate of 25% to income before income tax and income tax expense shown in the statements of operations and comprehensive income is as follows:

	Year Ended December 31		
	2004	2005	2006
	NT\$	NT\$	NT\$
Income tax expense computed at statutory tax rate	\$15,544	\$11,508	\$14,335
Permanent differences	(65)	3,158	149
Investment tax credits	(3,379)	(1,987)	(3,093)
10% undistributed earning tax	—	979	3,942
Prior year adjustment	49	(5)	(979)
Other	(890)	(920)	927
Income tax expense	<u>\$11,259</u>	<u>\$12,733</u>	<u>\$15,281</u>

The balance of income tax payable as of December 31, 2006 was shown net of prepaid income tax. Tax refund receivable and income tax payable as of December 31, 2005 were NT\$4,338 million (included in other current assets) and NT\$997 million, respectively.

Permanent differences consist primarily of tax-exempt income from the sale of available-for-sale securities, interest income on commercial paper purchased, which are subject to a separate income tax rate of 20% and employees stock compensation expense.

Deferred income taxes arise due to temporary differences in the book and tax bases of certain assets and liabilities. Significant components of deferred income tax assets (liabilities) are shown in the following table:

	December 31	
	2005 NT\$	2006 NT\$
Current:		
Provision for doubtful accounts	\$ 234	\$ —
Deferred income	1,039	1,227
Accrued pension costs	1,772	—
Investment tax credits	554	—
Other, net	1,202	84
	<u>4,801</u>	<u>1,311</u>
Non-current:		
Deferred income	2,541	2,837
Effect on application of SFAS 158	—	108
Other	1,136	582
	<u>3,677</u>	<u>3,527</u>
Less— valuation allowance	<u>2,499</u>	<u>110</u>
	<u>\$5,979</u>	<u>\$4,728</u>

Upon the completion of the privatization, a significant portion of the deferred income tax assets related to accrued pension costs was reversed due to the settlement of the related pension obligations.

The above deferred income tax assets were computed based on a tax rate of 25% in 2005 and 22.5% in 2006. Before privatization, the Company had been required by government regulations to distribute all earnings to ROC governments within six months subsequent to year-end and it had required a minimal amount of tax under this regulation; therefore the Company's earnings are not subject to 10% undistributed earnings tax; however, after privatization, the Company does not have to distribute earnings to government so the Company begins to be subject to 10% undistributed earnings tax from 2006. In addition, the basis of 10% undistributed earnings tax was amended from tax-basis undistributed earnings to book-basis undistributed earnings in May 2006. As such, the tax rate applied to temporary difference has been changed.

20. TRANSACTIONS WITH RELATED PARTIES

As the Company was a state-owned enterprise, the ROC Government is one of the Company's customers. The Company provides Fixed-line services, wireless services, Internet and other services to the various departments and agencies of the ROC Government and other state-owned enterprises in the normal course of business and at arm's-length prices before and after privatization. The information on service revenues from government bodies and related organizations have not been provided because the aforementioned transactions were not summarized by the Company. The Company believes that all costs of doing business are reflected in the financial statements and that no additional expenditures would be incurred as a result of the privatization being completed.



- a. The Company engages in business transactions with the following related parties:

Company	Relationship
Taiwan International Standard Electronics ("TISE")	Equity investee
Chunghwa System Integration ("CSI")	Subsidiary of CHI
Chunghwa Precision Test Technical Co., Ltd. ("CHPT")	Subsidiary of CHI
Chunghwa Telecom Global, Inc. ("CHTG")	Subsidiary of CHI
Tai, Zhong-He	Former chairman of CHIEF (resigned on September 6, 2006); as a current member of the board of directors of CHIEF.

- b. Significant transactions with the above related parties are summarized as follows:

	December 31			
	2005		2006	
	Amount NT\$	%	Amount NT\$	%
1) Receivables				
Trade notes and accounts receivable				
CHTG	\$ 49	—	\$ 44	—
CHPT	21	—	—	—
	<u>\$ 70</u>	<u>—</u>	<u>\$ 44</u>	<u>—</u>
2) Payables				
Trade notes and accounts payable				
TISE	\$ 41	—	\$ 202	2
CSI	55	1	192	2
CHTG	28	—	18	—
	<u>\$ 124</u>	<u>1</u>	<u>\$ 412</u>	<u>4</u>
Accrued expenses				
TISE	\$ 49	—	\$ 92	—
CHTG	11	—	19	—
CSI	27	—	1	—
	<u>\$ 87</u>	<u>—</u>	<u>\$ 112</u>	<u>—</u>
Payable to construction supplier (included in "other current liabilities")				
TISE	\$ 319	2	\$ 345	3
CSI	22	—	13	—
	<u>\$ 341</u>	<u>2</u>	<u>\$ 358</u>	<u>3</u>
3) Other payables (included in other current liabilities)				
Tai, Zhong-He	\$ —	—	\$ 20	—

(Continued)

	December 31			
	2005		2006	
	Amount NT\$	%	Amount NT\$	%
4) Revenues				
CHTG	\$ 101	—	\$ 95	—
CHPT	25	—	14	—
	<u>\$ 126</u>	<u>—</u>	<u>\$ 109</u>	<u>—</u>
5) Cost of revenues				
TISE	\$ 135	—	\$ 374	—
CSI	89	—	306	—
CHTG	81	—	101	—
	<u>\$ 305</u>	<u>—</u>	<u>\$ 781</u>	<u>—</u>
6) Acquisition of equipments				
TISE	\$ 478	2	\$ 920	3
CSI	316	1	283	1
CHTG	13	—	1	—
	<u>\$ 807</u>	<u>3</u>	<u>\$ 1,204</u>	<u>4</u>

The foregoing terms were conducted as arm's length transactions except for other payable to Tai, Zhong-He. In 2005, CHIEF agreed to provide compensation to 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 as collateral and was calculated at an interest rate below 5%.

