

**Chunghwa Telecom Co., Ltd. and
Subsidiaries**

**Consolidated Financial Statements as of
December 31, 2008 and 2009, and for
Each of the Three Years in the Period Ended
December 31, 2009 and
Report of Independent Registered Public
Accounting Firm**

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of
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, 2008 and 2009, and the related consolidated statements of income, changes in stockholders’ equity, and cash flows for the years ended December 31, 2007, 2008 and 2009, 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 auditing standards generally accepted in the Republic of China and 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, such consolidated financial statements present fairly, in all material respects, the financial position of Chunghwa Telecom Co., Ltd. and subsidiaries as of December 31, 2008 and 2009, and the results of their operations and their cash flows for the years ended December 31, 2007, 2008 and 2009, in conformity with accounting principles generally accepted in the Republic of China.

As discussed in Note 4 to the consolidated financial statements, on January 1, 2008, the Company adopted Interpretation 96-052 issued by the Accounting and Research Development Foundation of the Republic of China that requires companies to record bonuses paid to employees, directors and supervisors as an expense rather than an appropriation of earnings. The Company early adopted the new Statement of Financial Accounting Standards No. 41, “Operating Segments” (“SFAS No. 41”) beginning from September 1, 2009.

Accounting principles generally accepted in the Republic of China vary in certain significant respects from accounting principles generally accepted in the United States of America. Information relating to the nature and effect of such differences is presented in Note 34 to the consolidated financial statements.

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 3. Such U.S. dollar amounts are presented solely for the convenience of the readers.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company's internal control over financial reporting as of December 31, 2009, 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 10, 2010 expressed an unqualified opinion on the Company's internal control over financial reporting.

/s/ DELOITTE & TOUCHE

Deloitte & Touche
Taipei, Taiwan
The Republic of China

March 10, 2010

CHUNGHWA TELECOM CO., LTD. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(In Millions of New Taiwan or U.S. Dollars, Except Par Value)

ASSETS	Notes	December 31			LIABILITIES AND STOCKHOLDERS' EQUITY	Notes	December 31		
		2008 NT\$	2009 NT\$	US\$ (Note 3)			2008 NT\$	2009 NT\$	US\$ (Note 3)
CURRENT ASSETS					CURRENT LIABILITIES				
Cash and cash equivalents	2, 5	\$ 81,288	\$ 73,259	\$ 2,293	Short-term loans	17	\$ 258	\$ 763	\$ 24
Financial assets at fair value through profit or loss	2, 6	259	41	1	Financial liabilities at fair value through profit or loss	2, 6	107	1	-
Available-for-sale financial assets	2, 7	14,182	17,537	549	Trade notes and accounts payable	21	11,360	10,155	318
Held-to-maturity financial assets	2, 8	769	1,100	34	Payables to related parties	29	524	336	11
Trade notes and accounts receivable, net	2, 9	10,845	11,973	375	Income tax payable	2, 26	5,687	4,312	135
Receivables from related parties	29	2	94	3	Accrued expenses	4, 18	16,346	17,449	546
Other monetary assets	10	2,226	1,840	58	Due to stockholders for capital reduction	22	19,116	9,697	303
Inventories, net	2, 11, 21	3,901	4,049	128	Current portion of long-term loans	20	8	117	3
Deferred income tax assets	2, 26	119	101	3	Other current liabilities	2, 19, 21, 29, 32	16,530	16,870	528
Restricted assets	21, 30, 31	59	178	6					
Other current assets	12, 21	4,557	4,320	135	Total current liabilities		69,936	59,700	1,868
Total current assets		118,207	114,492	3,585					
LONG-TERM INVESTMENTS					NONCURRENT LIABILITIES				
Investments accounted for using equity method	2, 13	2,337	1,622	51	Long-term loans	20	29	221	7
Financial assets carried at cost	2, 14	2,537	2,537	79	Deferred income		2,072	2,484	78
Held-to-maturity financial assets	2, 8	3,044	3,930	123	Total noncurrent liabilities		2,101	2,705	85
Other monetary assets	15, 31	1,000	1,000	31					
Total long-term investments		8,918	9,089	284	RESERVE FOR LAND VALUE INCREMENTAL TAX	16	95	95	3
PROPERTY, PLANT AND EQUIPMENT, NET	2, 16, 29, 30, 31	323,050	313,022	9,797					
INTANGIBLE ASSETS	2				OTHER LIABILITIES				
3G concession		7,486	6,737	211	Accrued pension liabilities	2, 28	5,173	1,217	38
Goodwill		226	282	9	Customers' deposits		6,160	5,998	188
Others		559	598	18	Others		431	318	10
Total intangible assets		8,271	7,617	238	Total other liabilities		11,764	7,533	236
OTHER ASSETS					Total liabilities		83,896	70,033	2,192
Refundable deposits		1,374	1,551	49	EQUITY ATTRIBUTABLE TO STOCKHOLDERS OF THE PARENT	2, 16, 22, 24			
Deferred income tax assets	2, 26	1,543	483	15	Common stock - NT\$10 par value				
Others	2, 28, 29, 30, 31	2,227	2,743	85	Authorized: 12,000,000 thousand shares				
Total other assets		5,144	4,777	149	Issued: 9,696,808 thousand shares		96,968	96,968	3,035
					Preferred stock - NT\$10 par value		-	-	-
					Additional paid-in capital		179,206	169,510	5,305
					Retained earnings		96,812	103,413	3,237
					Other adjustments				
					Cumulative translation adjustments		29	8	-
					Unrealized loss on financial instruments		(2,272)	(447)	(14)
					Unrealized revaluation increment		5,813	5,803	182
					Unrecognized net loss of pension		-	(44)	(1)
					Total other adjustments		3,570	5,320	167
					Total equity attributable to stockholders of the parent		376,556	375,211	11,744
					MINORITY INTERESTS IN SUBSIDIARIES		3,138	3,753	117
					Total stockholders' equity		379,694	378,964	11,861
TOTAL		<u>\$ 463,590</u>	<u>\$ 448,997</u>	<u>\$ 14,053</u>	TOTAL		<u>\$ 463,590</u>	<u>\$ 448,997</u>	<u>\$ 14,053</u>

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

(With Deloitte & Touche audit report dated March 10, 2010)

CHUNGHWA TELECOM CO., LTD. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

(In Millions of New Taiwan or U.S. Dollars, Except Earnings Per Share that are in New Taiwan or U.S. Dollars)

	Notes	Year Ended December 31			
		2007 NT\$	2008 NT\$	2009 NT\$	2009 US\$ (Note 3)
NET REVENUES	29	\$ 197,391	\$ 201,670	\$ 198,361	\$ 6,208
OPERATING COSTS	29	<u>106,650</u>	<u>113,546</u>	<u>112,736</u>	<u>3,528</u>
GROSS PROFIT		<u>90,741</u>	<u>88,124</u>	<u>85,625</u>	<u>2,680</u>
OPERATING EXPENSES	29				
Marketing		23,732	22,732	22,293	698
General and administrative		3,423	3,680	3,765	118
Research and development		<u>3,237</u>	<u>3,144</u>	<u>3,173</u>	<u>99</u>
Total operating expenses		<u>30,392</u>	<u>29,556</u>	<u>29,231</u>	<u>915</u>
INCOME FROM OPERATIONS		<u>60,349</u>	<u>58,568</u>	<u>56,394</u>	<u>1,765</u>
NON-OPERATING INCOME AND GAINS	29				
Interest income		1,453	1,916	479	15
Valuation gain on financial instruments, net		-	551	99	3
Foreign exchange gain, net		-	336	89	3
Equity in earnings of equity method investees, net		141	64	-	-
Gain on disposal of financial instruments, net		99	-	-	-
Others		<u>757</u>	<u>509</u>	<u>755</u>	<u>24</u>
Total non-operating income and gains		<u>2,450</u>	<u>3,376</u>	<u>1,422</u>	<u>45</u>
NON-OPERATING EXPENSES AND LOSSES					
Loss arising from natural calamities	16	42	-	149	5
Loss on disposal of financial instruments, net		-	672	142	5
Impairment loss on assets	7, 14	24	1,168	110	4
Equity in losses of equity method investees, net		-	-	23	-
Interest expense		15	4	15	-
Loss on disposal of property, plant and equipment		89	278	7	-
Foreign exchange loss, net		54	-	-	-
Valuation loss on financial instruments, net		585	-	-	-
Others		<u>189</u>	<u>138</u>	<u>132</u>	<u>4</u>
Total non-operating expenses and losses		<u>998</u>	<u>2,260</u>	<u>578</u>	<u>18</u>
INCOME BEFORE INCOME TAX		61,801	59,684	57,238	1,792
INCOME TAX EXPENSE	2, 26	<u>13,059</u>	<u>13,892</u>	<u>12,743</u>	<u>399</u>
CONSOLIDATED NET INCOME		<u>\$ 48,742</u>	<u>\$ 45,792</u>	<u>\$ 44,495</u>	<u>\$ 1,393</u>
ATTRIBUTABLE TO:					
Stockholders of the parent		\$ 48,249	\$ 45,011	\$ 43,757	\$ 1,370
Minority interests		<u>493</u>	<u>781</u>	<u>738</u>	<u>23</u>
		<u>\$ 48,742</u>	<u>\$ 45,792</u>	<u>\$ 44,495</u>	<u>\$ 1,393</u>

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CHUNGHWA TELECOM CO., LTD. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

(In Millions of New Taiwan or U.S. Dollars, Except Earnings Per Share that are in New Taiwan or U.S. Dollars)

	Notes	Year Ended December 31			
		2007	2008	2009	
		NT\$	NT\$	NT\$	US\$ (Note 3)
BASIC EARNINGS PER SHARE	27				
Before income tax		\$ 6.25	\$ 6.03	\$ 5.79	\$ 0.18
After income tax		\$ 4.94	\$ 4.64	\$ 4.51	\$ 0.14
DILUTED EARNINGS PER SHARE	27				
Before income tax		\$ 6.25	\$ 6.02	\$ 5.77	\$ 0.18
After income tax		\$ 4.93	\$ 4.63	\$ 4.50	\$ 0.14
BASIC EARNINGS PER EQUIVALENT ADS					
Before income tax		\$ 62.49	\$ 60.30	\$ 57.96	\$ 1.81
After income tax		\$ 49.35	\$ 46.42	\$ 45.16	\$ 1.41
DILUTED EARNINGS PER EQUIVALENT ADS					
Before income tax		\$ 62.49	\$ 60.16	\$ 57.77	\$ 1.81
After income tax		\$ 49.35	\$ 46.31	\$ 45.01	\$ 1.41
BASIC WEIGHTED AVERAGE SHARES OUTSTANDING (THOUSANDS)	27	9,776,237	9,696,808	9,696,808	
DILUTED WEIGHTED AVERAGE SHARES OUTSTANDING (THOUSANDS)	27	9,776,237	9,717,489	9,726,542	

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

(With Deloitte & Touche audit report dated March 10, 2010)

(Concluded)

CHUNGHWA TELECOM CO., LTD. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
(In Millions of New Taiwan or U.S. Dollars, Except Shares Data and Par Value)

	Equity Attributable to Stockholders of the Parent												Total Stockholders' Equity
	Capital Stock (NT\$10 Per Value)				Additional Paid-in Capital	Retained Earnings	Cumulative Translation Adjustments	Unrecognized Net Loss of Pension	Unrealized Loss on Financial Instruments	Unrealized Revaluation Increment	Treasury Stock	Minority Interests	
	Common Stock	Preferred Stock	Shares (Thousands)	Amount									
BALANCE, JANUARY 1, 2007	9,667,845	\$ 96,678	-	\$ -	\$ 210,273	\$ 86,702	\$ (3)	\$ -	\$ 541	\$ 5,825	\$ -	\$ 98	\$ 400,114
Adjustment of additional paid-in capital from revaluation of land to income upon disposal	-	-	-	-	-	-	-	-	-	(2)	-	-	(2)
Appropriation of 2006 earnings	-	-	-	-	-	-	-	-	-	-	-	-	-
Cash dividend - NT\$3.58 per share	-	-	-	-	-	(34,611)	-	-	-	-	-	-	(34,611)
Employees' bonus - cash	-	-	-	-	-	(1,256)	-	-	-	-	-	-	(1,256)
Remuneration to board of directors and supervisors	-	-	-	-	-	(36)	-	-	-	-	-	-	(36)
Capital surplus transferred to common stock	966,785	9,668	-	-	(9,668)	-	-	-	-	-	-	-	-
Capital reduction	(966,785)	(9,668)	-	-	-	-	-	-	-	-	110	-	(9,558)
Increase in minority interests	-	-	-	-	-	-	-	-	-	-	-	2,185	2,185
Consolidated net income in 2007	-	-	-	-	-	48,249	-	-	-	-	-	493	48,742
Unrealized gain on financial instruments held by investees	-	-	-	-	-	-	-	-	2	-	-	-	2
Equity adjustments in investees	-	-	-	-	-	(15)	-	-	-	-	-	-	(15)
Cumulative translation adjustment for foreign-currency investments held by investees	-	-	-	-	-	-	1	-	-	-	-	-	1
Defined benefit pension plan adjustments of investees	-	-	-	-	-	-	-	-	-	-	-	-	-
Purchase of treasury stock - 121,075 thousand common shares	-	-	-	-	-	-	-	-	-	-	(7,217)	-	(7,217)
Unrealized loss on financial instruments	-	-	-	-	-	-	-	-	(506)	-	-	(1)	(507)
BALANCE, DECEMBER 31, 2007	9,667,845	96,678	-	-	200,605	99,033	(2)	-	37	5,823	(7,107)	2,775	397,842
Adjustment of additional paid-in capital from revaluation of land to income upon disposal	-	-	-	-	-	-	-	-	-	(10)	-	-	(10)
Appropriation of 2007 earnings	-	-	-	-	-	-	-	-	-	-	-	-	-
Cash dividend - NT\$4.26 per share	-	-	-	-	-	(40,716)	-	-	-	-	-	-	(40,716)
Stock dividend - NT\$0.1 per share	95,578	956	-	-	-	(956)	-	-	-	-	-	-	-
Employees' bonus - cash	-	-	-	-	-	(1,304)	-	-	-	-	-	-	(1,304)
Employees' bonus - stock	43,453	435	-	-	-	(435)	-	-	-	-	-	-	-
Remuneration to board of directors and supervisors	-	-	-	-	-	(43)	-	-	-	-	-	-	(43)
Capital surplus transferred to common stock	1,911,555	19,116	-	-	(19,116)	-	-	-	-	-	-	-	-
Capital reduction	(1,911,555)	(19,116)	-	-	-	-	-	-	-	-	-	-	(19,116)
Decrease in minority interests	-	-	-	-	-	-	-	-	-	-	-	(419)	(419)
Consolidated net income in 2008	-	-	-	-	-	45,011	-	-	-	-	-	781	45,792
Unrealized loss on financial instruments held by investees	-	-	-	-	-	-	-	-	(7)	-	-	-	(7)
Equity adjustments in investees	-	-	-	-	-	(55)	-	-	-	-	-	-	(55)
Cumulative translation adjustment for foreign-currency investments held by investees	-	-	-	-	-	-	31	-	-	-	-	-	31
Defined benefit pension plan adjustments of investees	-	-	-	-	-	-	-	-	-	-	-	-	-
Cancellation of treasury stock - 110,068 thousand common shares	(110,068)	(1,101)	-	-	(2,283)	(3,723)	-	-	-	-	7,107	-	-
Unrealized loss on financial instruments	-	-	-	-	-	-	-	-	(2,302)	-	-	1	(2,301)
BALANCE, DECEMBER 31, 2008	9,696,808	96,968	-	-	179,206	96,812	29	-	(2,272)	5,813	-	3,138	379,694
Adjustment of additional paid-in capital from revaluation of land to income upon disposal	-	-	-	-	-	-	-	-	-	(10)	-	-	(10)
Appropriation of 2008 earnings	-	-	-	-	-	-	-	-	-	-	-	-	-
Cash dividend - NT\$3.83 per share	-	-	-	-	-	(37,139)	-	-	-	-	-	-	(37,139)
Capital surplus transferred to common stock	969,680	9,697	-	-	(9,697)	-	-	-	-	-	-	-	-
Cancellation of preferred stock	-	-	-	-	-	-	-	-	-	-	-	-	-
Decrease in minority interests	-	-	-	-	-	-	-	-	-	-	-	(129)	(129)
Capital reduction	(969,680)	(9,697)	-	-	-	-	-	-	-	-	-	-	(9,697)
Consolidated net income in 2009	-	-	-	-	-	43,757	-	-	-	-	-	738	44,495
Equity adjustments in investees	-	-	-	-	1	(17)	-	-	-	-	-	-	(16)
Cumulative translation adjustment for foreign-currency investments held by investees	-	-	-	-	-	-	(21)	-	-	-	-	(1)	(22)
Defined benefit pension plan adjustments of investees	-	-	-	-	-	-	-	(44)	-	-	-	(1)	(45)
Unrealized gain on financial instruments	-	-	-	-	-	-	-	-	1,825	-	-	8	1,833
BALANCE, DECEMBER 31, 2009	9,696,808	96,968	-	-	169,510	103,413	8	(44)	(447)	5,803	-	3,753	378,964
BALANCE, DECEMBER 31, 2009 (IN MILLIONS OF US\$ - Note 3)		\$ 3,035			\$ 5,305	\$ 3,237		\$ (1)	\$ (14)	\$ 182		\$ 117	\$ 11,861

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

(With Deloitte & Touche audit report dated March 10, 2010)

CHUNGHWA TELECOM CO., LTD. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(In Millions of New Taiwan or U.S. Dollars)

	Year Ended December 31			
	2007	2008	2009	
	NT\$	NT\$	NT\$	US\$ (Note 3)
CASH FLOWS FROM OPERATING ACTIVITIES				
Consolidated net income	\$ 48,742	\$ 45,792	\$ 44,495	\$ 1,393
Adjustments to reconcile net income to net cash provided by operating activities:				
Provision for doubtful accounts	606	505	462	14
Depreciation and amortization	39,815	38,216	36,320	1,137
Amortization of premium of financial assets	-	3	16	-
Loss (gain) on disposal of financial instruments, net	(99)	672	142	4
Valuation loss on inventory	19	59	56	2
Valuation loss (gain) on financial instruments, net	585	(551)	(99)	(3)
Loss on disposal of property, plant and equipment, net	89	278	7	-
Equity in losses (earnings) of equity method investees, net	(141)	(64)	23	1
Dividends received from equity investees	44	217	89	3
Loss arising from natural calamities	42	-	149	5
Impairment loss on assets	24	1,168	110	4
Loss on disposal of leased assets, net	-	1	-	-
Deferred income taxes	(825)	(156)	1,099	34
Other	(2)	-	-	-
Changes in operating assets and liabilities:				
Decrease (increase) in:				
Financial assets held for trading	(265)	(207)	221	7
Trade notes and accounts receivable	1,763	127	(1,492)	(47)
Receivables from related parties	(506)	(389)	(70)	(2)
Other monetary assets	(194)	4,841	350	11
Inventories	(155)	(270)	(144)	(5)
Other current assets	(344)	(1,181)	510	16
Increase (decrease) in:				
Financial liabilities held for trading	-	-	-	-
Trade notes and accounts payable	340	190	(1,565)	(49)
Payables to related parties	684	656	(206)	(6)
Income tax payable	(1,385)	(1,571)	(1,377)	(43)
Accrued expenses	(3,378)	907	950	30
Other current liabilities	355	809	777	24
Deferred income	550	567	422	13
Accrued pension liabilities	2,640	1,244	(3,960)	(124)
Net cash provided by operating activities	<u>89,004</u>	<u>91,863</u>	<u>77,285</u>	<u>2,419</u>
CASH FLOWS FROM INVESTING ACTIVITIES				
Acquisition of designated financial assets at fair value through profit or loss	-	-	(45)	(1)
Proceeds from disposal of financial assets at fair value through profit or loss	-	-	63	2
Acquisition of available-for-sale financial assets	(22,695)	(8,759)	(9,263)	(290)
Proceeds from disposal of available-for-sale financial assets	11,736	8,425	8,097	253
Acquisition of held-to-maturity financial assets	(1,198)	(3,327)	(2,100)	(66)
Proceeds from disposal of held-to-maturity financial assets	49	660	869	27
Acquisition of financial assets carried at cost	(188)	(486)	(142)	(4)
Proceeds from disposal of financial assets carried at cost	-	355	302	9
Decrease in other monetary assets	-	(30)	-	-
Proceeds from sale of other monetary assets	-	29	-	-
Acquisition of investments accounted for using equity method	(1,177)	(555)	(560)	(18)
Proceeds from disposal of long-term investment	70	44	-	-
Acquisition of property, plant and equipment	(25,068)	(30,119)	(25,478)	(797)
Proceeds from disposal of property, plant and equipment	108	14	65	2

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CHUNGHWA TELECOM CO., LTD. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(In Millions of New Taiwan or U.S. Dollars)

	Year Ended December 31			
	2007	2008	2009	
	NT\$	NT\$	NT\$	US\$ (Note 3)
Increase in intangible assets	\$ (273)	\$ (208)	\$ (274)	\$ (9)
Increase in restricted assets	-	(3)	(91)	(3)
Increase in other assets	<u>(47)</u>	<u>(566)</u>	<u>(914)</u>	<u>(28)</u>
Net cash used in investing activities	<u>(38,683)</u>	<u>(34,526)</u>	<u>(29,471)</u>	<u>(923)</u>
CASH FLOWS FROM FINANCING ACTIVITIES				
Increase (decrease) in short-term loans	(90)	222	485	15
Increase in long-term loans	22	-	400	13
Repayment of long-term loans	(911)	(37)	(124)	(4)
Decrease in customers' deposits	(325)	(127)	(118)	(4)
Increase (decrease) in other liabilities	171	(294)	(198)	(7)
Cash dividends paid	(34,751)	(41,202)	(37,836)	(1,184)
Remuneration to board of directors and supervisors and bonus to employees	(1,300)	(1,394)	-	-
Purchase of treasury stock	(7,217)	-	-	-
Proceeds from exercise of employee stock option granted by subsidiary	29	64	58	2
Cash proceeds from subsidiary's stock issuance	78	-	-	-
Capital reduction	<u>-</u>	<u>(9,558)</u>	<u>(19,116)</u>	<u>(598)</u>
Net cash used in financing activities	<u>(44,294)</u>	<u>(52,326)</u>	<u>(56,449)</u>	<u>(1,767)</u>
EFFECT OF EXCHANGE RATE CHANGES	<u>(1)</u>	<u>31</u>	<u>(7)</u>	<u>-</u>
EFFECT OF CHANGE ON CONSOLIDATED SUBSIDIARIES	<u>(466)</u>	<u>13</u>	<u>613</u>	<u>20</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	5,560	5,055	(8,029)	(251)
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	<u>70,673</u>	<u>76,233</u>	<u>81,288</u>	<u>2,544</u>
CASH AND CASH EQUIVALENTS, END OF YEAR	<u>\$ 76,233</u>	<u>\$ 81,288</u>	<u>\$ 73,259</u>	<u>\$ 2,293</u>
SUPPLEMENTAL INFORMATION				
Interest paid (excluding capitalized interest expense)	<u>\$ 17</u>	<u>\$ 4</u>	<u>\$ 14</u>	<u>\$ -</u>
Income tax paid	<u>\$ 15,268</u>	<u>\$ 15,620</u>	<u>\$ 13,024</u>	<u>\$ 408</u>
NON-CASH FINANCING ACTIVITIES				
Current portion of long-term loans	<u>\$ 20</u>	<u>\$ 8</u>	<u>\$ 117</u>	<u>\$ 3</u>
Reclassification from common capital stock to due to stockholders for capital reduction	<u>\$ 9,558</u>	<u>\$ 19,116</u>	<u>\$ 9,697</u>	<u>\$ 303</u>
CASH AND NON-CASH INVESTING ACTIVITIES				
Increase in property, plant and equipment	\$ 25,493	\$ 31,162	\$ 25,151	\$ 787
Payables to suppliers	(428)	(1,071)	359	11
Prepayments for equipment	<u>3</u>	<u>28</u>	<u>(32)</u>	<u>(1)</u>
	<u>\$ 25,068</u>	<u>\$ 30,119</u>	<u>\$ 25,478</u>	<u>\$ 797</u>