21. COMMITMENTS AND CONTINGENCIES

As of December 31, 2006, the Company has commitments under non-cancelable contracts with various parties as follows:

(a) acquisitions of land and buildings of NT\$1,575 million, and (b) acquisitions of telecommunications equipment of NT\$15,479 million.

The Company also has non-cancelable operating leases covering certain buildings, computers, computer peripheral equipment and operating system software under contracts that expire in various years. Minimum rental commitments under those leases are as follows:

	December 31, 2006 NT\$
Within the following year	\$ 1,234
During the second year	870
During the third year	611
During the fourth year	276
During the fifth year and thereafter	131
	<u>\$ 3,122</u>

As of December 31, 2006, the Company had unused letters of credit of NT\$1,364 million.



As a part of the government's effort to upgrade the existing telecommunication infrastructures, the Company and other public utility companies were required by the ROC government to contribute a total of NT\$4,500 million to funds called the Fixed-Line Fund and the Piping Fund (collectively referred to as the "funds"). Under the Fixed-Line Fund, the Company contributed NT\$1,000 million to the fund, administered by the ROC Ministry of Interior Affairs, on June 30, 1995. Under the Piping Fund, the Company contributed NT\$1,000 million to the fund, administered by the Taipei City Government, on August 15, 1996. Both contributions were accounted for by the Company as "other assets—other" on the Company's balance sheets.

Through the use of the Funds, the governmental agencies will construct new underground fixed-lines and conduits and perform on-going maintenance operations. Currently, a portion of the fixed-lines and conduits are constructed and ready to be used. If the contributions to the funds were 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 funds and the amounts of such contributions from each party.

The Company understands that (a) upon completion of the projects, the Company will receive a proportionate legal interest in the assets; or (b) if the projects are incomplete upon dissolution of the funds, the Company will receive its money back. No expiration or dissolution date is specified in the related documents.

22. SUBSEQUENT EVENTS

On January 8, 2007, the Company acquired 31.5% shares of SENAO International Co., Ltd. ("SENAO") totaled 70,373 thousand common shares by tender offer at purchase price of NT\$15.1 per share, for NT\$1,063 million thousand. The main business of SENAO is to provide sales of telecommunication facilities and software services. The Company is in the process of evaluating the accounting treatment for this investment.

23. LITIGATION

A portion of the land used by the Company during the period July 1, 1996 to December 31, 2004 was co-owned by the Company and Taiwan Post Co., Ltd. (the former Chunghwa Post Co., Ltd, Directorate General of Postal Service). In accordance with the claims process in Taiwan, on July 12, 2005, the Taiwan Taipei District Court sent a claim notice to the Company to reimburse Taiwan Post Co., Ltd. in the amount of NT\$768 million for land usage compensation due to the portion of land usage area in excess of the Company's ownership, along with interest calculated at 5% interest rate from June 30, 2005 to the payment date. However, the Company believes that the computation used to derive the land usage compensation amount is inaccurate because most of the compensation amount has expired as result of the expiration clause. Therefore, the Company has filed an appeal at the Taiwan Taipei District court. As of March 13, 2007, the case is still in the procedure of the first instance at the Taiwan Taipei District Court. While the Company cannot make any assurance regarding the eventual resolution of the litigation, the Company does not believe the final outcome will have a material adverse effect on its results of operations or financial condition. As of December 31, 2006, no provision was provided for the litigation.

The Company is involved in various legal proceedings of a nature considered normal to its business. It is the Company's policy to accrue for amounts related to these legal matters when it is probable that a liability has been incurred and the amount is reasonably estimable.

The Company believes that the various asserted claims and litigation in which it is involved will not materially affect its financial position, future operating results or cash flows, although no assurance can be given with respect to the ultimate outcome of any such claim or litigation.

24. INFORMATION ON FINANCIAL INSTRUMENTS

a. Derivative financial instruments

The Company entered into forward exchange contracts and index future contracts to reduce its exposure to foreign currency risk and variability in operating results due to fluctuations in exchange rates underlying the value of assets denominated in foreign currencies until such assets are received and fluctuations in stock prices. The Company engaged in foreign currency forward exchange contracts and index future contracts during the year ended December 31, 2006. Net losses arising from derivative financial instruments for the year ended December 31, 2006 were NT\$52 million (including realized settlement losses of NT\$32 million and valuation losses of NT\$20 million).

Outstanding forward exchange contracts as of December 31, 2006:

	Currency	Holding Period	Contract Amount (in Million)
<i>December 31, 2006</i>			
Sell	JPY/USD	2006.11-2007.01	JPY 490
	EUR/USD	2006.11-2007.01	EUR 7
	GBP/USD	2006.11-2007.01	GBP 2

Outstanding index future contracts as of December 31, 2006:

	Maturity Date	Units	Contract Amount (in Million)
<i>December 31, 2006</i>			
Index future contracts			
AMSTERDAM IDX FUT	2007.01	8	EUR 1
CAC40 10 EURO FUT	2007.01	45	EUR 2
DAX INDEX FUTURE	2007.03	11	EUR 2
IBEX 35 INDEX FUTR	2007.01	7	EUR 1
MINI S&P/MIB FUT	2007.03	23	EUR 1
FTSE 100 IDX FUT	2007.03	33	GBP 2
TOPIX INDEX FUTURE	2007.03	32	JPY 513
S&P 500 FUTURE	2007.03	23	USD 8
S&P 500 EMINI FUTURE	2007.03	13	USD 1