(Continued)

CHUNGHWA TELECOM CO., LTD. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(In Millions of New Taiwan or U.S. Dollars)

The following table presents the aggregate allocation of acquisition costs of CHSI, CHTG and DHT as well as that of SENAO during 2007, including professional fees and other related acquisition costs, to the assets acquired and liabilities assumed, based on their fair values:

	Allocation of the Acquisition Cost	
	SENAO	CHSI, CHTG and DHT
	NT\$	NT\$
Cash and cash equivalents	\$ 617	\$ 152
Financial assets at fair value through profit or loss	87	326
Trade notes and accounts receivable	2,024	476
Inventories	1,626	136
Other current assets	334	136
Long-term investment	13	-
Property, plant, and equipment	1,317	30
Identifiable intangible assets	366	47
Other assets	135	55
Total assets acquired	<u>6,519</u>	<u>1,358</u>
Short-term loan and current portion of long-term loan	(100)	-
Trade notes and accounts payable	(1,629)	(482)
Other current liabilities	(715)	(82)
Long-term debt	(580)	(8)
Other liabilities	(93)	(2)
Total liabilities assumed	<u>(3,117)</u>	<u>(574)</u>
Net assets acquired	<u>3,402</u>	<u>784</u>
Percentage of ownership	<u>31.3285%</u>	<u>100%</u>
	1,066	784
Goodwill	<u>-</u>	<u>136</u>
Acquisition cost of acquired subsidiaries	<u>\$ 1,066</u>	<u>\$ 920</u>

The acquisition of InfoExplorer Co., Ltd. ("IFE") was made on January 20, 2009. The following table presents the allocation of acquisition costs of IFE to assets acquired and liabilities assumed based on their fair values on the basis of the final data on May 7, 2009:

Cash and cash equivalents	\$ 458
Receivables	13
Other current assets	15
Property, plant, and equipment	40
Identifiable intangible assets	53
Refundable deposits	3
Other assets	2
Payables	(83)
Income tax payable	-
Other current liabilities	-
Total	<u>501</u>
Percentage of ownership	<u>49.07%</u>
	245
Goodwill	<u>38</u>
Acquisition costs of acquired subsidiary (cash prepaid for long-term investments in December 2008)	<u>\$ 283</u>

(Continued)

CHUNGHWA TELECOM CO., LTD. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(In Millions of New Taiwan or U.S. Dollars)

The acquisition of additional interest of Chunghwa Investment Co., Ltd. ("CHI") and its subsidiaries was made on September 9, 2009. The following table presents the allocation of acquisition costs of Chunghwa Investment Co., Ltd. and its subsidiaries to assets acquired and liabilities assumed based on their fair values on the basis of the final data performed:

Cash and cash equivalents	\$	914
Financial assets at fair value through profit or loss		51
Available-for-sale financial assets		568
Trade notes and accounts receivable		76
Inventories		60
Other current assets		19
Investments accounted for equity method		57
Financial assets carried at cost		156
Property, plant, and equipment		90
Identifiable intangible assets		34
Other assets		22
Trade notes and accounts payable		(34)
Accrued expenses		(16)
Income tax payable		(1)
Short-term loans		(20)
Long-term loans		(24)
Other liabilities		(1)
Subtotal		<u>1,951</u>
Minority interests		<u>(100)</u>
Total		<u>1,851</u>
Percentage of additional ownership		<u>40%</u>
Goodwill		<u>741</u>
Acquisition costs of acquired subsidiary paid in cash	\$	<u>759</u>

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

(With Deloitte & Touche audit report dated March 10, 2010)

(Concluded)

CHUNGHWA TELECOM CO., LTD. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. GENERAL

Chunghwa Telecom Co., Ltd. (“Chunghwa”) was incorporated on July 1, 1996 in the Republic of China (“ROC”) pursuant to the Article 30 of the Telecommunications Act. Chunghwa 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 to as Chunghwa which continues to carry out the business and the DGT continues to be the industry regulator.

As the dominate telecommunications service provider of fixed-line and Global System for Mobile Communications (“GSM”) in the ROC, Chunghwa is subject to additional regulations imposed by ROC.

Effective August 12, 2005, the MOTC had completed the process of privatizing Chunghwa by reducing the government ownership to below 50% in various stages. In July 2000, Chunghwa received approval from the Securities and Futures Commission (the “SFC”) for a domestic initial public offering and its common shares were listed and traded on the Taiwan Stock Exchange (the “TSE”) on October 27, 2000. Certain of Chunghwa’s common shares had been sold, in connection with the foregoing privatization plan, in domestic public offerings at various dates from August 2000 to July 2003. Certain of Chunghwa’s common shares had also been sold in an international offering of securities in the form of American Depository Shares (“ADS”) on July 17, 2003 and were listed and traded on the New York Stock Exchange (the “NYSE”). The MOTC sold common shares of Chunghwa by auction in the ROC on August 9, 2005 and completed the second international offering on August 10, 2005. Upon completion of the share transfers associated with these offerings on August 12, 2005, the MOTC owned less than 50% of the outstanding shares of Chunghwa and completed the privatization plan.

Senao International Co., Ltd. (“SENAO”) was incorporated in 1979. SENAO engages mainly in selling and maintaining mobile phones and its peripheral products. Chunghwa acquired 31.33% shares of SENAO on January 15, 2007 and has substantial control in SENAO by obtaining half of the seats of the board of directors of SENAO on April 12, 2007. On March 27, 2009, the board of directors of Chunghwa resolved to purchase 48,000 thousand common shares of SENAO through SENAO’s private placement. However, Chunghwa and SENAO did not complete the required procedures within the legal payment period; therefore, Chunghwa and SENAO decided to discontinue the private placement.

Senao International (Samoa) Holding Ltd. (SIS) was established by SENAO in 2009. SIS will engage mainly in international investment activities; however, no capital is injected in SIS and SIS is not on operation stage yet by the end of 2009.

Senao International HK Limited (SIHK) was established by SIS in 2009. SIHK will engage mainly in the sales of telecommunication business; however, no capital is injected in SIHK and SIHK is not on operation stage yet by the end of 2009.

Chunghwa established Chunghwa International Yellow Pages Co., Ltd. (“CIYP”) in January 2007. CIYP engages mainly in yellow pages sales and advertisement services.

CHIEF Telecom Inc. (“CHIEF”) was incorporated in 1991. CHIEF engages mainly in internet communication and internet data center (“IDC”) service. Chunghwa acquired 70% of the shares of CHIEF on September 2006.

Unigate Telecom Inc. (“Unigate”) was established by CHIEF in 1999. Unigate engages mainly in telecommunication and information software service.

CHIEF Telecom (Hong Kong) Limited (“CHIEF (HK)”) was established by CHIEF in 2003. CHIEF (HK) engages mainly in internet communication and internet data center (“IDC”) service. On August 20, 2009, the stockholders of CHIEF (HK) resolved to dissolve CHIEF (HK). CHIEF (HK) will enter into liquidation process upon receiving the local government authorization. This procedure is still in the application phase as of the date of the audit report.

Chief International Corp. (“CIC”) was established by CHIEF in 2008. CIC engages mainly in internet communication and internet data center (“IDC”) services.

Chunghwa System Integration Co., Ltd. (“CHSI”) was incorporated in 2002. CHSI engages mainly in providing communication and information integration services. Chunghwa has acquired 100% shares of CHSI in December 2007.

Concord Technology Co., Ltd. (“Concord”), a subsidiary of CHSI, was incorporated in 2006. Concord engages mainly in investment.

Glory Network System Service (Shanghai) Co., Ltd. (“GNSS (Shanghai)”), a subsidiary of Concord, was incorporated in 2006. GNSS (Shanghai) engages mainly in planning and designing of systems and communications and information integration services. On March 20, 2009, the stockholders of CHSI resolved to dissolve GNSS (Shanghai). On July 23, 2009, the board of directors of CHSI revoked the original resolution of dissolution.

Chunghwa Telecom Global, Inc. (“CHTG”) was incorporated in 2004. CHTG engages mainly in international data and internet services and long distance call wholesales to carriers. Chunghwa acquired 100% shares of CHTG in December 2007.

Donghwa Telecom Co., Ltd. (“DHT”) was incorporated in 2004. DHT engages mainly in international telecommunications, IP fictitious internet and internet transfer services. Chunghwa acquired 100% shares of DHT in December 2007.

Spring House Entertainment Inc. (“SHE”) was incorporated in 2000. SHE engages mainly in network services, producing digital entertainment contents and broadband visual sound terrace development. SHE was an equity method investee before Chunghwa obtained control interest over it in January 2008.

Chunghwa established Light Era Development Co., Ltd. (“LED”) in January 2008. LED engages mainly in development of property for rent and sale.

LED signed the contract with Good Neighbor Labuan Holdings Ltd. to acquire 100% ownership interest of Yao Yong Real Property. The consideration for this transaction is NT\$2,790 million in cash to acquire 83,290 thousand shares at NT\$33.494 per share on March 1, 2010. Yao Yong Real Property Co., Ltd. engages mainly in real estate leasing business.

Chunghwa established Chunghwa Telecom Singapore Pte. Ltd. (“CHTS”) in July 2008, CHTS engages mainly in telecommunication wholesale, internet transfer services, international data, long distance call wholesales to carriers and the world satellite business.

Chunghwa established Chunghwa Telecom Japan Co., Ltd. (“CHTJ”) 100% owned subsidiary in October 2008. CHTJ engages mainly in telecommunication business, information processing and information providing service, development and sale of software and consulting services in telecommunication.

InfoExplorer Co., Ltd. (“IFE”) was incorporated in 2008. IFE engages mainly in information system planning and maintenance, software development, and information technology consultation services. Chunghwa acquired 49% shares of IFE on January 5, 2009 and has control over IFE by obtaining half of seats of the board of directors of IFE on January 20, 2009.

Chunghwa Investment Co., Ltd. (“CHI”) was established in 2002. CHI engages mainly in professional investing in telecommunication business, telecommunication valued-added services, and system integration. Chunghwa acquired additional 40% of the shares of CHI on September 9, 2009 for NT\$759 million. Chunghwa increased its ownership interest in CHI from 49% to 89% and became the parent company of CHI. As a result of additional acquisition of CHI, the accounts of CHI and its subsidiaries are included in the consolidated financial statements starting from September 9, 2009.

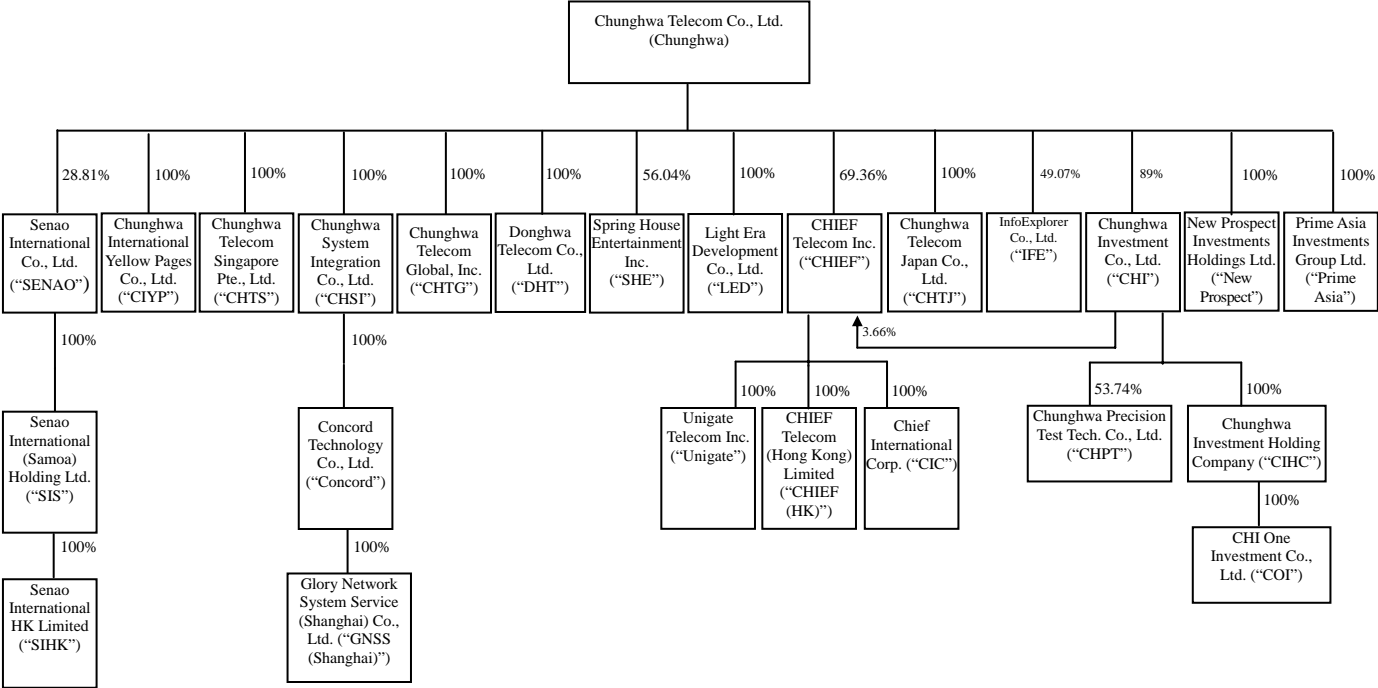
Chunghwa Precision Test Tech. Co., Ltd. (“CHPT”) was established in 2005 as the subsidiary of CHI. CHPT engages mainly in production and marketing in semiconductor testers and printed circuit boards.

Chunghwa Investment Holding Company (“CIHC”) was established by CHI in 2004. CIHC engages mainly in investment activities.

CHI One Investment Co., Ltd. (COI) was established by CHI in 2009. COI engages mainly in investment activities. There was no capital injection by the end of 2009. The capital injection in January 2010 was amounted to NT\$14 million.

Chunghwa has established New Prospect Investments Holdings Ltd. (“New Prospect”) and Prime Asia Investments Group Ltd. (“Prime Asia”) in March 2006, but not on operation stage yet. Both holding companies are operating as investment companies and Chunghwa has 100% ownership right in an amount of US\$1 in each holding company.

The following diagram presents information regarding the relationship and ownership percentages between Chunghwa and its subsidiaries as of December 31, 2009:



Chunghwa together with its subsidiaries are hereinafter referred to collectively as the “Company”. Minority interests in the aforementioned subsidiaries are presented as a separate component of stockholders’ equity.

As of December 31, 2008 and 2009, the Company had 27,165 and 27,915 employees, respectively.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying consolidated financial statements were prepared in conformity with the accounting principles generally accepted in the ROC ("ROC GAAP"). The preparation of consolidated financial statements requires management to make reasonable estimates and assumptions on allowances for doubtful accounts, valuation allowances on inventories, depreciation of property, plant and equipment, impairment of assets, bonuses paid to employees, directors and supervisors, pension plans and income tax which are inherently uncertain. Actual results may differ from these estimates. The significant accounting policies are summarized as follows:

Principle of Consolidation

The accompanying consolidated financial statements include the accounts of all directly and indirectly majority owned subsidiaries of the Company, and the accounts of investees in which the Company's ownership percentage is less than 50% but over which the Company has a controlling interest. All significant intercompany transactions and balances are eliminated upon consolidation.

The consolidated financial statements for the year ended December 31, 2008 include the accounts of Chunghwa, SENA, CIYP, CHIEF, Unigate, CHIEF (HK), CIC, CHSI, Concord, GNSS (Shanghai), CHTG, DHT, SHE, LED, CHTS, CHTJ, New Prospect and Prime Asia. The consolidated financial statements for the year ended December 31, 2009 include the accounts of Chunghwa, SENA, SIS, SIHK, CIYP, CHIEF, Unigate, CHIEF (HK), CIC, CHSI, Concord, GNSS (Shanghai), CHTG, DHT, SHE, LED, CHTS, CHTJ, IFE, CHI, CHPT, CIHC, COI, New Prospect and Prime Asia.

For foreign subsidiaries using their local currency as their functional currency, assets and liabilities are translated into New Taiwan dollars at the exchange rates in effect on the balance sheet date; stockholders' equity accounts are translated into New Taiwan dollars at historical exchange rates and income statement accounts are translated into New Taiwan dollars at average exchange rates during the year.

Business Combination

Acquisitions are accounted for using the purchase method of accounting. 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.

Classification of Current and Noncurrent Assets and Liabilities

Current assets are assets expected to be converted to cash, sold or consumed within one year from balance sheet date. Current liabilities are obligations expected to be settled within one year from balance sheet date. Assets and liabilities that are not classified as current are noncurrent assets and liabilities, respectively.

LED engages mainly in development of property for rent and sale. The assets and liabilities of LED related to property development within its operating cycle which is over one year are classified as current items. For assets and liabilities related to property development over its operating cycle are classified as noncurrent items.

Cash Equivalents

Cash equivalents is commercial paper with maturity of three months or less from the date of acquisition. The carrying amount approximates fair value.

Financial Assets and Liabilities at Fair Value Through Profit or Loss

Financial instruments classified as financial assets or financial liabilities at fair value through profit or loss (“FVTPL”) include financial assets or financial liabilities held for trading and those designated as at FVTPL on initial recognition. The Company recognizes a financial asset or a financial liability when the Company becomes a party to the contractual provisions of the financial instrument. A financial asset is derecognized when the Company loses control of its contractual rights over the financial asset. A financial liability is derecognized when the obligation specified in the relevant contract is discharged, cancelled or expired.

Financial instruments at FVTPL are initially measured at fair value. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at FVTPL are recognized as expenses as incurred. Financial assets or financial liabilities at FVTPL are remeasured at fair value, with subsequent changes in fair value recognized in earnings. Cash dividends received subsequently (including those received in the period of investment) are recognized as income. On derecognition of a financial asset or a financial liability, the difference between its carrying amount and the sum of the consideration received and receivable or consideration paid and payable is recognized in earnings. A regular way purchase or sale of financial assets is accounted for using trade date accounting.

Derivatives that do not meet the criteria for hedge accounting are classified as financial assets or financial liabilities held for trading. When the fair value is positive, the derivative is recognized as a financial asset; when the fair value is negative, the derivative is recognized as a financial liability.

Available-for-sale Financial Assets

Available-for-sale financial assets are initially recognized at fair value plus transaction costs that are directly attributable to the acquisition. Changes in fair value from subsequent remeasurement are reported as a separate component of stockholders’ equity. The corresponding accumulated gains or losses are recognized in earnings when the financial asset is derecognized from the balance sheet. A regular way purchase or sale of financial assets is accounted for using trade date accounting.

The recognition and derecognition of available-for-sale financial assets are similar to those of financial assets at FVTPL.

Fair values are determined as follows: Listed stocks - at closing prices at the balance sheet date; open-end mutual funds - at net asset values at the balance sheet date; bonds - quoted prices provided by the Taiwan GreTai Securities Market; and financial assets and financial liabilities without quoted prices in an active market - at values determined using valuation techniques.

Cash dividends are recognized in earnings on the ex-dividend date, except for the dividends declared before acquisition which are treated as a reduction of investment cost. Stock dividends are recorded as an increase in the number of shares and do not affect investment income. The total number of shares subsequent to the increase of stock dividends is used for recalculate cost per share.

An impairment loss is recognized when there is objective evidence that the financial asset is impaired. If, in a subsequent period, the amount of the impairment loss decreases, for equity securities, the previously recognized impairment loss is reversed to the extent of the decrease and recorded as an adjustment to stockholders' equity; for debt securities, the amount of the impairment loss decrease is recognized in earnings, provided that the decrease is clearly attributable to an event which occurred after the impairment loss was recognized.

Held-to-maturity Financial Assets

Held-to-maturity financial assets are carried at amortized cost using the effective interest method. Those financial assets are initially recognized at fair value plus transaction costs that are directly attributable to the acquisition. Gains and losses are recognized at the time of derecognition, impairment or amortization. A regular way purchase or sale of financial assets is accounted for using trade date accounting.

If there is objective evidence which indicates that a financial asset is impaired, a loss is recognized. If, in a subsequent period, the amount of the impairment loss decreases and the decrease is clearly attributable to an event which occurred after the impairment loss was recognized, the previously recognized impairment loss is reversed to the extent of the decrease. The reversal may not result in a carrying amount that exceeds the amortized cost that would have been determined as if no impairment loss had been recognized.

Revenue Recognition, Account Receivables and Allowance for Doubtful Receivables

Revenues are recognized when they are realized or realizable and earned. Revenues are realized or realizable and earned 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.

Revenue is measured at the fair value of the consideration received or receivable and represents amounts agreed between the Company and the customers for goods sold in the normal course of business, net of sales discounts and volume rebates. For trade receivables due within one year from the balance sheet date, as the nominal value of the consideration to be received approximates its fair value and transactions are frequent, fair value of the consideration is not determined by discounting all future receipts using an imputed rate of interest.

Usage revenues from fixed-line services (including local, domestic long distance and international long distance), cellular services, Internet and data services, and interconnection and call transfer fees from other telecommunications companies and carriers are billed in arrears and are recognized based upon minutes of traffic processed when the services are provided in accordance with contract terms.