- b. Non-derivative financial instruments are as follows:

	December 31, 2005		December 31, 2006	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
	NT\$	NT\$	NT\$	NT\$
Assets				
Cash and cash equivalents	\$41,891	\$41,891	\$70,673	\$70,673
Short-term investments	14,171	14,171	6,951	6,951
Long-term Investments for which it is:				
— Practicable to estimate fair value	1,790	1,790	—	—
— Not practicable	76	—	1,945	1,945
Refundable deposits (included in “other assets — other”)	3,577	3,577	3,545	3,545
Liabilities				
Short-term loans	—	—	126	126
Customers’ deposits	7,392	6,169	6,654	5,641
Long-term loans (including current portion of long-term loans)	500	500	323	323

The following methods and assumptions were used to estimate the fair value of each class of financial instruments for which it is practicable to estimate that value:

- Cash and cash equivalents, trading account assets and liabilities, and short-term investments—the carrying amounts approximate fair values because of the short maturity of those instruments.
- Long-term investments—the fair values of some investments are estimated based on quoted market prices for those or similar investments. For other investments for which there are no quoted market prices, a reasonable estimate of fair value could not be made without incurring excessive costs. Additional information pertinent to the value of an unquoted investment is provided above.
- Refundable deposits—the carrying amounts approximate fair values as the carrying amounts are the amount receivable on demand at the reporting date.
- Customers’ deposits—the fair value is the discounted value based on projected cash flows. The projected cash flows were discounted using the average expected customer service periods.
- Short-term loans and long-term loans (including current portion)—the fair value is based on the current rates offered to the Company for debt of the same remaining maturities.

25. SEGMENT REPORTING

Operating segments are defined as components of an enterprise regarding which separate financial information is available for regular evaluation by the chief operating decision maker, or decision making group, in deciding how to allocate resources and in assessing performance.

The Company organizes its business segments based on the various types of telecommunications services provided to customers. The operating segments are segregated as below:

- Local operations—the provision of local telephone services;
- DLD operations—the provision of domestic long distance call services;
- ILD operations—the provision of international long distance call services;
- Cellular operations—the provision of cellular and related services;
- Internet and data operation—the provision of Internet access, lease line, and related services;

- All other operations—the services other than the above five categories, such as paging operations and carrying out project research and providing training.

The operating segments are managed separately because each operating segment represents a strategic business unit that serves different markets.

The Company evaluates performance based on several factors using information prepared on the ROC government regulations basis. The information below is provided on this basis with a summary of US GAAP adjustments to reconcile to the amounts presented in the statement of operations. The Company does not allocate interest and other income, interest expense or taxes to operating segments, nor does the Company's chief operating decision maker evaluate operating segments on these criteria. Except as discussed above, the accounting policies for segment reporting are the same as for the company as a whole. The Company's primary measure of segment profit is based on income or loss from operations.

As of and for the year ended December 31, 2005

	Local	Fixed-line		Cellular Service	Internet and Data	All Other	Total
	NT\$	DLD NT\$	ILD NT\$	NT\$	NT\$	NT\$	NT\$
Revenues for reportable segments	\$ 57,873	\$13,268	\$14,482	\$ 73,938	\$ 56,951	\$ 3,317	\$219,829
Elimination of intersegment amount	(17,360)	(2,400)	—	(1,167)	(14,806)	(17)	(35,750)
US GAAP adjustments	228	83	99	238	(1)	(30)	617
Total revenues from external customers	<u>\$ 40,741</u>	<u>\$10,951</u>	<u>\$14,581</u>	<u>\$ 73,009</u>	<u>\$ 42,144</u>	<u>\$ 3,270</u>	<u>\$184,696</u>
Operating costs and expenses, excluding depreciation and amortization	\$ 35,625	\$ 4,786	\$10,549	\$ 35,565	\$ 27,227	\$ 3,173	\$116,925
Elimination of intersegment amount	(4,027)	(3,359)	(3,183)	(13,838)	(10,848)	(495)	(35,750)
US GAAP adjustments	4,365	82	262	1,025	5,981	541	12,256
	<u>\$ 35,963</u>	<u>\$ 1,509</u>	<u>\$ 7,628</u>	<u>\$ 22,752</u>	<u>\$ 22,360</u>	<u>\$ 3,219</u>	<u>93,431</u>
Unallocated corporate amount							4,941
Total operating costs and expenses, excluding depreciation and amortization							<u>\$ 98,372</u>
Depreciation and amortization	\$ 19,256	\$ 728	\$ 662	\$ 7,474	\$ 12,495	\$ 800	\$ 41,415
US GAAP adjustments	(233)	(8)	(10)	(65)	(105)	27	(394)
	<u>\$ 19,023</u>	<u>\$ 720</u>	<u>\$ 652</u>	<u>\$ 7,409</u>	<u>\$ 12,390</u>	<u>\$ 827</u>	<u>41,021</u>
Unallocated corporate amount							142
Total depreciation and amortization							<u>\$ 41,163</u>
Income from operations	\$ 2,992	\$ 7,754	\$ 3,271	\$ 30,899	\$ 17,229	\$ (656)	\$ 61,489
Elimination of intersegment amount	(13,333)	959	3,183	12,671	(3,958)	478	—
US GAAP adjustments	(3,904)	9	(153)	(722)	(5,877)	(598)	(11,245)
	<u>\$ (14,245)</u>	<u>\$ 8,722</u>	<u>\$ 6,301</u>	<u>\$ 42,848</u>	<u>\$ 7,394</u>	<u>\$ (776)</u>	<u>50,244</u>
Unallocated corporate amount							(5,083)
Total income from operations							<u>\$ 45,161</u>
Segment income before income tax	\$ 3,215	\$ 8,003	\$ 3,417	\$ 31,368	\$ 17,653	\$ (1,149)	\$ 62,507
Elimination of intersegment amount	(13,333)	959	3,183	12,671	(3,958)	478	—
US GAAP adjustments	(3,762)	(152)	(301)	(1,010)	(6,089)	(228)	(11,542)
	<u>\$ (13,880)</u>	<u>\$ 8,810</u>	<u>\$ 6,299</u>	<u>\$ 43,029</u>	<u>\$ 7,606</u>	<u>\$ (899)</u>	<u>50,965</u>
Unallocated corporate amount							(4,933)
Total segment income before income tax							<u>\$ 46,032</u>
Segment assets	\$192,398	\$ 6,342	\$11,779	\$ 62,004	\$ 98,573	\$17,639	\$388,735
US GAAP adjustments	(40,455)	(1,510)	(1,573)	(4,591)	(13,827)	(4,619)	(66,575)
	<u>\$151,943</u>	<u>\$ 4,832</u>	<u>\$10,206</u>	<u>\$ 57,413</u>	<u>\$ 84,746</u>	<u>\$13,020</u>	<u>322,160</u>
Unallocated corporate amount							73,008
Total segment assets							<u>\$395,168</u>
Expenditures for segment assets	<u>\$ 4,518</u>	<u>\$ 403</u>	<u>\$ 229</u>	<u>\$ 4,449</u>	<u>\$ 12,707</u>	<u>\$ 608</u>	<u>\$ 22,914</u>
Unallocated corporate amount							16
Total expenditures for segment assets							<u>\$ 22,930</u>