The costs of providing services are recognized as incurred. Incentives to third party dealers for inducing business which are payable when the end user enters into an airtime contract are recognized in marketing expenses as incurred.

Other revenues are recognized as follows: (a) one-time subscriber connection fees (on fixed-line services) are deferred and recognized over the average expected customer service periods, (b) monthly fees (on fixed-line services, wireless and Internet and data services) are accrued every month, and (c) prepaid services (fixed line, cellular and Internet) are recognized as income based upon actual usage by customers or when the right to use those services expires.

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

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.

An allowance for doubtful receivables is provided based on a review of the collectibility of accounts receivable. The Company determines the amount of allowance for doubtful receivables by examining the aging analysis of outstanding accounts receivable as well as historical collection experience.

Inventories

Inventories including merchandise and work-in-process are stated at the lower of cost (weighted-average cost) or net realizable value item by item, except for those that may be appropriate to group items of similar or related inventories. Net realizable value is the estimated selling price of inventories less all estimated costs of completion and costs necessary to make the sale. The calculation of the cost of inventory is derived using the weighted-average method.

Inventories of LED are stated at the lower of cost or net realizable value. Prepayments for licensing and other miscellaneous costs have been capitalized as part of inventory. Profit shall be recognized in full when the land is sold, provided (a) the profit is determinable, that is, the collectibility of the sales price is reasonably assured or the amount that will not be collectible can be estimated, and (b) the earnings process is virtually completed.

The effect on changes in accounting principles of inventory is discussed in Note 4.

Investments Accounted for Using Equity Method

Investments in companies in which Chunghwa exercises significant influence over the operating and financial policy decisions are accounted for by the equity method. Under the equity method, the investment is initially stated at cost and subsequently adjusted for its proportionate share in the net earnings of the investee companies. Any cash dividends received are recognized as a reduction in the carrying value of the investments.

Gains or losses on sales from the Company to equity method investees wherein Chunghwa exercises significant influence over these equity investees are deferred in proportion to the Company's ownership percentage in the investees until such gains or losses are realized through transactions with third parties. Gains or losses on sales from equity method investees to Chunghwa are deferred in proportion to Chunghwa's ownership percentages in the investees until they are realized through transactions with third parties.

When the Company subscribes for additional investees shares at a percentage different from its existing ownership percentage, the resulting carrying amount of the investment in the investee differs from the amount of the Company share of the investee's equity. The Company records such a difference as an adjustment to long-term investments with the corresponding amount charged or credited to additional paid-in capital to the extent available, with the balance charged to retained earnings.

Financial Assets Carried at Cost

Investments in equity instruments that do not have a quoted price in an active market and whose fair values cannot be reliably measured such as non-publicly traded stocks are measured at their original cost. If there is objective evidence which indicates that a financial asset is impaired, a loss is recognized. A subsequent reversal of such impairment loss is not allowed.

The accounting treatment for cash dividends and stock dividends arising from financial assets carried at cost is the same as that for cash dividends and stock dividends arising from available-for-sale financial assets.

Property, Plant and Equipment

Property, plant and equipment are stated at cost plus a revaluation increment, if any, less accumulated depreciation and accumulated impairment loss. The interest costs that are directly attributable to the acquisition, construction of a qualifying asset are capitalized as property, plant and equipment. Major renewals and betterments are capitalized, while maintenance and repairs are expensed as incurred.

When an indication of impairment is identified, any excess of the carrying amount of an asset over its recoverable amount is recognized as a loss. If the recoverable amount increases in a subsequent period, the amount previously recognized as impairment would be reversed and recognized as a gain. However, the adjusted amount may not exceed the carrying amount that would have been determined, net of depreciation, as if no impairment loss had been recognized.

An impairment loss on a revalued asset is charged to “unrealized revaluation increment” under equity to the extent available, with the balance recognized as a loss in earnings. If the recoverable amount increases in a subsequent period, the amount previously recognized as impairment loss could be reversed and recognized as a gain, with the remaining credited to “unrealized revaluation increment”.

Depreciation expense is computed using the straight-line method over the following estimated service lives: land improvements - 10 to 30 years; buildings - 10 to 60 years; computer equipment - 3 to 10 years; telecommunication equipment - 5 to 30 years; transportation equipment - 5 to 10 years; and miscellaneous equipment - 2 to 12 years.

Upon sale or disposal of property, plant and equipment, the related cost, accumulated depreciation, accumulated impairment losses and any unrealized revaluation increment are deducted from the corresponding accounts, and any gain or loss recorded as non-operating gains or losses in the year of sale or disposal.

Intangible Assets

Intangible assets mainly include 3G Concession, computer software, patents and goodwill.

The 3G Concession is valid through December 31, 2018. The 3G Concession fee is amortized on a straight-line basis from the date operations commence through the date the license expires. Computer software costs and patents are amortized using the straight-line method over the estimated useful lives of 2-20 years.

The Company adopted the newly released Statements of Financial Accounting Standards No. 37, “Intangible Assets.” Expenditure on research shall be expensed as incurred. Development costs are capitalized when those costs meet relative criteria and are amortized using the straight-line method over estimated useful lives. Development costs that do not meet relative criteria shall be expensed as incurred.

When an indication of impairment is identified other than goodwill, any excess of the carrying amount of an asset over its recoverable amount is recognized as a loss. If the recoverable amount increases in a subsequent period, the amount previously recognized as impairment would be reversed and recognized as a gain. However, the adjusted amount may not exceed the carrying amount that would have been determined, as if no impairment loss had been recognized.

Goodwill represents the excess of the consideration paid over the fair value of identifiable net assets acquired. Goodwill is tested for impairment annually. If an event occurs or circumstances change which indicates that the fair value of goodwill is below its carrying amount, an impairment loss is recognized. A subsequent reversal of such impairment loss is not allowed.

Pension Costs

For defined benefit pension plans, net periodic pension benefit cost is recorded in the consolidated statement of income and includes service cost, interest cost, expected return on plan assets, amortization of prior service costs, amortization of pension gains (losses) and curtailment or settlement gains (losses).

The Company recognizes into income, any unrecognized actuarial net gains or losses that exceed 10% of the larger of projected benefit obligations or plan assets, defined as the “corridor”. Amounts inside this 10% corridor are amortized over the average remaining service life of active plan participants. Actuarial net gains and losses occur when actual experience differs from any of the many assumptions used to value the plans. Differences between the expected and actual returns on plan assets and changes in interest rate, which affect the discount rate used to value projected plan obligations, can have a significant impact on the calculation of pension net gains and losses from year to year.

The curtailments and settlement gains (losses) resulted from the Chunghwa’s early retirement programs. Curtailment/settlement gains or losses are equal to the changes of underfunded status plus a pro rata portion of the unrecognized prior service cost, unrecognized net gains (losses), and unrecognized transition obligations/assets, before the settlement/curtailment event multiplied by the percentage reduction in projected benefit obligation.

The projected benefit obligation represents the actuarial present value of benefits expected to be paid upon retirement based on estimated future compensation levels.

The carrying amount of accrued pension liability should be the sum of the following amounts: (a) projected benefit obligation as of balance sheet date, (b) minus (plus) unamortized actuarial loss (gain), (c) minus unamortized prior service cost, and (d) minus the fair value of plan assets. If the amount determined by above calculation is negative, it is viewed as prepaid pension cost. The prepaid pension cost is measured at the lower of: (a) the amount determined above, and (b) the sum of the following amounts: (i) unamortized actuarial loss, (ii) unamortized prior service cost, and (iii) the present value of refunds from the plan or reductions in future contributions to the plan.

The measurement of benefit obligations and net periodic cost (income) is based on estimates and assumptions approved by the Company’s management such as compensation, age and seniority, as well as certain assumptions, including estimates of discount rates, expected return on plan assets and rate of compensation increases.

For employees under defined contribution pension plans, pension costs are recorded based on the actual contributions made to employees’ individual pension accounts during their service periods.

Expense Recognition

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

Treasury Stock

Treasury stock is recorded at cost and shown as a reduction to stockholders’ equity. Upon cancellation of treasury stock, the treasury stock account is reduced and the common stock and capital surplus are reversed on a pro rata basis. If capital surplus is not sufficient for debiting purpose, the difference is charged to retained earnings.

Share-based Compensation

Employee stock options granted on or after January 1, 2008 are accounted for using fair value method in accordance with under SFAS No. 39, “Accounting for Share-based Payment.” The adoption of SFAS No. 39 did not have any impact on the Company.

Employee stock options granted between January 1, 2004 and December 31, 2007 were accounted for under the interpretations issued by the Accounting Research and Development Foundation (the "ARDF"). The Company adopted the intrinsic value method, under which compensation cost was amortized over the vesting period.

Income Tax

The Company applies inter-period allocations for its income tax, whereby deferred income tax assets and liabilities are recognized for the tax effects of temporary differences and unused tax credits. Valuation allowances are provided to the extent, if any, that it is more likely than not that deferred income tax assets will not be realized. A deferred tax asset or liability is classified as current or noncurrent in accordance with the classification of its related asset or liability. However, if a deferred tax asset or liability does not relate to an asset or liability in the financial statements, then it is classified as either current or noncurrent based on the expected length of time before it is realized or settled.

Any tax credits arising from purchases of machinery, equipment and technology, research and development expenditures, personnel training, and investments in important technology-based enterprises are recognized using the flow-through method.

Adjustments of prior years' tax liabilities are added to or deducted from the current year's tax provision.

Income taxes (10%) on undistributed earnings is recorded in the year of stockholders approval which is the year subsequent to the year the earnings are generated.

Foreign-currency Transactions

Foreign-currency transactions are recorded in New Taiwan dollars at the rates of exchange in effect when the transactions occur. Exchange gains or losses derived from foreign-currency transactions or monetary assets and liabilities denominated in foreign currencies are recognized in earnings. At the balance sheet date, monetary assets and liabilities denominated in foreign currencies are revalued at prevailing exchange rates with the resulting gains or losses recognized in earnings.

The financial statements of foreign equity investees and consolidated subsidiaries are translated into New Taiwan dollars at the following exchange rates. Assets and liabilities - spot rates at year-end; stockholders' equity - historical rates, income and expenses - average rates during the year. The resulting translation adjustments are recorded as a separate component of stockholders' equity.

Hedge Accounting

A hedging relationship qualifies for hedge accounting only if, all of the following conditions are met: (a) at the inception of the hedge, there is formal documentation of the hedging relationship and the entity's risk management objective and strategy for undertaking the hedge; (b) the hedge is expected to be highly effective in achieving offsetting changes in fair value attributable to the hedged risk, consistently with the risk management strategy documented for that particular hedging relationship; (c) the effectiveness of the hedge can be reliably measured; (d) the hedge is assessed on an ongoing basis and determined actually to have been highly effective throughout the financial reporting periods for which the hedge was designated.

The gain or loss from remeasuring the hedging instrument at fair value and the gain or loss on the hedged item attributable to the hedged risk are recognized in earnings.

The hedging items that do not meet the criteria for hedge accounting were classified as financial assets or financial liabilities at fair value through profit or loss.

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 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.

Earnings Per Share and Per Equivalent ADS

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

Per share data has been restated for all periods presented to reflect capital reductions in 2007, 2008 and 2009 and the declaration of the stock dividends.

Securities issued by a subsidiary that enable their holders to obtain the subsidiary's common stock shall be included in computing the subsidiary's earnings per share data. Those per-share earnings of the subsidiary shall then be included in the consolidated earnings per share computations based on the consolidated Company's holding of the subsidiary's securities.

3. US DOLLAR AMOUNTS

The Company maintains its accounts and expresses its consolidated financial statements in New Taiwan dollars. For convenience only, US dollar amounts presented in the accompanying consolidated financial statements have been translated from New Taiwan dollars at the noon buying rate in The City of New York for cable transfers in New Taiwan dollars as certified for customs purposes by the Federal Reserve Bank of New York as of December 31, 2009, which was NT\$31.95 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.

4. EFFECT OF CHANGES IN ACCOUNTING PRINCIPLES

In March 2007, the ARDF issued an Interpretation 96-052 that requires companies to recognize bonuses paid to employees, directors and supervisors as an expense rather than an appropriation of earnings beginning from January 1, 2008. For purposes of the statement of cash flows, such bonuses represent appropriations of the earnings from prior years and have been classified as financing activities for 2007, 2008. Beginning from 2009, such bonuses are classified as operating activities for purposes of the statement of cash flows when paid.

The Company adopted the newly-revised Statement of Financial Accounting Standards No. 10, "Accounting for Inventories," ("SFAS No. 10") beginning from January 1, 2009, which requires inventories to be stated at the lower of cost (weighted-average cost) or net realizable value item by item, except for those that may be appropriate to group items of similar or related inventories. The inventory-related incomes and expenses shall be classified as operating cost. The adoption of the revised SFAS No. 10 did not have significant impact on the Company's consolidated net income and basic earnings per share (after income tax) for the year ended December 31, 2009. The Company reclassified non-operating losses of NT\$19 million and NT\$59 million to operating costs for the years ended December 31, 2007 and 2008.

The Company early adopted the Statement of Financial Accounting Standards No. 41 “Operating Segments” (“SFAS No. 41”) starting from September 1, 2009. This Statement supersedes the Statement of Financial Accounting Standards No. 20 “Segment Reporting”. This new statement allows users of financial statements to see performance of segments from viewpoint of chief operating decision maker. For comparative purposes, the segment information for the years ended December 31, 2007, 2008 and 2009 was presented in accordance with SFAS No. 41.

5. CASH AND CASH EQUIVALENTS

	December 31	
	2008	2009
	NT\$	NT\$
(In Millions)		
Cash		
Cash on hand	\$ 148	\$ 142
Bank deposits	12,830	8,199
Negotiable certificate of deposit, annual yield rate - ranging from 0.31%-2.45% and 0.25%-0.37% for 2008 and 2009, respectively	<u>48,486</u>	<u>63,350</u>
	<u>61,464</u>	<u>71,691</u>
Cash equivalents		
Commercial paper, annual yield rate - ranging from 0.70%-1.55% and 0.19%-0.24% for 2008 and 2009, respectively	<u>19,824</u>	<u>1,568</u>
	<u>\$ 81,288</u>	<u>\$ 73,259</u>

6. FINANCIAL ASSETS AND LIABILITIES AT FAIR VALUE THROUGH PROFIT OR LOSS

	December 31	
	2008	2009
	NT\$	NT\$
(In Millions)		
Derivatives - financial assets		
Currency swap contracts	\$ -	\$ 7
Index future contracts	243	-
Forward exchange contracts	16	-
Designated financial assets at fair value through profit or loss		
Convertible bonds	<u>-</u>	<u>34</u>
	<u>\$ 259</u>	<u>\$ 41</u>
Derivatives - financial liabilities		
Forward exchange contracts	\$ 96	\$ 1
Index future contracts	<u>11</u>	<u>-</u>
	<u>\$ 107</u>	<u>\$ 1</u>

Chunghwa entered into investment management agreements with well-known financial institutions (fund managers) to manage its investment portfolios in 2006. The investment portfolios managed by these fund managers aggregated to an original amount of US\$100 million. Chunghwa terminated the investment management agreements on March 2, 2009 and asked fund managers to dispose of all the investment portfolios. The fund managers had disposed of all investment portfolios before June 23, 2009 and returned the proceeds to Chunghwa.

The Company entered into currency swap contracts, 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 and stock prices. However, the aforementioned derivatives did not meet the criteria for hedge accounting and were classified as financial assets or financial liabilities held for trading.

Outstanding currency swap contracts and forward exchange contracts as of December 31, 2008 and 2009:

	Currency	Maturity Period	Contract Amount (In Millions)
<u>December 31, 2008</u>			
Buy	NTD/USD	2009.01	NTD 131
Sell	EUR/USD	2009.01	EUR 4
	JPY/USD	2009.01	JPY 446
	GBP/USD	2009.01	GBP 2
	USD/NTD	2009.01	USD 96
	USD/JPY	2009.01	USD 2
	USD/EUR	2009.01	USD 1
	USD/GBP	2009.01	USD -
<u>December 31, 2009</u>			
Currency swap contracts	USD/NTD	2010.01-2010.04	USD45/NTD1,448
Forward exchange contracts - buy	NTD/USD	2010.01	NTD87

Outstanding index future contracts on December 31, 2008 were as follows:

	Maturity Period	Units	Contract Amount (In Millions)
<u>December 31, 2008</u>			
AMSTERDAM IDX FUT	2009.01	13	EUR 1
CAC40 10 EURO FUT	2009.01	14	EUR 1
DAX INDEX FUTURE	2009.03	3	EUR -
IBEX 35 INDX FUTR	2009.01	7	EUR 1
MINI S&P/MIB FUT	2009.03	37	EUR 1
FTSE 100 IDX FUT	2009.03	19	GBP 1
TOPIX INDEX FUTURE	2009.03	35	JPY 284
S&P 500 FUTURE	2009.03	16	USD 4
S&P 500 EMINI FUTURE	2009.03	53	USD 2

As of December 31, 2008, the deposits paid for index future contracts were NT\$243 million.

The Company did not have any outstanding index future contracts on December 31, 2009.

The convertible bonds owned by CHI are hybrid financial instruments that shall be measured and designated as at fair value through profit or loss.

In September 2007, Chunghwa entered into a 10-year, foreign currency derivative contract with Goldman Sachs Group Inc. (“Goldman”) and valuations were made biweekly starting from September 20, 2007 which were 260 valuation periods totally. Under the terms of the contract, if the NT dollar/U.S. dollar exchange rate was less than NT\$31.50 per U.S. dollar at any two consecutive bi-weekly valuation dates during the valuation period starting from October 4, 2007 to September 5, 2017, Chunghwa was required to make a cash payment to Goldman. The settlement amount was determined by the difference between the applicable exchange rates and the base amount of US\$4 million. Conversely, if the NT dollar/U.S. dollar exchange rate was above NT\$31.50 per U.S. dollar using the same valuation methodology, Goldman would have a settlement obligation to Chunghwa determined using a base amount of US\$2 million. Further, if the exchange rate was at or above NT\$32.70 per U.S. dollar starting from December 12, 2007 at any time, the contract would be terminated at that time. In accordance with the terms of the contract, Chunghwa deposited US\$3 million with Goldman with annual yield rate of 8%. On October 21, 2008, the exchange rate was above NT\$32.70 per U.S. dollar, so the contract was terminated at that time.

Net gains arising from financial assets and liabilities at fair value through profit or loss for the years ended December 31, 2008 and 2009 were NT\$486 million (including realized settlement loss of NT\$38 million and valuation gain of NT\$524 million), and NT\$72 million (including realized settlement loss of NT\$26 million and valuation gain of NT\$98 million), respectively.

7. AVAILABLE-FOR-SALE FINANCIAL ASSETS

	<u>December 31</u>	
	<u>2008</u>	<u>2009</u>
	NT\$	NT\$
	(In Millions)	
Open-end mutual funds	\$ 13,442	\$ 16,832
Domestic listed stocks	-	500
Corporate bonds	-	103
Real estate investment trust fund	194	102
Foreign listed stocks	<u>546</u>	<u>-</u>
	<u>\$ 14,182</u>	<u>\$ 17,537</u>

Movements of unrealized gain (loss) on available-for-sale financial assets were as follows:

	<u>Year Ended December 31</u>	
	<u>2008</u>	<u>2009</u>
	NT\$	NT\$
	(In Millions)	
Balance, beginning of year	\$ 37	\$ (2,265)
Impact on acquisition of subsidiaries	-	2
Recognized in stockholders' equity	(3,185)	1,685
Transferred to profit or loss	<u>883</u>	<u>131</u>
Balance, end of year	<u>\$ (2,265)</u>	<u>\$ (447)</u>

Global economic and financial circumstances have significantly changed. As a result, Chunghwa determined that the impairment losses of available-for-sale financial assets is other-than-temporary in nature, and recorded impairment losses of NT\$1,139 million and NT\$85 million for the years ended December 31, 2008 and 2009, respectively. There was no other-than-temporary impairment loss for the year ended December 31, 2007.

8. HELD-TO-MATURITY FINANCIAL ASSETS

	December 31	
	2008	2009
	NT\$	NT\$
	(In Millions)	
Corporate bonds, nominal interest rate ranging from 1.93%-2.95% and 0.76%-4.75% for 2008 and 2009, respectively; effective interest rate ranging from 1.80%-2.95% and 0.45%-2.95%, respectively	\$ 2,635	\$ 4,532
Bank debentures, nominal interest rate ranging from 2.11%-3.85% and 1.87%-2.11% for 2008 and 2009, respectively; effective interest rate ranging from 2.33%-2.90% and 1.14%-2.90%, respectively	1,137	498
Collateralized loan obligation, nominal and effective interest rate was 2.18% for 2008	<u>41</u>	<u>-</u>
	3,813	5,030
Less: Current portion	<u>769</u>	<u>1,100</u>
	<u>\$ 3,044</u>	<u>\$ 3,930</u>

9. ALLOWANCE FOR DOUBTFUL ACCOUNTS

	Year Ended December 31		
	2007	2008	2009
	NT\$	NT\$	NT\$
	(In Millions)		
Balance, beginning of year	\$ 3,550	\$ 3,430	\$ 3,051
Provision for doubtful accounts	608	501	455
Impact on acquisition of subsidiaries	113	1	-
Accounts receivable written off	<u>(841)</u>	<u>(881)</u>	<u>(707)</u>
Balance, end of year	<u>\$ 3,430</u>	<u>\$ 3,051</u>	<u>\$ 2,799</u>

10. OTHER MONETARY ASSETS - CURRENT

	December 31	
	2008	2009
	NT\$	NT\$
	(In Millions)	
Accrued custodial receipts from other carriers	\$ 484	\$ 433
Other receivables	<u>1,742</u>	<u>1,407</u>
	<u>\$ 2,226</u>	<u>\$ 1,840</u>

11. INVENTORIES, NET

	December 31	
	2008	2009
	NT\$	NT\$
	(In Millions)	
Merchandise	\$ 2,304	\$ 2,034
Work in process	<u>319</u>	<u>647</u>
	2,623	2,681
Land held under development	706	706
Land held for development	532	563
Prepayment for construction	<u>40</u>	<u>99</u>
	<u>\$ 3,901</u>	<u>\$ 4,049</u>

The operating costs related to inventories were NT\$19,613 million (including the valuation loss on inventories of NT\$19 million), NT\$24,283 million (including the valuation loss on inventories of NT\$59 million) and NT\$23,116 million (including valuation loss on inventories of NT\$56 million) for the years ended December 31, 2007, 2008 and 2009, respectively.

Land held under development on December 31, 2009 was for Wan-Xi project which is expected to be completed in 2012.

12. OTHER CURRENT ASSETS

	December 31	
	2008	2009
	NT\$	NT\$
	(In Millions)	
Spare parts	\$ 2,511	\$ 2,349
Prepaid rents	843	812
Prepaid expenses	682	652
Miscellaneous	<u>521</u>	<u>507</u>
	<u>\$ 4,557</u>	<u>\$ 4,320</u>

13. INVESTMENTS ACCOUNTED FOR USING EQUITY METHOD

	December 31			
	2008		2009	
	Carrying Amount	% of Owner- ship	Carrying Amount	% of Owner- ship
	NT\$ (In Millions)		NT\$ (In Millions)	
Non-listed				
Taiwan International Standard Electronics Co., Ltd. ("TISE")	\$ 594	40	\$ 428	40
ST-2 Satellite Ventures Pte., Ltd. ("STS")	108	38	408	38
Senao Networks, Inc. ("SNI")	264	45	288	41
Viettel-CHT Co., Ltd. ("Viettel-CHT")	96	33	270	30
Skysoft Co., Ltd. ("SKYSOFT")	85	30	90	30
KingWay Technology Co., Ltd. ("KWT")	77	33	70	33
Tatung Technology Inc.	-	-	37	28
So-net Entertainment Co., Ltd. ("So-net")	-	-	31	30
Chunghwa Investment Co., Ltd. ("CHI")	830	49	-	-
PandaMonium Company Ltd.	-	-	-	43
	<u>2,054</u>		<u>1,622</u>	
Prepayments for long-term investments				
InfoExplorer Co., Ltd. ("IFE")	<u>283</u>		<u>-</u>	
	<u>\$ 2,337</u>		<u>\$ 1,622</u>	

ST-1 telecommunications satellite is expected to be retired in 2011; therefore, CHTS and SingTelSat Pte., Ltd. established a joint venture, ST-2 Satellite Ventures Pte., Ltd. ("STS") in Singapore in October 2008 in order to maintain the current service. By December 31, 2009, Chunghwa has invested NT\$409 million in STS. STS will engage in the installation and the operation of ST-2 telecommunications satellite.

Chunghwa established Viettel-CHT Co., Ltd. with Viettel Co., Ltd. in Vietnam in April 2008, by investing NT\$91 million cash. Chunghwa participated in the capital increase of Viettel-CHT in September 2009, by investing NT\$197 million cash and its ownership interest of Viettel-CHT decreased from 33% to 30%. Viettel-CHT engages mainly in IDC services.

Chunghwa invested in KingWay Technology Co., Ltd. ("KWT") in January 2008, for a purchase price of NT\$72 million. KWT engages mainly in publishing books, data processing and software services.

PandaMonium Company Ltd. and Tatung Technology Inc are the subsidiaries of Chunghwa Investment Co., Ltd. They engage mainly in making animations and selling the product of SET TOP BOX, respectively.

Chunghwa participated in So-net Entertainment Co., Ltd.'s capital increase on April 3, 2009, by investing NT\$60 million cash, and acquired 30% of its shares. So-net Entertainment Co., Ltd. engages mainly in online service and sale of computer hardware.

The equity in earnings for the years ended December 31, 2008 and 2009 are based on the audited financial statements.

14. FINANCIAL ASSETS CARRIED AT COST

	December 31			
	2008		2009	
	Carrying Amount	% of Owner- ship	Carrying Amount	% of Owner- ship
	NT\$ (In Millions)		NT\$ (In Millions)	
Non-listed				
Taipei Financial Center (“TFC”)	\$ 1,790	12	\$ 1,790	12
Industrial Bank of Taiwan II Venture Capital Co., Ltd. (“IBT II”)	200	17	200	17
Global Mobile Corp. (“GMC”)	127	11	127	11
iD Branding Ventures (“iDBV”)	75	8	100	11
Giga Solar Materials Corp.	-	-	55	2
UnDisplay Inc.	-	-	46	3
RPTI International (“RPTI”)	34	12	34	10
Digimax Inc. (“DIG”)	-	-	24	4
ChipSip Technology Co.	-	-	23	3
Superior Industries Co., Ltd.	-	-	23	2
N.T.U. Innovation Incubation	12	9	12	9
Crystal Media Inc.	-	-	12	5
LightHouse Technology Co.	-	-	11	-
Join Well Technology Co.	-	-	8	-
Tatung Fine Chemicals Co.	-	-	8	-
Win Semiconductors Corp.	-	-	8	-
Huga Optotech Inc.	-	-	7	-
DelSolar Co.	-	-	5	-
J Touch Corporation	-	-	4	-
Taidoc Technology Corporation	-	-	3	-
3 Link Information Service Co.	4	10	4	10
Subtron Technology Co.	-	-	3	-
Cando Corporation	-	-	3	-
XinTec Inc.	-	-	1	-
Daxon Technology Inc.	-	-	-	-
Essence Technology Solution, Inc. (“ETS”)	10	9	-	9
eASPNet Inc.	-	2	-	2
	<u>2,252</u>		<u>2,511</u>	
Prepayments for long-term investments in stocks				
GoaTronics Inc.	-	-	25	-
Huga Optotech Inc.	-	-	1	-
Cando Corporation	-	-	-	-
Taipei Financial Center (“TFC”)	285	-	-	-
	<u>285</u>		<u>26</u>	
	<u>\$ 2,537</u>		<u>\$ 2,537</u>	

Chunghwa invested in IBT II in January 2008, for a purchase price of NT\$200 million. IBT II completed its incorporation on February 13, 2008 and engages mainly in investment activities.

Chunghwa invested in GMC in December 2007, for a purchase price of NT\$168 million for 16,796 thousand shares. GMC engages mainly in wire communication services and computer software wholesale and circuit engineering. The National Communications Commission (“NCC”) informed Chunghwa with the Communication Letter (#0974102087) on April 1, 2008 that its investment in GMC was not authorized by NCC, and notified Chunghwa on May 5, 2008 that Chunghwa should dispose of its investment in GMC no later than June 30, 2008, otherwise, NCC would fine Chunghwa according to the Telecommunication Act. In April 2008, Chunghwa disposed of a portion of its investment in GMC (4,100 thousand shares) and filed an appeal to NCC to suspend the enforcement. In July 2008, NCC resolved that according to the Administrative Penalty Act, Chunghwa could not divest of its investment in the short time period provided and that Chunghwa would not be subject to fines as noted above. In October 2008, NCC revoked the original decree about Chunghwa’s investment in GMC; therefore, Chunghwa did not dispose of its remaining holding in GMC.

After evaluating the financial assets carried at cost, Chunghwa determined the investment in RPTI was impaired and recognized an impairment loss of NT\$15 million for the year ended December 31, 2008. RPTI completed a capital reduction to offset its deficits and as a result the number of shares held by Chunghwa was reduced from 9,234 thousand shares to 4,765 thousand shares. Subsequent to this capital reduction, RPTI raised additional capital through cash contributions. Chunghwa did not participate in the RPTI’s capital increase plan; therefore, Chunghwa’s ownership of RPTI is decreased to 10%.

After evaluating the financial assets carried at cost, CHI determined the investment in DIG was impaired and recognized an impairment loss of NT\$10 million for the year ended December 31, 2009.

After evaluating the financial assets carried at cost, Chunghwa determined the investment in ETS was impaired and recognized an impairment loss of NT\$10 million both in 2008 and 2009.

Chunghwa participated in TFC’s capital increase in October 2008 and prepaid NT\$285 million. However, TFC is not expected to be able to collect enough amount of capital increase within a specific period; therefore TFC’s board of directors held a meeting on April 10, 2009 and resolved to withdraw its capital increase plan from Financial Supervisory Commission, Executive Yuan (“FSC”). TFC returned the prepayment to Chunghwa on May 8, 2009.

The above investments that do not have a quoted market price in an active market and whose fair values cannot be reliably measured are carried at original cost.

15. OTHER MONETARY ASSETS - NONCURRENT

	December 31	
	2008	2009
	NT\$	NT\$
	(In Millions)	
Piping Fund	<u>\$ 1,000</u>	<u>\$ 1,000</u>

As part of the government’s effort to upgrade the existing telecommunications infrastructure, Chunghwa and other public utility companies were required by the ROC government to contribute a total of NT\$1,000 million to a Piping Fund administered by the Taipei City Government. This fund was used to finance various telecommunications infrastructure projects.

In January 2008, CHSI invested in Taiwan Goal Co., Ltd. (“TG”) for a purchase price of NT\$30 million. TG engages mainly in import and export activities for machine wholesale, arms and ammunition products. On March 17, 2008, the stockholders of TG resolved to dissolve TG at a special meeting. Therefore, CHSI has reclassified its investment to other monetary assets and recognized a loss of NT\$1 million for the three months ended March 31, 2008. As of December 31, 2008, TG has completed its dissolution process. CHSI received NT\$29 million for the liquidation and recognized additional loss of NT\$1 million in 2008.

16. PROPERTY, PLANT AND EQUIPMENT, NET

	December 31	
	2008	2009
	NT\$	NT\$
	(In Millions)	
Cost		
Land	\$ 101,460	\$ 102,132
Land improvements	1,495	1,535
Buildings	63,029	63,184
Computer equipment	16,130	16,344
Telecommunications equipment	650,204	656,016
Transportation equipment	2,406	2,113
Miscellaneous equipment	<u>7,332</u>	<u>7,231</u>
Total cost	842,056	848,555
Revaluation increment on land	<u>5,811</u>	<u>5,801</u>
	<u>847,867</u>	<u>854,356</u>
Accumulated depreciation		
Land improvements	898	951
Buildings	16,299	17,395
Computer equipment	11,846	12,150
Telecommunications equipment	503,425	518,609
Transportation equipment	2,195	1,886
Miscellaneous equipment	<u>6,159</u>	<u>6,030</u>
	<u>540,822</u>	<u>557,021</u>
Construction in progress and advances payments related to acquisition of equipment	<u>16,005</u>	<u>15,687</u>
Property, plant and equipment, net	<u>\$ 323,050</u>	<u>\$ 313,022</u>

Pursuant to the related regulation, Chunghwa revalued its land owned as of April 30, 2000 based on the publicly announced value on July 1, 1999. These revaluations which have been approved by the Ministry of Auditing resulted in increases in the carrying values of property, plant and equipment of NT\$5,986 million, liabilities for land value incremental tax of NT\$211 million, and stockholders' equity - other adjustments of NT\$5,775 million.

The amendment to the Land Tax Act, relating to the article to permanently lower land value incremental tax, went effective from February 1, 2005. In accordance with the lowered tax rates, Chunghwa recomputed its land value incremental tax, and reclassified the reserve for land value incremental tax of NT\$116 million to stockholders' equity - other adjustments. As of December 31, 2009, the unrealized revaluation increment was decreased to NT\$5,803 million by disposal of revaluation assets.

Depreciation expense on property, plant and equipment was NT\$38,816 million, NT\$37,101 million and NT\$35,114 million for the years ended December 31, 2007, 2008 and 2009, respectively. Interest expense capitalized for the years ended December 31, 2007, 2008 and 2009 were NT\$1 million, NT\$2 million and NT\$1 million. The capitalized interest rates were 2.850%-3.215%, 2.268%-2.928% and 1.165%-1.604%, respectively, for the years ended December 31, 2007, 2008 and 2009.

Losses on property, plant and equipment arising from natural calamities such as earthquakes and typhoons were recorded in non-operating expenses.

17. SHORT-TERM LOANS

	December 31	
	2008	2009
	NT\$	NT\$
	(In Millions)	
Secured loans - annual rate - 0.81% for 2009	\$ -	\$ 488
Unsecured loans - annual rate - 1.70% and 1.15%-1.23% for 2008 and 2009, respectively	<u>258</u>	<u>275</u>
	<u>\$ 258</u>	<u>\$ 763</u>

18. ACCRUED EXPENSES

	December 31	
	2008	2009
	NT\$	NT\$
	(In Millions)	
Accrued salary and compensation	\$ 9,254	\$ 9,876
Accrued franchise fees	2,369	2,224
Accrued employees' bonuses and remuneration to directors and supervisors	1,891	1,964
Other accrued expenses	<u>2,832</u>	<u>3,385</u>
	<u>\$ 16,346</u>	<u>\$ 17,449</u>

19. OTHER CURRENT LIABILITIES

	December 31	
	2008	2009
	NT\$	NT\$
	(In Millions)	
Advances from subscribers	\$ 6,151	\$ 6,908
Payables to contractors	1,546	2,229
Amounts collected in trust for others	2,535	2,225
Payables to equipment suppliers	2,526	1,533
Refundable customers' deposits	981	1,045
Miscellaneous	<u>2,791</u>	<u>2,930</u>
	<u>\$ 16,530</u>	<u>\$ 16,870</u>

20. LONG-TERM LOANS (INCLUDING LONG-TERM LOANS - CURRENT PORTION)

	<u>December 31</u>	
	<u>2008</u>	<u>2009</u>
	NT\$	NT\$
	(In Millions)	
Unsecured loans - annual rate 2.01%-2.04% for 2009	\$ -	\$ 310
Secured loans - annual rate 1.00% and 1.00%-1.37% for 2008 and 2009, respectively	<u>37</u>	<u>28</u>
	37	338
Less: Current portion of long-term loans	<u>8</u>	<u>117</u>
	<u>\$ 29</u>	<u>\$ 221</u>

CHIEF obtained an unsecured loan from Bank of Taiwan in January 2009. Interest and principal amount are repaid monthly from January 2009 and due in January 2013.

SHE applied to the Industrial Development Bureau, Ministry of Economic Affairs and obtained a secured loan from Taiwan Business Bank. Interest is paid monthly and the principal is repaid every three months from January 2009 and due in April 2013.

CHPT obtained a secured loan from the E. Sun Commercial Bank in December 2006. Interest and the principal are repaid monthly from January 2007 and due in December 2009. CHI obtained another loan from the E. Sun Commercial Bank in February 2009. Interest and the principal are repaid monthly from 2009 and due in February 2013.

The scheduled maturities of our long-term debt are as follows:

For the year ending December 31

2010	\$ 117
2011	111
2012	102
2013	<u>8</u>
Total long-term debt	<u>\$ 338</u>

21. MATURITY ANALYSIS OF ASSETS AND LIABILITIES

The Company classified LED's assets and liabilities of the construction operations as current and noncurrent according to the length of the operating cycle of the construction operations. Maturity analysis of LED's related current assets and liabilities was as follows:

	December 31, 2008		
	With in	Over	Total
	One Year	One Year	NT\$
	NT\$	NT\$	NT\$
	(In Millions)		
<u>Assets</u>			
Inventories	\$ -	\$ 1,278	\$ 1,278
Deferred expenses (classified as other current assets)	-	92	92
Restricted assets	-	55	55
	<u>\$ -</u>	<u>\$ 1,425</u>	<u>\$ 1,425</u>
<u>Liabilities</u>			
Trade notes and accounts payable	\$ 4	\$ -	\$ 4
Advance from land and building (classified as other current liabilities)	-	227	227
	<u>\$ 4</u>	<u>\$ 227</u>	<u>\$ 231</u>
December 31, 2009			
	With in	Over	Total
	One Year	One Year	NT\$
	NT\$	NT\$	NT\$
	(In Millions)		
<u>Assets</u>			
Inventories	\$ -	\$ 1,369	\$ 1,369
Deferred expenses (classified as other current assets)	-	93	93
Restricted assets	-	101	101
	<u>\$ -</u>	<u>\$ 1,563</u>	<u>\$ 1,563</u>
<u>Liabilities</u>			
Trade notes and accounts payable	\$ 6	\$ -	\$ 6
Advance from land and building (classified as other current liabilities)	-	328	328
	<u>\$ 6</u>	<u>\$ 328</u>	<u>\$ 334</u>

22. STOCKHOLDERS' EQUITY

Under Chunghwa's Articles of Incorporation, Chunghwa's authorized capital is NT\$120,000 million, which is divided into 12,000,000,000 common shares (at \$10 par value per share), among which 9,696,808,181 shares are issued and outstanding as of December 31, 2009.

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. In accordance with the Articles of Incorporation of Chunghwa, the preferred shares would be redeemed by Chunghwa three years from the date of issuance at their par value. These preferred shares expired on April 4, 2009 and were redeemed on April 6, 2009.

For the purpose of privatizing Chunghwa, the MOTC sold 1,109,750 thousand common shares of Chunghwa in an international offering of securities in the form of American Depositary Shares ("ADS") amounting to 110,975 thousand units (one ADS represents ten common shares) on the New York Stock Exchange on July 17, 2003. Afterwards, the MOTC sold 1,350,682 thousand common shares in the form of ADS amounting to 135,068 thousand units on August 10, 2005. Subsequently, the MOTC and Taiwan Mobile Co., Ltd. sold 505,389 thousand and 58,959 thousand common shares of Chunghwa, respectively, in the form of ADS totally amounting to 56,435 thousand units on September 29, 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. As of December 31, 2009, the outstanding ADSs were 1,182,888 thousand common shares, which equaled approximately 118,289 thousand units and represented 12.20% of Chunghwa's total outstanding common shares.

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:

- a. Exercise their voting rights,
- b. Sell their ADSs, and
- c. Receive dividends declared and subscribe to the issuance of new shares.

Under the ROC Company Law, additional paid-in capital may only be utilized to offset deficits. For those companies having no deficits, additional paid-in capital arising from capital surplus can be used to increase capital stock and distribute to stockholders in proportion to their ownership at the ex-dividend date. Also, such amounts can only be declared as a stock dividend by Chunghwa at an amount calculated in accordance with the provisions of existing regulations. The combined amount of any portions capitalized each year may not exceed 10 percent of common stock issued. However, where a company undergoes an organizational change (such as a merger, acquisition, or reorganization) that results in the capitalization of undistributed earnings after the organizational change, the above restriction does not apply.

In addition, before distributing a dividend or making any other distribution to stockholders, Chunghwa 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 remaining earnings comprising remaining balance of net income, if any, plus cumulative undistributed earnings shall be distributed in the following order: (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; and (c) cash dividends to be distributed shall not be less than 50% of the total amount of dividends to be distributed. 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.

Chunghwa operates in a capital-intensive and technology-intensive industry and requires capital expenditures to sustain its competitive position in a high-growth market. Thus, Chunghwa's dividend policy takes into account future capital expenditure outlays. In this regard, a portion of the earnings may be retained to finance these capital expenditures. The remaining earnings can then be distributed as dividends if approved by the stockholders in the following year and will be recorded in the financial statements of that year.

For the years ended December 31, 2008 and 2009, the accrual amounts for bonuses to employees and remuneration to directors and supervisors were accrued on past experiences and probable amount to be paid in accordance with Chunghwa's Articles of Incorporation and Implementation Guidance for the Employee's Bonus Distribution of Chunghwa Telecom Co., Ltd.

If the initial accrual amounts of the aforementioned bonus are significantly different from the amounts proposed by the board of directors, the difference is charged to the earnings of the year making the initial estimate. Otherwise, the difference between initial accrual amount and the amount resolved in the shareholders' meeting is charged to the earnings of the following year as a result of change in accounting estimate.

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 Chunghwa. 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 Chunghwa, up to 50% of the reserve may, at the option of Chunghwa, be declared as a stock dividend and transferred to capital.

The appropriations and distributions of the 2007 and 2008 earnings of Chunghwa have been approved and resolved by the stockholders on June 19, 2008 and June 19, 2009 as follows:

	<u>Appropriation of Earnings</u>		<u>Dividends Per Share</u>	
	<u>For Fiscal Year 2007</u>	<u>For Fiscal Year 2008</u>	<u>For Fiscal Year 2007</u>	<u>For Fiscal Year 2008</u>
	<u>NT\$</u>	<u>NT\$</u>	<u>NT\$</u>	<u>NT\$</u>
Legal reserve	\$ 4,823	\$ 4,128	\$ -	\$ -
Special reserve	-	-	-	-
Reversal of special reserve	3	-	-	-
Cash dividends	40,716	37,139	4.26	3.83
Stock dividends	956	-	0.10	-
Employee bonus - cash	1,304	-	-	-
Employee bonus - stock	435	-	-	-
Remuneration to board of directors and supervisors	43	-	-	-

The amounts for bonuses to employees and remuneration to directors and supervisors approved in the stockholders' meeting on June 19, 2009, were NT\$1,630 million and NT\$39 million, respectively. The bonuses to employees were all settled in cash. The aforementioned approved amounts of the bonuses to employees and the remuneration to directors and supervisors were different from the accrual amounts of NT\$1,724 million and NT\$41 million, respectively, reflected in the statement of income for the year ended December 31, 2008. The differences of NT\$94 million and NT\$2 million, respectively, were treated as change in estimates and were adjusted against earnings for the year ended December 31, 2009.

The stockholders, at a meeting held on June 19, 2009, resolved to transfer capital surplus in the amount of NT\$9,697 million to common capital stock. The abovementioned 2009 capital increase proposal was effectively approved by FSC. The board of directors authorized the chairman of directors to decide the ex-dividend date of the aforementioned proposal and the chairman decided the ex-dividend date as August 9, 2009.

The stockholders, at the stockholders' meeting held on June 19, 2009, also resolved to reduce the amount of capital in Chunghwa by a cash distribution to its stockholders in order to improve the financial condition of Chunghwa and better utilize its excess funds. The abovementioned 2009 capital reduction proposal was effectively approved by FSC. The board of directors of Chunghwa further authorized the chairman of board of directors of Chunghwa to designate the record date of capital reduction as of October 26, 2009. Subsequently, common capital stock was reduced by NT\$9,697 million and the stock transfer date of capital reduction was January 28, 2010. The amount due to stockholders for capital reduction was paid in February 2010.

The stockholders, at a special meeting held on August 14, 2008, resolved to transfer capital surplus in the amount of NT\$19,116 million to common capital stock. The abovementioned 2008 capital increase proposal was effectively registered with FSC. The board of directors resolved the ex-dividend date of the aforementioned proposal as October 25, 2008.

The stockholders, at the stockholders' meeting held on August 14, 2008, also resolved to reduce the amount of capital in Chunghwa by a cash distribution to its stockholders in order to improve the financial condition of Chunghwa and better utilize its excess funds. The capital reduction plan was effected by a transfer of capital surplus in the amount of NT\$19,116 million to common capital stock and was effectively registered with FSC. Chunghwa designated December 30, 2008 as the record date and March 9, 2009 as the stock transfer date of capital reduction. Subsequently, common capital stock was reduced by NT\$19,116 million and a liability for the same amount of cash to be distributed to stockholders was recorded. Such cash payment to stockholders was made in March 2009.

The stockholders, at a meeting held on June 15, 2007, resolved to transfer capital surplus in the amount of NT\$9,668 million to common capital stock and the capital increase proposal was effectively registered with FSC.