As significance of paging operations has been decreased below quantitative thresholds required by SFAS 131 in 2006 and thereafter, the Company did not disclose paging operations separately, and prior years disclosure was changed in conformity with the disclosure of 2006.

b. Geographic information

The users of the Company's services are mainly from Taiwan, ROC. The revenues it derived outside Taiwan are mainly inter-connection fees from other telecommunication carriers. The geographic information for revenues is as follows:

	Year Ended December 31		
	2004	2005	2006
	NT\$	NT\$	NT\$
Taiwan, ROC	\$180,031	\$180,793	\$182,687
Overseas	5,132	3,903	3,655
	<u>\$185,163</u>	<u>\$184,696</u>	<u>\$186,342</u>

c. Gross sales to major customers

The Company has no single customer account representing 10% or more of its total revenues for all periods presented.

The Company has non-revenue generating offices in Thailand, U.S. and Vietnam. All non-current assets (including investments in unconsolidated companies, property, plant and equipment, intangible assets, and other assets) except for NT\$0.01 million and NT\$0.06 million at December 31, 2005 and 2006, respectively, are located in Taiwan, ROC.



Exhibit 1.2

[Translation]

Articles of Incorporation of Chunghwa Telecom Co., Ltd.

1. All 26 articles adopted by Promoters Meeting on June 11, 1996.
2. Article 15 amended by General Shareholders Meeting on December 26, 1997.
3. Articles 2 and 22 amended by General Shareholders Meeting on November 25, 1998.
4. Paragraph 1 of Article 21, amended by Special Shareholders Meeting on July 13, 1999.
5. Articles 2, 3, 6, 7, 10, 12, 13, 19, 21, and 22 amended, and Articles 6-1 and 7-1 inserted by General Shareholders Meeting on June 4, 2001.
6. Articles 2, 7, 8, 9, 10, 19, 21, and 22 amended and Article 5 deleted by General Shareholders Meeting on June 21, 2002.
7. Articles 2 amended by General Shareholders Meeting on June 17, 2003.
8. Articles 2 and 22 amended by General Shareholders Meeting on June 25, 2004.
9. Articles 2, 3, 6, 10, 11, 12, 14, 17, 19, 20, 22, 23, and 25 amended, and Articles 12-1, 18-1, and 18-2 inserted by General Shareholders Meeting on May 30, 2006.

Chapter I—General Provisions

Article 1—The Company is promoted by the Ministry of Transportation and Communications (“MOTC”) and others and organized under the Telecommunication Law, the Statute of Chunghwa Telecom Co., Ltd. (hereinafter referred to as the “Corporation Statute”) and the provisions of the Company Law pertaining to companies limited by shares and is named “Chunghwa Telecom Co., Ltd.”.

The English name of the Company is “Chunghwa Telecom Co., Ltd.”.

Article 2—The scope of business of the Company shall be as follows:

- 1) Telecommunications Enterprise of Type 1 (G901011);
- 2) Telecommunications Enterprise of Type 2 (G902011);
- 3) Installation of the Computer Equipment Business (E605010);
- 4) Telecommunication Equipment Wholesale Business (F113070);
- 5) Telecommunication Equipment Retail Business (F213060);
- 6) Telecommunication Engineering Business (E701010);
- 7) Installation of the Radio-Frequency Equipment whose operation is controlled by the Telecommunication Business (E701030);
- 8) Information Software Service Business (I301010);
- 9) Other Designer Businesses [the design of the computer information hardware] (I599990);
- 10) Rental Business (JE01010);
- 11) Publishing Business (J304010);
- 12) Other Wholesale Businesses [telephone card and IC card] (F199990);
- 13) Management and Consulting Service Business (I103060);
- 14) Other Corporation Service Businesses [telephone card, IC card, the research and development of the telecommunication facilities and devices, accepting payment on behalf of businesses and institutions, telecommunication equipment inspection services, and agency sale of entry tickets and travel fares] (IZ99990);