The stockholders, at the stockholders' meeting held on June 15, 2007, also resolved to reduce the amount of capital in Chunghwa by a cash distribution to its stockholders in order to improve the financial condition of Chunghwa and better utilize its excess funds. The capital reduction plan was effected by a transfer of capital surplus in the amount of NT\$9,668 million to common capital stock and was effectively registered with FSC. Chunghwa designated October 19, 2007 and December 29, 2007 as the record date and the stock transfer date of capital reduction, respectively. Subsequently, common capital stock was reduced by NT\$9,668 million and a liability for the actual amount of cash to be distributed to stockholders of NT\$9,558 million was recorded. The difference between the reduction in common capital stock and the distribution amount represents treasury stock of NT\$110 million held by Chunghwa and concurrently cancelled. Such cash payment to stockholders was made in January 2008.

The appropriation of Chunghwa's 2009 earnings has not been resolved by the board of directions as of the report date. Information on the appropriation of Chunghwa's 2009 earnings, employee bonus and remuneration to directors and supervisors resolved by the board of directors and approved by the stockholders will be available at the Market Observation Post System website.

23. SHARE-BASED COMPENSATION PLANS

SENAO's share-based compensation plans ("SENAO Plans") described as follows:

Effective Date	Grant Date	Stock Options Units (Thousands)	Exercise Price
2003.09.03	2003.10.17	3,981	\$ 14.7 (Original price \$20.2)
2003.09.03	2004.03.04	385	17.6 (Original price \$23.9)
2004.12.01	2004.12.28	6,500	10.0 (Original price \$11.6)
2004.12.01	2005.11.28	1,500	14.4 (Original price \$18.3)
2005.09.30	2006.05.05	10,000	13.3 (Original price \$16.9)
2007.10.16	2007.10.31	6,181	42.6 (Original price \$44.2)
		<u>28,547</u>	

Each option is eligible to subscribe for one common share when exercisable. Under the terms of the Plans, the options are granted at an exercise price equal to the closing price of the SENAO's common shares listed on the TSE on the higher of closing price or par value. The SENAO Plans have exercise price adjustment formula upon the issuance of new common shares, capitalization of retained earnings and/or capital reserves, stock split as well as distribution of cash dividend (except for 2007 Plan), except (i) in the case of issuance of new shares in connection with mergers and in the case of cancellation of outstanding shares in connection with capital reduction (2007 Plan is out of this exception), and (ii) except if the exercise price after adjustment exceeds the exercise price before adjustment. The options of all the Plans are valid for six years and the graded vesting schedule for which 50% of option granted will vest two years after the grant date and another two tranches of 25% will vest three and four years after the grant date respectively.

Information about SENAO's outstanding stock options for the years ended December 31, 2008 and 2009 was as follows:

	Stock Options Outstanding			
	2008		2009	
	Number of Options (Thousands)	Weighted Average Exercise Price NT\$	Number of Options (Thousands)	Weighted Average Exercise Price NT\$
Options outstanding, beginning of year	18,592	\$24.70	13,818	\$26.34
Options exercised	(4,299)	13.64	(4,076)	13.75
Options expired	<u>(475)</u>	23.10	<u>(419)</u>	31.35
Options outstanding, end of year	<u>13,818</u>	26.34	<u>9,323</u>	30.92
Options exercisable, end of year	<u>2,559</u>		<u>4,545</u>	

As of December 31, 2008, information about SENAO's outstanding and exercisable options was as follows:

Range of Exercise Price (NT\$)	Options Outstanding			Options Exercisable	
	Number of Options (Thousand)	Weighted-average Remaining Contractual Life (Years)	Weighted Average Exercise Price (NT\$)	Number of Options (Thousand)	Weighted Average Exercise Price (NT\$)
\$10.0-\$14.3	6,852	3.08	\$13.49	1,959	\$13.38
\$15.5-\$18.9	933	2.25	15.60	600	15.65
\$42.6	<u>6,033</u>	4.92	42.60	<u>-</u>	-
	<u>13,818</u>	3.83	26.34	<u>2,559</u>	13.91

As of December 31, 2009, information about SENAO's outstanding and exercisable options was as follows:

Range of Exercise Price (NT\$)	Options Outstanding			Options Exercisable	
	Number of Options (Thousand)	Weighted-average Remaining Contractual Life (Years)	Weighted Average Exercise Price (NT\$)	Number of Options (Thousand)	Weighted Average Exercise Price (NT\$)
\$10.0-\$13.3	3,427	2.20	\$12.96	1,512	\$12.54
\$14.4-\$17.6	259	1.92	14.40	259	14.40
\$42.6	<u>5,637</u>	3.92	42.60	<u>2,774</u>	42.60
	<u>9,323</u>	3.23	30.92	<u>4,545</u>	30.99

No compensation cost was recognized under the intrinsic value method for the years ended December 31, 2007, 2008 and 2009. Had SENAO used the fair value method to recognize the compensation cost, there would have been no significant impact on the consolidated net income and earnings per share.

Had SENAO used the fair value method to evaluate the options using the Black-Scholes model, the assumptions of SENAO for the year ended December 31, 2009 would have been as follows:

	March 4, 2004	December 28, 2004	November 28, 2005	May 5, 2006	October 31, 2007
Expected dividend yield	-	-	-	-	1.49%
Risk free interest rate	1.88%	1.88%	2.00%	1.75%	2.00%
Expected life	4.375 years	4.375 years	4.375 years	4.375 years	4.375 years
Expected volatility	52.65%	49.88%	43.40%	39.63%	39.82%
Weighted-average fair value of grants	\$10.56	\$4.91	\$6.93	\$5.88	\$13.69

24. TREASURY STOCK (COMMON STOCK IN THOUSANDS OF SHARES)

	Year Ended December 31	
	2008	2009
	(Shares in Thousands)	
Balance, beginning of the period	110,068	-
Decrease	<u>(110,068)</u>	<u>-</u>
Balance, end of the period	<u> -</u>	<u> -</u>

According to the Securities and Exchange Act of the ROC, total shares of treasury stock shall not exceed 10% of Chunghwa's stock issued. The total amount of the repurchased shares shall not be more than the total amount of retained earnings, capital surplus and realized additional paid-in capital. The Company shall neither pledge treasury stock nor exercise stockholders' rights on these shares, such as rights to dividends and to vote.

In order to maintain its credit and stockholders' equity, Chunghwa repurchased 121,075 thousand shares of treasury stock for NT\$7,218 million from August 29, 2007 to October 25, 2007. On December 29, 2007, Chunghwa cancelled 11,007 thousand shares of treasury stock by reducing common stock of NT\$110 million. The remaining 110,068 thousand shares of treasury stock amounted to NT\$7,107 million was cancelled on February 21, 2008.

25. COMPENSATION, DEPRECIATION AND AMORTIZATION EXPENSES

	Year Ended December 31, 2008		
	Operating Costs	Operating Expenses	Total
	NT\$	NT\$	NT\$
	(In Millions)		
Compensation expense			
Salaries	\$ 12,335	\$ 9,790	\$ 22,125
Insurance	915	704	1,619
Pension	1,617	1,237	2,854
Other compensation	<u>8,494</u>	<u>5,838</u>	<u>14,332</u>
	<u>\$ 23,361</u>	<u>\$ 17,569</u>	<u>\$ 40,930</u>
Depreciation expense	<u>\$ 35,018</u>	<u>\$ 2,083</u>	<u>\$ 37,101</u>
Amortization expense	<u>\$ 889</u>	<u>\$ 186</u>	<u>\$ 1,075</u>

	Year Ended December 31, 2009		
	Operating Costs	Operating Expenses	Total
	NT\$	NT\$	NT\$
		(In Millions)	
Compensation expense			
Salaries	\$ 12,544	\$ 9,901	\$ 22,445
Insurance	999	771	1,770
Pension	1,517	1,138	2,655
Other compensation	<u>8,807</u>	<u>6,031</u>	<u>14,838</u>
	<u>\$ 23,867</u>	<u>\$ 17,841</u>	<u>\$ 41,708</u>
Depreciation expense	<u>\$ 33,169</u>	<u>\$ 1,945</u>	<u>\$ 35,114</u>
Amortization expense	<u>\$ 957</u>	<u>\$ 232</u>	<u>\$ 1,189</u>

26. INCOME TAX

- a. The components of income taxes are as follows:

	Year Ended December 31		
	2007	2008	2009
	NT\$	NT\$	NT\$
		(In Millions)	
Current	\$ 13,884	\$ 14,048	\$ 11,644
Deferred	<u>(825)</u>	<u>(156)</u>	<u>1,099</u>
	<u>\$ 13,059</u>	<u>\$ 13,892</u>	<u>\$ 12,743</u>

- b. 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 income and comprehensive income is as follows:

	Year Ended December 31		
	2007	2008	2009
	NT\$	NT\$	NT\$
		(In Millions)	
Income tax expense computed at statutory tax rate	\$ 15,204	\$ 15,026	\$ 14,404
Permanent differences	(465)	(144)	(188)
Investment tax credits	(2,403)	(1,505)	(1,425)
10% undistributed earning tax	9	2	7
Prior year adjustment	76	78	(196)
Other	<u>638</u>	<u>435</u>	<u>141</u>
Income tax expense	<u>\$ 13,059</u>	<u>\$ 13,892</u>	<u>\$ 12,743</u>

The balance of income tax payable as of December 31, 2007, 2008 and 2009 was shown net of prepaid income tax.

c. Income tax expense consisted of following:

	Year Ended December 31		
	2007	2008	2009
	NT\$	NT\$	NT\$
		(In Millions)	
Income tax payable	\$ 13,565	\$ 13,667	\$ 11,777
Income tax - separated	243	303	63
Income tax - deferred	(825)	(156)	1,099
Adjustments of prior years' income tax	<u>76</u>	<u>78</u>	<u>(196)</u>
	<u>\$ 13,059</u>	<u>\$ 13,892</u>	<u>\$ 12,743</u>

In May 2009, the Legislative Yuan passed the amendment of Article 5 of the Income Tax Law, which reduces the income tax rate of profit-seeking enterprises from 25% to 20% since 2010. The Company recalculated its deferred income tax assets and liabilities in accordance with the amended Article and recorded the resulting difference as an income tax expense or benefit.

d. 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 are shown in the following table:

	December 31	
	2008	2009
	NT\$	NT\$
	(In Millions)	
Current		
Deferred income tax assets:		
Provision for doubtful accounts	\$ 490	\$ 351
Unrealized accrued expense	22	50
Estimated warranty liabilities	13	19
Valuation loss on inventory	31	17
Abandonment of equipment not approved by National Tax Administration	40	5
Unrealized foreign exchange loss (gain)	(35)	3
Loss carryforward	11	2
Investment tax credit	-	1
Valuation loss (gain) on financial instruments, net	14	(9)
Other	<u>11</u>	<u>13</u>
	597	452
Valuation allowance	<u>(478)</u>	<u>(351)</u>
Net deferred income tax assets-current	<u>\$ 119</u>	<u>\$ 101</u>
Noncurrent		
Accrued pension cost	\$ 1,405	\$ 333
Loss carryforward	137	113
Impairment loss	138	64
Investment tax credit	-	17
Loss on disposal of property, plant and equipment	3	1
Other	<u>6</u>	<u>15</u>
	1,689	543
Valuation allowance	<u>(146)</u>	<u>(60)</u>
Net deferred income tax assets-noncurrent	<u>\$ 1,543</u>	<u>\$ 483</u>

As of December 31, 2009, details for investment tax credit of CHI and CHPT are as follows:

Law/Statue	Items	Remaining Creditable Amount	Expiry Year
		NT\$ (In Millions)	
Statute for Upgrading Industries	Pioneer Industry Investment Tax Credit	\$ 7	2011
Statute for Upgrading Industries	Personnel training expenditures	\$ 1	2011
	Personnel training expenditures	4	2012
	Personnel training expenditures	3	2013
	Purchase of machinery and equipment	1	2011
	Purchase of machinery and equipment	1	2012
	Purchase of machinery and equipment	-	2013
		<u>\$ 10</u>	

e. As of December 31, 2009, loss carryforward of CHIEF, Unigate, SHE, LED and CIYP are as follows:

Company	Total Amounts	Unused Amounts	Expiry Year
	NT\$	NT\$	
	(In Millions)		
CHIEF	\$ 23	\$ 23	2013
	18	18	2014
	20	20	2015
	18	18	2016
	10	10	2017
	3	3	2018
	1	1	2019
Unigate	-	-	2017
	-	-	2018
	5	4	2016
SHE	1	1	2017
LED	6	6	2018
	9	9	2019
CIYP	<u>2</u>	<u>2</u>	2019
	<u>\$ 116</u>	<u>\$ 115</u>	

f. The related information under the Integrated Income Tax System is as follows:

	December 31	
	2008	2009
	NT\$	NT\$
Balance of Imputation Credit Account (“ICA”)		
Chunghwa	<u>\$ 7,286</u>	<u>\$ 7,430</u>

The actual and the estimated creditable ratios distribution of Chunghwa’s 2008 and 2009 for earnings were 30.61% and 26.50%, respectively. The imputation credit allocated to stockholders is based on its balance as of the date of dividend distribution. The estimated creditable ratio may change when the actual distribution of imputation credit is made.

g. Undistributed earnings information

All Chunghwa's earnings generated prior to June 30, 1998 have been appropriated.

Chunghwa's income tax returns have been examined by tax authorities through 2005. SENAO's income tax returns have been examined by tax authorities through 2006. The following subsidiaries' income tax returns have been examined by tax authorities through 2007: CHIEF, CHSI, SHE, CIYP, CHI and CHPT. Unigate's income tax returns have been examined by tax authorities through 2008.

27. EARNINGS PER SHARE

EPS was calculated as follows:

	<u>Amount (Numerator)</u>		<u>Weighted-average Number of Common Shares (Thousand) (Denominator)</u>	<u>Earnings Per Share (NT\$)</u>	
	<u>Income Before Income Tax</u>	<u>Net Income</u>		<u>Income Before Income Tax</u>	<u>Net Income</u>
	<u>NT\$</u>	<u>NT\$</u>			
	<u>(In Millions)</u>				
<u>Year ended December 31, 2007</u>					
Basic EPS					
Income attributable to stockholders of the parent	\$ 61,096	\$ 48,249	9,776,237	<u>\$ 6.25</u>	<u>\$ 4.94</u>
Effect of dilutive potential common stock SENAO's stock options	<u>(8)</u>	<u>(8)</u>	<u>-</u>		
Diluted EPS					
Income attributable to stockholders of the parent (including effect of dilutive potential common stock)	<u>\$ 61,088</u>	<u>\$ 48,241</u>	<u>9,776,237</u>	<u>\$ 6.25</u>	<u>\$ 4.93</u>
<u>Year ended December 31, 2008</u>					
Basic EPS					
Income attributable to stockholders of the parent	\$ 58,473	\$ 45,011	9,696,808	<u>\$ 6.03</u>	<u>\$ 4.64</u>
Effect of dilutive potential common stock SENAO's stock options	(14)	(14)	-		
Employee bonus	<u>-</u>	<u>-</u>	<u>20,681</u>		
Diluted EPS					
Income attributable to stockholders of the parent (including effect of dilutive potential common stock)	<u>\$ 58,459</u>	<u>\$ 44,997</u>	<u>9,717,489</u>	<u>\$ 6.02</u>	<u>\$ 4.63</u>
<u>Year ended December 31, 2009</u>					
Basic EPS					
Income attributable to stockholders of the parent	\$ 56,163	\$ 43,757	9,696,808	<u>\$ 5.79</u>	<u>\$ 4.51</u>
Effect of dilutive potential common stock SENAO's stock options	(7)	(7)	-		
Employee bonus	<u>-</u>	<u>-</u>	<u>28,806</u>		
Diluted EPS					
Income attributable to stockholders of the parent (including effect of dilutive potential common stock)	<u>\$ 56,156</u>	<u>\$ 43,750</u>	<u>9,725,614</u>	<u>\$ 5.77</u>	<u>\$ 4.50</u>

In March 2007, the ARDF issued an Interpretation 96-052 that requires companies to recognize bonuses paid to employees, directors and supervisors as an expense rather than an appropriation of earnings beginning from January 1, 2008. According to the Interpretation 97-169 issued by ARDF in May 2008, Chunghwa presumed that the employees bonuses to be paid will be settled in shares and takes those shares into consideration when calculating the weighted average number of outstanding shares used in the calculation of diluted EPS if the shares have a dilutive effect for the years ended December 31, 2008 and 2009. The number of shares is calculated by dividing the amount of bonuses by the closing price of the Chunghwa's shares of the balance sheet date. The dilutive effect of the shares needs to be considered until the stockholders resolve the number of shares to be distributed to employees in their meeting in the following year.

The diluted earnings per share for the years ended December 31, 2007, 2008 and 2009 were also due to the effect of potential common stock of stock options issued by SENA0.

28. PENSION PLANS

Chunghwa completed privatization plans on August 12, 2005. Chunghwa is required to pay all accrued pension obligations including service clearance payment, lump sum payment under civil service plan, additional separation payments, etc. 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 of Chunghwa should be transferred to the Fund for Privatization of Government-owned Enterprises (the "Privatization Fund") under the Executive Yuan. On August 7, 2006, Chunghwa transferred the remaining balance of fund to the Privatization Fund. However, according to the instructions of MOTC, Chunghwa is requested to pay all accrued pension obligations including service clearance payment, lump sum payment under civil service plan, additional separation payments, etc. on behalf of the MOTC upon the completion of the privatization.

The pension plan under the Labor Pension Act of ROC (the "LPA") is effective beginning July 1, 2005 and this pension mechanism is considered as a defined contribution plan. Based on the LPA, Chunghwa, SENA0, CIYP, CHIEF, Unigate, CHSI, SHE, LED make monthly contributions to employees' individual pension accounts at 6% of monthly salaries and wages.

The Company's pension plan is considered as a defined benefit plan under the Labor Standards Law that provide benefits based on an employee's length of service and average six-month salary prior to retirement. Chunghwa, SENA0, CHIEF and SHE contribute an amount no more than 15% of salaries paid each month to their respective pension funds (the Funds), which are administered by the Labor Pension Fund Supervisory Committee (the Committee) and deposited in the names of the Committees in the Bank of Taiwan.

The Company used December 31 as the measurement date for their pension plans.

Pension costs of the Company amounted to NT\$3,139 million (NT\$3,027 million subject to defined benefit plan and NT\$112 million subject to defined contribution plan), NT\$2,938 million (NT\$2,774 million subject to defined benefit plan and NT\$164 million subject to defined contributed plan) and NT\$2,948 million (NT\$2,737 million subject to defined benefit plan and NT\$211 million subject to defined contributed plan) for the years ended December 31, 2007, 2008 and 2009, respectively.

Pension information of the Company of the defined benefit plan is summarized as follows:

a. Components of net periodic pension cost

	Year Ended December 31		
	2007	2008	2009
	NT\$	NT\$	NT\$
	(In Millions)		
Service cost	\$ 2,810	\$ 2,661	\$ 2,695
Interest cost	110	189	189
Expected return on plan assets	(80)	(85)	(144)
Amortizations	8	(2)	(3)
Curtailement/settlement loss to be recognized	<u>179</u>	<u>11</u>	<u>-</u>
Net periodic benefit pension cost	<u>\$ 3,027</u>	<u>\$ 2,774</u>	<u>\$ 2,737</u>

b. The changes in benefits obligation and plan assets and the reconciliation of funded status for the pension plans of subsidiaries are as follows:

	Year Ended December 31		
	2007	2008	2009
	NT\$	NT\$	NT\$
	(In Millions)		
Change in benefits obligation:			
Projected benefits obligation, beginning of year	\$ (4,534)	\$ (6,761)	\$ (9,565)
Services cost	(2,810)	(2,661)	(2,695)
Interest cost	(110)	(189)	(187)
Curtailement/settlement effect	462	79	-
Actuarial (loss) gain	310	(110)	71
Plan Amendments	-	61	-
Benefits paid	20	19	221
Impact on acquisition of subsidiary	<u>(99)</u>	<u>(3)</u>	<u>-</u>
Projected benefits obligation, end of year	<u>\$ (6,761)</u>	<u>\$ (9,565)</u>	<u>\$ (12,155)</u>
Change in plan assets:			
Fair value of plan assets, beginning of year	\$ 2,922	\$ 2,864	\$ 4,407
Actual return on plan assets	82	87	142
Actuarial (loss) gain	(3)	30	(104)
Employer contributions	372	1,522	6,652
Benefits paid - settlement	(606)	(87)	-
Benefits paid	-	(12)	(178)
Impact of acquisition of subsidiary	<u>97</u>	<u>3</u>	<u>-</u>
Fair value of plan assets, end of year	<u>\$ 2,864</u>	<u>\$ 4,407</u>	<u>\$ 10,919</u>

c. Reconciliation between the funded status and accrued pension liabilities, vested benefit, actuarial assumptions and contributions and payments of the fund is summarized as follows:

1) Reconciliation between the fund status and accrued pension cost is summarized as follows:

	Year Ended December 31	
	2008	2009
	NT\$	NT\$
	(In Millions)	
Benefit obligation		
Vested benefit obligation	\$ (5,672)	\$ (7,455)
Non-vested benefit obligation	<u>(2,917)</u>	<u>(3,262)</u>
Accumulated benefit obligation	(8,589)	(10,717)
Additional benefit obligation	<u>(976)</u>	<u>(1,438)</u>
Projected benefit obligation	(9,565)	(12,155)
Fair values of plan assets	<u>4,407</u>	<u>10,919</u>
Funded status	(5,158)	(1,236)
Unrecognized net transition	-	7
Unrecognized net loss (gain)	55	24
Unrecognized prior service cost effect	<u>(58)</u>	<u>3</u>
Net amount recognized	<u>\$ (5,161)</u>	<u>\$ (1,202)</u>

The amounts recognized in the accompanying balance sheets at December 31, 2007, 2008 and 2009 are as follows:

	Year Ended December 31	
	2008	2009
	NT\$	NT\$
	(In Millions)	
Amounts recognized		
Prepaid pension (included in other assets)	\$ 12	\$ 15
Accrued pension liability	<u>(5,173)</u>	<u>(1,217)</u>
Net amount recognized	<u>\$ (5,161)</u>	<u>\$ (1,202)</u>

2) Vested benefit

	Year Ended December 31	
	2008	2009
	NT\$	NT\$
	(In Millions)	
Vested benefit	<u>\$ 7,683</u>	<u>\$ 10,654</u>

3) Actuarial assumptions

	Year Ended December 31		
	2007	2008	2009
	NT\$	NT\$	NT\$
		(In Millions)	
Discount rate used in determining present value	2.50%	2.00%	2.00%
Rate of compensation increase	1.50%	1.00%	1.00%
Expected long-term rate of return on plan assets	2.75%	2.50%	1.50%

d. Contributions and payments for defined benefit plan

	Year Ended December 31	
	2008	2009
	NT\$	NT\$
	(In Millions)	
Contributions	<u>\$ 1,522</u>	<u>\$ 6,652</u>
Payments	<u>\$ 106</u>	<u>\$ 221</u>

e. Expected benefit payments

<u>Year</u>	<u>Amount</u> <u>NT\$</u> (In Millions)
2010	\$ 185
2011	275
2012	387
2013	534
2014	779
2015 and thereafter	9,577

f. Plan assets allocation

Under the Labor Standards Law, the government is responsible for the administration of the Funds and determination of the investment strategies and policies. As of December 31, 2008 and 2009, the asset allocation was primarily in cash, equity securities and debt securities. Furthermore, under the Labor Standards Law, the rate of return on assets shall not be less than the average interest rate on a two-year time deposit published by the local banks. The government is responsible for any shortfall in the event that the rate of return is less than the required rate of return.