- 15) Other Retail Businesses [telephone card and IC card] (F299990);
- 16) Online Certification Service Businesses (IZ13010);
- 17) Supply of Electronic Information Service Businesses (I301030);
- 18) Information Process Service Business (I301020);
- 19) Telecommunication Account Application Agency Businesses (IE01010);
- 20) Management of Overdue Accounts Payable Service Businesses (IZ11010);
- 21) Real Estate Rental Businesses (H703100);
- 22) Technique and Performing Arts Training (J201031)
- 23) Waste Disposal Businesses (J101040);
- 24) Community Common Cable Television Equipment Businesses (J502020);
- 25) Exhibition Service Businesses (JB01010);
- 26) General Advertising Service Businesses (I401010);
- 27) Department Store Businesses (F301010);
- 28) Communication Newsletter Businesses (J302010);
- 29) Industry and Commerce Credit Investigation Service Businesses (JD01010);
- 30) Public Notarization Businesses (IZ07010);
- 31) Parking Lot Operation Businesses (G202010);
- 32) Environmental Assessment Service Businesses (J101050);
- 33) Engineering Technology Consultation Services (I101061);
- 34) Computer and Accessories Manufacturing Service (CC01110);
- 35) Information Storage and Process Equipment Manufacturing Businesses (CC01120);
- 36) Electronic Component Manufacturing Businesses (CC01080);
- 37) Other Electrical and Electronic Machinery & Equipment Manufacturing Businesses [IC or Optical Card Scanners] (CC01990);
- 38) Radio-Frequency Equipment Import Business (F401021);
- 39) Cable System Operator Business (J504011);
- 40) General Hotel Business (J901020);
- 41) Tourism Hotel Business (J901011);
- 42) Computer and Administrative Device Wholesale Businesses (F113050);
- 43) Information Software Wholesale Businesses (F118010);
- 44) Computer and Administrative Device Retail Businesses (F213030);
- 45) Information Software Rental Businesses (F218010)
- 46) Except the permitted business, the Company may engage in other businesses not prohibited or restricted by laws and regulations.

The Company may handle endorsement and guaranty affairs in accordance with the Operation Procedures for the Endorsement and Guaranty of the Company if there is any business need.





Article 3—In the event that the Company invests in another business as a limited-liability shareholder, the total investment amount may not exceed the total paid-in capital of the Company. Investment not related to telecommunications may not exceed 20% of the total paid-in capital of the Company.

Article 4—The head office of the Company is located in Taipei City and the Company may establish branch office(s) and liaison office(s) at appropriate locations within or outside the territory of the Republic of China.

Article 5—(Deleted)

Chapter II—Shares

Article 6—The registered capital of the Company shall be One Hundred Twenty Billion and Twenty New Taiwan Dollars (NT\$120,000,000,020), divided into One Billion Twenty Million (12,000,000,000) common shares and Two (2) preferred shares with a par value of Ten New Taiwan Dollars (NT\$10) per share. All the common shares shall be issued in increments by the Board of Directors pursuant to the laws and regulations.

Article 6-1—The rights, obligations, and other important conditions regarding the preferred shares issued by the Company are stated as follows:

- 1) The rights of the preferred shares with respect to the distribution of dividends and bonuses, the Company's retained properties, and the Company's profits and capital reserve in cash or the appropriated capital, etc. shall be equal to those of the common shares.
- 2) The shareholder(s) of the preferred shares has/have the same right to vote or election with those of the shareholder(s) of the common shares at a common shareholders' meeting.
- 3) During the term of the preferred shares, the shareholder(s) of the preferred share shall be the director(s) and supervisor(s) and may be re-appointed by MOTC at any time.
- 4) When the Company issues new shares in cash, the shareholder(s) of the preferred shares shall have the same preemptive rights with respect to the new shares as those of the shareholder(s) of the common shares.
- 5) The Company shall obtain the consents of the shareholder(s) of the preferred shares before engaging in the following matters and, failing so, the action will be deemed void:
 - (1) To amend the Company's name
 - (2) To amend the Company's business scope
 - (3) To transfer all or the essential part of the Company's business or assets
- 6) The preferred shares issued by the Company shall not be transferred. At the end of the third year from the issuance date of the preferred shares, the Company shall reacquire the preferred shares by their par value and then cancel them. The issuance date shall be the record date of the capital increase of the preferred shares.

Article 7—The share certificates of the Company shall bear the shareholders' names, be signed or sealed by the Chairman and at least two other directors, be serially numbered, affixed with the corporate seal of the Company, and legalized by the Ministry of Economic Affairs ("MOEA") (hereinafter referred to as the "Competent Authority") or its certified issuance registration agency before they are issued in accordance with the relevant laws.

When issuing new shares, the Company may print a share certificate in respect of the full number of shares to be issued at that time, and shall arrange for the certificate to be kept by a centralized securities custodian institution, in which case the preceding requirement for serial numbering of share certificates shall not apply.

Shares issued by the Company may also be exempt from printing of share certificates, and the Company shall arrange for such shares to be recorded by a centralized securities custodian institution, in which case the preceding 2 paragraphs shall not apply.

Any affair with regard to the shares of the Company shall be handled in accordance with the Guidelines for Handling Stock Affairs by a Public Issuing Company.

Article 7-1—The share certificates issued by the Company may be jointly exchanged for the share certificates with a larger par value upon the request of the Taiwan Securities Centralized Depository Company Limited by Shares.

Chapter III—Shareholders' Meeting

Article 8—Shareholders' meetings shall be of two types: general shareholders' meeting and special shareholders' meeting. Except as otherwise provided in the Company Law, shareholders' meetings shall be convened by the Board of Directors.

The general shareholders' meeting shall be convened at least once every year and shall be convened within six (6) months after the close of each fiscal year except as otherwise approved by the Competent Authority for good cause shown.

The special shareholders' meeting shall be convened at such time as may be deemed necessary pursuant to relevant laws and regulations.

Article 9—Where a shareholders' meeting is convened by the board of directors, the chairman of the Company shall act as the chairman of the shareholders' meeting. In the event that the chairman is to be on leave of absence or cannot attend the meeting for any cause whatsoever, the vice-chairman, or where the chairman and the vice-chairman are both to be on leave of absence or cannot attend the meeting for any cause whatsoever, one of the directors appointed by the chairman, or, where there is no appointment, a director elected among all the directors, may act on behalf of the chairman.

Where a shareholders' meeting is convened by a person with authority other than the board of directors, such convener shall act as the chairman of the shareholders' meeting. Where there are two (2) or more conveners, the chairman of the meeting shall be elected amongst such conveners.

Article 10—Unless otherwise specified by the law, each shareholder of the Company shall be entitled to one vote for each share held.

Article 11—(Deleted)

Chapter IV—Directors and Supervisors

Article 12—The Company shall have seven (7) to fifteen (15) directors to form the Board of Directors, one-fifth (1/5) of whom shall be expert representatives.

The Board of Directors shall have one (1) chairman elected by and from among the directors with the concurrence of a general majority of the directors present at a meeting attended by at least two-thirds (2/3) of the directors and shall have one (1) vice-chairman elected in the same way.

The Company shall have three (3) to five (5) supervisors.

During the term of the preferred shares, there shall be at least one (1) seat of the directors and the supervisors each reserved for the shareholders of the preferred shares.

Article 12-1 In accordance with Articles 181-2 and 183 of the Securities and Exchange Law, the Company shall, beginning in the fifth commencement, establish three (3) independent directors to be included in the number of directors designated in the preceding Article.

The elections for independent directors shall proceed with the candidate nomination system; the shareholders shall elect the independent directors from among the nominees listed in the roster of independent director candidates.



Elections for independent and non-independent directors shall proceed concurrently, and the number of elected directors shall be calculated separately.

The professional qualifications, restrictions on shareholding and concurrent post, affirmation of independence, nomination and election processes, exercise of authority and other requirements of independent directors shall be determined and executed in accordance with the Securities and Exchange Law and related regulations.

Article 13—The tenure of office of the directors and supervisors will be three (3) years and they will be eligible for re-election.

The tenure of the directors and supervisors of the shareholders of the preferred shares appointed without election and who are not subject to any restriction of the tenure set forth in the previous paragraph ends upon the termination of the issuance period of the preferred shares.

In the event that the representative of a government or corporate body is elected as the director or the supervisor, the government or corporate body may reappoint such representative at anytime to supplement the original tenure.

Article 14—The following items shall be decided by the board of directors:

- (1) Increase or reduction of capital of the Company.
- (2) Regulations with regard to the organization of the Company.
- (3) Establishment, amendment, and abolishment of the branch offices within or outside the territory of the Republic of China.
- (4) Examination of annual business budgets and final budgets.
- (5) Distribution of profits or off-set of deficit.
- (6) The amount and term of domestic and foreign loan.
- (7) The amount of Investment.
- (8) Issuance of corporate bonds.
- (9) Policies regarding personnel matters, material purchase, accounting, and internal control.
- (10) Amendment and modifications of regulations of organization of the board of directors and guidelines on establishing functional committee.
- (11) Amendment and modification of regulations with regard to the scope of duties of independent directors.
- (12) Appointment and removal of the president, vice presidents, presidents of Telecommunication Laboratories and Telecommunication Training Institute, and audit and accounting section chiefs.
- (13) The remuneration standard for employees.
- (14) Policies regarding recommendation of chairman and president to subsidiaries.
- (15) Other duties and powers granted by the law or by shareholders meeting.

Article 15—The board of directors' meeting shall be convened every two (2) months. The special board of directors' meeting shall be convened at such time as may be deemed necessary. Both meetings shall be convened by the chairman of the Company and such chairman shall act as the chairman of the meeting. In the event that the chairman cannot attend the meeting for any cause whatsoever, the vice-chairman, or where the chairman and the vice-chairman are both to be on leave of absence or cannot attend the meeting for any cause whatsoever, one of the directors appointed by the chairman, or, where there is no appointment, a director elected among all the directors, may act on behalf of the chairman.

Article 16—All directors shall attend every board of directors' meeting; in case any of the directors cannot attend the meeting for any cause whatsoever, he/she may designate the other directors to act on his/her behalf and such agent shall present the proxy setting forth the vested power of the purpose of the meeting each time. However, each agent shall only accept one appointment from the directors.

Except as otherwise provided in the relevant laws or this Articles of Incorporation, any resolution of a board of directors' meeting shall be adopted at a meeting which at least general majority of the directors attend and at which meeting a general majority of the directors present vote in favor of such resolution.

Minutes of meetings shall be prepared for all resolutions adopted at a board of directors' meeting.

Article 17—The supervisors shall perform the following functions:

- (1) To investigate the business and financial condition of the Company;
- (2) To inspect the books, records and documents of the Company; and
- (3) Other powers granted by the laws and regulations.