29. RELATED PARTY TRANSACTIONS

The ROC Government, one of Chunghwa's customers held significant equity interest in Chunghwa. Chunghwa provides fixed-line services, wireless services, Internet and data and other services to the various departments and institutions of the ROC Government and other state-owned enterprises in the normal course of business and at arm's-length prices. The information on service revenues from government bodies and related organizations have not been provided because details of the type of transactions were not summarized by Chunghwa. Chunghwa believes that all costs of doing business are reflected in the financial statements.

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

<u>Company</u>	<u>Relationship</u>
Chunghwa Precision Test Technical Co., Ltd. ("CHPT")	Subsidiary of CHI before Chunghwa obtained control over CHI on September 9, 2009
Taiwan International Standard Electronics Ltd. ("TISE")	Equity-method investee
Skysoft Co., Ltd. ("SKYSOFT")	Equity-method investee
So-net Entertainment Taiwan ("So-net")	Equity-method investee
KingWay Technology Co., Ltd. ("KWT")	Equity-method investee
Senao Networks, Inc. ("SNI")	Equity-method investee of SENAO
ST-2 Satellite Ventures Pte., Ltd. ("STS")	Equity-method investee of CHTS
SENAO Technology Education Foundation ("STEF")	A nonprofit organization of which the funds donated by SENAO exceed one third of its total funds
Institute for Information Industry ("III")	Equity- method investor of InfoExplorer
e-To You International Inc. ("ETY")	Chairman of ETY is the vice chairman of InfoExplorer
ELTA Technology Co., Ltd. ("ELTA")	Equity-method investee before Chunghwa sold all shares in July 2008

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

	<u>Year Ended December 31</u>	
	<u>2008</u>	<u>2009</u>
	<u>NT\$</u>	<u>NT\$</u>
(In Millions)		
1) Receivables		
Trade notes and accounts receivable		
III	\$ -	\$ 85
ETY	-	9
CHPT	1	-
Others	<u>1</u>	<u>-</u>
	<u>\$ 2</u>	<u>\$ 94</u>
2) Payables		
Trade notes payable, accounts payable, and accrued expenses		
TISE	\$ 493	\$ 271
SKYSOFT	-	14
STEF	3	3
ETY	-	3
Others	<u>2</u>	<u>3</u>
	498	294
Payables to contractors		
TISE	<u>26</u>	<u>42</u>
	<u>\$ 524</u>	<u>\$ 336</u>

	Year Ended December 31	
	2008	2009
	NT\$	NT\$
(In Millions)		
3) Advances from customers (include in other current liabilities)		
SNI	\$ 3	\$ 2
Others	<u>-</u>	<u>-</u>
	<u>\$ 3</u>	<u>\$ 2</u>
4) Revenues		
III	\$ -	\$ 127
So-net	-	61
SKYSOFT	33	34
ETY	-	11
ELTA	10	-
CHPT	7	-
Others	<u>4</u>	<u>4</u>
	<u>\$ 54</u>	<u>\$ 237</u>
5) Operating costs and expenses		
TISE	\$ 538	\$ 482
SKYSOFT	-	22
STEF	11	19
III	-	18
ETY	-	13
KWT	-	6
SNI	9	-
ELTA	190	-
Others	<u>6</u>	<u>1</u>
	<u>\$ 754</u>	<u>\$ 561</u>
6) Non-operating income and gains		
SNI	\$ 31	\$ 26
Others	<u>-</u>	<u>-</u>
	<u>\$ 31</u>	<u>\$ 26</u>
7) Acquisition of property, plant and equipment		
TISE	\$ 850	\$ 1,337
III	-	19
Others	<u>-</u>	<u>-</u>
	<u>\$ 850</u>	<u>\$ 1,356</u>

8) Financing to related parties

Financing to related parties (include in other assets - others) was as follows:

Related Party	Year Ended December 31, 2009			
	Maximum Balance	Ending Balance	Interest Rate	Interest Income
STS	\$ 546	\$ 546	6.38%	\$ 4

The Company did not have any financing to related parties for the year ended December 31, 2008.

SENAO rents out part of its plant to SNI, and the rent is collected monthly. The foregoing transactions with related parties were conducted as arm's length transactions, except for the transactions with SNI, STEF, III and ETY which were determined in accordance with mutual agreements.

c. The compensation of directors, supervisors and managements is showed as follows:

	Year Ended December 31	
	2008	2009
	NT\$	NT\$
	(In Millions)	
Salaries	\$ 137	\$ 144
Compensations	57	64
Bonus	58	60
	\$ 252	\$ 268

30. PLEDGED ASSETS

The following assets are pledged as collateral for short-term and long-term bank loans and contract deposits by LED, SENAO, CHIEF, SHE, IFE, CHPT and CHTS.

	December 31	
	2008	2009
	NT\$	NT\$
	(In Millions)	
Property, plant and equipment, net	\$ 338	\$ 661
Leased assets, net	435	-
Restricted assets	12	100
	\$ 785	\$ 761

31. SIGNIFICANT COMMITMENTS AND CONTINGENCIES

As of December 31, 2009, the Company's remaining commitments under non-cancelable contracts with various parties were as follows:

- a. Acquisition of land and buildings of NT\$230 million.
- b. Acquisition of telecommunications equipment of NT\$18,006 million.
- c. Unused letters of credit of NT\$400 million.
- d. Contract to print billing, envelopes and marketing gifts of NT\$60 million.
- e. LED has already contracted to advance sale of land for NT\$2,244 million, and collected NT\$328 million according to the contracts.
- f. For the purpose of completing the construction, acquisition of the building construction license and registration ownerships of all buildings for Wan-Xi Project, LED signed the trust deeds with Hua Nan Bank and China Real Estate Management Co., Ltd. for the fund management, property rights and related development to the extent of authority they are given.

Trust assets are as follow:

	December 31, 2009
	NT\$
	(In Millions)
Restricted assets bank deposits	\$ 101
Land held under development	<u>1,822</u>
	<u>\$ 1,923</u>

- g. The Company also has non-cancelable operating leases covering certain buildings, computers, computer peripheral equipment and operation system software under contracts that expire in various years. Future lease payments are as follows:

<u>Year</u>	<u>Amount</u>
	<u>NT\$</u>
	<u>(In Millions)</u>
2010	\$ 1,732
2011	1,381
2012	1,053
2013	815
2014 and thereafter	453

- h. A commitment to contribute NT\$2,000 million to a Piping Fund administered by the Taipei City Government, of which NT\$1,000 million was contributed by Chunghwa on August 15, 1996 (classified as long-term investment - other monetary assets). If the fund is not sufficient, Chunghwa will contribute the remaining NT\$1,000 million upon notification from the Taipei City Government. Based on Chunghwa's understanding of the Piping Fund terms, if the project is considered to be no longer necessary by the ROC government, Chunghwa will receive back its proportionate share of the net equity of the Piping Fund upon its dissolution. The Company does not know when its contribution to the Piping Fund will be returned; therefore, the Company did not discount the face amount of its contribution to the Piping Fund.

- i. A portion of the land used by Chunghwa during the period July 1, 1996 to December 31, 2004 was co-owned by Chunghwa and Chunghwa 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 Chunghwa to reimburse Chunghwa 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 Chunghwa's ownership and along with interest calculated at 5% interest rate from June 30, 2005 to the payment date. Chunghwa stated that both parties have the right to use co-management land without consideration. Chunghwa Post Co., Ltd. can't request payment for land compensation. Furthermore, Chunghwa 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, Chunghwa has filed an appeal at the Taiwan Taipei District Court. On March 30, 2009, the Taiwan Taipei District Court rendered its judgment that Chunghwa only need to pay NT\$17 million along with interest calculated at 5% per annum from July 23, 2005 and 4% of the court fees as the court judgment compensation. However, Chunghwa Post Co., Ltd. did not accept the judgment and filed an appeal at Taiwan High Court. Chunghwa also filed an appeal at the Taiwan High Court within the statutory period. As of March 10, 2010, the appeal is still in process.
- j. Giga Media filed a civil action against Chunghwa with the Taiwan Taipei District Court (the "Court") on June 12, 2008. The complaint alleged that Chunghwa infringed Giga Media's ROC Patent No. I258284 which is a Point-to-Point Protocol over Ethernet ("PPPoE") technique used to launch fixed IP of ADSL. Giga Media sought damages of NT\$500 million and interest calculated at 5% for the period from one day following the date Chunghwa received the official notification from the Court to the payment date. Afterwards Giga Media withdrew this civil action on October 2, 2009.

32. DISCLOSURES FOR FINANCIAL INSTRUMENTS

- a. Carrying amounts and fair values of financial instruments were as follows:

	December 31			
	2008		2009	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
	NT\$	NT\$	NT\$	NT\$
(In Millions)				
Assets				
Cash and cash equivalents	\$ 81,288	\$ 81,288	\$ 73,259	\$ 73,259
Financial assets at fair value through profit or loss	259	259	41	41
Available-for-sale financial assets	14,182	14,182	17,537	17,537
Held-to-maturity financial assets - current	769	769	1,100	1,100
Trade notes and accounts receivable, net	10,845	10,845	11,973	11,973
Receivables from related parties	2	2	94	94
Other current monetary assets	2,226	2,226	1,840	1,840
Restricted assets - current	59	59	178	178
Investments accounted for using equity method	2,337	2,499	1,622	1,743
Financial assets carried at cost	2,537	2,537	2,537	2,537
Held-to-maturity financial assets - noncurrent	3,044	3,044	3,930	3,930
Other noncurrent monetary assets	1,000	1,000	1,000	1,000
Refundable deposits	1,374	1,374	1,551	1,551
Restricted assets-noncurrent (included in "other assets - others")	9	9	23	23

(Continued)

	December 31			
	2008		2009	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
	NT\$	NT\$	NT\$	NT\$
	(In Millions)			
Liabilities				
Short-term loans	\$ 258	\$ 258	\$ 763	\$ 763
Financial liabilities at fair value through profit or loss	107	107	1	1
Trade notes and accounts payable	11,360	11,360	10,155	10,155
Payables to related parties	524	524	336	336
Accrued expenses	16,346	16,346	17,449	17,449
Due to stockholder for capital reduction	19,116	19,116	9,697	9,697
Payables to contractors (included in “other current liabilities”)	1,546	1,546	2,229	2,229
Amounts collected in trust for others (included in “other current liabilities”)	2,535	2,535	2,225	2,225
Payables to equipment suppliers (included in “other current liabilities”)	2,526	2,526	1,533	1,533
Refundable customers’ deposits (included in “other current liabilities”)	981	981	1,045	1,045
Hedging derivative financial liabilities (included in “other current liabilities”)	28	28	-	-
Current portion of long-term loans	8	8	117	117
Long-term loans	29	29	221	221
Customers’ deposits	6,160	6,160	5,998	5,998
				(Concluded)

b. Methods and assumptions used in the estimation of fair values of financial instruments:

- 1) The fair values of certain financial instruments recognized in the balance sheet generally correspond to the market prices of the financial assets. Because of the short maturities of these instruments, the carrying value represents a reasonable basis to estimate fair values. This method does not apply to the financial instruments discussed in Notes 2, 3, and 4 below.
- 2) If the financial instruments have quoted market prices in an active market, the quoted market prices are viewed as fair values. If the market prices of the other financial instruments are not readily available, valuation techniques are used incorporating estimates and assumptions that are consistent with prevailing market conditions.
- 3) Long-term investments are based on the net asset values or carrying values of the investments in unconsolidated companies if quoted market prices are not available.
- 4) The fair value of long-term loans (including current portion) is discounted based on projected cash flow which approximate their carrying amounts. The projected cash flows were discounted using the interest rate of similar long-term loans.

- c. Fair values of financial assets and liabilities using quoted market prices or valuation techniques were as follows:

	Amount Based on Quoted Market Price		Amount Determined Using Valuation Techniques	
	December 31		December 31	
	2008	2009	2008	2009
	NT\$	NT\$	NT\$	NT\$
(In Millions)				
<u>Assets</u>				
Financial assets at fair value through profit or loss	\$ 259	\$ 41	\$ -	\$ -
Available-for-sale financial assets	14,182	17,537	-	-
<u>Liabilities</u>				
Financial liabilities at fair value through profit or loss	107	1	-	-
Hedging derivative financial liabilities (classified as other current liabilities)	28	-	-	-

- d. Information about financial risks

1) Market risk

The foreign exchange rate fluctuations would result in the Company's foreign-currency-dominated assets and liabilities, outstanding currency swap contracts, forward exchange contracts and currency option contracts being exposed to rate risk.

The fluctuations of market price would result in the index future contracts exposed to price risk.

The financial instruments categorized as available-for-sale financial assets are mainly listed stocks and open-end mutual funds. Therefore, the market risk is the fluctuations of market price. In order to manage this risk, the Company would assess the risk before investing; therefore, no material market risk are anticipated.

2) Credit risk

Credit risk represents the potential loss that would be incurred by the Company if the counter-parties or third-parties breached contracts. Financial instruments with positive fair values at the balance sheet date are evaluated for credit risk. The counter-parties or third-parties of the aforementioned financial instruments are reputable financial institutions and corporations. Management does not expect the Company's exposure to default by those parties to be material.

3) Liquidation risk

The Company has sufficient operating capital to meet cash needs upon settlement of derivative financial instruments. Therefore, the liquidation risk is low.

The financial instruments of the Company categorized as available-for-sale financial assets are publicly-traded, easily converted to cash. Therefore, no material liquidation risks are anticipated. The financial instruments categorized as financial assets carried at cost are investments that do not have a quoted market price in an active market. Therefore, material liquidation risks are anticipated.

4) Cash flow interest rate risk

The Company engages in investments in fixed-interest-rate debt securities. Therefore, cash flows from such securities are not expected to fluctuate significantly due to changes in market interest rates.

In addition, the Company engages in investments in floating-interest-rate debt securities. The changes in market interest rate would impact the floating-interest rate; therefore, cash flows from such securities are expected to fluctuate due to changes in market interest rates.

e. Fair value hedge

Chunghwa entered into currency swap contracts and forward exchange contracts to hedge the fluctuation in exchange rates of open-end mutual funds denominated in foreign currency, which is fair value hedge. The transaction was assessed as highly effective for the years ended December 31, 2008 and 2009.

None of the hedge currency swap contracts and forward exchange contracts existed as of December 31, 2009.

Outstanding forward exchange contracts for hedge as of December 31, 2008:

	Currency	Maturity Period	Contract Amount (In Millions)
Forward exchange contracts - sell	USD/NTD	2009.01	US\$30

As of December 31, 2008, the forward exchange contract measured at fair value resulting in hedging derivative financial liability of NT\$28 million (classified as other current liabilities).

33. SEGMENT FINANCIAL INFORMATION

Beginning from September 1, 2009, the Company redefined its financial reporting operating segments into five operating segments: (a) domestic fixed communications business, (b) mobile communications business, (c) internet business, (d) international fixed communications business and (e) others. Prior to September 1, 2009, Chunghwa Telecom had seven operating segments: (a) local operations, (b) domestic long distance operations, (c) international long distance operations, (d) cellular service operations, (e) internet and data operations, (f) cellular phone sales and (g) all others. The redefinition of the Company's operating segments is expected to facilitate the management's ability to assess the performance of each operating segment by conforming the Company's operating segments to the international trends of other telecommunications companies in general. The Company also early adopted the Statement of Financial Accounting Standards No. 41 "Operating Segments" ("SFAS No. 41") starting from September 1, 2009. For the comparative purpose, the segment information for the years ended December 31, 2007 and 2008 was presented in accordance with SFAS No. 41.

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 in deciding how to allocate resources and in assessing performance.

The Company organizes its reporting segments based on types of organizational business. The five reporting segments are segregated as below: Domestic fixed communications business, mobile communications business, internet business, international fixed communications business and others.

- o Domestic fixed communications business - the provision of local telephone services, domestic long distance telephone services, broadband access, and related services;
- o Mobile communications business - the provision of mobile services, sales of mobile handsets and data cards, and related services;
- o Internet Business - the provision of HiNet services and related services;
- o International fixed communications business - the provision of international long distance telephone services and related services;
- o Others - the provision of non-telecom services and the corporate related items not allocated to reportable segments.

The operating segments are managed separately because each operating segment represents a strategic business unit that serves different markets. The Company's measure of segment performance is mainly based on revenues and income before tax.

a. Segment information

	<u>Domestic Fixed Communications Business</u> NT\$	<u>Mobile Communications Business</u> NT\$	<u>Internet Business</u> NT\$	<u>International Fixed Communications Business</u> NT\$	<u>Others</u> NT\$	<u>Adjustment</u> NT\$	<u>Total</u> NT\$
<u>Year ended December 31, 2007</u>							
Revenues from external customers	\$ 74,273	\$ 85,865	\$ 20,973	\$ 15,790	\$ 490	\$ -	\$ 197,391
Intersegment service revenues	11,399	2,531	328	1,425	1	(15,684)	-
Interest income	4	7	3	16	1,423	-	1,453
Other income	125	318	11	122	421	-	997
	<u>\$ 85,801</u>	<u>\$ 88,721</u>	<u>\$ 21,315</u>	<u>\$ 17,353</u>	<u>\$ 2,335</u>	<u>\$ (15,684)</u>	<u>\$ 199,841</u>
Interest expense	<u>\$ -</u>	<u>\$ 9</u>	<u>\$ 6</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 15</u>
Depreciation and amortization	<u>\$ 26,639</u>	<u>\$ 9,070</u>	<u>\$ 2,561</u>	<u>\$ 1,346</u>	<u>\$ 199</u>	<u>\$ -</u>	<u>\$ 39,815</u>
Other expense	<u>\$ 277</u>	<u>\$ 150</u>	<u>\$ 18</u>	<u>\$ 17</u>	<u>\$ 521</u>	<u>\$ -</u>	<u>\$ 983</u>
Segment income before tax	<u>\$ 15,748</u>	<u>\$ 36,280</u>	<u>\$ 9,315</u>	<u>\$ 2,117</u>	<u>\$ (1,659)</u>	<u>\$ -</u>	<u>\$ 61,801</u>
Total assets	<u>\$ 245,544</u>	<u>\$ 72,281</u>	<u>\$ 18,018</u>	<u>\$ 18,010</u>	<u>\$ 115,773</u>	<u>\$ -</u>	<u>\$ 469,626</u>
Capital expenditures for segment assets	<u>\$ 15,518</u>	<u>\$ 5,370</u>	<u>\$ 1,684</u>	<u>\$ 1,934</u>	<u>\$ 562</u>	<u>\$ -</u>	<u>\$ 25,068</u>
<u>Year ended December 31, 2008</u>							
Revenues from external customers	\$ 73,058	\$ 88,808	\$ 23,022	\$ 15,936	\$ 846	\$ -	\$ 201,670
Intersegment service revenues	11,929	1,933	563	1,527	2	(15,954)	-
Interest income	3	14	4	35	1,860	-	1,916
Other income	209	175	22	34	1,020	-	1,460
	<u>\$ 85,199</u>	<u>\$ 90,930</u>	<u>\$ 23,611</u>	<u>\$ 17,532</u>	<u>\$ 3,728</u>	<u>\$ (15,954)</u>	<u>\$ 205,046</u>
Interest expense	<u>\$ -</u>	<u>\$ 1</u>	<u>\$ 2</u>	<u>\$ -</u>	<u>\$ 1</u>	<u>\$ -</u>	<u>\$ 4</u>
Depreciation and amortization	<u>\$ 25,501</u>	<u>\$ 8,859</u>	<u>\$ 2,354</u>	<u>\$ 1,326</u>	<u>\$ 176</u>	<u>\$ -</u>	<u>\$ 38,216</u>
Other expense	<u>\$ 324</u>	<u>\$ 37</u>	<u>\$ 9</u>	<u>\$ 2</u>	<u>\$ 1,843</u>	<u>\$ -</u>	<u>\$ 2,215</u>
Segment income before tax	<u>\$ 15,473</u>	<u>\$ 33,175</u>	<u>\$ 10,086</u>	<u>\$ 2,911</u>	<u>\$ (1,961)</u>	<u>\$ -</u>	<u>\$ 59,684</u>
Total assets	<u>\$ 243,102</u>	<u>\$ 66,971</u>	<u>\$ 17,004</u>	<u>\$ 18,244</u>	<u>\$ 118,269</u>	<u>\$ -</u>	<u>\$ 463,590</u>
Capital expenditures for segment assets	<u>\$ 20,710</u>	<u>\$ 5,207</u>	<u>\$ 2,186</u>	<u>\$ 1,200</u>	<u>\$ 816</u>	<u>\$ -</u>	<u>\$ 30,119</u>

(Continued)

	Domestic Fixed Communications Business NT\$	Mobile Communications Business NT\$	Internet Business NT\$	International Fixed Communications Business NT\$	Others NT\$	Adjustment NT\$	Total NT\$
<u>Year ended December 31, 2009</u>							
Revenues from external customers	\$ 71,467	\$ 86,524	\$ 23,653	\$ 15,244	\$ 1,473	\$ -	\$ 198,361
Intersegment service revenues	13,650	1,915	717	1,523	3	(17,808)	-
Interest income	3	8	4	11	453	-	479
Other income	77	104	74	10	678	-	943
	<u>\$ 85,197</u>	<u>\$ 88,551</u>	<u>\$ 24,448</u>	<u>\$ 16,788</u>	<u>\$ 2,607</u>	<u>\$ (17,808)</u>	<u>\$ 199,783</u>
Interest expense	<u>\$ 3</u>	<u>\$ 1</u>	<u>\$ 10</u>	<u>\$ -</u>	<u>\$ 1</u>	<u>\$ -</u>	<u>\$ 15</u>
Depreciation and amortization	<u>\$ 23,984</u>	<u>\$ 8,373</u>	<u>\$ 2,327</u>	<u>\$ 1,404</u>	<u>\$ 232</u>	<u>\$ -</u>	<u>\$ 36,320</u>
Other expense	<u>\$ 156</u>	<u>\$ 98</u>	<u>\$ 11</u>	<u>\$ 2</u>	<u>\$ 279</u>	<u>\$ -</u>	<u>\$ 546</u>
Segment income before tax	<u>\$ 17,452</u>	<u>\$ 30,184</u>	<u>\$ 9,356</u>	<u>\$ 2,550</u>	<u>\$ (2,304)</u>	<u>\$ -</u>	<u>\$ 57,238</u>
Total assets	<u>\$ 231,177</u>	<u>\$ 63,537</u>	<u>\$ 17,154</u>	<u>\$ 18,700</u>	<u>\$ 118,429</u>	<u>\$ -</u>	<u>\$ 448,997</u>
Capital expenditures for segment assets	<u>\$ 15,877</u>	<u>\$ 5,028</u>	<u>\$ 2,097</u>	<u>\$ 1,299</u>	<u>\$ 1,177</u>	<u>\$ -</u>	<u>\$ 25,478</u>

(Concluded)

b. Products and service revenues from external customer information

	Year Ended December 31		
	2007	2008	2009
	NT\$	NT\$	NT\$
(In Millions)			
Mobile services revenue	\$ 73,644	\$ 72,290	\$ 71,295
Local telephone services revenue	36,109	35,188	34,116
Leased line services revenue	27,620	27,644	27,477
Internet services revenue	21,250	21,770	21,511
Sales revenue	13,169	16,340	15,058
International long distance telephone services revenue	14,254	14,051	12,922
Domestic long distance telephone services revenue	9,095	8,480	7,407
Others	<u>2,250</u>	<u>5,907</u>	<u>8,575</u>
	<u>\$ 197,391</u>	<u>\$ 201,670</u>	<u>\$ 198,361</u>

c. Geographic information

The users of the Company's services are mainly from Taiwan, ROC. The revenues it derived outside Taiwan are mainly revenues from international long distance telephone and leased line services. The geographic information for revenues is as follows:

	Year Ended December 31		
	2007	2008	2009
	NT\$	NT\$	NT\$
(In Millions)			
Taiwan, ROC	\$ 192,461	\$ 196,334	\$ 193,003
Overseas	<u>4,930</u>	<u>5,336</u>	<u>5,358</u>
	<u>\$ 197,391</u>	<u>\$ 201,670</u>	<u>\$ 198,361</u>

The Company has long-lived assets in U.S., Singapore, Hong Kong, China, Vietnam, Thailand, and Japan and except for NT\$32 million and NT\$175 million at December 31, 2008 and 2009, respectively, in the aforementioned areas, the other long-lived assets are located in Taiwan, ROC.

d. Major customers

For the years ended December 31, 2007, 2008 and 2009, the Company did not have any single customer whose net revenue exceeded 10% of the total net revenues.

34. SUMMARY OF SIGNIFICANT DIFFERENCES BETWEEN ACCOUNTING PRINCIPLES FOLLOWED BY THE COMPANY AND GENERALLY ACCEPTED ACCOUNTING PRINCIPLES IN THE UNITED STATES OF AMERICA

The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the Republic of China (ROC GAAP), which differ in the following respects from accounting principles generally accepted in the United States of America (US GAAP):

a. Property, plant and equipment

Under ROC GAAP, property, plant and equipment, excluding land, may be revalued when the price fluctuation is greater than 25% and upon approval from the tax authority. Similarly, land may be revalued if there is any appreciation of land based on the present value of land announced by the government. This revaluation component is recorded as a special reserve in equity at the time of revaluation and is subsequently depreciated. Upon sale or disposal of property, plant and equipment, the cost and any related revaluation increment less accumulated depreciation calculated after the revaluation are removed from the accounts, and any gain or loss is credited or charged to income. This revaluation adjustment also created differences in the opening balances of additional paid-in capital upon incorporation of the Company on July 1, 1996.

Under US GAAP, no revaluation of property, plant and equipment is permitted.

b. 10% tax on unappropriated earnings

In ROC, a 10% tax is imposed on unappropriated earnings (excluding earnings from foreign consolidated subsidiaries). Under ROC GAAP, the Company records the 10% tax on unappropriated earnings in the year of stockholders' approval.

Under US GAAP, the 10% tax on unappropriated earnings is accrued during the period the earnings arise and adjusted to the extent that distributions are approved by the stockholders in the following year.

c. Employee bonuses and remuneration to directors and supervisors

According to ROC regulations and the Company's Articles of Incorporation, a portion of the Company's distributable earnings should be set aside as bonuses to employees and remuneration to directors and supervisors. Such bonuses and remuneration give rise to the following GAAP differences due to the nature, measurement and timing of recording the transaction.

Under ROC GAAP:

- 1) Nature - employee bonuses and remuneration of directors and supervisors are treated as an expense rather than an appropriation of retained earnings in 2008. Before 2008, the bonuses are treated as appropriations of retained earnings.

- 2) Measurement and recognition - such bonuses to employees and remuneration to directors and supervisors are initially accrued based on management's estimate pursuant to the Articles of Incorporation of the Company. If the amounts initially accrued are significantly different from the amounts proposed subsequently by the board of directors in the following year, the difference needs to be retroactively adjusted. Otherwise, any difference between the amount initially accrued and actual amount of the bonuses approved by the stockholders is adjusted subsequently. If all or a portion of such bonuses and remuneration are in the form of shares, compensation expense remains the same but the actual number of shares to be distributed are determined by dividing the fair value of the Company's stock price as of one day prior to the stockholders' meeting held in the following year.

Under US GAAP:

- 1) Nature - employee bonuses and remuneration of directors and supervisors are treated as compensation expenses.
 - 2) Measurement and recognition - such bonuses to employees and remuneration to directors and supervisors are initially accrued based on management's estimate pursuant to the Articles of Incorporation of the Company. However, the Company's stockholders ultimately decide the amount and form of bonus (i.e., cash, stock or combination) at the stockholders' meeting held in the following year. Any difference between the amount initially accrued and actual amount of the bonuses approved by the stockholders is adjusted subsequently. If all or a portion of such bonuses and remuneration are in the form of shares, compensation expense is recognized at the fair value of the Company's stock price on the relevant grant date determined which is not until after stockholders' approval in the following year and subsequently remeasure to fair value until the settlement date in accordance with the share-based payments guidance.
- d. Deferred income from prepaid phone cards

Prior to incorporation and privatization, the Company was subject to the laws and regulations applicable to state-owned enterprises in Taiwan which differed from ROC GAAP as applicable to commercial companies. As such, revenue from selling prepaid phone cards was recognized at the time of sale by the Company. Upon incorporation, net assets greater than capital stock was credited as additional paid-in capital. Part of additional paid-in capital was from unearned revenues generated from prepaid cards as of that day. Upon privatization, unearned revenue generated from prepaid cards was deferred at the time of sale and recognized as revenue as consumed in accordance with ROC GAAP.

Under US GAAP, revenue from prepaid cards is deferred at the time of sale and recognized as revenue as consumed.

The GAAP adjustments related to prepaid cards subsequent to privatization are: (1) adjustments for prepaid cards transaction before incorporation from additional paid-in capital and (2) adjustments for such transactions occurred between incorporation and privatization from retained earnings which still have remaining expected customer service periods.

- e. One-time connection fees income

Similar to prepaid phone cards, according to the laws and regulations applicable to state-owned enterprises in Taiwan, the Company recorded revenue from providing fixed line connection service at the time the service was performed. Upon incorporation, net assets greater than capital stock was credited as additional paid-in capital. Part of additional paid-in capital was from unearned revenues from connection fees as of that date. Upon privatization, unearned revenue generated from one-time connection fees was deferred at the time of service performed and recognized as revenue over time as the service is continuously performed in accordance with ROC GAAP.

Under US GAAP, following the revenue recognition guidance, the above service revenue should be treated as deferred income at the time of service rendered and the recognition of revenue should occur over time as the service is continuously performed.

The GAAP adjustments related to one-time connection fees income subsequent to privatization are: (1) adjustments for one time connection fees before incorporation from additional paid-in capital, and (2) adjustments for such transactions occurred between incorporation and privatization from retained earnings which still have remaining expected customer service periods.

f. Share-based compensation

- 1) The Company's major stockholder, 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 in 2006.

Under ROC GAAP, such an offer was regarded as a transaction between stockholders and no entry was recorded on the Company's books and records.

Under US GAAP, the offer was deemed as compensation expense to employees and measured as the difference between the fair value of common stock offered and the amount of the discounted price at the grant date in 2006.

- 2) One of the Company's subsidiaries, SENA, granted options to employees.

Under ROC GAAP, employee stock option plans were accounted for using the intrinsic value method and no stock-based compensation expense was recognized for the employee stock options granted by its subsidiary under ROC GAAP prior to January 1, 2008. In August 2007, the ARDF issued ROC SFAS No. 39, "Accounting for Share-based Payment", which required companies to record share-based payment transactions granted on or after January 1, 2008 using the fair value method. There is no impact of the adoption this statement since the Company did not grant options on or after January 1, 2008.

Under US GAAP, the Company recognized compensation expense for such employee stock options granted by its subsidiary using fair value method in accordance with the share-based payments guidance.

g. Defined benefit pension plan

Pension accounting under ROC GAAP is similar in many respects to US GAAP. However, under ROC GAAP, companies are not required to recognize the overfunded or underfunded positions of their defined benefit pension plans as an asset or liability on the balance sheet.

Under US GAAP, employers are required to recognize the overfunded or underfunded status of a defined benefit pension plan as an asset or liability on its balance sheet and to recognize changes in that funded status in the year in which the changes occur through comprehensive income. US GAAP defines the funded status of a benefit plan as the difference between the fair value of the plan assets and the projected benefit obligation ("PBO"). Previously unrecognized item such as unrealized actuarial loss is recognized in other comprehensive income and are subsequently recognized through net periodic benefit cost.

Furthermore, the accounting treatment of settlements and curtailments are different under ROC GAAP and US GAAP. Under ROC GAAP, settlement/curtailment gains or losses are equal to the changes of underfunded status plus a pro rata portion of the unrecognized prior service cost, unrecognized net gains (losses), and unrecognized transition obligations/assets, before the settlement/curtailment event multiplied by the percentage reduction in PBO.

Under US GAAP, settlement gain (loss) is the total unrecognized net gain or losses including any gain or loss that arose from the measurements at the settlement date and unrecognized transition assets before settlement multiplied by the percentage reduction in PBO. Curtailment gain (loss) includes the following items: (1) total unrecognized prior service cost and net transition obligation before curtailment multiplied by the curtailment ratio (the ratio of reduction in future service over such future service before curtailment) and (2) decrease in PBO to the extent that such gain exceeds the net unrecognized loss (sum of unrecognized net gain or loss and net unrecognized transition asset before curtailment) or the entire gain if a net unrecognized gain exists or increase in PBO to the extent that such loss exceeds unrecognized gain (sum of unrecognized net gain or loss and net unrecognized transition asset before curtailment) or the entire loss if net unrecognized loss exists.

h. Pension plan upon privatization

In order to increase operational efficiency, the Company approved several special retirement incentive programs during the process of privatization.

Under ROC GAAP, 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 as the adjustment for the pension cost of that year.

Under US GAAP, 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.

i. Income tax

This line item includes the tax effects of the pre-tax ROC GAAP to US GAAP adjustments described above.

j. Noncontrolling interests of acquired subsidiaries

The adjustment to net income for the year ended December 31, 2009 and to stockholders' equity as of December 31, 2009 represents a difference between ROC GAAP and US GAAP for the accounting for business combinations.

Under ROC GAAP, the noncontrolling interest in the acquiree is measured at historical cost whereas under US GAAP, the noncontrolling interest in the acquiree is measured at fair value at acquisition date upon the adoption of the new accounting standard discussed in Note 1 beginning from January 1, 2009. Such adjustment for the year ended December 31, 2009 was caused by the Company's acquisition of IFE in January 2009 and of CHI in September 2009. The adjustment to ROC GAAP net income represents additional depreciation and amortization expenses recognized under US GAAP due to the difference between the measurement of noncontrolling interests at historical cost and fair value. The adjustment to stockholders' equity represents the difference for the measurement of noncontrolling interests at historical cost and fair value after the aforementioned net income adjustment.

k. Earnings per share

Under ROC GAAP, earnings per share is computed by dividing income attributable to stockholders of the parent by the weighted average number of shares outstanding in each period, which is retroactively adjusted to the beginning of the year for stock dividends and stock bonuses issued subsequently in 2007. Starting from 2008, stock bonuses to employees, shares are included in the calculation of weighted-average number of shares outstanding from the date of issuance.

Under US GAAP, earnings per share is calculated by dividing net income, which represents income attributable to stockholders of the parent, by the weighted-average number of shares outstanding in each period, which is retroactively adjusted for stock dividends issued subsequently. For stock bonuses to employees, shares are included in the calculation of weighted-average number of shares outstanding from the date of issuance.

The following is a reconciliation of consolidated net income and stockholders' equity under ROC GAAP as reported in the consolidated financial statements to the consolidated net income and equity determined under US GAAP, giving effect to the differences listed above.

	Year Ended December 31			
	2007 As Adjusted (Note 1, Below)	2008 As Adjusted (Note 1, Below)	2009	
	NT\$	NT\$	NT\$	US\$ (Note 3)
	(In Millions)			
<u>Net income</u>				
Consolidated net income under ROC GAAP	\$ 48,742	\$ 45,792	\$ 44,495	\$ 1,393
Adjustments:				
a. Property, plant and equipment				
1. Adjustments of gains and losses on disposal of property, plant and equipment	60	2	24	1
2. Adjustments for depreciation expenses	402	312	158	5
b. 10% tax on unappropriated earnings	(372)	191	110	3
c. Employee bonuses and remuneration to directors and supervisors	(1,369)	(3,993)	-	-
d. Revenues recognized from deferred income of prepaid phone cards	671	798	615	19
e. Revenues recognized from deferred one-time connection Fees	2,914	1,918	1,426	45
f. Share-based compensation	(14)	(22)	(17)	(1)
g. Defined benefit pension plan	(10)	(1)	1	-
i. Income tax effect of US GAAP adjustments	(1,102)	(743)	(982)	(31)
j. Noncontrolling interests of acquired subsidiaries	-	-	(8)	-
Other minor GAAP differences not listed above	(132)	(42)	(7)	-
Net adjustment	<u>1,048</u>	<u>(1,580)</u>	<u>1,320</u>	<u>41</u>
Consolidated net income based on US GAAP	<u>\$ 49,790</u>	<u>\$ 44,212</u>	<u>\$ 45,815</u>	<u>\$ 1,434</u>
Attributable to				
Stockholders of the parent	\$ 49,451	\$ 43,664	\$ 45,096	\$ 1,411
Noncontrolling interests	<u>339</u>	<u>548</u>	<u>719</u>	<u>23</u>
	<u>\$ 49,790</u>	<u>\$ 44,212</u>	<u>\$ 45,815</u>	<u>\$ 1,434</u>

	December 31			
	2007 As Adjusted (Note 1, Below)	2008 As Adjusted (Note 1, Below)	2009	
	NT\$	NT\$	NT\$	US\$ (Note 3)
	(In Millions)			
<u>Stockholders' equity</u>				
Total stockholders' equity based on ROC GAAP	\$ 397,842	\$ 379,694	\$ 378,964	\$ 11,861
Adjustments:				
a. Property, plant and equipment				
1. Capital surplus reduction	(60,168)	(60,168)	(60,168)	(1,883)
2. Adjustment on depreciation expenses, and disposal gains and losses	3,645	3,959	4,141	130
3. Adjustments of revaluation of land	(5,823)	(5,813)	(5,803)	(182)
b. 10% tax on unappropriated earnings	(4,313)	(4,147)	(4,037)	(126)
c. Employee bonuses and remuneration to directors and supervisors	(964)	-	-	-
d. Deferred income of prepaid phone cards				
1. Capital surplus reduction	(2,798)	(2,798)	(2,798)	(88)
2. Adjustment on deferred income recognition	1,127	1,925	2,540	79
e. Revenues recognized from deferred one-time connection fees				
1. Capital surplus reduction	(18,487)	(18,487)	(18,487)	(579)
2. Adjustment on deferred income recognition	11,239	13,156	14,582	456
f. Share-based compensation				
1. Adjustment on capital surplus	15,675	15,683	15,700	491
2. Adjustment on retained earnings	(15,675)	(15,683)	(15,700)	(491)
g. 1. Accrual for accumulative other comprehensive income under pension guidance	32	22	(1)	-
2. Accrual for pension cost	(27)	(29)	(28)	(1)
h. Adjustment for pension plan upon privatization				
1. Adjustment on capital surplus	1,782	1,782	1,782	56
2. Adjustment on retained earnings	(9,665)	(9,665)	(9,665)	(302)
i. Income tax effect of US GAAP adjustments	6,962	6,217	5,238	164
j. Noncontrolling interests of acquired subsidiaries	-	-	28	1
Other GAAP differences not listed above	154	201	184	6
Net adjustment	<u>(77,304)</u>	<u>(73,845)</u>	<u>(72,492)</u>	<u>(2,269)</u>
Total equity based on US GAAP	<u>\$ 320,538</u>	<u>\$ 305,849</u>	<u>\$ 306,472</u>	<u>\$ 9,592</u>
Attributable to				
Stockholders of the parent	\$ 317,883	\$ 302,802	\$ 302,799	\$ 9,477
Noncontrolling interests	<u>2,655</u>	<u>3,047</u>	<u>3,673</u>	<u>115</u>
	<u>\$ 320,538</u>	<u>\$ 305,849</u>	<u>\$ 306,472</u>	<u>\$ 9,592</u>

Note 1: Prior to the adoption of the new guidance for noncontrolling interests in consolidated financial statements issued by FASB in December 2007, the noncontrolling interests in the income of subsidiaries is deducted in arriving at net income. Upon the adoption of the new guidance beginning from January 1, 2009, the noncontrolling interests forms part of net income. In addition, prior to the adoption of the new guidance, the noncontrolling interests in subsidiaries is classified as mezzanine equity. Upon the adoption of the new guidance beginning from January 1, 2009, the non-controlling interest in subsidiaries is classified as a separate component of shareholders' equity and the presentation and disclosure requirements of the new guidance are applied retrospectively for all periods presented. Therefore, from January 1, 2009, there are no differences in presentation for non-controlling interest (or minority interests as referred to under ROC GAAP) between ROC GAAP and US GAAP.

	Year Ended December 31			
	2007 As Adjusted (Note 1, Above)	2008 As Adjusted (Note 1, Above)	2009	
	NT\$	NT\$	NT\$	US\$ (Note 3)
	(In Millions)			
<u>Changes in equity based on US GAAP</u>				
Balance, beginning of year	\$ 320,145	\$ 320,538	\$ 305,849	\$ 9,572
Consolidated net income	49,790	44,212	45,815	1,434
Unrealized gain (loss) on available-for-sale securities	(507)	(2,301)	1,833	57
Unrealized gain on available-for-sale securities held by investees	2	(7)	-	-
Employee stock bonus	-	3,302	-	-
Cumulative translation adjustment for foreign-currency investments held by investees	1	31	(22)	(1)
Purchase of treasury stock	(7,217)	-	-	-
Increase in interest on issuance of stock by investees	17	64	(10)	-
Cash dividends	(34,611)	(40,716)	(37,139)	(1,162)
Capital reduction	(9,558)	(19,116)	(9,697)	(303)
Defined benefit pension plan adjustment	258	(11)	(68)	(2)
Increase (decrease) in noncontrolling interests	<u>2,218</u>	<u>(147)</u>	<u>(89)</u>	<u>(3)</u>
Balance, end of year	<u>\$ 320,538</u>	<u>\$ 305,849</u>	<u>\$ 306,472</u>	<u>\$ 9,592</u>
Attributable to				
Stockholders of the parent	\$ 317,883	\$ 302,802	\$ 302,799	\$ 9,477
Noncontrolling interests	<u>2,655</u>	<u>3,047</u>	<u>3,673</u>	<u>115</u>
	<u>\$ 320,538</u>	<u>\$ 305,849</u>	<u>\$ 306,472</u>	<u>\$ 9,592</u>

The following US GAAP condensed balance sheets as of December 31, 2008 and 2009, and statements of income for the years ended December 31, 2007, 2008 and 2009 have been derived from the audited consolidated financial statements and reflect the adjustments presented above.

	December 31		
	2008	2009	
	NT\$	NT\$	US\$ (Note 3)
		(In Millions)	
Assets			
Current assets	\$ 118,712	\$ 115,050	\$ 3,600
Long-term investments	7,917	8,072	252
Property, plant and equipment, net	258,631	248,797	7,787
Intangible assets	8,271	7,680	241
Other assets	<u>7,128</u>	<u>5,734</u>	<u>180</u>
Total assets	<u>\$ 400,659</u>	<u>\$ 385,333</u>	<u>\$ 12,060</u>
Liabilities and equities			
Liabilities			
Current liabilities	\$ 82,299	\$ 70,907	\$ 2,219
Long-term liabilities	<u>12,511</u>	<u>7,954</u>	<u>249</u>
Total liabilities	<u>94,810</u>	<u>78,861</u>	<u>2,468</u>
Equity attributable to stockholders of the parent			
Capital stock - NT\$10 (US\$0.3) par value	96,968	96,968	3,035
Capital surplus	142,503	132,742	4,154
Retained earnings	65,543	73,553	2,303
Other comprehensive income	(2,212)	(464)	(15)
Treasury stock	<u>-</u>	<u>-</u>	<u>-</u>
Total equity attributable to stockholders of the parent	<u>302,802</u>	<u>302,799</u>	<u>9,477</u>
Noncontrolling interests	<u>3,047</u>	<u>3,673</u>	<u>115</u>
Total equity	<u>305,849</u>	<u>306,472</u>	<u>9,592</u>
Total liabilities and equity	<u>\$ 400,659</u>	<u>\$ 385,333</u>	<u>\$ 12,060</u>

Certain accounts have been reclassified to conform to the US GAAP presentation requirements. Under US GAAP, incentives paid to third party dealers for inducing business are included in cost of revenues whereas under ROC GAAP such account is included in operating expenses. Under US GAAP, gains and losses on disposal of property, plant and equipment and other assets and loss arising from natural calamities are included in operating expenses whereas under ROC GAAP, such accounts are included in non-operating expenses.