Article 18—In addition to performing the functions of a supervisor in accordance with the relevant laws, the supervisors may attend the board of directors' meeting to express his/her opinion but may not participate in any voting.

Article 18-1 Remunerations of the directors and supervisors shall be examined and proposed by the compensation committee of board of directors, and be adopted by the resolution of board of the directors.

Article 18-2 The Company may purchase liability insurance policies for directors and supervisors during the term of their offices and within the scope of damages results from the performances of their official duties in order to reduce and disperse the risks for the Company and shareholders due to the fault, mistake, violation of duty, and inaccurate or misleading statements on part of the directors and supervisors during the performance of their duties.

Chapter V—Managerial Officers

Article 19—The Company shall have one (1) chief executive officer, to be served as a concurrent post by the chairman or by the president, to lead the managers in proposing and making significant policy decisions regarding to the Company and all affiliates of the Company.

The Company shall have one (1) president, several executive vice presidents, senior vice presidents, and the presidents of laboratory and institute. The president shall be a director with professional knowledge in telecommunication business.

Article 20—The president shall, in accordance with the decision made by the board of directors and with instruction from the chief executive officer, take charge of the affairs of the Company, and shall have the authority to sign on behalf of the Company; the executive vice presidents and senior vice presidents shall assist the president in all affairs, and shall have the power to sign on behalf of the Company within the scope set by rules decided by the president or authorized in writing by the president.

The division of powers and duties between the board of directors and the president shall be determined in accordance with the Powers and Duties Chart.

Chapter VI—Accounting

Article 21—The fiscal year of the Company shall be from January 1 to December 31 of each year.





At the end of each fiscal year, the board of directors shall prepare the following statements and reports, and submit the same to the supervisor(s) for examination thirty (30) days prior to the annual shareholders' meeting, and then shall submit the same to the annual shareholders' meeting for adoption.

- (1) Report of Operations;
- (2) Financial statements;
- (3) Resolution governing the distribution of profit or the making-up of losses.

Article 22—After the Company has paid all taxes due at the end of each fiscal year, the Company shall offset its accumulated losses and set aside ten percent (10%) of the net profit as the statutory revenue reserve before distribution of profits, except when the accumulated amount of such legal reserve equals to the Company's total authorized capital. The Company may also set aside special reserve(s) according to the business need or laws and regulations. A minimum of fifty percent (50%) of the total amount of the balance, including the accumulated retained profits from the previous year, shall be distributed in the following manner:

- 1) Employee bonuses between two percent (2%) to five percent (5%);
- 2) Remuneration for directors and supervisors not higher than 0.2%.
- 3) The remainder after deducting amounts in subparagraphs 1) and 2) shall be shareholders' dividends. Cash dividends shall not be below fifty percent (50%) of the total dividends, but when the cash dividends fall below NT\$0.1 per share, dividends shall be distributed in the form of stocks.

Subparagraphs 1) and 2) of the preceding paragraph shall apply upon the privatization of the Company, however, with respect to the year in which privatization occurred, the dividends shall be distributed based on the profits derived during the period after privatization.

The percentage of distribution stipulated in paragraph 1 shall take into consideration of the actual profitability of the year, capital budgeting, and status of finance, and shall be executed following the resolution of shareholders meeting.

Dividends and bonuses shall not be distributed where the Company has no profits, provided that where the statutory revenues reserve exceeds fifty percent (50%) of paid-up capital of the Company, the portion in excess may be distributed as shareholders' dividends.

Article 23—In the event that the Company issues new shares, excluding ad hoc ratification by the central competent authority, the Company shall reserve ten percent (10%) to fifteen percent (15%) of the total newly issued shares for preemptive subscription by employees of the Company.

Chapter VII—Supplementary Provisions

Article 24—The regulations with regard to the organization of the Board of Directors and the Company shall be separately adopted.

Article 25—Matters not specified herein shall be resolved in accordance with the Company Law.

Article 26—This Articles of Incorporation was adopted on June 11, 1996.

LIST OF SUBSIDIARIES

<u>NAME OF ENTITY</u>	<u>JURISDICTION OF INCORPORATION</u>
Chunghwa International Yellow Pages Corporation	Taiwan
Chief Telecom Inc.	Taiwan
Unigate Telecom Inc.	Taiwan
Chief Telecom (Hong Kong) Limited	Hong Kong
New Prospect Investment Holdings Ltd.	British Virgin Islands
Prime Asia Investments Group Ltd.	British Virgin Islands





CERTIFICATION OF OUR CHIEF EXECUTIVE OFFICER

I, Tan Ho Chen, certify that:

1. I have reviewed this annual report on Form 20-F of Chunghwa Telecom Co., Ltd.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the consolidated financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the company as of, and for, the periods presented in this report;
4. The company's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the company and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the company, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the company's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the company's internal control over financial reporting that occurred during the period covered by this report that has materially affected, or is reasonably likely to materially affect, the company's internal control over financial reporting; and
5. The company's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the company's auditors and the audit committee of the company's board of directors (or persons performing the equivalent function):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal controls over financial reporting which are reasonably likely to adversely affect the company's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the company's internal controls over financial reporting.