	Year Ended December 31			
	2007	2008	2009	
	NT\$	NT\$	NT\$	US\$ (Note 3)
	(In Millions Except Per Share Amounts)			
Net revenues	\$ 200,911	\$ 204,352	\$ 200,369	\$ 6,272
Operating costs and expenses	<u>138,139</u>	<u>147,086</u>	<u>141,817</u>	<u>4,439</u>
Income from operations	62,772	57,266	58,552	1,833
Non-operating income, net	<u>1,561</u>	<u>1,391</u>	<u>877</u>	<u>27</u>
Income before income tax	64,333	58,657	59,429	1,860
Income tax expense	<u>(14,543)</u>	<u>(14,445)</u>	<u>(13,614)</u>	<u>(426)</u>
Consolidated net income	<u>\$ 49,790</u>	<u>\$ 44,212</u>	<u>\$ 45,815</u>	<u>\$ 1,434</u>
Attributable to				
Stockholders of the parent	\$ 49,451	\$ 43,664	\$ 45,096	\$ 1,411
Noncontrolling interests	<u>339</u>	<u>548</u>	<u>719</u>	<u>23</u>
	<u>\$ 49,790</u>	<u>\$ 44,212</u>	<u>\$ 45,815</u>	<u>\$ 1,434</u>
Basic earnings per share	<u>\$ 5.08</u>	<u>\$ 4.52</u>	<u>\$ 4.65</u>	<u>\$ 0.14</u>
Diluted earnings per share	<u>\$ 5.08</u>	<u>\$ 4.51</u>	<u>\$ 4.64</u>	<u>\$ 0.14</u>
Weighted-average number of common shares outstanding (in 1,000 shares)				
Basic	<u>9,732,783</u>	<u>9,661,309</u>	<u>9,696,808</u>	<u>9,696,808</u>
Diluted	<u>9,732,783</u>	<u>9,681,990</u>	<u>9,725,614</u>	<u>9,725,614</u>
Net income per pro forma equivalent ADSs				
Basic	<u>\$ 50.81</u>	<u>\$ 45.19</u>	<u>\$ 46.51</u>	<u>\$ 1.45</u>
Diluted	<u>\$ 50.80</u>	<u>\$ 45.09</u>	<u>\$ 46.36</u>	<u>\$ 1.45</u>
Weighted-average number of pro forma equivalent ADSs (in 1,000 shares)				
Basic	<u>973,278</u>	<u>966,131</u>	<u>969,681</u>	<u>969,681</u>
Diluted	<u>973,278</u>	<u>968,199</u>	<u>972,561</u>	<u>972,561</u>

The Company reports comprehensive income in accordance with related guidance. The guidance requires that in addition to net income (loss), a company should report other comprehensive income consisting of the changes in equity of the Company during the year from transactions and other events and circumstance from nonowner sources. It includes all changes in equity during the year except those resulting from investments by stockholders and distribution to stockholders. The components of other comprehensive income for the Company consist of unrealized gains and losses relating to the translation of financial statements maintained in foreign currencies, unrealized gains and losses on available-for-sale securities held by the Company and its investees and changes in the funded status of the defined benefit pension plan.

Statements of comprehensive income for the years ended December 31, 2007, 2008 and 2009 are as follows:

	Year Ended December 31			
	2007	2008	2009	
	NT\$	NT\$	NT\$	US\$ (Note 3)
	(In Millions)			
Comprehensive income				
Consolidated net income	\$ 49,790	\$ 44,212	\$ 45,815	\$ 1,434
Other comprehensive income:				
Cumulative translation adjustments for foreign-currency investments held by investees	1	31	(22)	(1)
Unrealized gain on available-for-sale securities held by investees	2	(7)	-	-
Unrealized gain (loss) on available-for-sale securities	(507)	(2,301)	1,833	57
Defined benefit pension plan adjustment	258	(11)	(68)	(2)
	<u>(246)</u>	<u>(2,288)</u>	<u>1,743</u>	<u>54</u>
	<u>\$ 49,544</u>	<u>\$ 41,924</u>	<u>\$ 47,558</u>	<u>\$ 1,488</u>
Attributable to				
Stockholders of the parent	\$ 49,205	\$ 41,385	\$ 46,843	\$ 1,466
Noncontrolling interests	<u>339</u>	<u>539</u>	<u>715</u>	<u>22</u>
	<u>\$ 49,544</u>	<u>\$ 41,924</u>	<u>\$ 47,558</u>	<u>\$ 1,488</u>

The components of accumulated other comprehensive income (loss) were as follows:

	December 31		
	2008	2009	
	NT\$	NT\$	US\$ (Note 3)
	(In Millions)		
Cumulative translation adjustments for foreign-currency investments held by investees	\$ 29	\$ 7	\$ -
Unrealized loss on available-for-sale securities	(2,272)	(439)	(14)
Defined benefit pension plan adjustment	<u>21</u>	<u>(47)</u>	<u>(1)</u>
	<u>\$ (2,222)</u>	<u>\$ (479)</u>	<u>\$ (15)</u>

Disclosures about defined benefit plan recognized in other comprehensive income were as follows:

	Year Ended December 31			
	2007	2008	2009	
	NT\$	NT\$	NT\$	US\$ (Note 3)
	(In Millions)			
Amounts recognized in other comprehensive income				
Net prior service cost, pretax	\$ -	\$ (57)	\$ 6	\$ -
Net actuarial loss (gain), pretax	(381)	72	73	2
Deferred tax asset (liability)	<u>123</u>	<u>(4)</u>	<u>(11)</u>	<u>-</u>
Net impact in accumulated other comprehensive loss (gain)	<u>\$ (258)</u>	<u>\$ 11</u>	<u>\$ 68</u>	<u>\$ 2</u>

The Company applies ROC SFAS No. 17, "Statement of Cash Flows". Its objectives and principles are similar to those set out in U.S. standards. The principal differences between the two standards relate to classification. Cash flows from investing activities for changes in other assets, and cash flows from financing activities for changes in customers' deposits, other liabilities and cash bonuses paid to employees, directors and supervisors are reclassified to operating activities under U.S. standards. As discussed in Note 4, beginning from 2009, bonuses paid to employees, directors and supervisors are classified as operating activities for purposes of the statement of cash flows when paid under R.O.C. standards. Therefore, the reclassification of bonuses paid to employees, directors and supervisors under U.S. standards is no longer required beginning from 2009. Summarized cash flow data by operating, investing and financing activities in accordance with U.S. standards are as follows:

	Year Ended December 31			
	2007	2008	2009	
	NT\$	NT\$	NT\$	US\$ (Note 3)
	(In Millions)			
Net cash flows (outflows) from:				
Operating activities	\$ 87,248	\$ 89,484	\$ 77,246	\$ 2,418
Investing activities	(39,405)	(33,961)	(28,755)	(900)
Financing activities	(42,840)	(50,512)	(56,513)	(1,769)
Effects of exchange rate change on cash and cash equivalents	(1)	31	(7)	-
Cash balance of SENAIO upon its consolidation	801	-	-	-
Cash balance of SHE upon its consolidation	-	13	-	-
Cash balance of SENAIO Networks and its subsidiaries upon its deconsolidation	<u>(243)</u>	<u>-</u>	<u>-</u>	<u>-</u>
Net increase in cash and cash equivalents	5,560	5,055	(8,029)	(251)
Cash and cash equivalents, beginning of year	<u>70,673</u>	<u>76,233</u>	<u>81,288</u>	<u>2,544</u>
Cash and cash equivalents, end of year	<u>\$ 76,233</u>	<u>\$ 81,288</u>	<u>\$ 73,259</u>	<u>\$ 2,293</u>

35. ADDITIONAL DISCLOSURES REQUIRED BY US GAAP

a. Recent accounting pronouncements

In June 2009, the FASB issued the FASB Accounting Standards Codification ("Codification"). The Codification has become the single source for all authoritative GAAP recognized by the FASB to be applied for financial statements issued for periods ending after September 15, 2009. The Company applied the Codification to its Quarterly Report for the period ended September 30, 2009. The Codification does not change GAAP and the Company believes that it did not have an effect on its financial position or results of operations.

In December 2008, the FASB issued new guidance relating to the disclosure requirements for defined benefit plans, which provides guidance on an employer's disclosures about plan assets of a defined benefit pension or other postretirement plan. As discussed in Note 28, pension funds are administered by the Labor Pension Fund Supervisory Committee ("the Committee") and the investment policies, strategies and plan assets allocation is under the Committee's control. In addition, the Committee does not provide detailed information to the public for the investment portfolios of the pension plan assets. Therefore, the Company cannot meet the pension plan asset disclosure requirements included in the new guidance.

In June 2009, the FASB issued new guidance relating to the disclosure requirements for transfers of financial assets. This new guidance is intended to improve the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial statements about transfers of financial assets. The new guidance is effective for annual reporting periods that begin after November 15, 2009, for interim periods within that first annual reporting period and for interim and annual reporting periods thereafter. The Company is currently evaluating the impact of the adoption of the guidance.

In June 2009, the FASB issued new guidance to improve financial reporting by enterprises involved with variable interest entities (VIE). This accounting standard clarified that the determination of whether a company is required to consolidate an entity is based on, among other things, an entity's purpose and design and a company's ability to direct the activities of the entity that most significantly impact the entity's economic performance. This accounting standard is effective as of the beginning of each reporting entity's first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period, and for interim and annual reporting periods thereafter. The Company is currently evaluating the impact of the adoption of the standards.

In September 2009, the FASB issued new guidance relating to revenue arrangements with multiple deliverables which established the accounting and reporting guidance for arrangements under which the vendor will perform multiple revenue-generating activities. Specifically, the update addresses how to separate deliverables and how to measure and allocate arrangement consideration to one or more units of accounting. The update is effective for fiscal years beginning on or after June 15, 2010. The Company is currently evaluating the impact of the adoption of the update.

In January 2010, the FASB issued new guidance, to clarify that the scope of the decrease in ownership provisions and provides amendments that affect the accounting and reporting by an entity that exchanges a group of assets that constitutes a business or nonprofit for an equity interest in another entity. The new accounting standard is effective beginning for the first interim and annual reporting period on or after December 15, 2009. The Company does not expect the new accounting standard will have a material impact on the Company financial statements.

b. Share-based compensation

The Company adopted share-based compensation guidance to recognize compensation cost of options granted by SENAO. The guidance requires companies to estimate the fair value of share-based payment awards on the date of grant using an option-pricing model. The value of the portion of the award that is ultimately expected to vest is recognized as expense ratably over the requisite service period. The Company has estimated the fair value of stock options as of the date of grant using the Black-Scholes option pricing model.

The Compensation expenses related to stock options were NT\$14 million, NT\$22 million and NT\$17 million for 2007, 2008 and 2009, respectively. There is no income tax benefit effect related to share-based compensation arrangements.

The weighted average remaining contractual term and aggregate intrinsic value of options under the foregoing plans as of December 31, 2009 were as follows:

	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value
	<u>(In Years)</u>	<u>NT\$ (In Millions)</u>
Options outstanding	3.23	160
Options exercisable	3.17	78

The aggregate intrinsic value in the above table represents the total intrinsic value (the difference between the Company's closing stock price on the last trading day of fiscal year 2009 and the exercise price, multiplied by the number of in-the-money options) that would have been received by the option holders had all option holders exercised their options on December 31, 2009. Intrinsic value will change in future periods based on the fair market value of the Company's stock and the number of shares outstanding.

The weighted-average grant-date fair value of stock options granted during the year ended December 31, 2007 was NT\$15.60. SENAO did not grant any option in 2008 and 2009.

Total intrinsic value of options exercised for the years ended December 31, 2007, 2008 and 2009 were NT\$110 million, NT\$117 million and NT\$113 million, respectively. Total fair value of shares vested during the years ended December 31, 2007, 2008 and 2009 were NT\$152 million NT\$238 million and NT\$252 million, respectively.

A summary of the status of the Company's nonvested shares as of December 31, 2009 and changes during the year ended December 31, 2009 is presented below:

	Shares in Thousand	Weighted- average Grant-date Fair Value
Nonvested at January 1, 2009	13,818	\$26.34
Granted	-	-
Vested	(4,076)	13.75
Forfeited	<u>(419)</u>	31.35
Nonvested at December 31, 2009	<u>9,323</u>	30.92

As of December 31, 2009, there was NT\$7 million of total unrecognized compensation expense related to nonvested options. The expense is expected to be recognized over a weight-average period of 2.29 years.

The compensation expenses were determined by calculating the fair value of each option grant using the Black-Scholes option-pricing model. SENAO used the following weighted-average assumptions in calculating the fair value of the options granted:

	Year Ended December 31, 2009
Expected dividend yield	0-1.49%
Expected volatility	39.63%-52.65%
Risk free interest rate	1.75%-2.00%
Expected life	4.375 years

SENAO did not grant any options in 2009.

Risk-free interest rate is based on the rate of the Taiwan government bonds in effect at the time of grant. Expected volatilities are based on historical volatilities of stock prices of the similar company in the same industry and SENAO. Expected life represents the periods that SENAO's share-based awards are expected to be outstanding and was determined based on historical experience regarding similar awards, giving consideration to the contractual term of the share-based awards. The dividend yield is zero as share-based awards agreeing on that the price will be adjusted when SENAO pays dividends, with the exception of the options granted in 2007. The expected dividend yield for SENAO's 2007 Plan is based on anticipated future cash dividends yield at the time of grant.

c. Marketable securities

	December 31			
	2008		2009	
	Carrying Amount	Unrealized Gain (Loss)	Carrying Amount	Unrealized Gain (Loss)
	NT\$	NT\$	NT\$	NT\$
(In Millions)				
Available-for-sale securities				
Open-end mutual funds	\$ 13,442	\$ (2,069)	\$ 16,832	\$ (462)
Domestic listed stocks	-	-	500	24
Corporate bonds	-	-	103	1
Real estate investment trust fund	194	(29)	102	(2)
Foreign listed stocks	<u>546</u>	<u>(167)</u>	<u>-</u>	<u>-</u>
	<u>14,182</u>	<u>(2,265)</u>	<u>17,537</u>	<u>(439)</u>
Held-to-maturity securities				
Corporate bond	2,635	(15)	4,532	(38)
Financial institution bonds	1,137	-	498	2
Collateralized loan obligation	<u>41</u>	<u>3</u>	<u>-</u>	<u>-</u>
	<u>3,813</u>	<u>(12)</u>	<u>5,030</u>	<u>(36)</u>
	<u>\$ 17,995</u>	<u>\$ (2,277)</u>	<u>\$ 22,567</u>	<u>\$ (475)</u>

The Company's gross realized gains on the sale of investments for the years ended December 31, 2008 and 2009 were NT\$131 million and NT\$553 million, respectively. The Company's gross realized losses on the sale of investments for the years ended December 31, 2008 and 2009 were NT\$1,014 million and NT\$695 million, respectively.

The carrying amounts at December 31, 2009 for debt securities classified as available-for-sale securities and held-to-maturity by contractual maturity are shown below.

	December 31, 2009
	NT\$
	(In Millions)
Due within one year or less	\$ 1,100
Due after one year through four years	<u>4,033</u>
	<u>\$ 5,133</u>

The following table shows the gross unrealized losses and fair value of the investments with unrealized losses that are not deemed to be other-than-temporary impaired, aggregated by investment category and length of time that have been in a continuous unrealized loss position as of December 31, 2009:

	<u>Less than 12 Months</u>		<u>12 Months or Greater</u>		<u>Total</u>	
	<u>Fair Value</u>	<u>Unrealized Losses</u>	<u>Fair Value</u>	<u>Unrealized Losses</u>	<u>Fair Value</u>	<u>Unrealized Losses</u>
	<u>NT\$</u>	<u>NT\$</u>	<u>NT\$</u>	<u>NT\$</u>	<u>NT\$</u>	<u>NT\$</u>
	(In Millions)					
Open-end-mutual funds	\$ 951	\$ (12)	\$ 6,059	\$ (541)	\$ 7,010	\$ (553)
Real estate investment trust fund	<u>-</u>	<u>-</u>	<u>38</u>	<u>(8)</u>	<u>38</u>	<u>(8)</u>
	<u>\$ 951</u>	<u>\$ (12)</u>	<u>\$ 6,097</u>	<u>\$ (549)</u>	<u>\$ 7,048</u>	<u>\$ (561)</u>

The Company has determined that the gross unrealized losses related to mutual funds, real estate investment trust fund at December 31, 2009 were due to the fact that global economic and financial circumstances have changed. The Company reviewed its investment portfolio to identify and evaluate investments that have indications of possible impairment. Factors considered in determining whether a loss is other-than-temporary including but not limited to the length of time and extent to which fair value has been less than the cost basis, credit quality and the Company's ability and intent to hold the investment for a period of time sufficient to allow for any anticipated recovery in market value. As a result, the Company determined that aforementioned investments with unrealized losses were not deemed to be other- than-temporary impaired as of December 31, 2009.

d. Fair value measurements

The fair value guidance requires disclosure that establishes a framework for measuring fair value and expands disclosure about fair value measurements. The standard describes a fair value hierarchy based on three levels of inputs that may be used to measure fair value. The level in the fair value hierarchy within which the fair value measurement in its entirety falls shall be determined based on the lowest level input that is significant to the fair value measurement in its entirety. These levels are:

Level 1: Quoted prices in active markets for identical assets or liabilities that the Company has the ability to access at the measurement date;

Level 2: Quoted prices in markets that are not active, or inputs which are observable, either directly or indirectly, for substantially the full term of the asset or liability; or

Level 3: Prices or valuation techniques that require inputs that are both significant to the fair value measurement and are unobservable.

Assets and liabilities measured at fair value on a recurring basis

The following table presents our assets and liabilities measured at fair value on a recurring basis at December 31, 2008 and 2009:

	December 31, 2008			
	Level 1	Level 2	Level 3	Total
	NT\$	NT\$	NT\$	NT\$
	(In Millions)			
Assets				
Derivatives				
Index future contracts	\$ 243	\$ -	\$ -	\$ 243
Forward exchange contracts	-	16	-	16
Available-for-sale securities				
Open-end mutual funds	13,442	-	-	13,442
Real estate investment trust	194	-	-	194
Foreign listed stocks	<u>546</u>	<u>-</u>	<u>-</u>	<u>546</u>
	<u>\$ 14,425</u>	<u>\$ 16</u>	<u>\$ -</u>	<u>\$ 14,441</u>
Liabilities				
Derivative				
Forward exchange contracts (including contract for fair value hedge)	\$ -	\$ 124	\$ -	\$ 124
Index future contracts	<u>11</u>	<u>-</u>	<u>-</u>	<u>11</u>
	<u>\$ 11</u>	<u>\$ 124</u>	<u>\$ -</u>	<u>\$ 135</u>
	December 31, 2009			
	Level 1	Level 2	Level 3	Total
	NT\$	NT\$	NT\$	NT\$
	(In Millions)			
Assets				
Derivatives - currency swap contracts	\$ -	\$ 7	\$ -	\$ 7
Convertible bonds	34	-	-	34
Available-for-sale securities				
Open-end mutual funds	16,832	-	-	16,832
Domestic listed stocks	500	-	-	500
Corporate bonds	-	103	-	103
Real estate investment trust	<u>102</u>	<u>-</u>	<u>-</u>	<u>102</u>
	<u>\$ 17,468</u>	<u>\$ 110</u>	<u>\$ -</u>	<u>\$ 17,578</u>
Liabilities				
Derivative - forward exchange contracts	<u>\$ -</u>	<u>\$ 1</u>	<u>\$ -</u>	<u>\$ 1</u>

Index future contracts and convertible bonds are actively traded or have quoted prices. For forward exchange and currency swap contracts, fair values are estimated using industry standard valuation models. These models use market-based observable inputs including interest rate curves, foreign exchange rates, and forward and spot prices for currencies to project fair value.

Available-for-sale financial assets include open-end mutual funds, domestic listed stocks, foreign listed stocks, and real estate investment trust fund that are actively traded or have quoted prices.

Corporate bonds are using market-based observable inputs including duration, yield rate and credit rating for fair value valuation.

Assets measured at fair value on a nonrecurring basis

The tables below set out the balances for those assets required to be measured at fair value on a nonrecurring basis and the associated losses recognized during the years ended December 31, 2008 and 2009:

	For the Year Ended December 31, 2008			
	Level 1	Level 2	Level 3	Total
	NT\$	NT\$	NT\$	Losses
	(In Millions)			
Assets				
Cost method investees - RPTI and ETS	\$ _____ -	\$ _____ -	\$ _____ 44	\$ _____ 25

	For the Year Ended December 31, 2009			
	Level 1	Level 2	Level 3	Total
	NT\$	NT\$	NT\$	Losses
	(In Millions)			
Assets				
Cost method investees - ETS, and DIG	\$ _____ -	\$ _____ -	\$ _____ 24	\$ _____ 20
Other assets	\$ _____ -	\$ _____ -	\$ _____ -	\$ _____ 5

The Company evaluated its cost method investees for impairment by using valuation models based on future cash flow because there are no quoted fair value for such investments. Cost method investees held with a carrying amount of NT\$69 million were written down to their fair value of NT\$44 million, resulting in an impairment charge of NT\$25 million, which was included in earnings for year ended December 31, 2008.

The Company evaluated its cost method investees for impairment by using valuation models based on future cash flow because there are no quoted fair value for such investments. Cost method investees held with a carrying amount of NT\$44 million were written down to their fair value of NT\$24 million, resulting in an impairment charge of NT\$20 million, which was included in earnings for the period for year ended December 31, 2009.

Certain non-financial assets and non-financial liabilities measured at fair value on a recurring basis include reporting units measured at fair value in the first step of a goodwill impairment test and other non-financial long-lived assets measured at fair value for impairment assessment. Other assets held with a carrying amount of NT\$5 million were written down to their fair value of nil, resulting in an impairment charge of NT\$5 million, which was included in earnings for the period.

e. Income tax

Effective January 1, 2007, the Company adopted the guidance of income taxes uncertainties. The guidance prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The guidance also provides guidance on derecognition, classification, interest and penalties, disclosure and transition. The evaluation of a tax position in accordance with the guidance is a two step process. The first step is recognition, where we evaluate whether an individual tax position has a likelihood of greater than 50% of being sustained upon examination based on the technical merits of the position, including resolution of any related appeals or litigation processes. For tax positions that are currently estimated to have a less than 50% likelihood of being sustained, zero tax benefit is recorded. For tax positions that have met the recognition threshold in the first step, we perform the second step of measuring the benefit to be recorded. The actual benefits ultimately realized may differ from the Company's estimates. The adoption of the guidance did not have a material impact on the Company.

36. SUBSEQUENT EVENT (UNAUDITED)

On April 7, 2010, the Taiwan High Court rendered its judgment, ruling that we need to pay NT\$23 million as compensation in addition to the NT\$17 million from the Taiwan Taipei District Court judgment, along with interest calculated at 5% per annum from July 23, 2005 to the payment date and 12.5% of Chunghwa Post Co., Ltd.'s court fees from its original suit and subsequent appeal as compensation. Chunghwa did not accrue the settlement amount related to the judgment from the Taiwan High Court on its consolidated financial statement as of and for the year ended December 31, 2009.