Date: April 23, 2007

By: /s/ Tan Ho Chen
Name: **Tan Ho Chen**
Title: **Chairman and Chief Executive Officer**

CERTIFICATION OF OUR CHIEF FINANCIAL OFFICER

I, Joseph C.P. Shieh, certify that:

1. I have reviewed this annual report on Form 20-F of Chunghwa Telecom Co., Ltd.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the consolidated financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the company as of, and for, the periods presented in this report;
4. The company's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the company and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the company, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the company's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the company's internal control over financial reporting that occurred during the period covered by this report that has materially affected, or is reasonably likely to materially affect, the company's internal control over financial reporting; and
5. The company's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the company's auditors and the audit committee of the company's board of directors (or persons performing the equivalent function):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal controls over financial reporting which are reasonably likely to adversely affect the company's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the company's internal controls over financial reporting.

Date: April 23, 2007

By: /s/ Joseph C.P. Shieh
Name: **Joseph C.P. Shieh**
Title: **Chief Financial Officer**





Exhibit 13

Pursuant to 18 U.S.C. § 1350, the undersigned, Tan Ho Chen, Chairman and Chief Executive Officer of Chunghwa Telecom Co., Ltd. (the "Company"), and Joseph C. P. Shieh, Chief Financial Officer of the Company, each hereby certifies, to his knowledge, that:

1. The Company's Annual Report on Form 20-F for the year ended December 31, 2006 (the "Report") fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: April 23, 2007

By: /s/ Tan Ho Chen
Name: **Tan Ho Chen**
Title: **Chairman and Chief Executive Officer**

By: /s/ Joseph C.P. Shieh
Name: **Joseph C.P. Shieh**
Title: **Chief Financial Officer**

MEMO





Chunghwa Telecom Co., Ltd.

Chairman & CEO

Tan Ho Chen

President

Shyue-Ching Lu

Financial Spokesperson

Joseph Shieh

CFO and Senior Vice President

Tel: 886-2-2344-4238

jshieh@cht.com.tw

Business Spokesperson

Feng-Hsiung Chang

Senior Executive Vice President

Tel: 886-2-2344-5768

fh5768@cht.com.tw

Transfer Agent

Taiwan Securities Co., Ltd.

B1, 96 Jianguo N. Rd., Sec. 1, Taipei

Tel: 886-2-2504-8125

<http://www.tsc.com.tw>

Auditor

Deloitte & Touche

12F, 156 Min Sheng E. Rd., Sec. 3, Taipei

Tel: 886-2-2545-9988

<http://www.deloitte.com.tw>

Exchange of ADR Listing

The New York Stock Exchange

Ticker symbol: CHT

<http://www.nyse.com>

ADR Depositary Bank

The Bank of New York

101 Barclay Street

New York, NY 10286, U.S.A.

<http://www.adrbny.com>

Inquires on ADR Investment

Toll free in USA: 1-888 - BNY-ADRS

Outside USA: 1-610-382-7836

shareowners@bankofny.com

<http://www.stockbny.com>

Chunghwa Telecom Overseas Office

Ho Chi Minh Representative Office

Saigon Trade Center Suite 2701, 37, Ton Duc Thang St.,

Dist.1, Ho Chi Minh City, Vietnam

General Manager : Tung-Ming Chen

Assistant : Le Thanh Vu

Tel : 84-89106173

Mobile : 84-903972369

Fax : 84-89106174

grant@cht.com.tw

Deputy Manager : Ta-Sheng Chang

Tel : 84-89106175

Mobile : 84-918692921

Fax : 84-89106174

frederic@cht.com.tw

Bangkok Representative Office

252/98 19F Muang Thai Phatra Office

Tower 2 Rachadaphisek Rd.,

Huay-Kwang, Bangkok 10320, Thailand

General Manager : Lawrence Wei

Assistant : Muang Kamonpiman

Tel : 66-2-693-2158

Mobile : 66-1-828-6506

Fax : 66-2-693-2157

lawr7422@cht.co.th

Contact Information for Chunghwa Telecom and Affiliates

Headquarters

21-3 Hsinyi Rd., Sec. 1, Taipei 100
Tel: 886-2-2344-3691
Fax: 886-2-2356-8306
<http://www.cht.com.tw>

Northern Taiwan Business Group

42 Renai Rd., Sec. 1, Taipei 100
Tel: 886-2-2344-2485
Fax: 886-2-2397-0539

Central Taiwan Business Group

161 Shanmin Rd., Sec. 1, Taichung 403
Tel: 886-4-2344-2511
Fax: 886-4-2344-2516

Southern Taiwan Business Group

230 Linsen 1st Rd., Kaohsiung 800
Tel: 886-7-344-3350
Fax: 886-7-344-3391

Telecommunication Laboratories

12 Minzu Rd., Sec. 5, Lane 551
Yangmei Jen, Taoyuan County 326
Tel: 886-3-424-4239
Fax: 886-3-424-4444

Mobile Business Group

35 Aikuo E. Rd., Taipei 106
Tel: 886-2-2344-2825
Fax: 886-2-2356-3023

Data Communications Business Group

21 Hsinyi Rd., Sec. 1, Taipei 100
Tel: 886-2-2344-4756
Fax: 886-2-2394-8404

Enterprise Business Group

4F, 21-3 Hsinyi Rd., Sec. 1, Taipei 100
Tel: 886-2-2344-5899
Fax: 886-2-2392-1170

International Business Group

31 Aikuo E. Rd., Taipei 106
Tel: 886-2-2344-3580
Fax: 886-2-2394-0944

Telecommunication Training Institute

168 Minzu Rd., Panchiao, Taipei County 220
Tel: 886-2-2963-9587
Fax: 886-2-2963-9453







Chunghwa Telecom

21-3, Hsinyi Rd., Sec. 1, Taipei, Taiwan 100, R.O.C.

Tel: 886-2-2344-5488

Fax: 886-2-3393-8188

<http://www.cht.com.tw>